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ANALYSIS OF THE FIRST YEAR IMPLEMENTATION OF THE
DIRECTIVE 2014/95/EU IN THE ITALIAN CONTEXT”**

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INTRODUCTION

Nowadays it is clear that promoting financial stability and sustainable development by enhancing the links among investment decisions, corporate behavior and reporting has become a global need. In recent years, companies and users of corporate information have recognized that financial outcomes alone do not present a true and fair view of companies' business performance. Besides traditional financial information, they also have to consider material non-financial information (NFI) in order to understand companies' current performance and future prospects.

There is no standard universally agreed definitions of the term. However, for the purpose of this Thesis, NFI reporting indicates the disclosure of qualitative performance measures that are not expressed in monetary units, such as ethical, social and environmental issues, and that are expressly requested to be disclosed by the *European Directive 2014/95/EU on non-financial and diversity information by certain large undertakings and groups*.

In the past years in fact, the EU has taken a soft approach with no general legal obligation on companies to adopt policies on sustainability issues or to report on them. Many European companies already published sustainability reports on a voluntary basis, but with the introduction of the Directive on NFI the European Commission expressly mandated specific requirements on sustainability issues.

Generally, companies within the scope of the Directive should disclose information on policies, risks and outcomes in regard to environmental matters and social and employee-related aspects for human rights. Also international standard setter Organizations such as Global Reporting Initiative (GRI) and International Integrated Reporting (IIR) Framework contribute to the diffusion of practices on sustainability reporting, helping companies in their NFI disclosure.

The Directive makes a focus also on the role of the External Auditor in the process of NFI reporting, establishing at least a compulsory check “*whether the required information is included in either the management report or a separate report*”. In addition, Member States may require that also the content of NFI report should be “*verified by an independent assurance service provider*”. With the implementation of the Legislative Decree 2016/254, Italy is one of the Member States that chose to tighten the control over NFI with the request of the auditors' check on both the presence and the content of the NFI report.

Thus, the scope of this Thesis is to provide an overview of the changing corporate sustainability reporting and assurance landscape, outlining its components, addressing current

challenges and performing an empirical analysis on the 2018 NFI reports published by listed companies in the first year of implementation of the Directive in the Italian context.

More in detail, in the first chapter a general introduction on the history and literature of corporate sustainability reporting and assurance development is reported.

The second chapter of the Thesis gives specific information about the regulatory environment which companies must be in compliance with. Standard setter, both for reporting and assurance, need to address investors' and companies' challenges avoiding that leading companies implement a “tick-box” approach that adds no value for users of corporate reports.

The third chapter focuses on the role of the auditor in the assurance of NFI. While current assurance practice is often focused on historic performance, nowadays auditors have to be familiar also in the assurance of more qualitative and forward-looking information about the long-term viability of the company. Auditors will be expected to look beyond the numbers and they will need to collaborate with people in other sectors of the business and outside the business. They will have to think and behave more strategically and become more involved in decision-making than before.

Finally, in the last chapter an empirical analysis on the NFI reports published by Italian listed companies in 2018 is performed. In detail, the main trends resulting from the first-year implementation of the European Directive 2014/95/EU are identified in order to give the readers a general understanding of the Italian sustainability reporting landscape in light of the new adoption regulation on NFI. At the end of the analysis it is also reported an example of a corporate NFI reporting process to show how a company can concretely comply with the legislative requirements in an efficient and useful manner both for the company itself and for external users of corporate report such as current shareholders or future investors.

CHAPTER I

SUSTAINABILITY REPORTING AND ASSURANCE - TRENDS AND THEORETICAL BACKGROUND

1.1 CORPORATE SUSTAINABLE DEVELOPMENT

The concept of corporate Sustainable Development has drawn significant attention globally within scientists, experts, politicians and in the business press. There are several definitions of sustainability and in addition its meaning seems to vary over time. According to the well-known Brundtland Report, the most common definition of Sustainable Development is “*a development which meets the needs of the present without compromising the ability of future generations to meet their own needs*”¹.

The concept of Sustainable Development was the central objective of a series of conferences started in 1992 with the Rio Earth Summit in which the United Nations defined a political plan for sustainable development called “Agenda 21”. In 2012, a second Earth Summit, Rio+20, took place to renew the previous agreements and to make the global sustainable strategy more concrete. In September 2015, at the UN Sustainable Development Summit the United Nations General Assembly adopted the document “Transforming our world: the 2030 Agenda for Sustainable Development”. The 2030 Agenda is the new global sustainable development strategy. At the core of the 2030 Agenda there is a list of 17 Sustainable Development Goals (SDGs) and 169 related targets to end poverty, protect the planet, and ensure prosperity and peace². The SDGs go far beyond the previous Millennium Development Goals (MDGs) by setting a wide range of economic, social and environmental objectives and calling all countries to take action despite their income levels.

Monitoring the SDGs will take place at various level – global, national, regional, and thematic – first of all by the ONU with the activities of the High Level Political Forum (HLPF). Despite the difficulty in SDGs measurement due to their multidimensional and qualitative nature, ad hoc indicators have been created to monitor the level of the achievement of any single goal and target.

¹ World Commission on Environment and Development (WCED), *Our Common Future*, Oxford University Press, 1987. Page 5

² See figure 1 in the next page

Fig. 1: List of Sustainable Development Goals (SDGs)

| Sustainable Development Goals | |
|--------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Goal 1. | End poverty in all its forms everywhere |
| Goal 2. | End hunger, achieve food security and improved nutrition and promote sustainable agriculture |
| Goal 3. | Ensure healthy lives and promote well-being for all at all ages |
| Goal 4. | Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all |
| Goal 5. | Achieve gender equality and empower all women and girls |
| Goal 6. | Ensure availability and sustainable management of water and sanitation for all |
| Goal 7. | Ensure access to affordable, reliable, sustainable and modern energy for all |
| Goal 8. | Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all |
| Goal 9. | Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation |
| Goal 10. | Reduce inequality within and among countries |
| Goal 11. | Make cities and human settlements inclusive, safe, resilient and sustainable |
| Goal 12. | Ensure sustainable consumption and production patterns |
| Goal 13. | Take urgent action to combat climate change and its impacts* |
| Goal 14. | Conserve and sustainably use the oceans, seas and marine resources for sustainable development |
| Goal 15. | Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss |
| Goal 16. | Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels |
| Goal 17. | Strengthen the means of implementation and revitalize the Global Partnership for Sustainable Development |

* Acknowledging that the United Nations Framework Convention on Climate Change is the primary international, intergovernmental forum for negotiating the global response to climate change.

Source: UNGA, *Transforming our world: The 2030 Agenda for Sustainable Development*, 2015. Page 14.

From a European perspective, according to Eurostat³, over the last five years the EU area made progress towards all goals even if it should be noted that progress towards a given goal does not necessarily mean that the status of the goal is satisfactory. For a general overview, the EU made significant progress towards the overall achievement of SDG 7, SDG 12, SDG 15, SDG 11 and SDG 3 while it made moderate progress in SDG 4, SDG 17, SDG 9, SDG 5, SDG 8, SDG 1, SDG 2 and SDG 10. In the case of four goals – SDG 6, SDG 13, SDG 14 and SDG 16 - trends cannot be calculated due to insufficient data over the last five years.

At a national level, according to Alleanza Italiana per lo Sviluppo Sostenibile (ASviS), the Italian situation is described as follow: “ *Malgrado i passi avanti compiuti in alcuni campi, l'Italia resta in una condizione di non sostenibilità economica, sociale e ambientale. Se i partiti non manterranno lo sviluppo sostenibile al centro della legislatura, le condizioni dell'Italia saranno destinate a peggiorare anche in confronto ad altri paesi*”⁴. These are the words of Enrico Giovannini, representative of AsviS, to underline the fact that, despite some progress in limited goals, Italy remains in a situation of no sustainable development. Nowadays, our nation has no possibility to reach Agenda 2030 targets unless it would change radically its sustainable development's policies. According to AsviS analysis, between 2010 and 2017 Italy makes progress towards seven areas - SDG 3, SDG 4, SDG 5, SDG 9, SDG 12, SDG 13, SDG 17 - while six SDGs declined: SDG , SDG 8, SDG 10, SDG 6, SDG 11, SDG 15. For the remaining four SDGs – SDG 2, SDG 7, SDG 14 and SDG 16 – the situation remains stable.

Despite the single country situation, it is important to underline that the SDGs explicitly call on all businesses to apply their creativity and innovation to solve sustainable development challenges. Art.67 of 2030 Agenda reports as follow: “*Private business activity, investment and innovation are major drivers of productivity, inclusive economic growth and job creation. We acknowledge the diversity of the private sector, ranging from micro enterprises to cooperatives to multinationals. We call on all businesses to apply their creativity and innovation to solving sustainable development challenges.*”⁵

As the SDGs form the global agenda for the development of our societies, these goals will allow leading companies to demonstrate how their business helps to advance sustainable development by both maximizing positive impacts and minimizing negative externalities on people and on the planet. Furthermore, a concentrated effort to meet the SDGs will be a key

³ Eurostat, *Sustainable Development in the European Union: Monitoring report on progress towards the SDGs in an EU context*. 2017

⁴ Alleanza Italiana per lo Sviluppo Sostenibile (ASviS), Press release of 21 February 2018, 2018.

⁵ United Nations General Assembly (UNGA), 2015. Page 30

driver of the economic growth, an estimated US \$ 12 trillion a year in business savings and revenue by 2030 according to the Business and Sustainable Development Commission.⁶

Covering a wide spectrum of sustainable development topics relevant to companies the SDGs can help to connect business strategies with global priorities. Companies can use the SDGs as an overarching framework to shape, steer, communicate and report their strategies, goals and activities, which will allow them to capitalize in a range of benefits. First of all, reporting on SDGs improves companies' transparency and accountability towards their stakeholders. To this purpose, in 2015 a task of experts of Global Reporting Initiatives, United Nations Global Compact and World Business Council for Sustainable Development published the *SDG Compass Guide*, to support companies in developing a strategic approach to the SDGs and in integrating the SDGs into existing sustainability reporting practices. In addition, during the UN Private Sector Forum held in 2018 in New York the *Business reporting on SDGs* was presented, prepared by UN Global Compact, GRI and PwC. This guide, divided into a Practical Guide and an Analysis of the Goals and Targets, aims to help companies of all types and in all countries to move beyond the current trend of simply mapping activities and programs versus the SDGs. The contents of this publication are aligned with the United Nation Guiding Principles on Business and Human Rights, the ten Principles of UN Global Compact and the GRI Framework. The publication outlines a process of “principle prioritization” aimed at helping companies to identify and prioritize their SDG targets and to report on their progress. Based on a research recently conducted by PwC⁷ on a sample of 470 companies around the world, it seems clear that the majority of companies already know that the SDGs will shape the future of business. The results of this research are eye-opening. As detailed in the report, 62% of the companies analysed currently discuss the SDGs in their reporting. However, only 37% of these companies that report on SDGs have prioritised individual SDGs. The other 25% continue to discuss the goals in general terms. That leaves 38% of companies who still have not addressed the goals at all. In its conclusion, the research highlights the fact that when companies incorporate the goals into their growth strategies, core options, value chains and policy positions, they will benefit from new opportunities and markets, achieve big efficiency gains and also enhance their reputations in the eyes of governments and society. Moreover, in the most recent KPMG survey⁸ on corporate social responsibility reporting, it is clear that companies start to link sustainability reporting and SDGs. Analysing a sample of the 100 largest companies in each country (N100), the results

⁶ Business and Sustainable Development Commission (BSDC), *Better Business, Better world*. 2017. Page 12

⁷ PwC, *SDG Reporting Challenge 2017: Exploring business communication on the global goals*. 2017. Page 10

⁸ KPMG, *The road ahead: Survey of Corporate Responsibility Reporting 2017*, KPMG International, 2017.

show that all the top 10 countries where N100 companies reporting on the SDGs are European or Latin American countries. Italy is positioned at the tenth place with 41 companies on N100 Italian companies reporting on these issues.

1.2 CORPORATE SUSTAINABILITY REPORTING

Around the mid-sixties the interest in social accounting developed. The concept of social accounting can take different forms and be presented under various labels: *"social responsibility accounting, social audits, corporate social reporting, employee and employment reporting, stakeholder dialogue reporting as well as environmental accounting and reporting"*. However, the "social accounting" is about accounting for non-financial information, such as ethical, social and environmental issues. In recent years, after the publication of EU Directive 2014/95/EU, the term Non-Financial Information (NFI) Disclosure was introduced to indicate the disclosure of performance's measures that are not expressed in monetary units.

Despite the attention that the issue of reporting and verification of social and environmental performance of companies had initially aroused, during most of the '70s there was a clear reversal of the trend. Between the '70s and '80s, companies were more focused on economic performance and profit maximization than on social issues. However, in this second phase, companies started to implement social and environmental goals but without making any connection with the company's activities. This phase was marked by "green washing" reports and eco-marketing campaigns which were deceptive marketing tools that include little in the way of substance. The rebirth of interest on the topic of social accounting returned towards the end of the '80s. The publication of the Brundtland Report and the affirmation of the concept of sustainable development highlight the need to protect the ecological environment and form the basis for the doctrinal developments in the 1990s. These years are characterized by an increase in the number of reports voluntary prepared by companies, an increasing recourse to the verification of these documents by independent third parties and the intensification of legislative measures promoted by European and non-European countries. Moreover, in the first years of 2000, international guidelines and standards were approved which, even with subsequent modifications, are still today a point of reference for the preparation of sustainability reports and for their verification.

⁹ Gray R., The social accounting project and Accounting Organization and Society. Privileging engagement, imaginings, new accounting and pragmatism over critique?, Accounting, Organization and Society, vol. 27, 2002. Page 687

From a normative point of view, sustainable development is firmly anchored in the European Treaties and has been at the heart of the European policy for a long time. In this regard, recently EU issued the Directive 2014/95/EU and the subsequent European Guidelines (EUG) 2017/C215/01 to mandate European Public Interest Entities (PIEs) to convey non-financial information. The main aim of this EU Directive is to improve organizations' accountability toward stakeholders. Current accounting systems based on retrospective financial data have, in fact, been considered inadequate to satisfy the need for information of investors and other stakeholders and thus provide an acceptable level of transparency and accountability.

Moreover, the specific purpose of EUG is to “*help companies to disclose high quality, relevant, useful, consistent and more comparable non-financial information in a way that fosters resilient and sustainable growth and employment, and provide transparency to stakeholders (...). They are intended to help companies draw up relevant, useful and concise non-financial statements according to the requirements of the Directive*”¹⁰.

According to 2017 KPMG survey, “*the real impact of the Directive will start to become evident during 2019 or even 2020, following some delays in transportation and a transitional period as companies become familiar with the legislation and introduce new internal reporting system or adapt their existing ones. Despite the delays and teething troubles, the Directive is a key step to increase the importance of sustainability reporting, particularly in those EU Member States where no such requirements previously existed*”¹¹.

European legislation regarding the disclosure of “non-financial and diversity information” by large companies was adopted by the Italian Legislature on December 30, 2016 by means of the Legislative Decree 254, which entered into force on January 25, 2017 (to be applied starting from the fiscal year 2017). It should be noted that, in break with normal practice in Italy, this Decree was adopted by the Italian Legislation in a not entirely faithful way introducing modification and additions, as it is explained in Chapter 2 of this Thesis.

According to the EU Directive, NFI reports could be prepared following international frameworks, Union-based frameworks or national frameworks. The idea behind this approach is to best utilise already existing tools and also to create bridges between European and international reporting, thereby making NFI comparable.

Therefore, there is no single universal guideline or disclosure format based upon which companies can report their activities. Some standards only address social issues, while others only cover environmental issues. Some standards are general in nature, while others have more specific reporting requirements. Moreover, some standards more closely resemble

¹⁰ European Commission, *Communication of Guidelines on non-financial reporting*, Official Journal of the European Union, 5.7.2017. Page 4

¹¹ KPMG, 2017. Page 12

guidelines or recommendations while others have specific criteria for certification or external reporting purposes. There are many international guidelines formulated by different organizations such as the United Nations (UN), Global Reporting Initiative (GRI) and the International Standard Organization (ISO). There are also hundreds of domestic sustainability reporting guidelines, principles and regulations and several other global initiatives such as the Organization for Economic Cooperation and Development (OECD) Guidelines or International Labour Organization (ILO) Conventions. However, currently the most widely recognized sustainability reporting standards are the Global Reporting Initiative (GRI) guidelines and the International Integrated Reporting Council (IIRC) Framework, both at international and national levels. Given their predominance, only these two main frameworks are chosen to be analysed in the following chapters, in particular in the last paragraph of Chapter 2, where it is provided an in depth analysis of GRI and IIRC frameworks in the light of EU Directive 2014/95/EU.

Before to analyse the corporate reporting on sustainability issues from a theoretical perspective, it is necessary to clarify the meaning of *sustainability report* and of *NFI report* used in the following paragraphs. While the term sustainability report are generally indicated all the forms of social and environmental disclosures published by companies, both on mandatory and voluntary basis. Instead, the term NFI report refers specifically to the mandatory disclosure requested by the EU Directive, largely explained in the Chapter 2 of this Thesis.

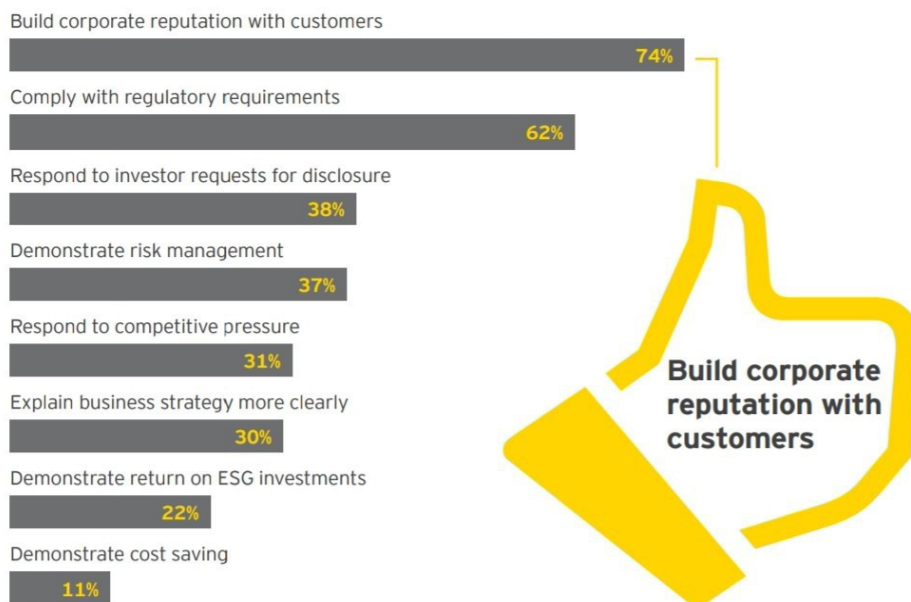
Given these clarifications, it can be argued that there are two main reasons that led to the growing sustainability reporting scale. The first reason is corporate awareness that the public information on the implemented social and environmental initiatives is good for business and the second reason is the increasing pressure of various stakeholders' groups.

There are, in fact, numerous benefits that company can get by successfully implementing sustainability reporting, such as transparency, branding, identify cost savings, reputation, legitimacy, competitive advantage and enhanced moral among the employees. Disincentives regarding establishment of a sustainability report are for example high costs or a perception that it will not increase sales because of customers' disinterest¹². Moreover, companies need to gain especially the approval of their current and potential investors. According to a survey on investors' usefulness of sustainability information conducted by EY and the Institutional

¹² Gray R., Current Developments and Trend in Social and Environmental Auditing, Reporting and Attestation: A Review and Comment, *International Journal of Auditing*, vol. 4, n.3, 2000. and Kolk, A decade of sustainability reporting: Developments and significance, *International Journal of Environment and Sustainable Development*, 2004.

Investor's (II) Research Lab in 2017¹³, the reasons why companies disclose that information are summarized as follow:

Fig. 2: Reasons why a company reports details on its sustainability information



Source: EY and II Research Lab, *Is your non-financial performance revealing the true value of your business to investors?*, 2017, Pag. 8.

According to the surveyed investors, the biggest motivating factor for most companies remains building their corporate reputation with customers, followed by complying with regulatory requirements. Investor demands play a role as well, along with the incentive of improving stock valuations, but to a much lesser degree.

On the other side, investors and the users of sustainability reports in general want the company to give a true and fair view of the companies' achievements¹⁴, making the company itself more accountable. The concept of accountability can be defined as the duty to provide an account through the recognition of those actions of which a subject is held responsible. Accountability therefore presupposes the recognition of a social responsibility by an organization, which in general terms is the responsibility of the accountant to provide a report of company's actions to the accountee¹⁵.

¹³ EY and II Reaserach Lab, *Is your non-financial performance revealing the true value of your business to investors?*, 2017. The sample is composed by 320 responses from senior decision-makers at buy-side institutions around the world, plus 10 investors' interviews to capture contextual details.

¹⁴ Gray R., 2000.

¹⁵ Gray R., Owen D., Adams C., *Accounting & Accountability. Changes and Challenges in corporate social and environmental reporting*, Financial Times-Prentice Hall, 1996. Page 37-38

Therefore, a sustainability report made with accountability purposes will be structured with the aim of responding to stakeholders. If the goal is to satisfy the demands of stakeholders, it is necessary that the company involves its stakeholders in their reporting process. According to some studies, the more the companies realize stakeholder engagement, the more they are responsible. Elkington specifies that stakeholder engagement means the involvement of stakeholders in a dialogue with the company in order to "*understand if the priorities of the company take into account their expectations and their needs, and to understand the impact that processes and company policies have on them*"¹⁶. The accountability of the reports resulting from the effective participation of the stakeholders could therefore be considered as better than the accountability attributable to reports of a unilateral composition, which could be considered only self-referential documents.

Once the concept of stakeholder engagement is identified, it is opportune to reflect on which and how many stakeholders to be part of the engagement process. Recalling the 1996 work of Gray et al., companies are responsible and must be accountable to all stakeholders that may be affected by their activities. This ideal model of engagement, however, clashes with reality, which is characterized by the presence of numerous and often conflicting interests of stakeholders and the objective difficulty of communicating with some of them such as future generations or the ecological environment. It is therefore necessary to identify criteria that can guide the "prioritization" of the stakeholders. For example, Elkington notes that only the stakeholders having a "critical role in relations with the company" must be part of the engagement process, i.e. those considered capable of producing more relevant influences on business decision-making models. On the other hand, Mitchell et al. identified as highly qualified stakeholders those who, in the perception of the managers, are bearers of three main attributes (power, legitimacy and urgency)¹⁷. The involvement of the stakeholders considered critical or relevant in the reporting process should therefore guarantee the accountability of the company. However, the sustainability disclosure does not always pursue the aim of accountability. The management can in fact implement reporting practices whose purpose is not so much that of accountability as the much more utilitarian scope of *managerial capture*. In the presence of managerial capture, sustainability reporting is subordinate to the needs of management that controls the entire process of preparing reports often for purposes of image, public relations, management of stakeholders, reconquering an eroded legitimacy, etc. In this perspective, the stakeholder engagement itself ends up as a mere exercise of stakeholder

¹⁶ Interview to John Elkington, in Rusconi G., Dorigatti M., *Teoria generale del bilancio sociale e applicazioni pratiche*, Franco Angeli, Milano, 2005. Page 227

¹⁷ Mitchell R.K., Agel B.R., Wood D.J., *Toward a Theory of Stakeholder Identification and Salience: Defining the principle of who and what really counts*, *Academy of Management review*, 1997.

management control. In order to not translate stakeholder involvement into a mere sophisticated managerial tool only, it is necessary to find a mechanism through which stakeholders opinion can directly influence the company decision-making processes.

To this end, Owen, Swift and Hunt stress the need of an administrative reform aimed at developing the accounting models suitable to increase the transparency of the company on one hand and on the other hand, the need of an institutional reform aimed at guaranteeing the empowerment of the stakeholders through models of a more stakeholder-oriented corporate governance¹⁸.

In summary, the most obvious problem is that companies can write whatever they want. For this reason, the diffusion of sustainability reports is linked to an increase in the number of critics. According to some studies, sustainability reports are not important tools in the company's accountability system, based on the recognized ethical duty to provide a faithful and transparent representation of the actions undertaken. These studies, in fact, highlight that the adoption of some sustainability reporting practices is merely symbolic because it is poorly linked to a better quality of sustainability reporting, and consider these documents as mere corporate green washing tools¹⁹.

These aspects are strictly connected to the consideration of sustainability reporting as a management tool aimed at providing a favourable, but not neutral, representation of the company performance with the evident effect of altering the perception that stakeholders have of the business strategy. Moreover, it has been found that, unlike what companies claim, the sustainability reports remain incomplete (reporting performance portrayal gap)²⁰ and their content is of dubious reliability (credibility gap)²¹. In fact seems that the current trend in increasing levels of sustainability disclosure by companies is being undermined by a lack of confidence in both the data and the sincerity of the reported information. In the presence of the relative gaps, the same accountability towards the stakeholders is in serious discussion.

If we consider the important role that accounting and sustainability reporting can play in order to support both the decision-making process of management and of the stakeholders who are interested in the company activity, the importance to reduce the credibility gap is clear.

¹⁸ Owen D.L., Swift T., Hunt K., Questioning the role of stakeholder engagement in social and ethical accounting, auditing and reporting, *Accounting Forum*, vol. 25, n.3, 2001. Page 272

¹⁹ Michelon G., Pilonato S., Ricceri F., CSR reporting practices and the quality of disclosure: An empirical analysis, *Critical Perspective on Accounting*, vol. 33, 2015.

²⁰ Adams C.A., The ethical, social and environmental reporting-performance portrayal gap, *Accounting, Auditing & Accountability Journal*, vol. 17, n.5, 2004.

²¹ Dando N., Swift T., Transparency and Assurance: Minding the Credibility Gap, *Journal of Business Ethics*, vol. 44, n. 2, 2003.

Moreover, it seems the greater transparency is not enough to engender trust in sustainability report users.

A large part of the literature suggests that a greater credibility of the reports could be achieved through the use of a report verification performed by an independent and competent third party²².

Current Trends on Sustainability Reporting

Below are reported the most recent available data on the spread of sustainability reporting practices. For a correct data interpretation, is necessary to underline that in the years taken into reference in the following surveys the publication of a sustainability report was for a large part on a voluntary basis.

In Europe, the obligation to publish specific NFI was introduced by the EU Directive 2014/95 with different implementation's years among the EU Member States, as it is explain in the following Chapter of this Thesis. In the US, for example, the publication of sustainability information is currently on a voluntary basis.

The number of entities that report on sustainability information has significantly increase over the last years. According to a survey published by KPMG in 2017²³, 93% of the world's 250 largest companies by revenue (G250) are reporting on sustainability issues.

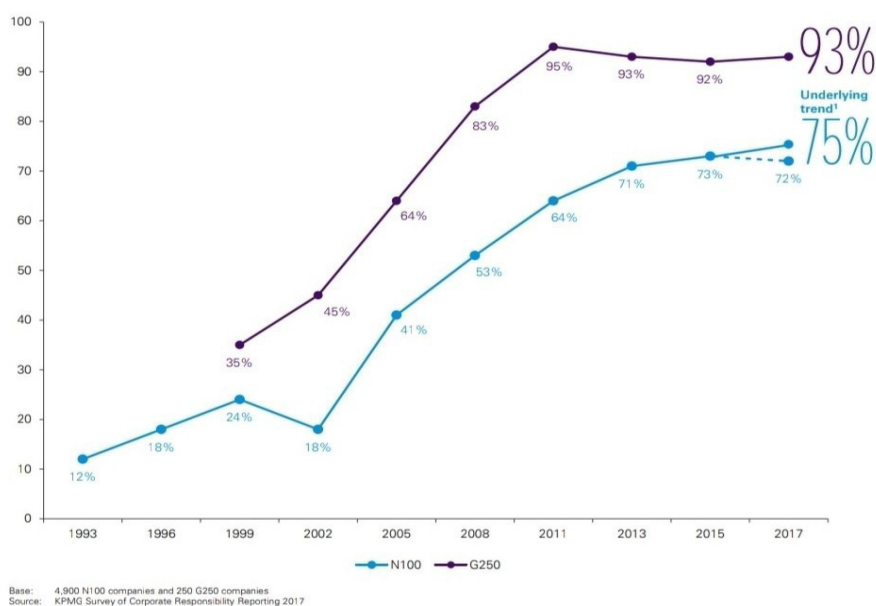
Overall, 75% of the 100 largest companies in several countries around the world (N100) are reporting on those issues, comparing to 12% in year 1993. KPMG 2017 survey projections over the next five years are *“to see greater alignment and consistency among the various reporting standards and frameworks. This should make reporting easier for companies and give governments and regulators greater clarity when formulating new, or reviewing existing, legislation. This should contribute to continued growth in reporting rates in that same period.”*²⁴

²² Dando N.,Swift T., 2003.

²³ KPMG, 2017. Page 9

²⁴ KPMG, 2017. Page 10

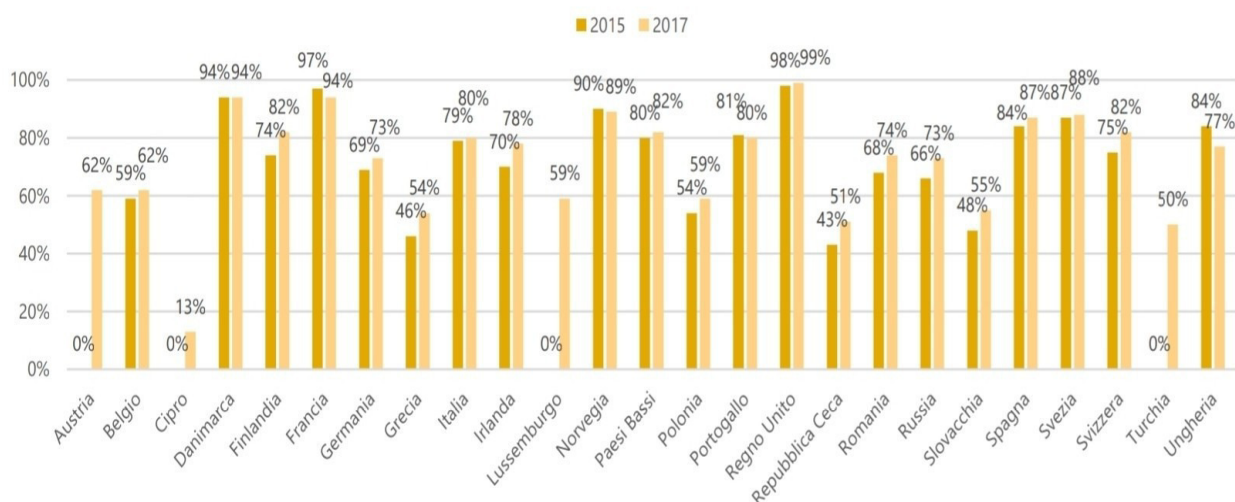
Graph. 1: Growth in global sustainability reporting rates since 1993



Source: KPMG, 2017. Page 9.

On EU level, the underlying trend is one of growth (up to 3 percentage points) but the divergence between Western and Eastern Europe observed in 2015 remains. The rate of reporting in Eastern Europe is still relatively low at 65%, despite an increase of 4 percentage points since 2015. Eastern European countries may be closing the gap with the rest of the region but are doing so slowly.²⁵

Graph. 2: Growth in EU sustainability reporting rate in 2015 and 2017

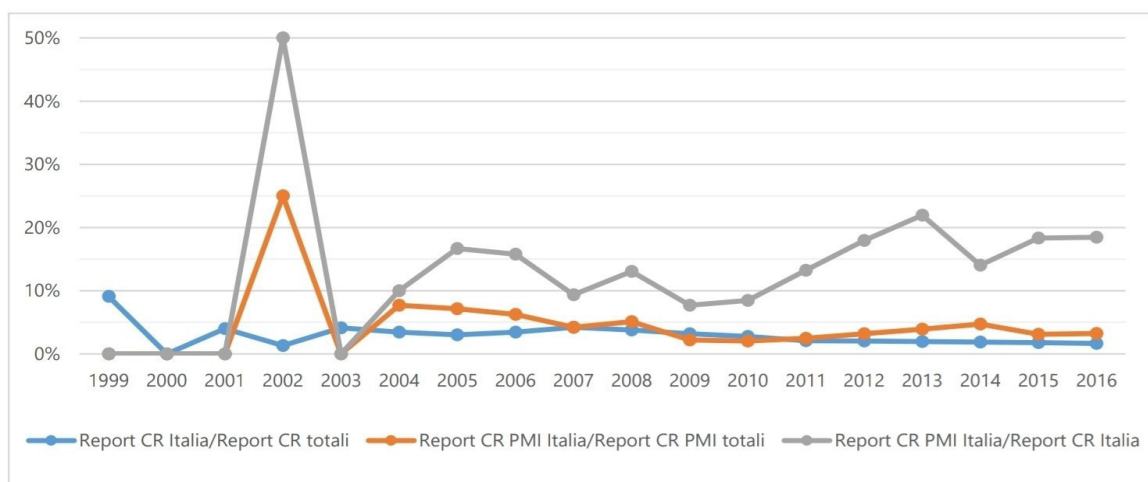


Source: Consiglio Nazionale dei Dottori Commercialisti (CNDC), 2017. Page 23.

²⁵ KPMG, 2017. Page 11

On a national level, according to a CNDC survey²⁶, 64% of the biggest 50 listed companies of the sample (BI 50) have published a sustainability report during the financial year 2014. However, the high rate of sustainability disclosure among listed companies has a relative significance considering the Italian context. The majority of the subjects operating in the Italian system are, in fact, SMEs with fewer resources to devote to sustainability reporting and with less immediate incentives considering their individual socio-environmental impact. CNDC survey, analysing the GRI Sustainability Disclosure Database, shows how the trend of sustainability disclosure in Italy is growing also for SMEs with an increasing number of SMEs sustainability reports published in the database, comparing to all published sustainability reports by Italian companies.

Graph. 3: Italian SMEs sustainability reporting rate in comparison to overall SMEs sustainability reporting rate and overall companies' sustainability reporting rate in GRI-SDD since 1999.



Source: Consiglio Nazionale dei Dottori Commercialisti (CNDC), 2017. Page 24.

Another research conducted by Venturelli et al.²⁷ analyses the quality of information disclosed in Italian sustainability reports in light of the approaching EU Directive application. In order to analyse the level of non-financial and diversity disclosure, an assessment model which records the required information as a percentage was created. The results show an average overall NFI score of 49% on a sample of 223 large companies considered entities of public interest in accordance with the EU Directive. The conclusion of Venturelli's research is that at

²⁶ Consiglio Nazionale dei Dottori Commercialisti (CNDC), *Disclosure di NFI, tendenze internazionali e nazionali sulle attività di rendicontazione e di asservazione*, 2017 2017.

²⁷ Venturelli A., Caputo F., Cosma S., Leopizzi R., Pizzi S., *Directive 2014/95/EU: Are Italian Companies Already Compliant?*, *Sustainability*, 2017.

the end of 2015 financial year, Italian companies had an important information gap to fill in order to be in line with the EU Directive requirements.

Despite every single countries situation, what is clear on a global scale is the growing use of GRI and IR as international guidelines for the reporting of sustainability issues. According to the recent data in the KPMG survey²⁸, both the majority of N100 (74%) and of G250 (89%) companies are using some kind of guidance or framework for their reporting while 63% of N100 reports and 75% of G250 reports use specifically the GRI framework. Moreover, one in ten N100 companies using GRI has reported in line with the new standards introduced at the end of 2016. Also the number of companies that specifically label their reports as “Integrated” is growing even if with a slow trend. In 2017, 14% of companies both in the G250 and N100 groups implement this labelling, compared to 11% of N100 and 15% of G250 at the end of year 2015. Around two thirds of these companies also refer to the International Integrated Reporting Council (IIRC) framework for integrated reporting.

1.3 THIRD PARTY ASSURANCE OF SUSTAINABILITY REPORTING

The growth in sustainability reporting has brought an almost concomitant growth in sustainability assurance. There is also similar confusion over terminology and similar ambiguity regarding the aim of the service²⁹. The terminological confusion that continues to distinguish the sustainability reports also concerns the labels used to identify both the verification activity of these reports (audit, verification, assurance, validation, etc.) and the documents issued by the third party at the end of its verification process (assurance statement, assurance report, auditor's verification statement, CSR assurance statement, etc.). The term that is currently most often used to refer to the checks made on the sustainability reports is "external assurance".

Particularly widespread in the context of audit studies is the concept of assurance on sustainability information as an activity carried out by a verifier with the aim of obtaining *"sufficient and appropriate evidence to express a conclusion that improves the reliability of information for the subjects interested in it"*. This definition, proposed by an accounting organization (IASB), is opposed to that provided by AccountAbility, an organization that operates at an international level with the aim of providing solutions to support social responsibility and sustainable development of companies. As outlined by the AA1000 AS, the assurance activity proposes to *"go beyond the mere verification of data, and to evaluate the*

²⁸ KPMG, 2017. Page 24 and 28

²⁹ Gray, 2000.

way in which the reporting organizations manage their sustainability". The IASB's more accountancy-based approach contrasts the more stakeholder-centred approach proposed by AccountAbility. It is important to underline that even if both the IASB and the AccountAbility gave their contribution in shaping the concept and the principles to follow in the assurance of sustainability information, the two organizations approach the issue from different perspective. The IASB follows the accounting schemes and procedures also for the assurance of sustainability information. Instead, the AccountAbility principles are used to provide suggestions and recommendation on the overall sustainability reporting process, focusing especially on the verification of the stakeholder engagement process. The main differences between the two organizations' principles are explained in detail in the next chapters of this Thesis.

Historically, there have been discussions and some confusion regarding the reasons why a company may benefit from an external assurance. The most acceptable reason is the lack of confidence in the fairness of what is reported by the companies in the reports. In fact, if the adoption of some sustainability reporting practices is perceived as merely symbolic and the reports are considered mere corporate green washing instruments, it is inevitable that also the accountability and transparency of these reports get lost. On the other hand, some theorists as Michelin, Pilonato and Ricceri³⁰ conclude that there is no relationship between sustainability assurance and quality of the sustainability information. They argue that not only the process of sustainability reporting, but also the assurance process could be seen as a symbolic action that companies use to influence stakeholders' perception. According to Ball et al.³¹, an assured company controls the assurance process to a considerable degree focusing on internal systems at the expense of comments on the performance. It implies that the assurance service is used as a managerial tool rather than an instrument for external transparency and accountability. A similar conclusion was made by Bepari and Mollik³². According to them, sustainability assurance do not produce accountability, but it is used only as a managerial tool with focus on internal systems, data and processes.

To avoid this problem, in the literature has been identified as a key factor for a successful assurance of sustainability reports the stakeholder inclusiveness (stakeholder engagement).

³⁰ Michelin G., Pilonat S., Ricceri F., 2015.

³¹ Ball A., Owen D.L., Gray R., External Transparency or Internal Capture? The role of Third Party Statements in Adding Value to Corporate Environmental Reports, in *Business Strategy and the Environment*, vol. 9, n. 1, 2000.

³² Bepari M.K., Mollik A.T., Stakeholders' interest in sustainability assurance process: An examination of assurance statements reported by Australian companies, *Managerial Auditing Journal*, vol. 31, n. 6-7, 2016.

Edgley et al.³³ investigated stakeholder inclusiveness and managerial capture in the assurance process. They concluded that it is increasingly important to include stakeholders in the assurance process, to enhance accountability. Therefore, assume greater importance assurance stakeholder-centred models, in which the assurance issuers interacts directly with the stakeholders and provides feedback to the company. This dialogue between assurance issuers and stakeholders contributes to the creation of an assurance process that goes far beyond the verification of the facts. It becomes a process in which the stakeholders' requests are part of the assurance report itself. The stakeholder engagement activity helps to increase the credibility and reliability at both levels of sustainability reporting process and assurance process itself. With reference to the sustainability reports, the involvement of the stakeholders in the identification of the data and information to be reported can help to ensure that what is reported is truthful and therefore worthy of trust. The same considerations can also apply to the assurance process.

Despite the lack of a common vision on assurance importance in the literature, what is clear is that assurance issuers are seeking general legitimization of their role and of the assurance process³⁴. They are risking impoverished reputation if they do not perform a sufficient assurance. In addition, there is the risk of expectational gaps. For these reasons assurance issuers are pressured to rationalize and standardize the assurance process, and make it transparent.

In the absence of an agreed-upon set of standards for the reporting of sustainability information, also specific guidance on the assurance of this information is currently not available, even if some general standards could be applied. Just to anticipate the contents of the following chapters of this Thesis, the two main assurance standards for sustainability information are the International Standards on Assurance Engagements ISAE 3000 (Revised) and the AccountAbility AA1000 Assurance Standard (AA1000AS).

ISAE 3000 were launched by the International Auditing and Assurance Standard Board (IAAS) and come into force in January 2005. According to ISAE 3000, Assurance engagement is *"an engagement in which a practitioner expresses a conclusion, designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against a criteria"*. The AccountAbility AA1000 Assurance Standard (AA1000AS) is the other of the two main

³³ Edgley C.R., Jones M.J., Solomon J.F., Stakeholder inclusivity in social and environmental reporting Assurance, *Accounting, Auditing and Accountability Journal*, vol. 23, 2010.

³⁴ Power M.K., Auditing and the Production of Legitimacy, *Accounting, Organizations and Society*, vol. 28, n.4, 2003

assurance standards. It was launched by the organization Account Ability in March 2003 as the world's first sustainability assurance standard covering sustainability reporting and performance, and based on principles of materiality, completeness and responsiveness.

It was last revised in 2008 to *“provide a platform to align the non-financial aspects of sustainability with financial reporting and assurance”*. It provides a means for assurance issuers to go beyond mere verification of data, to evaluate the way reporting organizations manage sustainability, and to reflect that management and resulting performance in its assurance statements. However, according to both standards, assurance refers to the reassurance of completeness, accuracy, honesty and balance of the information provided in the reports in which company's stakeholders can rely on.

Therefore, assurance statement should answer two questions, namely: *“Does this report give an account of the company and its performance that readers can rely on?”* and *“Is the report complete, accurate, honest and balance in its portrayal of the organization?”*³⁵.

Current Trends on third party Assurance of sustainability information

Below are reported the most recent available data on the spread of sustainability information's assurance by an independent third party. For a correct data interpretation, is necessary to underline that the in the years taken into reference in the following surveys also the request by companies of an assurance on sustainability information was for a large part on a voluntary basis.

In Europe, the obligation to assure specific NFI was introduced by the EU Directive 2014/95 with different implementation's years and different implementation's requirements among the EU Member States, as it is explain in the following Chapter of this Thesis.

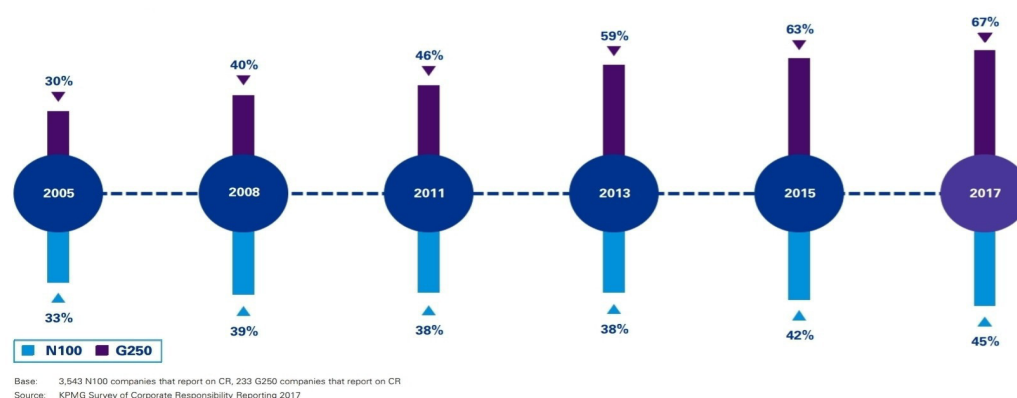
In the US, for example, also the assurance of sustainability information is currently on a voluntary basis.

The latest KPMG survey³⁶ on sustainability reporting shows that a growing number of companies engage an independent third party to assurance their sustainability information. Globally, in 2017 67% of the 250 largest global companies (G250) have their sustainability information assured by an independent third party during the year 2017.

³⁵ Adams C.A., Evans R., 2004.

³⁶ KPMG, 2017.

Fig. 3: Growth in Independent assurance of non-financial information.



Source: KPMG, 2017. Page 26.

On a national level, assurance rates among N100 companies remain low (currently 45%), but KPMG projections support a growing trend within the next two to five years also in N100 companies. The data suggests that assurance rates increase most rapidly in countries where high rates of sustainability reporting have been achieved. Based on the data reported in 2008 and 2011 KPMG surveys, the assurance rates on a single country level are as follow:

Tab. 1: Assured Sustainability reports for country (in percentage values)

| Paese | 2002 | 2005 | 2008 | 2011 |
|---------------------|------|------|------|------|
| Europa | | | | |
| Danimarca | 45 | 31 | 46 | 65 |
| Finlandia | 29 | 19 | 30 | 29 |
| Francia | 14 | 40 | 73 | 60 |
| Italia | 66 | 70 | 61 | 64 |
| Paesi Bassi | 38 | 40 | 44 | 41 |
| Spagna | 27 | 44 | 70 | 65 |
| Svezia | 15 | 5 | 33 | 42 |
| UK | 53 | 53 | 55 | 56 |
| Asia Pacific | | | | |
| Australia | 52 | 43 | 42 | 51 |
| Giappone | 26 | 31 | 24 | 23 |
| Africa | | | | |
| Sud Africa | 100* | 22 | 36 | 31 |
| America | | | | |
| Canada | 10 | 10 | 19 | 21 |
| USA | 2 | 3 | 14 | 13 |

* Only one sustainability report

Source: KPMG, 2008. Page 58 and KPMG, 2011. Page 29.

The table shows also the differences between the various countries analysed. In 2011 survey, the countries with the highest rate of assurance reports are Denmark, Spain and Italy.

On the Italian level, a CNDC survey³⁷ shows that 19 sustainability reports were assured on 32 sustainability reports published in 2014 by BI 50 sample of companies. This value represents 47.5% of the total, compared to 42% of N100 in KPMG 2015 survey.

1.4 THEORETICAL BACKGROUND

A number of theoretical frameworks have been used to explain the motivations, trends and nature of sustainability reporting and assurance. Despite the current interest in sustainability issues, for years corporate performance has been measured mainly in terms of profit maximization. This approach has significantly changed over the recent decades due to the growing demand of sustainability information by the public and especially by the company's stakeholders.

Sustainability reporting is the way that firms use to meet those demands from stakeholders and sustainability assurance is the instrument used by companies to improve the reliability and credibility of their sustainability report.

There are efforts to explain sustainability reporting and assurance in theory, and the most prolific theories used in literature to this purpose are Agency Theory, Legitimacy Theory and Stakeholder Theory. The Agency Theory is linked to the use of assurance statements as a managerial tool only for a company's self-interest. The self-interested behavior could be explained by the Legitimacy Theory. The Legitimacy Theory states that a company needs to have legitimacy, a “license to operate”³⁸ obtainable towards sustainability reporting disclosure. The Stakeholder Theory explains why and how firms disclose sustainability information. This theory suggests that the firms' stakeholders interest has to be taken into account when a strategy for operating is set. Since stakeholders are part of the society, the stakeholder theory and the legitimacy theory are said to be “*overlapping perspectives of the issue of reporting behavior*”³⁹ and can both be influential in describing sustainability disclosure practices.

³⁷ Consiglio Nazionale dei Dottori Commercialisti (CNDC), 2017.

³⁸ Deegan C., Introduction: The legitimizing effect of social and environmental disclosure. A theoretical foundation, *Accounting, Auditing and Accountability Journal*, vol. 15, n. 3, 2002.

³⁹ Deegan C., 2002.

Agency Theory

The Agency Theory considers the relationship between a principal and an agent, in which the principal engages the agent to perform the work on his behalf. The theory assumes self-interested behavior, which implies that the agent, who has decision-making authority, will not always act in the principals' best interests. When it is hard or expensive for the principal to monitor the agent and there are conflict of interests, agency problems can occur. The problem is that the principal cannot know whether the agent has behaved appropriately⁴⁰. The agency problem covers two aspects: moral hazard (hidden action) and adverse selection (hidden information), and both involve unobservable behavior by the agent. The agency theory can also be applied in the context of sustainability reporting and assurance. Then the society including organizational stakeholders represents the principal, and the reporting company represents the agent. Society receives information through sustainability reports and assurance statements, which should reduce information asymmetry⁴¹. However, it is unclear whether these sustainability disclosures indeed reduce information asymmetry. Literature has ascertained the existence of an information gap between companies and society on sustainability topics. Companies are the first to know the environmental and social consequences of their actions and can determine whether to disclose this information. This can result in companies taking actions in their self-interest (managerial capture).⁴²

Legitimacy Theory

The Legitimacy theory is closely related to stakeholder theory. They both find their origin in the political economy theory defined by Gray et al.⁴³ as “*the social, political and economic framework within which human life takes place*”. The legitimacy theory broadens stakeholder perception to the whole society. Organizations need to legitimate their activities by getting the approval of the society. The society has expectations and organizations need to interact by meeting the expectations of the society in order to survive⁴⁴. The legitimacy theory refers to a contract between society and companies whereby the latter adopt socially oriented behaviors in order to gain social approval. The existence of a social contract between companies and society is fundamental to the purpose of legitimation. Such contract is stipulated, though in

⁴⁰ Jensen M.C., Meekling W.H., Theory of firm: Managerial behaviour, agency costs and ownership structure, *Journal of Financial Economics*, vol. 3, n.4, 1976.

⁴¹ Power M., Auditing and Environmental Expertise: Between Protest and Professionalisation, *Accounting, Auditing & Accountability Journal*, vol. 4, n. 3, 1991.

⁴² See par. 1.2 of this Thesis.

⁴³ Gray R., Owen D., Adams C., 1996.

⁴⁴ Deegan C., 2002.

abstract terms, between the companies and the individuals that form a local community. The contract is based on mutually beneficial exchanges. The local community supplies companies with the natural and human resources; companies produce the goods and services for the community and they generate waste. Companies do not have an inherent right to resources or to exist, but they only have these rights when the society considers the company as legitimate, which is the case when a society regards companies as acting in an acceptable (legitimate) way. The terms of this social contract reflect the social expectations on the management of the company. Such expectations could be explicit or implicit. The first is about the firm's compliance with the laws and regulations; the latter concerns the interests of the community in the firm's activities. The legitimacy of a company could be threatened by the breach of explicit and implicit terms of the contract. A loss of the legitimacy creates serious hazards that might endanger the survival of the firm. The community in fact may react in different ways: consumers may reduce the demand for a specific good produced by a specific brand; on the other hand suppliers can eliminate the supply⁴⁵. Thus, legitimation is achieved when practices, outcome and methods of operation are congruent with the expectation of those who confer legitimacy.

In the literature, two different kinds of legitimacy theory can be found. The first variable has as objective the individual firm. From this point of view, the firm's actions are aimed at filling the gap of legitimacy in order to reach the desired level⁴⁶. According to Lindblom, legitimacy could be defined as *“a status, which exists when an entities value system is congruent with the value system of the large social system of which the entity is a part. When a disparity, actual or potential, exists between the two value systems, there is a threat to the entities legitimacy”*. Lindblom's definition emphasises that the entities should undertake actions consistent with social values and expectations, which should be adapted according to social pressures. Deegan suggests that in accordance with the legitimacy theory, entities disclose sustainability information in order to create, maintain or restore their legitimacy.

The undertaking of social oriented actions, among which is the implementation of social reporting systems, is instrumental in order to achieve the objective of legitimacy. Lindblom has identified four ways in which the company can get or maintain legitimacy. They are as follows:

(1) educate and inform a wide public it considers important of actual changes in the results of the activities and operations that are consistent with the social values and expectations;

⁴⁵ Deegan C., 2000.

⁴⁶ Lindblom C.K., *The implications of organizational legitimacy for corporate social performance and disclosure, Critical Perspective on Accounting Conference*, New York, 1994.

(2) change the perception of the results of activities and operations by relevant stakeholders without changing the actual behavior (disclosure in annual reports may falsely indicate that the results of the activities and operations have changed);

(3) manipulate the perception of its activities by others, directing their attention to such areas where it meets social expectations while, at the same time, diverting it from the critical issues;

(4) change social expectations with respect to its activities, indicating that some of them are ridiculous or too unreasonable. Sustainability reports may be a tool for the implementation of each of the aforementioned strategies.

The second variable concerns the legitimacy of the capitalist system as a whole. In this case, the development of social reporting processes is functional to the systemic legitimacy of entire industries and countries⁴⁷. Naturally, legitimacy processes change from firm to firm, in space and time due to different social context in which the companies operate.

However, to maintain, enhance or establish organizational legitimacy, the society has to know what actions companies have undertaken. The only way to change society's perceptions about the company's legitimacy is to provide them with information. Even when companies' actions are in line with society's norms and values, not communicating these actions can lead to a threatened legitimacy. Disclosures, such as sustainability reports, play a crucial role⁴⁸. The legitimacy theory explains that sustainability reporting is an organizational tool for influencing society's perceptions of a company's legitimacy and for reducing and responding to stakeholder pressures by demonstrating that the company behavior is acceptable. Companies have the duty to report credible information to the ones who have a "right-to-know" even when it is not in the best interests of the company⁴⁹.

Stakeholder Theory

In 1984, Freeman developed the stakeholder theory according to which a company needs to manage its relationship with its important stakeholders in an appropriate manner in order to survive⁵⁰. Freeman defines stakeholder as "*any group or individual who can affect or is affected by the achievement of the organization's objectives*". Freeman suggests that if a company is responsive to the needs of its stakeholders, the developed good relationships

⁴⁷ Gray R., Owen D., Adams C., 1996.

⁴⁸ Deegan C., 2000.

⁴⁹ Deegan C., 2000.

⁵⁰ Freeman et al., Stakeholder Theory and "The Corporate Objective Revisited", *Journal of Organization Science*, vol. 15, 2004.

provide a competitive advantage for the company. Later Freeman improved such definition, clarifying that stakeholders represents a “*group that the firm needs in order to exist, specifically customers, suppliers, employees, financiers and communities*”.

The differences between the legitimacy theory and the stakeholder theory is that legitimacy concerns the whole society whereas the stakeholder theory only concerns about a specific group – stakeholders – within the society. What stakeholder theory adds to legitimacy theory is the recognition that there are different stakeholder groups with different views and organizational impacts that companies have to take into account, and whose concerns and pressure they have to respond to. Such groups have been classified in different ways, e.g. primary VS secondary, social VS non-social, external VS internal, voluntary VS involuntary. It is believed that companies give more importance to more powerful stakeholders⁵¹ and therefore the information disclosed in the reports is based on the needs of the most important stakeholders. By the way, Freeman⁵² underlined that organizations must satisfy all stakeholders, referring then to all the individual involved in the organization activity and not just the stockholders. He attempted to balance economic and social goals. This attempt is not easy to be realized because different groups of stakeholders have different interests. Moreover, not all the stakeholders hold the same power in respect to the organization. The company will pay more attention to some of the stakeholders who are deemed to have a strategic role for the survival of the organization itself. This concept could be summarized in the recent expressions "stakeholder prioritization" and "materiality analysis" performed by the company at the beginning of its reporting process, as it is explained in the following chapters of this Thesis.

⁵¹ Gray et al., Corporate Social and Environmental Reporting: A Review of the literature and a longitudinal study of UK disclosure, *Account.Audit.Account*, 1995.

⁵² Freeman R., *Strategic Management: A stakeholder Approach*. Boston: Pitman, 1984.

CHAPTER II

REGULATION AND REPORTING STANDARDS

2.1 VOLUNTARY VS MANDATORY DISCLOSURE

Since the publication of the first sustainability reports in the early 1980s, the literature has been particularly interested in the voluntary nature, which has always characterized non-financial disclosure. Several studies have shown that the development of sustainability reporting is encouraged by the managers' attribution of strategic value to sustainable activities. The recognition of this strategic value has focused managers' attention on new issues related to the theme of corporate reputation including, for example, the process of stakeholder engagement. These aspects gain additional value in regulated markets, considering that the qualitative level of non-financial information is positively correlated with the share value of the company. The consolidation of shareholder value is one of the main objectives of companies listed on regulated markets, which need investors' confidence to obtain capital and to contain the negative effects deriving from negative financial events.

According to some part of the literature, initially the idea was supported that only regulation could improve the quality and comparability of non-financial reporting⁵³. Moreover, in the short term the imposition by national governments of specific rules and specific reporting models can favor the standardization of such practices and the consequent increase in the number of reports containing non-financial information as well as the benchmarking and best practice creation. However, a quantitative increase is not always associated with a qualitative increase in information. In fact, from subsequent empirical studies, it has emerged how the regulation is not always associated with an improvement in the quality of non-financial reporting or, at least, that the regulation alone is not able to guarantee a better level of non-financial disclosure.

As for regulation, even for voluntary adoption it seems that the scientific debate has not come to univocal considerations. Some studies have identified solutions that can counteract the criticism directed to voluntary adoption, such as the lack of completeness, accuracy, neutrality, objectivity and comparability⁵⁴, these critics. Among the most relevant aspects, the literature has identified the adoption of shared guidelines, the stakeholder engagement in the reporting process and the assertion by third parties of the documentation produced. Regardless

⁵³ Deegan C.A., Introduction: The legitimizing effect of social and environmental disclosures – a theoretical foundation, in *Accounting, Auditing & Accountability Journal*, vol. 15, n.3, 2002.

⁵⁴ Adams C.A., The ethical, social and environmental reporting-performance portrayal gap, in *Accounting, Auditing & Accountability Journal*, vol. 17, n.5, 2004.

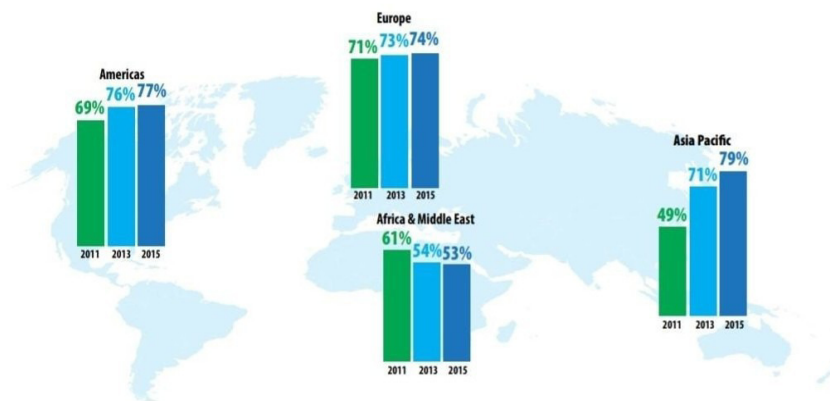
of this open debate on voluntary or mandatory non-financial information disclosure in the literature, on a practical level it seems that the increasing number of regulatory interventions by governments and the growing number of reporting instruments published by various Institutional Bodies confirms the regulation as a tool to improve the diffusion of non-financial reporting. A relevant contribution to the implementation of regulations is given by the increasing importance of the concept of Social Responsible Investment (SRI) for the investor community. This term means a medium-long term investment strategy that integrates, in the evaluation of companies, the financial analysis with the non-financial analysis in order to create value for the investor and for the company as a whole. The growing interest in SRI has led various institutions to take an interest in sustainable development issues introducing, for instance, an ethical stock exchange index or ethical rating agencies. An example is the recent introduction of sustainability reporting guidelines by the London Stock Exchange Group, a holding company established in 2007 from the merger between the London Stock Exchange and the Milan Stock Exchange. With the document "Revealing the full picture. Your guide to ESG reporting"⁵⁵ published in February 2017, the regulated market wanted to draw up a guide document for companies that, having to face socially responsible investors, can not disregard to acknowledge the priorities to be respected in the context of an ESG reporting process. An attempt in this direction was also made by the Sustainable Finance Forum which, since 2011, has asked Borsa Italiana to include, among the requirements for the IPO, the obligation of issuers to provide during the IPO process and subsequently also in the financial statements, information regarding the environmental and social aspects most relevant to the business activity in terms of risks and opportunities, the policies and management systems introduced to better manage these issues, and an accounting of KPIs that describes the company situation in a comprehensive manner. These requests are accepted at European level also thanks to the introduction of the Directive 2014/95/EU on the disclosure of non-financial and diversity information and on an Italian level with the legislative decree 2016/254, compelling the Public Interest Entities (PIEs) to communicate environmental and social information in company financial statements. With the publication of this Directive, the position of the European Union in the debate between voluntary and mandatory sustainability disclosure is therefore clear. A confirmation of the growing trend of regulatory initiatives is also given by the "Carrots & Sticks" report published in 2016 by KPMG in collaboration with GRI, the United Nations and the Center for Corporate Governance in Africa. The report "Global trends in sustainability reporting regulation and policy"⁵⁶ portray the state of sustainability reporting

⁵⁵ London Stock Exchange (2017), Revealing the full picture. Your guide to ESG reporting.

⁵⁶ KPMG (2016), Carrots & Sticks. Global Trend in sustainability reporting regulation and policy.

in 71 countries around the world. The research shows that the reporting instruments, both mandatory and voluntary, have gone from a number equal to 180 in 44 countries in 2013, to about 400 in 64 countries in 2016. The greatest growth was recorded in Europe, Asia and Latin America.

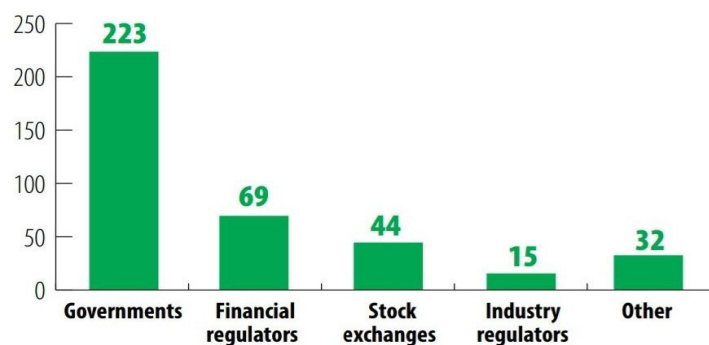
Graph. 1: Rate of sustainability reporting among the 100 largest companies per country



Source: KPMG, Global trend in sustainability reporting regulation and policy, 2016. Pag. 11.

About one in ten instruments adopt a “comply or explain” approach. In some countries this approach, even when applied to voluntary instruments, can result in a high level of sustainability reporting due to peer pressure. Almost 30% of reporting instruments is applied only to large listed companies and a further 14% applied to large companies, both listed and unlisted (where “large” is defined by various metrics, including the number of employees, equity and turnover). The research also shows that most of the interventions between 2013 and 2016 provided for mandatory reporting forms.

Graph. 2: Mandatory vs voluntary instruments, 2016 vs 2013

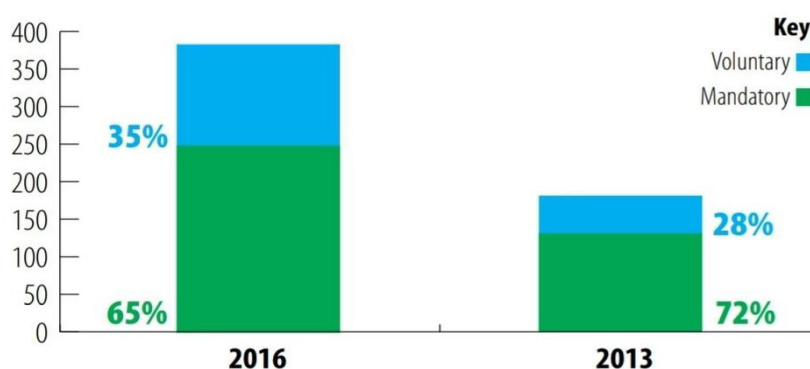


Source: KPMG, Global trend in sustainability reporting regulation and policy, 2016. Pag.12

Therefore, both governments and regulators increasingly require or encourage companies to disclose sustainability information. The first most active issuers of sustainability reporting instruments are governments, in fact in over 80% of the countries studied, governments have introduced some form of regulatory sustainability instrument. This does not mean that all governments instruments mandate sustainability reporting as over a quarter of governments instruments identified in 2016 are voluntary.

The second most active issuers of sustainability reporting instruments are financial market regulators where the number of reporting instruments issued by stock exchanges has almost doubled from 2013 to 2016.

Graph. 3: Number of instruments by issuing body, 2016



Source: KPMG, Global trend in sustainability reporting regulation and policy, 2016. Pag.14

These reflect a commendable effort by governments, regulators, stock exchanges and others to implement sustainability reporting policies through regulation, guidance and other instruments. While the trend is in the right direction, the bodies that issue reporting instruments need to make a further important step to focus on coordination and harmonization of all these reporting instruments.

2.2 EU REGULATION: DIR. 2014/95/EU and EUG 2017/C215/01

The 2014/95/EU⁵⁷ directive represents the most important result achieved by the EU in terms of sustainability reporting and in the broader concept of sustainable development. In 2017, three years after the publication of this Directive, the European Commission also published explanatory guidelines about the content of Directive, confirming that there is no homogeneity of views on the non-financial information disclosure. The EU Directive aims to

⁵⁷ European Commission, *Directive on the disclosure of non-financial and diversity information by certain large undertakings and groups* (2014/95/EU), Official Journal of European Union 15.11.2014.

ensure that organizations provide at least a 'package' of information that is considered unavoidable and comprehensive of non-financial information. Moreover, the specific purpose of the EUG is to *“help companies disclose high quality, relevant, useful, consistent and more comparable non-financial information in a way that fosters resilient sustainable growth and employment, and provide transparency to stakeholders (...). They are intended to help companies to draw up relevant, useful concise non-financial statements according to the requirements of the Directive”*⁵⁸.

At the EU level, the first intervention aimed at encouraging the debate on sustainable development issues can be considered the publication of the Green Paper called "Promoting a European framework for corporate social responsibility" in 2001 by the European Commission. In the same year the European Commission also made available the document called "The Act for the Single Market. Twelve levers to stimulate growth and strengthen trust. Together for a new growth". Both documents aim to raise awareness on the issues related to corporate social responsibility, and to highlight the need to improve the level of transparency and comparability of non-financial information disclosed by companies. These concepts were further reiterated in the communication called the "Renewed EU Strategy for the period 2011-2014 on corporate social responsibility". In this document, the European Commission has expressed the will to reformulate its own proposal for sustainability reporting in the context of the broader *Europe for 2020* strategy. In order to implement this impetus, in 2014 the Commission intends to modify part of the regulatory content present in the Directive 2013/34/EU concerning annual financial statements, consolidated financial statements and related reports of certain types of undertakings.

In this perspective, the 2014/95/EU directive on the disclosure of non-financial and diversity information by certain large companies and groups aimed to fill the limits of the previous regulatory intervention, in particular of the voluntary nature of information and the failure to forecast guidelines.

In this regards, given the fact that EU legislator had not established a common format to report non-financial information, Member States started a harmonization process. This harmonization process had to be done before the beginning of the financial year 2017, as reported by Article 4 of the Directive: *“Member States shall provide that the provisions referred to in the first sub paragraph are apply to all undertakings within the scope of Article 1 for the financial year starting on 1 January 2017 or during the calendar year 2017”*.

⁵⁸ European Commission, *Guidelines on non-financial reporting (methodology for reporting non-financial information)* (2017/C215/01), Official Journal of the European Union, 5.7.2017. Page 4.

With the release of Directive 2014/95/EU, the European Union Member States will have a common minimum standard for the disclosure of non-financial information to enable stakeholders to perform a quick and easy analysis between the undertakings.

On the other hand, in addition to this information, each undertaking can decide to disclose other non-financial information that does not appear on the list of compulsory topics specified by the Directive. In this way the EU legislator tries not to create a disclosure homologation but instead, to leave some grade of freedom to the companies in their disclosure of non-financial information. This point of the Directive is summarized in Recital 5 of the Directive: *“It is also necessary to establish a certain minimum legal requirement as regards the extent of the information that should be made available to the public and authorities by undertakings across the Union. The undertakings subject to this Directive should give a fair and comprehensive view of their policies, outcomes and risks.”*

The European Council's goal was in fact to create common legal disclosure frameworks not only among different industries, but also throughout European undertakings that are considered “large” and public interest entities (PIEs). The subjects affected by the directive are therefore the companies and parent companies with the qualification of PIEs, and that respect certain dimensional parameters *“referring to the average number of employees, total balance sheet and net sales. SMEs should be exempted from additional obligations and the obligation to publish the non-financial statement should be imposed only on large enterprises, in each case having on average more than 500 workers, in the case of a group, to be calculated on consolidated basis. This should not prevent Member States from requesting the disclosure of non-financial information to companies and groups other than companies that are subject to this Directive.”*⁵⁹

Therefore, according to the requirements of the Directive, the undertakings affected by the regulation are those considered first of all “large undertakings”. As defined by the Directive 2013/34/EU, large undertakings are those exceeding two out of three of the following criteria for two successive accounting periods:

- a balance sheet total of € 20 million, or
- a net turnover of € 40 million, or
- average number of employees of 250

The second condition under which an organization must produce a non-financial statement is to be considered a Public Interest Entity, meaning an entity which is:

⁵⁹ European Commission, Directive 2014/95/EU, Recital 14.

- trading transferable securities on the regulated market on the regulated market of any Member State, or
- a credit institution, or
- an insurance undertaking, or
- designated by a Member State as a PIE

This reported definition of PIE is generally accepted on EU level, but each Member State has also its own national definition of PIE, which could influence the “action range” of the regulation⁶⁰. Moreover, it is possible for Member States at the discretion of individual national laws, to extend the concept of Public Interest Entities to unlisted companies that issue financial instruments not listed on regulated markets but in any case present among the public in a relevant way. The Community legislator also recognizes the possibility for Member States to propose, at a national legislative level, voluntary participation in drafting the non-financial report also to SMEs that meet certain dimensional criteria specified by the individual Member State.

The third criterion to identify which subjects are affected by the Directive is that the undertaking has an average number of employees exceeding 500 during the financial year.

Moreover, as stated in Recital 14 of the Directive, the requirements have to be fulfilled by both single companies and group of companies, which are obliged to prepare, respectively, an individual non-financial statement and a consolidated non-financial statement.

The Directive also clarifies the only two possible cases of exception from these obligations. The first case is when an undertaking which is a subsidiary undertaking shall be exempted from the obligation to publish a non-financial statement as set in Art. 19 of the Directive if that undertaking and its subsidiary undertakings are included in the consolidated management report or the separate report of another undertaking drawn up in accordance with Art. 29 of the Directive on consolidated non-financial statement. The second case of exemption from the obligation set in Art. 19 is when an undertaking prepares a separate report that complies with the following requirements:

- The alternative report must refer to the same financial year as the management one.
- The two reports must be published through the same communication means or, as an alternative, the single non-financial information only report must cite the website of the management one.
- The alternative report must follow the minimum disclosure requirements demanded by the Directive 2014/95/EU on Corporate Social Responsibility matters.

⁶⁰ See paragraph 2.2.2 of this Thesis.

It must be pointed out that this exception has a subsection, which gives the undertakings the permission to except some themes in their non-financial information disclosure. To be exact, it was decided that a justification for the exclusion from reporting obligations that can harm the commercial position of the PIEs is requested. In this regard, Art. 9a(1) states as follows: *“Member States may allow information relating to impeding developments or matters in the course of negotiation to be omitted in exceptional cases where, in the duly justified opinion of the members of the administrative, management and supervisory bodies, acting within the competences assigned to them by national law and having collective responsibility for that opinion, the disclosure of such information would be seriously prejudicial to the commercial position of the undertaking, provided that such omission does not prevent a fair and balanced understanding of the undertaking's development, performance, position and impact of its activity.”* The same is true for a prejudicial to the commercial position of a group of undertakings, according to Art. 29a (1) of the Directive. The above mentioned article is called *Safe Harbour Principle* and is adopted by Member States at the discretion of each national legislation, as it will be pointed out in the following paragraphs⁶¹.

Similar to the provisions of the regulations for the preparation of the consolidated financial statements, there is the possibility of excluding information regarding entities acquired during the year from the reporting perimeter.

Once the subjects to which the European Directive is directed are outlined, the Community legislator, before explaining the content of the non-financial statement, underlines the concept of materiality of the information. Indeed companies are encouraged to report on a wide range of potential issues but they need to assess which information is material, disclosing *“...information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity...”*⁶².

This is supported by Recital 8 of the Directive, which states that:

“The undertakings which are subject to this Directive should provide adequate information in relation to matters that stand out as being most likely to bring about the materialisation of principal risks of severe impacts, along with those that have already materialised. The severity of such impacts should be judged by their scale and gravity. The risks of adverse impact may stem from the undertaking's own activities or may be linked to its operations, and, where relevant and proportionate, its products, services and business relationships, including

⁶¹ See paragraph 2.2.2 of this Thesis.

⁶² European Commission, Directive 2014/95/EU, art. 1.

its supply and subcontracting chains. This should not lead to undue additional administrative burdens for small and medium-sized undertakings.”⁶³

This concept is further analysed by the EU Guidelines as it will be explained in detail in the following section of this thesis⁶⁴. This materiality threshold is described exhaustively in Recital 6 and 7, in which five topics that every European PIE must disclose are highlighted:

1. Environmental matters: *“Undertakings must disclose details of the current and foreseeable impacts of their operations on the environment, health and safety, on the use of renewable and/or non-renewable energy, greenhouse gas emissions, water use and air pollution.”*⁶⁵
2. Social and employee-related matters: *“The information provided by the CSR statement may concern the actions taken to ensure: gender equality, implementation of fundamental conventions of the International Labour Organisation, working conditions, social dialogue, respect for the right of workers to be informed and consulted, respect for trade union rights, health and safety at work and the dialogue with local communities, and/or the actions taken to ensure the protection and the development of those communities.”*⁶⁶
3. Respect for human rights: *“Undertakings must include in the list of information disclosed a section in which the undertaking shows its policies to prevent human rights abuses.”*⁶⁷
4. Anti-corruption matters: *“The information provided in this regard must be a list of the instruments used by PIEs to fight corruption.”*
5. Anti-bribery matters: *“The information provided in this regard must be a list of the instruments used by PIEs to fight bribery.”*⁶⁸

All the above mentioned requirements must be disclosed throughout the following list of items:

- “(a) a brief description of the undertaking's business model;*
- (b) a description of the policies pursued by the undertaking in relation to those matters, including due diligence processes implemented;*
- (c) outcome of those policies;*
- (d) the principal risks related to those matters linked to the undertaking's operations including, where relevant and proportionate, its business relationships, products or services*

⁶³ European Commission, Directive 2014/95/EU, recital 8.

⁶⁴ See paragraph 2.2.1 of this Thesis.

⁶⁵ European Commission, Directive 2014/95/EU, Recital 7.

⁶⁶ European Commission, Directive 2014/95/EU, Recital 7.

⁶⁷ European Commission, Directive 2014/95/EU, Recital 7.

⁶⁸ European Commission, Directive 2014/95/EU, Recital 7.

which are likely to cause adverse impacts in those areas, and how the undertaking manages those risks;

(e) non-financial key performance indicators relevant to the particular business.”⁶⁹

It should be noticed that the aforementioned list regard the single undertaking, although the same components could also be found in the list for undertakings that are part of a group.

To provide a comprehensive picture of the contents of the Directive, it also provides a modification of Art. 20 of the Directive 2013/34/EU on the topic of Diversity Reporting Requirements. The Directive requires that an organisation considered PIE produces a diversity report with a *“description of the diversity policy applied in relation to the undertaking's administrative, management and supervisory bodies with regard to aspects such as, for instance, age, gender, or educational and professional backgrounds, the objectives of that diversity policy, how it has been implemented and the results in the reporting period. If no such policy is applied, the statement shall contain an explanation as to why this is the case”⁷⁰.*

It is important to underline that if a PIE does not disclose one of the matters mentioned by the Directive, it must offer a transparent and coherent motivation for this exclusion in its non-financial statement. This principle, called *“comply or explain”* principle, was adopted by the legislator based on the fact that it was easier for undertakings to disclose their sustainable actions rather than to publicly affirm their ineptitude. However, all information must be provided by comparing it with that of the previous years on the basis of the standards or guidelines used to draft the report. The methodology that must be used to divulge the previously mentioned topics is explained first of all in Recital 9, in which the frameworks that a company should refer to in its disclosure process are mentioned:

“In providing this information, undertakings which are subject to this Directive may rely on national frameworks, Union-based frameworks such the Eco-Management and Audit Scheme (EMAS), or international frameworks such as the United Nations (UN) Global Compact, the Guiding Principles on Business and Human Rights implementing the UN 'Protect, Respect and Remedy' framework, the Organisation for Economic Cooperation and Development (OECD) Guidelines for multinational Enterprises, the International Organization for Standardisation's ISO 26000, the International Labour Organization's Tripartite Declaration of principles concerning multinational enterprises and social policy, the Global Reporting Initiative, or other recognised international frameworks”.

⁶⁹ European Commission, Directive 2014/95/EU, Art. 1.

⁷⁰ European Commission, Directive 2014/95/EU, Art. 1.

It is also possible that company adopts an independent reporting methodology consisting of one or more reporting standards, principles, criteria and performance indicators considered functional to fulfil regulatory obligations.

It is also necessary to make some clarifications in the event that a company opts for the change of standards from one year to another. In compliance with the requirements of the Community Legislature, any change in reporting methodology requires an adequate justification from the body responsible for drafting the non-financial statement. Changes in the reporting methodology need to be explained to guarantee the comparability over time of the company performances. Moreover, the Directive recommends undertakings to disclose their non-financial information either in their management report or in another separate official document, which must be *“independent from the management report and comply with one or more than one between national, Union-based or international frameworks. It has also to comply with the requirements previously mentioned in regards of the publication of a separate report”*⁷¹.

Whit regards to the verification of the reporting process and of the issued report, the Directive 2014/95/EU only mentions a compulsory check by auditors. More precisely, Art. 19(5) and 19(6) of the Directive declared that: *“Member States shall ensure that statutory auditors or audit firms monitor the successful submission of the non-financial declaration referred to in paragraph 1 or the separate drafting referred to in paragraph 4. Member States may request that the information contained in in the non-financial declaration referred to in paragraph 1 or in the separate report referred to in paragraph 4, be verified by an independent provider of verification services.”* The auditor's involvement is one of those elements of distinction in the comparison between the Directive implementation of each Member States, that could choose a different level of auditor's involvement in addition to the simply check required by the Directive, as it is explained in detail in the following paragraphs⁷².

Focus on EU Guidelines principles on NFI disclosure

In accordance to the Art. 3 of the Directive, the purpose of the Guidelines is to provide companies with a principle-based model capable of guaranteeing an adequate level of information content. This approach is also supported by part of the literature, which highlights how to include greater flexibility in terms of regulation for institutions, and greater development of best practices for companies.

⁷¹ European Commission, Directive 2014/95/EU, Recital 9.

⁷² See paragraph 2.2.2 of this Thesis.

The guidelines are divided into two areas of intervention. The first deals with the definition of general principles on non-financial information disclosure, while the second deals with the identification of the essential contents to be presented in the non-financial statement. Based on what is reported in the previous paragraph, below only the first part of the guidelines regarding the cardinal principles of non-financial disclosure will be treated. According to the European Commission, the fundamental reporting principles are: materiality, correctness, completeness, long-term vision, stakeholder involvement and consistency. In explaining the principle of materiality, the information is considered material *"when its omission or incorrect indication could reasonably influence the decisions made by users on the basis of the corporate financial statements"*⁷³ as stated in the Directive 2013/34/EU on financial information. Moreover, Art. 1 of the Directive 2014/95/EU adds that the information is considered relevant *"to the extent necessary to understanding the impact of the business activity"*⁷⁴.

The guidelines also highlight how the concept of material information can change from company to company, from sector to sector, and how it must be assessed within a specific context. To assess the relevance of the information, the guidelines also state the usefulness of factors such as the business model and its intrinsic elements (risks, strategies, management systems, tangible and intangible assets, value chain), sectoral issues, stakeholder expectations, and the political and regulatory framework concerning the context in which the company operates. Given its multidimensionality, the principle of materiality represents one of the most controversial issue linked to the sustainability reporting. In addition to regulators, also standard setters as GRI and IR have contributed to shape the concept of materiality from different point of views, as explained further in this chapter⁷⁵.

The principle of correctness is an expression of equilibrium intended as an objective representation of data, and of comprehensibility, understood as the use of a simple language and a coherent terminology. To meet the principle of correctness, the guidelines suggest the formal assignment of management positions in the field of sustainability to independent directors, the adoption of internal control systems, and the assurance of non-financial disclosure by an external third party.

On the principle of completeness, the guidelines underline the need to report information about the environment, society, personnel, human rights and the active and passive corruption. Reporting on these issues in an effective manner is possible only linking the

⁷³ European Commission, Directive 2013/34/EU, Art. 2.16.

⁷⁴ European Commission, Directive 2014/95/EU, Art. 1.

⁷⁵ See paragraph 2.4.3 of this Thesis.

principle of completeness to those of materiality of information. In other words, the disclosure of these issues must be done in compliance with those that are the material aspects avoiding the reporting of useless information that weighs down the content of non-financial statement.

The long-term orientation is another basic principle pointed out by the Guidelines according to which the information must be strategic and forward-looking, and allow its use to better assess the resilience and sustainability of the trend, the position, results and impact of the company over time.

Finally, in the context of the principle of consistency, the Guidelines refer to the need to report non-financial information in a consistent way with other financial information present in the management report. The guidelines, in fact, focus on the importance of ensuring a comparison of non-financial performance over time through the use of performance indicators, which are constantly updated in order to maintain high levels of information quality.

MEMBER STATE IMPLEMENTATION OF THE DIR. 2014/95/EU

Prior to the introduction of Directive 2014/95/EU, the level of national regulations concerning the disclosure of non-financial information between Member States was very different. France, the United Kingdom, Sweden, Denmark, Spain, the Netherlands and Finland are among the states that first have introduced rules regarding this issue in their internal regulations.

In 2003 France was the first EU country to introduce the *Nouvelles Regulations Economique* (NRE), that provided for social and environmental reporting obligations for listed companies.

In the United Kingdom, the Companies Act of 2006 required all large companies to prepare an activity report in the annual directors' report. For these companies, it was requested to report information on the environment, personnel, as well as the contractual agreements between the companies themselves and the reference community. In addition, these companies were asked to explicitly state the lack of information on any of these issues.

In 2009 Sweden introduced the obligation to prepare reports according to the GRI model for publicly owned companies. According to the "comply or explain" approach, the companies falling within the scope of the application were asked to provide information on ethical and environmental issues, on human rights, on gender and diversity policy, on sustainability strategies and on non-financial risks.

Denmark approved the reform law of the Danish Financial Statements Act, which came into force on January 1, 2009, on the subject of ESG communication, which compelled large

companies (listed or not), as well as public and financial institutions in the country, to describe in a specific section of its annual report, the social responsibility policy and the related implementation methods, as well as the results achieved and future objectives.

In Spain, the "Sustainable Economy Act" was established in 2012. It compelled state-owned companies to publish annual reports on corporate governance and sustainability. These reports must be prepared in accordance with generally accepted standards and with a specific focus on gender equality and people with disabilities. In the case of companies with more than one thousand employees, the law provides that the report should be notified to the Consejo Estatal de Responsabilidad Social Empresarial (CERSE), a state committee instituted in 2007, composed of trade unions, companies, civil society and public administrations, the whose purpose is to identify common models and practices for the implementation of sustainability reports.

Since 2009 in the Netherlands, the Company Law Code has recognized a central role in the corporate strategies of companies to CSR. In particular, the code provides that the board of directors is required to formulate a policy to be submitted to the supervisory board for approval and that, within the responsibilities of the supervisory board, there is the supervision and approval of the sustainability policy. The code, to which listed companies are subject, has provided that the main elements of the company's CSR policy must be indicated in the annual report. The Civil Code, moreover, in implementing the Directive 2003/51/EC, provided that all listed companies and all large unlisted companies submit some information, financial and non-financial, relating to the environment, personnel and risks, if relevant and to the extent necessary to understand the development of the organization and its performance in their annual reports.

On the other hand, in Finland the topic of CSR has invested all the above aspects related to diversity. Since 2008, the Finnish company law code has recommended that a representation of both genders has to be guaranteed in each Board of Directors. In case of non-compliance, the company is obliged to communicate the reasons.

Unfortunately, Italy is not among the first EU countries that implemented effective regulation on sustainability reporting issues. In fact, before the Legislative Decree 254 on implementation of Directive 2014/95/EU, the Italian legislator devoted a residual space to non-financial issues and how information relating to these aspects must be reported.

The first legislative intervention was in March 2007 when the legislator implemented the content of the Directive 2003/51/EC⁷⁶ by issuing the legislative decree 32/2007 which

⁷⁶ European Commission, *Directive on the annual and consolidate accounts of certain types of companies, banks and other financial institutions and insurance undertakings* (2003/51/EC), Official Journal of

intervened on the content of art. 2428 of the Italian Civil Code, providing the introduction of the obligation to indicate in the management report information relating to the relationship with the environment and personnel to listed companies. In this case the legislative intent was to facilitate the understanding of the complex dynamics concerning the management of a company through the reporting of financial performance indicators and, where appropriate, non-financial performance indicators.

In compelling some companies to introduce the accounting standards IAS/IFRS the Decree 38/2005, has indirectly encouraged the non-financial reporting in the context of documents and reports outside the balance. Paragraph 14 of IAS 1 provides that the traditional accounting information (present in the financial statements for the year) should be extended to non-accounting information (present in separate reports with respect to the financial statements, such as environmental and social reports).

Both regulatory provisions have pushed towards a new form of corporate disclosure, also adding the disclosure of non-financial information regarding the environment and the composition of the personnel to financial information. However, after several years since the introduction of these rules, the results achieved in terms of diffusion of sustainability reporting tools were not satisfactory, registering a wide gap between SMEs and large companies. The partial overlap between the areas of application of the legislative decree 38/2005 and the legislative decree 254/2016 suggests how the latter regulatory intervention, in incorporating the content of Directive 2014/95/EU, formally invested non-financial information of a mandatory role. However, now that the deadline for the 28 Member States to transpose the Directive into their own national legislation has passed (December 6, 2016), it is interesting to analyse how each Member State has implemented the Directive requirements.

As a general overview, the document "Member State Implementation of Directive 2014/95/EU"⁷⁷ published in November 2017 by the GRI and the CSR Europe and Accountancy Europe networks, has provided a comprehensive classification of the differences that exist between the 28 countries of the European Union as well as two additional countries from the European Economic Area (Iceland and Norway) involved in the scope of the Directive, in terms of its implementation.

The different scenarios across the EU Member States and EEA members also mean that in some countries organisations still lack the knowledge on how effective reporting can serve as an important tool to enhance responsible business practices and integrate sustainability into business model. As stated in the Directive 2014/95/EU: "*Indeed, disclosure of non-financial*

European Union 17.07.2003.

⁷⁷ GRI, CSR Europe, Accountancy Europe (2017), Member State Implementation of Directive 2014/95/EU.

information is vital for managing change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection. In this context, disclosure of non-financial information helps the measuring, monitoring and managing of undertakings' performance and their impact on society... ”⁷⁸.

First of all, it is necessary to underline that the Community legislator, defining the legislative constraints related to the transposition of Directive 2014/95/EU within the Member States, has foreseen the prohibition of *golden plating*. In this way a state can not elaborate the content of the act of transposition with requirements different from those established by the directive, or introduce additional obligations, burdens and sanctions.

The need to add this prohibition derives from the will of the European Commission to mitigate the negative effects of over regulation arising from the extension of the object by the National Legislature or the non-repeal of the pre-existing legislation.

Although the Directive allows state specific requirements to ensure its implementation across the vary national practices, each Member State could differ in the definition of certain concepts or in the method of implementation of certain requirements. As a matter of fact each Member State has complied with the Directive in different manners. The Directive requirements could be transposed in the national regulation in a textual way, could be adapted to national existing regulation or could be omitted. The specific requirements analysed concern:

- Definition of a large undertaking: in 19 countries the legislative decree was implemented textually, while in 11 other countries it was adapted to the context of reference.
- Definition of a Public Interest Entity: in only 6 countries the legislative Decree was implemented textually, while in the other 24 countries it was adapted to the reference context.
- Report Topics and Content: in 22 countries the legislative regulation has been implemented textually, while in only 8 countries it has been adapted to the context of reference.
- Reporting Framework: in no fewer than 24 countries the legislative decree was implemented textually, while in only 6 countries it was adapted to the reference context.
- Disclosure Format: in only 7 countries the legislative decree has been implemented textually, while in 23 countries it has been adapted to the reference context.

⁷⁸ European Commission, Directive 2014/95/EU, Recital 3.

- Auditor's involvement: in 20 countries the legislation was implemented in text, in 9 countries it was adapted to the context of reference, in one case, Germany, it was omitted.
- Non-compliance Penalties: in no fewer than 27 countries the regulation has been amended, in only 3 countries it has been omitted.
- Safe Harbour Principle - i.e. the possibility of omitting information omissions in the event of damage to the company: in 25 countries the legislative decree has been implemented verbatim, while in only 5 countries has been omitted.
- Diversity Reporting Requirements: in 20 countries the legislative decree has been implemented textually, while in 10 other countries it has been adapted to the reference context.

Tab.1 Transposition summary table

| Country | Definition of a Large Undertaking | Definition of a Public Interest Entity | Report Topics and Content | Reporting Framework | Disclosure Format | Auditor's involvement | Non-compliance Penalties | Safe Harbour Principle | Diversity Reporting Required |
|-----------------|-----------------------------------|----------------------------------------|---------------------------|---------------------|-------------------|-----------------------|--------------------------|------------------------|------------------------------|
| Austria | = | ○ | = | = | ○ | = | ○ | = | ○ |
| Belgium | ○ | ○ | = | = | ○ | ○ | ○ | = | = |
| Bulgaria | = | ○ | = | ○ | ○ | ○ | ○ | = | ○ |
| Croatia | = | ○ | = | = | ○ | = | ○ | = | ○ |
| Cyprus | = | ○ | = | = | = | = | ○ | = | ○ |
| Czech Republic | ○ | ○ | = | = | ○ | = | ○ | = | = |
| Denmark | ○ | ○ | = | ○ | ○ | ○ | ○ | ✘ | ○ |
| Estonia | ○ | = | = | = | ○ | = | ✘ | ✘ | ○ |
| Finland | = | = | = | = | = | = | ○ | = | = |
| France | = | ○ | = | = | ○ | ○ | ○ | ✘ | = |
| Germany | = | ○ | = | = | ○ | = | ○ | = | = |
| Greece | ○ | ○ | ○ | = | ○ | = | ○ | = | = |
| Hungary | = | ○ | = | = | ○ | = | ○ | = | = |
| Iceland | ○ | ○ | = | = | ○ | ○ | ○ | = | ○ |
| Ireland | = | = | = | = | = | = | ○ | = | ○ |
| Italy | = | ○ | = | ○ | ○ | ○ | ○ | = | = |
| Latvia | = | ○ | ○ | = | ○ | ○ | ○ | = | = |
| Lithuania | = | ○ | ○ | = | ○ | = | ○ | = | ○ |
| Luxembourg | ○ | ○ | = | = | = | = | ○ | = | = |
| Malta | = | = | ○ | = | ○ | = | ○ | = | = |
| The Netherlands | = | ○ | = | = | ○ | ○ | ✘ | = | = |
| Norway | = | ○ | = | = | ○ | = | ○ | ✘ | = |
| Poland | = | ○ | = | ○ | = | = | ○ | = | = |
| Portugal | ○ | ○ | = | = | = | = | ○ | = | = |
| Romania | ○ | ○ | ○ | = | = | ○ | ○ | = | = |
| Slovakia | = | ○ | = | ○ | ○ | = | ○ | ✘ | = |
| Slovenia | = | = | ○ | = | ○ | = | ○ | = | ○ |
| Spain | = | ○ | ○ | ○ | ○ | = | ✘ | = | = |
| Sweden | ○ | ○ | ○ | = | ○ | = | ○ | = | = |
| United Kingdom | ○ | = | = | = | ○ | ○ | ○ | = | = |

Legend

- = Requirements are the same as in the Directive
- ✘ Requirements have been omitted
- Requirements have been adapted

source: GRI, CSR Europe, Accountancy Europe, Member State Implementation of Directive 2014/95/EU, 2017.

From the table above it is possible to have a general overview of the Directive implementation of each EU Member State, but what is the Italian specific situation? In the next paragraph the

Italian legislator decision about the topic of non-financial and diversity information disclosure will be discussed.

2.3 ITALIAN REGULATION: LEGISLATIVE DECREE 2016/254

The first step to the adoption of the Italian Legislation towards the EU Directive 2014/95/EU was completed on December 30, 2016 with the governmental approval of the Legislative Decree N.254, containing the new Italian principles and guidelines for non-financial information disclosure. The Legislative Decree finally became official on January 10, 2017 with its publication on the Official Gazette no. 7.

This provision marks the formal change in the status of non-financial information from voluntary to mandatory forcing the reporting of non-financial information to be in compliance with specific regulatory requirements.

Given the prohibition of *golden plating*, the Decree must implement the European directive in full of its requirements, so it will be useful to focus on the elements of differentiation emerged from the comparison between the Italian decree and the implementing regulations of the other Member States rather than on how the Italian Decree reported the mandatory requirements of the European Directive.

The transposition of the European Directive into the Italian regulation has, in fact, all the principal elements necessary to carefully constrain the disclosure of non-financial information. There are, however, some elements that differ among the Member States in the implementation of the EU Directive requirements. Those elements were summarized in the previous paragraph in a general EU overview. Focusing only on the Italian situation, the following table could be reported:

Tab.2 Italian transposition table:

| Country | Definition of a Large Undertaking | Definition of a Public Interest Entity | Report Topics and Content | Reporting Framework | Disclosure Format | Auditor's involvement | Non-compliance Penalties | Safe Harbour Principle | Diversity Reporting Required |
|---------|-----------------------------------|----------------------------------------|---------------------------|---------------------|-------------------|-----------------------|--------------------------|------------------------|------------------------------|
| Italy | = | ○ | = | ○ | ○ | ○ | ○ | = | = |

source: personal elaboration from GRI, CSR Europe, Accountancy Europe, Member State Implementation of Directive 2014/95/EU, 2017. Pag. 10

As can be noticed, the Italian legislator has decided to textually incorporate the legislative provisions with regard to: Definition of large undertakings, Report topics and content, and Safe Harbour Principles and Diversity reporting requirements. It has decided to adapt the

definition of PIE, the Reporting Framework, the Disclosure Format, the Auditor's involvement and the Non-compliance penalties to the Italian regulatory context to the existing national provisions. None of the Directive requirements has been omitted by the Italian legislator.

- **PIEs DEFINITION**

According to the national regulation, those entities, belonging to certain categories expressly indicated by the law, for which, in view of the particular visibility and economic importance, the activity of legal auditing is subject to stricter obligations are defined as PIEs. Art. 16, paragraph 1 of the Legislative Decree no. 39/2010 states that are considered PIEs:

- a) Italian companies issuing securities admitted to trading on regulated Italian and European Union markets;
- b) banks;
- c) insurance companies;
- d) reinsurance companies;
- e) companies issuing financial instruments that, even if not listed on regulated markets, are widespread among the public;
- f) the management companies of regulated markets;
- g) companies that manage compensation and guarantee systems;
- h) centralized management companies of financial instruments;
- i) brokerage firms to mobilize;
- j) asset management companies;
- k) investment companies with variable capital;
- l) payment institutions;
- m) electronic money institutions;
- n) financial intermediaries pursuant to art. 107 TUB.

In the Italian context, the legislator gives an extensive interpretation of the concept of PIEs, also including the case of unlisted companies issuing not regulated financial instruments but widely distributed on the public, provided that they also meet the dimensional requirements referred to by the definition of the large undertaking.

Moreover, art. 7 of the Decree identifies the prerequisites of a company not consider as a “large undertaking” to adopt the Directive. At the end of the financial year at least two of the following three dimensional limits have to be respected:

- less than 250 employees during the year;

- total balance sheet under 20 million euros;
- total net revenues from sales and services under 40 million euros;

The opportunity recognized by the Decree would contribute to the promotion of a CSR oriented corporate image recognizing the benefits deriving from a sustainability disclosure, such as an improvement of the corporate image, an improvement of the trust level of the stakeholders or a better access to the credit market as well for SMEs, which form the most important part of the Italian economic system.

- **REPORTING FRAMEWORK**

As stated in the EU Directive, to disclose required information, undertakings could adopt national, Union-based or international standards. The Italian legislator has adapted this requirement adding the possibility that undertakings to adopt a mixed reporting methodology constituted by one or more reporting standards. Given that, the two most used reporting standards, both at national and international levels, are GRI and IR frameworks, it is useful to understand what companies are required in order to correctly report following GRI or IR guidelines. It is also important to understand how these frameworks are in compliance with the requirements of the EU Directive. Those matters are explained in detail in the following paragraph⁷⁹.

- **DISCLOSURE FORMAT**

According to the Italian legislator, non-financial information shall be presented in the management report, or in a separate report, approved by the administrative body and at disposal of the supervisory body and the auditor, within the deadline of the financial statements, published on the company register, and alongside the management report.

- **AUDITOR'S INVOLVEMENT**

According to the Decree, there are two forms of control on the non-financial statement: an internal control of the Supervisory Board, and an external auditing by an independent third party. The Supervisory Board ensures the compliance of the company's statement with the provisions of the Decree within the functions assigned to it by the law, and reports the results of its control in the annual general meeting. External control, instead, is divided into a double form of control. The first type of control is also provided by the EU Directive and states that

⁷⁹ See paragraph 2.4.3 of this Thesis.

the subject responsible of auditing the financial statements has also to verify the presence of the non-financial statement.

The second type of control is about the content of the statement. The Directive states that Member States may require that the information in the non-financial statement to be verified by the same subject or another person authorized to carry out the legal audit, specifically designated for this task. This assurance statement is separated from the audit report of financial statements and has to be attached to the non-financial report. From the comparison between the Directive and the Italian Decree, it is evident that Italy has decided to avail itself of the right to request a third party verification of the non-financial statement, and has also prescribed that this subject does not have simply to be a "subject independent of certified professionalism" or an "accountant" with characteristics of independence but specifically a statutory auditor. The auditor's role is clarified in detail in the next chapter of this Thesis.

- **NON-COMPLIANCE PENALTIES**

Within the Decree the legislator has also dedicated some space to the issue of sanctions resulting from the failure to comply with the regulatory provisions, providing in art. 8 the responsibilities of the directors, whose obligations include the drafting of the non-financial statement, and of the persons responsible for the control of the statement and of the process for its drafting. In general terms, the unlawful acts identified by the Italian legislator concern the non-deposit or delayed filing of the report, the omitted allegation of the auditor's certification, the non-compliant declaration, the false declaration, and the unprofessional behavior of the auditors. The subject responsible for the control is also subject to additional penalties in the cases enunciated by the fifth paragraph of art. 8, such as in cases relating to the non-verification of the preparation of the non-financial statement and the failure to perform the conformity verification procedure. The pecuniary sanctions associated with these cases regard both the responsibilities of the directors and the auditors, and are equal to an amount that ranges from a minimum of € 20,000 to a maximum of € 150,000.

2.4 REPORTING FRAMEWORKS FOR NFI

After examining the non-financial disclosure contents and the subjects affected by the European Directive, it is appropriate to focus on the reporting standards that companies could refer to in their non-financial disclosure. The information required by the European legislation must be provided in accordance with the methodologies and principles set by the reporting standard used as a reference. "Reporting standards" means *"the standards and guidelines*

*issued by authoritative supranational, international or national bodies, of a public or private nature, functional, in whole or in part, to fulfil the non-financial reporting obligations"*⁸⁰. As already underlined, Recitals 9 of the Directive 2014/95/EU indicates standards to which companies can refer, providing a non-exhaustive list that includes: the principles of UN Global Compact, the Guiding Principles on Business and Human Rights, the lines Guide to the Global Reporting Initiative, etc.

Currently, Italian companies tend to refer to the standards prepared by the International Integrated Reporting Council (IIRC) and to those prepared by the Global Reporting Initiative (GRI). In the practice of reporting non-financial information of Italian companies there are also examples of companies that adopt two or more reporting standards together, or that have used an independent reporting methodology. Both alternatives are permitted by the Italian Legislative Decree, as already highlighted above. Despite these possible alternatives foreseen by the regulatory context, the technical reference points of non-financial reporting both at national and international level are the guidelines provided by the GRI and the IIRC. The main reasons for the importance of the two standards are their diffusion, the relevance of the two organizations that developed them and their contributions during the legislative process that led to the approval of the Directive 2014/95/EU. Both organizations mentioned above have had, from the beginning, a collaborative approach rather than a competitive one, making their research activities complementary and preparing non-conflicting documents. Obviously, having developed on different assumptions, they have some similarities but also some differences. At the basis of the conceptualizations of GRI and IIRC standards there are the same questions. How to rebuild stakeholders' trust in large corporations after the 2008 financial crisis and various corporate scandals? How to attract the attention of more investors through the use of non-financial additional information? Therefore, both standards frameworks aim to expand the boundaries of corporate accounting, including environmental, social and corporate governance issues. However, the way these issues are framed is quite different in terms of underlying assumptions, intended outcomes and expected impact on corporate governance, the environment and the society.

GLOBAL REPORTING INITIATIVE (GRI) GUIDELINES

The development of sustainability reporting is due in large part to the Global Reporting Initiative (GRI), a non-profit organization born in Boston in 1997 from an initiative promoted by the US organization *Coalition for Environmentally Responsible Economies* (CERES) and the *United Nations Environment Program* (UNEP). From the beginning the purpose of GRI

⁸⁰ Legislative Decree n. 254, 2016.

was to increase the effectiveness and quality of sustainability reporting. The GRI, whose headquarters are today in Amsterdam, has then developed over the years as a globally recognized international organization and has published several guidelines for sustainability reporting. Today, several categories of stakeholders from over 80 countries participate in GRI activities and programs, including governments, companies of all types and sizes, non-profit organizations, associations, universities, research institutes and private individuals. The first version of the guidelines was published in 2000, the second (G2) in 2002, the third (G3) in 2006, which was followed by a series of industry supplements that led to the publication of the update version G3.1 in 2011. In 2013 the fourth generation G4 of the guidelines was published. It was divided into two parts, a first part dedicated to the principles and a second part concerning an implementation manual. The current version, published in 2016 and entered into force on July 1, 2018, is the one denominated GRI Standards, composed by a set of thirty-six documents (one for each standard) which can be grouped into four sections: universal standards, standards for sustainability, economic standards, environmental standards and standards for society. This choice essentially derives from the presence of a double benefit: for the reader, who in this way is better oriented when searching information that are reported by type of standard, and for the standard setter, which in this way can update the single standard independently from the whole GRI Standards. In addition to the differences at the formal level, there are also some substantial differences between the current version of the guidelines and the earlier version G4. Before explaining the differences in content and requirements between the aforementioned version of the guidelines, it is necessary to point out that the degree of the modification made in the 2016 version is not comparable to that verified in the transition from version G3.1 to G4 that has strong elements of discontinuity. For this reason and for the fact that many sustainability reports in reference to the financial year 2017 still follow the G4 version, it is beneficial to previously explain the development path of the guidelines between the G3.1 and G4 versions⁸¹. Among the new elements introduced by the G4 version of the guidelines, it is possible to highlight first of all the greater importance assigned to the concept of materiality, in which respect organizations are asked to determine and focus only on aspects that reflect the significant economic, environmental and social impacts for the organization itself and that could substantially influence the decisions of its stakeholders. Among the aspects being revisited, a specific focus is assigned to the reporting perimeter, i.e. the description of the boundaries within which the impacts for each material aspect occur. The identification of the material aspects includes the consideration of

⁸¹ Venturelli A., Caputo F., 2017, *Informativa non finanziaria e regulation. Tendenze evolutive e relative implicazioni alla luce dell'emanazione del D.Lgs 254/16*. Pag. 113.

the impacts related to all the activities, products, services and relationships of an organization, regardless if they occur inside or outside it.

The GRI G4 also provides a more detailed discussion of the Disclosure on Management Approach (DMA) to explain in a more precise and detailed way how the environmental, social and economic impacts related to each material aspect have to be managed. The replacement of the Application Level provided by G3.1 (on the C-B-A scale), through two new options both based on the introduction of the phrase "in accordance" with the guidelines, had a great impact. The first, called "in Accordance-Core" contains the essential elements of a sustainability report, and provides a format through which an organization communicates the impacts of its economic, social, environmental and governance performance. The second, called "in Accordance-Comprehensive" is based on the Core option but it requires additional disclosure standards related to specific aspects such as strategy, analysis of governance, ethics and integrity of an organization.

In terms of sustainability governance, a broader consideration is given to the governance and the remuneration system in the perspective of guaranteeing a global comparability between companies operating in the same sectors but in different territorial contexts.

An expansion in terms of reporting was required by the G4 guidelines also in terms of supply chain through the addition of regulatory provisions such as the description of the supply chain and the related changes from one year to another, and possible conflicts of interest due to the presence of cross-holdings with suppliers, etc.

Although less fundamental than those highlighted in the comparison between G3.1 and G4, these innovations mentioned above constitute the knowledge base for approaching the contents of the new GRI Standards, and to understand the differences with the previous G4 version. From a formal point of view, it has already been anticipated how a separate document was created for each standard rather than a single overall document; the number of requested information has also been reduced, passing from a total number of 149 of the G4 version to 136 of the standard version (this reduction is essentially linked to a series of unifications).

Among the changes in form, GRI Standards point out with greater clarity what can be reported (use of the word "shall") and what is required to be reported (use of the word "should").

With regard to the changes in terms of substance, it should first be underlined that the GRI Standards clarify the possibility that a company writes its report respecting only some specific standards according to the "GRI-referenced" option, without necessarily aligning its disclosure with the entire content. This possibility derives from the fact that often in the same

report companies refer to several reporting standards, for example in Italy the presence of GRI and IIRC is very common. Moreover, the GRI Standards emphasize the required compliance with the 10 GRI Principles as listed below:

1. stakeholder inclusiveness: a company should identify its stakeholders and report how the company responds to their expectations and interests;
2. sustainability context: a company should present its performance in the wide context of sustainability describing how it contributes to a sustainable world, taking economic, social and environmental issues into consideration;
3. materiality: the report should include all relevant issues and the company is expected to prioritize between material issues to give them an appropriate scope in the report;
4. completeness: all material issues should be included in the report;
5. accuracy: a company should perform a sufficient level of accuracy and details;
6. balance: a company should include both negative and positive aspects;
7. clarity: a company should use a language that stakeholders understand;
8. comparability: a company should report consistently, in a way that enables stakeholders to compare their performance over time and with other companies;
9. reliability: a company should report information in a way that makes it possible to trace the original source;
10. timeliness: the report should be published regularly and in time, in line with stakeholders needs.

The first five principles are related to report content, while the last five are related to report quality.

Lastly, there is also no obligation to comply with industry standards. This flexibility derives from the renewed centrality that the GRI has placed in relation to the principle of materiality, whose compliance determines the choice of reporting in different information areas, with different levels of analysis.

<IR> FRAMEWORK

The International Integrated Reporting Council (IIRC) is an international association that includes a wide range of stakeholders such as regulatory bodies, companies, investors, standard setters, universities, individual professionals and NGOs. Its aim is to develop integrated reporting into a reporting model based on interconnection of economic, financial, social, environmental and governance information.

In December 2009, the English organization Accounting for Sustainability (A4S) promoted a meeting with various types of stakeholders. After that A4S and the GRI, together with other organizations, made some investments to establish an international body to develop integrated reporting. In 2010 the Integrated International Reporting Committee (IIRC) was formally established. Its main purposes were to raise awareness among the public on integrated reporting, to identify the priority areas in which further technical and scientific work is needed, and especially to set up a standard of reporting suitable to integrate financial and non-financial information in a transparent, coherent and complete way. In 2011, the IIRC presented in public consultation the first draft of its framework in the form of Discussion Paper "Towards Integrated Reporting - Communicating Value in the 21st Century".

The IR Pilot Program was launched in October, 2011, when more than 80 large organizations participated (Atlantia, Enel, Eni, Generali, Terna, Snam for Italy), aiming to test and apply the Discussion Paper and the integrated reporting starting from 2012, in order to provide the information necessary for the revision of the framework. In November 2011, IIRC changed its name from the "International Integrated Reporting Committee" to the "International Integrated Reporting Council".

In 2012, a review of the framework proposed in the 2011 Discussion Paper was carried out based on the comments of the public consultation and the results generated by the Pilot Program experimentation, as well as a series of consultations with various types of stakeholders. Finally, in December 2013 the <IR> Framework was published after three months of consultation. According to the IIRC, the framework applies principles and concepts that are focused on bringing greater cohesion to the reporting process, adopting *integrated thinking* as a way of breaking down internal silos and reducing duplication. The <IR> Principles⁸² are the following:

1. *Strategic focus and future orientation*: an integrated report should provide insight into the organization's ability to create value in the short, medium and long term.
2. *Connectivity of information*: an integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time.
3. *Stakeholder relationships*: an integrated report should provide insight into the nature and quality of the organization's relationships with its key stakeholders including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests.

⁸² IIRC, The <IR> Framework, 2013. Pag. 5.

4. *Materiality*: an integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term.

5. *Conciseness*: an integrated report should be concise.

6. *Reliability and completeness*: an integrated report should include all material matters, both positive and negative, in a balanced way and without material error.

7. *Consistency and comparability*: information in an integrated report should be presented on a basis that is consistent over time and in a way that enables comparison among organizations to the extent it is material to the organization's own ability to create value over time.

<IR> framework aims is to improve the quality of information available to providers of financial capital to enable a more efficient and productive allocation of capital. It focuses on a value creation process over time, including long-term value, rather than profits and losses. According to the framework, the value created by an organization over time manifests itself in increases, decreases or transformations of the capitals caused by the organization's business activities and outputs. That value has two interrelated aspects, such as value created for: a) the organization itself, which enables financial returns to the providers of financial capital; b) others, i.e. stakeholders and society at large. It explicitly goes beyond the conventional definition of “capital”, identifying six forms of capitals (financial, manufactured, intellectual, human, social, natural) used by the business to create value over time. The ability of an organization to create value for itself is linked to the value it creates for others. This happens through a wide range of activities, interactions and relationships. When these interactions, activities, and relationships are material to the organization's ability to create value for itself, they are included in the integrated report.

Also the <IR> Framework considers a “materiality determination process” that involves evaluating the magnitude of the matter's effect and, if it is uncertain, its likelihood of occurrence. The Key to the materiality determination process is the concept of the reporting boundary. Determining the boundary of an integrated report has two aspects: a) The financial reporting entity (i.e. the boundary used for financial reporting purposes); b) Risks, opportunities and outcomes attributable to or associated with other entities/stakeholders beyond the financial reporting entity that have a significant effect on the ability of the financial reporting entity to create value. To explain how an entity creates value, at the core of <IR> framework there is the disclosure of information about the entity's strategy and business model. In addition to that of materiality, another key principle is the principle of connectivity of information, since its application can favor the intelligibility of the financial statements and

the information effectiveness towards different categories of stakeholders. According to this principle the information of an integrated report does not follow a standard structure, but has to be presented in such a way to make evident the links between the various elements of content. More in detail, the framework specifies that the main forms of connectivity between information concern the relationship among:

- contents of the report,
- past, present and future,
- capitals,
- financial and non-financial information,
- quantitative and qualitative information,
- internal management information and information reported outside,
- information included in the integrated report and those contained in other reports.

Regarding the contents of the report, the information to be provided concerns the presentation of the organization and the external environment, governance, business model, risks and opportunities, strategies and allocation of resources and performance. The business model is the element that, above all, has elevated levels of connectivity with the others elements. In fact it is aimed in fact to show how the firm draws on various capitals as inputs and converts them to outputs (products, services and wastes), through its business activities.

The connection between past, present and future is expressed in the report with the presence of historical series of KPIs, making the reader able to compare performances over the time.

The connection among capitals is understood by the IIRC as the ability of an enterprise to perceive, in the context of the general process of representing value, the possible trade-offs among the six types of capital. Moreover, some types of capital may be of little relevance to the stakeholders, and therefore not material in the disclosure of information.

The connection between financial and non-financial information finds its best explanation in the framework underlying the numerous links that may exist between a financial variable such as the increase in turnover, and non-financial variables such as research policies and development, new technologies, new investments and customer satisfaction.

The connection between quantitative and qualitative information would seem to be a discounted binomial, but in many cases the two types of information are separated in the annual reports accentuating the distinction between quantitative statements and information documents.

On the contrary, to understand the level of interaction that exists between internal information and information to be communicated to the outside, is decidedly more complicated. It is not possible to verify if there is consistency between external or internal information.

The topic of consistency is also referred to the last type of connections, the ones among the integrated report and the other types of reports or other communication tools.

The main project innovation developed by the IIRC seems therefore to be the attempt to standardize a process and not a report, also considering the goal of spreading *Integrated Thinking* among the largest possible universe of companies.

GRI AND <IR> IN THE LIGHT OF THE DIR. 2014/95/EU

This paragraph focuses on the comparison between the two major reporting frameworks previously explained. Since the beginning, the two initiatives have advanced in parallel, dealing with the same major questions but approaching them from different perspectives.

In this paragraph, a comparison is made between the contents and the principles expressed by GRI and <IR> frameworks following the compulsory requirements of the European Directive. The aim is to understand if and how these two reporting standards are in line with what companies are requested to disclose by law. The frameworks' versions taken into analysis are those more recently issued, in particular the GRI Standards (2016) and the <IR> framework (2013). Before analysing the compliance of contents and principles and the two reporting standards with the requirements of the Directive, it is useful to focus on some general similarities and differences among the three frameworks⁸³.

The first difference between GRI Standards, <IR> framework and the EU Directive is the collocation of the non-financial information disclosure. Essentially, both the EU Directive and the GRI consider the disclosure of non-financial information separately from financial information (in a separated report or in a specific section of the annual report), while <IR> framework requires companies to issue a combined integrated report that comprises both financial and non-financial information, following the principle of connectivity of information. Although all the frameworks focus on non-financial information, they differ in terms of the audience they address. The EU Directive and GRI Standards concept of value is “value for society”, while the <IR> framework focuses on providers of financial capital, emphasizing the “value for shareholders”. The rationale that underpins the EU law and the GRI Standards is based on *the right to know* about the impact that large corporations have on

⁸³ Magrassi L. (2015), *GRI Sustainability Reporting Guidelines e IIRC Integrated Reporting Framework. Spunti di riflessione su due principali standard di sustainability reporting*. Documento della Fondazione Nazionale dei Commercialisti.

the environmental and local communities in which they operate. The key concept is the idea that large undertakings should report on their capacity to create “shared value” rather than “shareholder value”. On the other hand, the underlying rationale that underpins the <IR> framework is in line with the Anglo-American approach to accounting, according to which only non-financial information relevant to shareholders should be included in the report. Once explained the aforementioned similarities and differences, it is useful to make a comparison between the frameworks in terms of key principles and contents. Both the GRI Standards and the <IR> framework cover in a general manner all the disclosure required by the European Directive, but in some cases with different levels of details or from different point of view. The most relevant difference in terms of Principles refers to the materiality principle. According to GRI Standards, the report should cover all aspects that “*reflect the organization's significant economic, environmental and social impacts, or that substantively influence the assessments and decisions of stakeholders*”⁸⁴. In highlighting the importance of stakeholder interests, GRI refers to all the organization's potential stakeholders. GRI Standards focus on the organizations' impacts on sustainable development, rather than on the sustainability of the organization. In the document "Defining What Matters. Do companies and investors agree on what is material?"⁸⁵ the process that leads to the definition of the material aspects and related areas of reporting is illustrated, it consists of the following steps:

1. Identify all the material aspects that fall within the reporting boundary because of the impacts they might have on an organization's activities, products, services and relationships, regardless of whether these impacts occur in or out the organization itself;
2. Prioritize the previously identified aspects trying to understand what should be reported. The principle of materiality is satisfied by evaluating the influence on the decisions of the stakeholders and the relevance of the economic, social and environmental impact;
3. Validate the aspects considered as priority in material terms. The objective of this phase is to ensure that the company provides a reasonable and balanced representation of performance, and its impacts on sustainability issues;
4. Review the material aspects reported in the report. This phase takes place after the publication of the report.

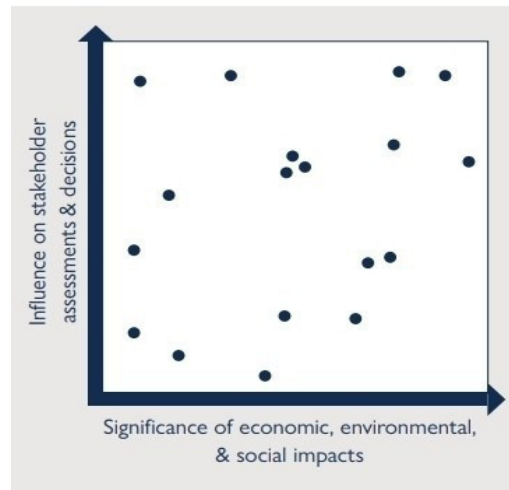
It is necessary that all four phases are standardized and that the specific activities carried out can be documented and evaluated, even by an independent external party.

⁸⁴ GRI, Consolidate Set of GRI Standards 2016, 2016.Pag.18.

⁸⁵ GRI, RobecoSAM (2016), *Defining What Matters. Do companies and investors agree on what is material?*

Fig.1: Example of Materiality Matrix

Visual representation of prioritization of topics



Source: Consolidated Set of GRI Sustainability Reporting Standards, 2016. Pag.11

The approach to materiality adopted in the <IR> framework differs both in terms of the purpose of the report (to explain how an organization creates value over time) and its primary target audience (providers of financial capital). Informed about these perspectives, the <IR> framework suggests that a matter is material if “it could substantively affect the organization's ability to create value over the short, medium and long term”. Although the <IR> framework focuses on the entity's longer-term prospects rather than explicitly on its contribution to a sustainable development, the framework makes it clear that the ability of an organization to create value for itself is also linked to the value it creates for others. From a technical point of view, the process of definition of materiality, is explained in the document "Materiality in <IR>. Guidance for the preparation of integrated reports", is divided into the following steps:

1. establishment of process parameters;
2. selection of the material topics;
3. definition of the reporting scope;
4. preparation of the disclosure;
5. review of the reporting process.

The definition of the reporting perimeter, in particular, is divided into three phases, from identifying the relevant subjects, to defining the level of importance of the same, and to conclude with the prioritization of the material aspects. The concept of materiality reported in the EU Directive includes both GRI and <IR> point of views. The material information is defined by the Directive 2013/34/EU as “the status of information where its omission or

*misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements of the undertaking*⁸⁶. Moreover, the Directive 2014/95/EU introduces a new element to be taken into account when assessing the materiality of non-financial information by referring to information as *“the extent necessary for an understanding of the impact of the company's activity”*⁸⁷.

In regard to the Contents required by the Directive, some differences emerge in the topic of *Business Model* information, of *Policies and Due Diligences* and of *Corruption and Anti-Bribery Matters*.

All the three frameworks agree on the fact that the business model is crucial when improving sustainability. However, GRI Standards do not grant the same importance to a company's business model as the other two frameworks do. In fact, while the EU Directive and the <IR> framework require disclosing information about how the company is creating value over time, the GRI Standards require companies to provide a long list of information about the “Organization Profile” and the “Strategy”.

In addition to the consideration of a company's business model, the frameworks differ in terms of Policies and Due Diligence. While the EU Directive and GRI Standards require companies to provide this information in a specific section, the <IR> framework asks companies to consolidate non-financial policies and their outcomes in the same content element (*Performance*). This approach follows the principle of Connectivity of information, which requires entities to *“show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organization's ability to create value over time”*⁸⁸.

Furthermore, while the EU Directive and GRI Standards require information regarding *Corruption and Anti-Bribery Matters*, the <IR> framework does not.

Given these similarities and differences, from a concrete point of view it is evident that in most of the large companies, obliged to meet the requirements of the European Directive, more than one reporting standards are used in the same report generating hybrid reporting models. In this regard, in October 2016 GRI and <IR> published the document "Forging a path to Integrated Reporting"⁸⁹ with the aim of explaining the similarities and differences between the sustainability report and the integrated report. The second objective of the document is to understand how the GRI standards and <IR> framework can be adopted at the same time.

⁸⁶ European Commission, Dir. 2013/34/EU, Art. 2.16

⁸⁷ European Commission, Dir. 2014/95/EU, Art. 1.1

⁸⁸ IIRC, 2013. Pag. 5.

⁸⁹ GRI, (2016), *Forging a path to integrated reporting*.

The starting point of the document is the centrality of the integrated report as a future business reporting tool. In underlining this aspect, the document highlights how, on the one hand GRI believes that the experience accumulated by a company in terms of sustainability reporting is a necessary prerequisite for building a good integrated reporting process, on the other, while recognizing a diversity of audience and purpose between the two reporting models, the IR framework does not exclude the possibility for companies to draft both the reports in the same financial year.

Unlike the first three years of IIRC activity, when it seemed to operate in competition with GRI, nowadays there is not a clear conflict between the two frameworks. Moreover, the European legislator, in formulating the requirements of the Directive, has tried to take into consideration the previously existing guidelines and standards leaving a great level of flexibility in the adoption of non-financial reporting frameworks.

Therefore, despite some differences, a prevailing convergence between the key principles and contents elements required by the frameworks emerges. Thus, the European Directive allows companies to choose the framework they wish to adopt. However, companies must bear in mind that some specific information must be included in their reports to comply with the requirements of the Directive. More specifically, in case the company adopts the GRI Standards, managers need to be aware about the need to include additional information on the business model. Conversely, whenever a company has adopted the IR framework, information on *Policies and Due Diligences* and on *Anti-corruption and bribery matters* need to be added⁹⁰. In conclusion, it seems reasonable to assume that the collaboration efforts between GRI and IIRC should be geared towards the development of a common tool in the near future, generally recognized by all operators and stakeholders.

⁹⁰ Manes-Rossi F., Tiron-Tudor A., Nicolò G., Zannellato G., (2018), *Ensuring More Sustainable Reporting in Europe Using Non-Financial Disclosure – De Facto and De Jure Evidence*.

CH. 3

EXTERNAL ASSURANCE ON NFI

3.1 GENERAL OVERVIEW

The term “Audit” derives from the Latin word “audire”, which means “to hear”. Auditors in fact have to evaluate processes or activities in which they are not usually involved, and before starting their activity, listening and acquiring information is fundamental for the success of their job. The audit evolved principally from the assurance need expressed by various stakeholders incapable of gathering information about an organization.

Auditing is an examination and verification of corporate statements, carried out by a qualified and registered auditor. The goal of auditing statements is to enable the auditor to express an opinion on whether the statements are prepared, in all material respects, in accordance with the rules in place for their preparation.

In a more formal definition, the International Federation of Accountants (IFAC) defines an external assurance engagement as one *“in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria”*⁹¹.

While the internal audit is a management tool and forms part of the company's internal control structure, external audit is undertaken by an auditor who is independent from the entity and has been appointed to express an opinion on the corporate financial and non-financial statements. As it is explained in the first chapter of this Thesis, the presence of an external assurance statement increases the perceptions of the users that the information disclosed presenting an accurate and unbiased picture of a company's performances.

The reason why the external assurance report enhances the credibility is that auditors have to follow rigorous ethical standards and quality control procedures (ISQC 1) during the whole assurance engagement. Just to summarize, the main reasons for companies to look for external assurance are⁹²:

- To reduce risk and increase value: disclosures which are viewed as robust and credible are more likely to be relied on, thus increasing the value of reporting.
- To improve Board and CEO level of engagement: disclosures and data which are more credible are more likely to be used for internal decision making.

⁹¹ IAASB, International Framework for Assurance Engagement (Revised), 2013. Pag. 6

⁹² Corporate Register, Assure View, The CSR Assurance Statement Report, 2008. Pag. 10.

- To strengthen internal reporting and management system: internal robust reporting systems and controls play an important role in managing sustainability performance and impacts. External assurance can help confirm that the internal systems and controls are robust, and can recommend any necessary improvements.
- To improve stakeholders' communication: assurance processes may involve the review of a reporter's stakeholders engagement processes. Some organizations use their reporting processes and sustainability reporting as the basis for an on-going dialogue with stakeholders.

As previously explained, from a normative point of view the statutory auditor shall “*check whether the required information is included in either the management report or a separate report*”⁹³. This check is not aimed at providing any reassurance to stakeholders about the quality of data reported, in fact no assurance is provided over the NFI reported. In addition to mandatory check from the statutory auditor, Member States may require that the NFI should be “*verified by an independent assurance service provider*”⁹⁴. The use of external, independent verification of sustainability reporting processes and final disclosure is intended to increase the robustness, accuracy and trustworthiness of disclosed information.

At a national level, the subjects involved in the audit of the non-financial disclosure required by Legislative Decree No. 254/2016 are essentially two: the auditing firm and the Supervisory Board whose role in the Italian context is attributable to the “Collegio Sindacale”. The auditing firm in charge of the statutory audit must:

- verify that the Board of Directors has made a non-financial statement;
- express, in ad hoc assurance report, a certificate about the compliance of the information provided with respect to the requirements of the Decree 254/2016 in the implementation of the Directive 2014/95/EU.

The certification of the auditing firm has to report the conclusions about the compliance of the information provided with respect to what is required by the regulations and with respect to the reporting standards to which the company has referred to for the preparation of the NFI report. These conclusions must be expressed on the basis of the knowledge and understanding that the auditor has of the public interest entity, the adequacy of the company’s systems, and the processes and the procedures used for the preparation of the NFI report. Based on the Directive 2014/95/EU and also on the CONSOB Consultation Document of July 21, 2017

⁹³ European Commission, *Directive on non-financial and diversity information by certain large undertakings and groups* (2014/95/EU), Official Journal of the European Union, 15.11.2014. Recital 16.

⁹⁴ European Commission, Directive 2014/95/EU. Art. 19(a).

“Implementing provisions of the Legislative Decree of December 30, 2016, no. 254 on the disclosure of non-financial information”, is considered appropriate to adopt a flexible approach that allows market participants to gradually approach the new obligations and to develop the necessary experience over time so that the systems set up by the companies and external controls can evolve towards more complex forms. On the basis of this approach, the conclusion requested by the auditor is provided in the form of *limited assurance*, even if also a *reasonable assurance* is permitted. More in detail, currently the engagement performed by the auditor is in the form of limited assurance because of the subjective nature of the information, the less maturity of the reporting processes in comparison with the financial one, and the lack of suitable assurance standards on NFI.

The elements that must be included in the assurance report depend on the type of engagement performed and the assurance standards adopted by the practitioner. An in-depth analysis of the assurance statement’s contents is performed further in this chapter. In this regard, it is interesting to note that both CONSOB regulation and the Legislative Decree 254/2016 do not mention the assurance standard ISAE 3000, one of the main universally recognized standards used for the assurance of NFI. This omission will allow to eventually use an assurance standard specifically defined for NFI reports in the future, instead of a standard for general assurance engagements such as ISAE 3000.

Despite the existence of frameworks and standards that can help the practitioners to perform their assurance engagement, there are a number of additional challenges that practitioners face when providing external assurance on NFI, as it is explained in the last paragraphs of this chapter.

In support of the growing importance of external assurance, it is possible to mention also the contribution given on the topic by international standard setters, in particular by the GRI and the IIRC. Both organizations published two documents in 2013 and 2014, respectively:

- GRI - The external assurance of sustainability reporting;
- IIRC - Assurance on <IR>.

The first document is directed to companies and users of the non-financial report and aims to contribute to the spread of external assurance. The second document focuses on the analysis of the main aspects and challenges in the assurance process of an integrated report, and on the importance of a reporting model appropriate to the variety of contents of the <IR> framework. The main purpose of this document is to stimulate a debate about the need to define an assurance standard that approaches the issue of reporting in different ways, verifying in a

single document the coexistence of financial and non-financial information. A specific focus on the topic is provided in the last paragraph of this chapter.

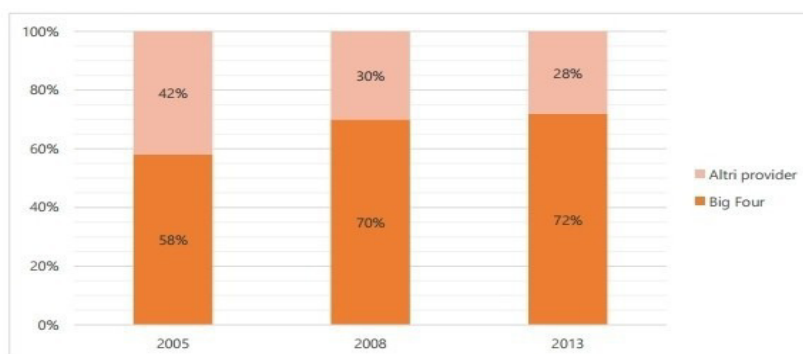
3.2 ASSURANCE ISSUERS AND ASSURANCE STANDARDS

First of all, it is necessary to underline that there is no internationally recognised standard for external assurance on corporate NFI reports. Moreover, there are also more than one type of assurance statements depending on the engaged assurance expert.

The main types of external assurance providers are: auditing firms, certification firms, consultancy and assurance firms on sustainability reports, individual professionals, opinion and NGO leaders, stakeholder panels, civil society organizations, and academic institutions.

However, the different types of providers do not correspond to a fair distribution in terms of market shares. In the international context, large auditing firms and certification firms play a major role in this sector even before professionals specializing in the field of NFI or stakeholder panels. According to the various surveys carried out by KPMG on corporate responsibility reporting⁹⁵ between 2005 and 2013 (to which reference was made also in the first chapter of this Thesis), the assurance of the NFI reports by the large auditing firms (*Big Four*) went from 60% to 67% in the N100 sample⁹⁶, and from 58% to over 70% in the G250 sample⁹⁷.

Graph. 1: External assurance providers on G250 non-financial report in 2005, 2008 and 2013.



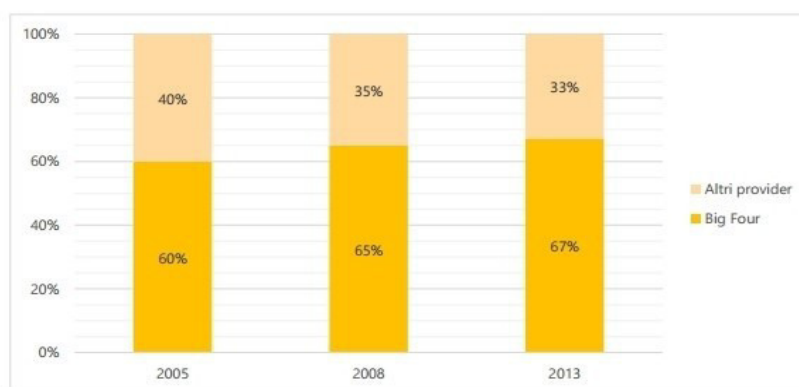
Source: Elaboration of data published in KPMG, *Global Sustainability Service*, 2008 and KPMG International, *The KPMG Survey of Corporate Responsibility Reporting 2013*, 2013.

⁹⁵ KPMG, Global Sustainability Services, 2008 and KPMG International, *The KPMG Survey of Corporate Responsibility Reporting 2013*, 2013.

⁹⁶ The N100 refers to a worldwide sample of 4.900 companies comprising the top 100 companies by revenue in each of the countries researched in the KPMG studies.

⁹⁷ The G250 refers to the world's 250 largest companies by revenue based on the Fortune 500 ranking of 2005, 2008 and 2013.

Graph. 2: External assurance providers on N100 non-financial report in 2005, 2008 and 2013.



Source: Elaboration of data published in KPMG, *Global Sustainability Service*, 2008 and KPMG International, *The KPMG Survey of Corporate Responsibility Reporting 2013*, 2013.

The data shows a gradual reduction in market shares held by the types of providers other than auditing and consulting firms, certification bodies and specialized professionals.

In the national context, reference is made to the survey conducted by CNDC⁹⁸ already cited in the first chapter of this Thesis. In the analysed BI50 sample⁹⁹, the situation is even more accentuated than the international one. In 95% of the NFI reports analysed (concerning the financial year 2015), the assurance engagement was carried out by one of the Big Four. The motivations for this preference are numerous, for example the acknowledged link between financial audit and assurance of NFI reports, the specific skills matured on the subject of corporate reporting, the greater credibility attributed to the checks carried out by them and the existence of ethical codes to which the auditors must comply with their activity.

Although there are differences between the various assurance providers, it is possible to divide them into two main categories: accounting issuers, which include the auditing firms and the individual auditors, and non-accounting providers, which include all the other providers listed above. The judgement expressed by an accounting provider as the auditor concerns the accuracy of the data and the systems that generate the information. In contrast, non-accounting providers have a more qualitative assurance approach, aimed at evaluating more the performance than the accuracy of the data. Moreover, while auditors generally adopt a more cautious assurance approach, which translates into a low level of assurance provided, non-accounting providers use a more strategic approach which translates into their involvement during the reporting process with the aim to provide a general considerations on

⁹⁸ CNDC, *Disclosure di NFI, tendenze internazionali e nazionali sulle attività di rendicontazione a asservazione*, 2017.

⁹⁹ The BI50 refers to a sample of the 50 largest companies by revenue in Borsa Italiana.

the adequacy of the information reported¹⁰⁰. Moreover, more competences on sustainability issues and more attention to stakeholder engagement are recognised to non-accounting assurance providers compared to the accounting ones. According to these differences, two assurance approaches could be identified¹⁰¹:

- The accounting based approach, adopted by the auditors and based on the accuracy of the information reported and on the minimization of the auditor's obligations. The international assurance standards taken into account are the auditing standards (ISA) issued by the International Federation of Accountants (IFAC), and specifically the ISAE 3000 *Assurance Engagement Other Than Audits or Reviews of Historical Financial Information*;
- The stakeholder-centred based approach, adopted by non-accounting providers and whose central focus is on stakeholder engagement. The international assurance standards taken into account are the principles of verification established in the AccountAbility's AA1000 Assurance Standard, issued by the Institute of Social and Ethical Accountability.

For the purposes of this Thesis, it is important to underline that in the Italian context the legislation explicitly requires the verification of the NFI report by a third party. Moreover, it requires that the subject in charge of the verification has to be not a mere independent subject with certified professionalism, but a statutory auditor, subject to the ISAE 3000 Standard. Despite this requirement, it is also considered appropriate to make a brief analysis of the AA1000 Assurance Standard, both for its global diffusion, and because in the assurance statements it is possible to find a reference to both standards jointly, as it will be highlighted in the following paragraphs.

The main features of these two assurance standards are described below.

Assurance Standards - ISAE 3000 (Revised)

The assurance of NFI contained in the non-financial reports is currently carried out on the basis of the *International Standard on Assurance Engagements (ISAE) 3000, Assurance Engagements other than Audits or Reviews of Historical Financial Information*, issued from the IAASB (International Auditing and Assurance Standards Board) of the International Federation of Accountants (IFAC) in 2003 and updated in 2013.

¹⁰⁰ CorporateRegister.com, 2008, Assurance View. Pag. 5.

¹⁰¹ Tarquinio L., *Corporate Responsibility Reporting e Assurance esterna: Profili teorici, criticità e prospettive*, G. Giappichelli Editore, 2018. Pag. 103.

According to ISAE 3000 (Revised) an auditor is required to follow specific standards and procedures in conducting the engagement with the aim to obtain sufficient and appropriate evidence in order to be able to express a conclusion useful for the interested stakeholders. First of all the auditor is required to demonstrate strong ethical behavior while providing assurance services, and following ethics standards such as *professional skepticism* and *professional judgement*.¹⁰²

The auditor has to plan and perform the audit (and the assurance engagement as well) with professional skepticism considering that the corporate statements may be affected by material misstatements. Professional skepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatement due to error or fraud, and a critical assessment of audit evidence. Moreover, the work that the auditor performs in order to issue the audit report has many elements on which he has to exercise its professional judgement, which is defined as “*the application of relevant training, knowledge and experience, within the context provided by auditing, accounting and ethical standards, in making informed decisions about the courses of action that are appropriate in the circumstances of the audit engagement*”¹⁰³. ISAE 3000 requires that the engaged auditor has competence in assurance skills and techniques developed through extensive training and practical application, and sufficient competence in the underlying subject matter and its measurement.

In addition to these two general principles, the auditor must apply the fundamental ethical Principles of the International Ethics Standards Board for Accountants Code of Ethics¹⁰⁴, namely:

- Integrity: to be straightforward and honest in all professional and business relationships;
- Objectivity: to not allow bias, conflict of interest or undue influence of others to override professional or business judgements;
- Professional competence and due care: to maintain professional knowledge and skills at the level required to ensure a competent professional service based on current developments in practice, legislation and techniques and act diligently and in accordance with applicable technical and professional standards;
- Confidentiality: to respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not to disclose any such

¹⁰² IAASB, International Standard for Assurance Engagement (ISAE 3000 Revised), 2013. Par. 33-34.

¹⁰³ IAASB, ISAE 3000 Revised. Par. 8 (s).

¹⁰⁴ International Ethics Standards Board for Accountants (IESBA), Code of Ethics for Professional Accountants.

information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor to use the information for the personal advantage of the professional accountant or third parties;

- Professional behavior: to comply with relevant laws and regulations and avoid any action that discredits the profession.

Given the fact that the primary aim of assurance statement is to increase the level of trust and confidentiality of stakeholders, the fundamental prerequisite of auditors is that of Independence, in the forms of:

- Independence of mind: the state of mind that permits the provision of an opinion without being affected by influences that could compromise professional judgement, allowing an individual to act with integrity, and exercise objectivity and professional skepticism.
- Independence in appearance: the avoidance of facts and circumstances that could lead an informed third party, having knowledge of all relevant information, to think that the integrity, objectivity or professional skepticism of the auditor is compromised.

In addition to these requirements, ISAE 3000 expressly cites the International Standard on Quality Control (ISQC 1) issued by the IAASB. The acceptance of the assignment should be subordinated to the identification of a subject responsible for the contents of the object investigated, other than from the final users and the auditor. Furthermore, in the case of an assurance service jointly conducted by more than one person, the auditor should only accept the task if he is reasonably certain that the persons who are part of the work team possess the necessary professional knowledge. In this regard, it may be recalled that independent external audits of sustainability reports necessarily require a multidisciplinary preparation that often goes beyond the traditional skills used by auditors in financial assurance engagements. The involvement of experts, who support the auditor in collecting sufficient and appropriate evidence to be able to express an opinion on the investigated NFI report, is an option expressly provided for by the standard. In this case, all the participants of the working group must adhere to the ethical principles contained in the IFAC-IAASB code, even though each of them will have different responsibilities depending on the assigned tasks. In general, every team member is required a basic knowledge of the overall work, but the auditor has a supervising role. In fact, he assigns tasks to the various experts, evaluates the reasonableness of the assumptions, methods and information sources used, as well as the conclusions expressed by each member of the working group. The auditor has the ultimate responsibility for the opinion expressed in the final assurance statement. His professional opinion will be the

result of the combination of the various empirical evidence gathered and interpreted by the experts. In turn, evidence must present the characteristics of sufficiency and appropriateness (respectively, measurement of the quantity and quality of the evidence collected).

Regarding the process to follow in order to complete the assurance engagement, ISAE 3000 identifies a number of steps, explained in the following sub-paragraphs.

STEP 1 – Preconditions and acceptance of the assurance engagement ¹⁰⁵

The practitioner shall accept or continue an assurance engagement only when:

- (a) The practitioner has no reason to believe that relevant ethical requirements, including independence, will not be satisfied;
- (b) The practitioner is satisfied that those persons who will collectively perform the engagement have the appropriate competence and capabilities;
- (c) The basis upon which the engagement is to be performed has been agreed, through:
 - (i) Establishing that the preconditions for an assurance engagement are present;
 - (ii) Confirming that there is a common understanding between the practitioner and the engaging party of the terms of the engagement, including the practitioner's reporting responsibilities.

Moreover, prior to accepting an assurance assignment the practitioner must assess if the following preconditions for the assurance engagement are present:

- (a) The roles and responsibilities of the appropriate parties are suitable in the circumstances;
- (b) The engagement exhibits all of the following characteristics:
 - i. The underlying subject matter is appropriate;
 - ii. The criteria to be applied in the preparation of the subject matter information are suitable and will be available to the intended users;
 - iii. The practitioner will have access to the evidence needed to support the practitioner's conclusion;
 - iv. The practitioner's conclusion, in the form of a reasonable assurance engagement or a limited assurance engagement, is to be contained in a written report;
 - v. A rational purpose including, in the case of a limited assurance engagement, that a meaningful level of assurance can be obtained.

Focusing on the assessment of the subject matter, assurance engagements can be performed on the NFI report as a whole or only on a part of it, i.e. specific aspects and KPIs, or only on reporting processes (and not on the report data itself). The challenge is to establish whether

¹⁰⁵ IAASB, ISAE 3000 Revised. Par. 17 and ss.

the subject matter and its characteristics are appropriate for a specific assurance engagement. The subject matter of the engagement should also be clear in the assurance report. It must be appropriate, which means identifiable, and capable of consistent evaluation or measurement against the identification criteria. Equally, it means that the information reported can be subject to procedures for gathering sufficient appropriate evidence to support a reasonable assurance or limited assurance conclusion, as appropriate.

Focusing on the assessment of the reporting criteria, it is important to understand how the management of the company determines the suitability of the criteria for reporting purposes. The main challenge for the assurance practitioner is in assessing the criteria and ensuring that the criteria are suitable for a particular assurance engagement. According to ISAE 3000, suitable criteria should follow certain characteristics:

- (a) **Relevance:** relevant criteria result in subject matter information that assists decision-making by intended users.
- (b) **Completeness:** criteria are complete when subject matter information prepared in accordance with them does not omit relevant factors that could reasonably be expected to affect decisions of the intended users will take on the basis of that subject matter information. Complete criteria include, where relevant, benchmarks for presentation and disclosure.
- (c) **Reliability:** reliable criteria allow reasonably consistent measurement or evaluation of the underlying subject matter including, where relevant, presentation and disclosure, when used in similar circumstances by different practitioners.
- (d) **Neutrality:** neutral criteria result in subject matter information that is free from bias.
- (e) **Understandability:** understandable criteria result in subject matter information that can be understood by the intended users.

The variety of reporting frameworks available for reporting purposes can also become an issue for an assurance practitioner. A company may choose between different reporting standards, as explained in chapter two of this Thesis, but it is not always possible to provide assurance against a chosen framework.

If these prerequisites are satisfied, the assurance practitioner shall accept the engagement and shall agree the terms of the engagement with the engaging party. The agreed terms of the engagement shall be specified in sufficient details in an engagement letter or other suitable form of written agreement. It is important to agree on the scope of the engagement in order to ensure a common understanding between the assurance practitioner and the engaging party.

Non-financial information is by nature broader than financial information. This is the reason why it is essential to properly determine the engagement.

After defining the letter of assignment, the auditor proceeds with the definition of the plan of activities defining the strategy and a plan of the assignment that include: purpose, timing and composition of the team (including the involvement of experts), roles and responsibilities.

STEP 2 – Planning and performing the assurance engagement¹⁰⁶

The practitioner shall plan the engagement to perform it in an effective manner, including setting the scope, timing and direction of the engagement, and determining the nature, timing and extent of planned procedures required to be carried out in order to achieve the objective of the engagement.

One of the most challenging procedures for the auditor is the assessment of materiality and its definition. The practitioner shall take materiality into consideration when:

- (a) Planning and performing the assurance engagement, including determining the nature, timing and extent of procedures; and
- (b) Evaluating whether the subject matter information is free from misstatement.

According to ISAE 3000, misstatements and omissions are material if they could reasonably affect the decisions that intended users take on the basis of the subject matter.

Moreover, the practitioner shall obtain an understanding of the underlying subject matter and other engagement circumstances sufficient to design and perform procedures in order to achieve the objectives of the engagement.

There are different levels of assurance engagement, which depend on the type of work that the assurance practitioner performs.

A *reasonable assurance* engagement indicates that, according to the verification procedures carried out and taking into account the object of verification, the assurance issuer has obtained sufficient probative elements suitable to reduce the risk associated with the audit engagement to an acceptably low level in relation to the circumstances of the assignment¹⁰⁷.

While the reasonable assurance obtained in an audit is a high level of assurance, it is not absolute assurance (a certification that the corporate statements are completely correct). Obtaining absolute assurance is not possible for a number of reasons, for example because it is impossible for the auditor to test and audit every transaction or issue, or because of the presence of estimates or qualitative information which often cannot be determined exactly or may be contingent on future events.

¹⁰⁶ IAASB, ISAE 3000 Revised. Par. 35 and ss.

¹⁰⁷ IAASB, ISAE 3000 Revised, par. 12.

A *limited assurance* engagement, instead, indicates that, in relation to the verification procedures and the characteristics of the object of verification, the issuer has obtained sufficient evidence to reduce the risk of engagement to an acceptable low level, but higher than that of a reasonable assurance.

Depending on the assurance level, the nature, timing and extent of the verification procedures carried out by an assurance issuer are different.

In the case of limited assurance, the assurance issuer could place more emphasis on collecting evidence through interviews and analytical procedures, while in the case of reasonable assurance, the assurance issuer has to perform more detailed procedures, such as substantive tests.

However, it should be noted that, even in the presence of a limited assurance, the procedures are planned in order to obtain a level of assurance that, in the opinion of the verifier, is adequate.

An assurance level is adequate if it is capable of reinforcing the degree of trust in the information reported up to a level that is "more than irrelevant"¹⁰⁸.

The form in which the conclusions are communicated is also linked to the level of assurance. In the case of reasonable assurance the conclusions are formulated in a positive form:

“In our opinion, the financial statements that the company has prepared in compliance with the law are, in all its material aspects, correctly prepared.”

In case of limited assurance, considering that the extension of the checks is lower than that required by the previous one, the assurance issuer expresses his opinion in a negative form, in which there is a double negation:

“Based on the work performed, nothing has come to our attention that causes us to believe that the non-financial statement of the Company has not been prepared, in all material respects, in compliance with the normative and the reporting standards”.

STEP 3 – Risk assessment and definition of appropriate procedures in relation to the subject matter and the desired level of assurance¹⁰⁹

¹⁰⁸ IAASB, ISAE 3000 Revised, par. A3-A4-A7.

¹⁰⁹ IAASB, ISAE 3000 Revised, par. 39 and ss.

The practitioner shall apply professional judgement to determine the nature, timing and extent of procedures in accordance with the circumstances of the engagement.

In a reasonable assurance engagement the practitioner shall:

- (a) Based on the practitioner's understanding, identify and assess the risks of material misstatement;
- (b) Respond to assessed risks, by
 - (i) developing and implementing overall responses; and
 - (ii) determining the nature, timing and extent of procedures that are clearly responsive to the assessed risks, and performing those procedures.

The procedures shall involve substantive procedures (including obtaining corroborating information from independent sources, when relevant), and when relevant to the engagement circumstances, tests of the operating effectiveness of controls over the measurer or evaluator's preparation of the subject matter information (in the case of an attestation engagement) or over data used by the practitioner in measuring or evaluating the underlying subject matter (in a direct engagement);

- (c) Based on the procedures performed and the evidence obtained, evaluate before the end of the engagement, whether the practitioner's assessment of the risks that the subject matter information may be materially misstated, remains appropriate.

In a limited assurance engagement, the practitioner shall:

- (a) Based on the practitioner's understanding and consideration of areas where material misstatements are likely to arise, determine the nature, timing and extent of procedures to be performed to obtain a level of assurance that is meaningful to the intended users;
- (b) Perform those procedures; and
- (c) If the practitioner becomes aware of a matter(s) that causes the practitioner to believe the subject matter information may be materially misstated, the practitioner shall design and perform additional procedures sufficient to enable the practitioner to:
 - (i) Conclude that the matter(s) is not likely to cause the subject matter information to be materially misstated; or
 - (ii) Determine that the matter(s) causes the subject matter information to be materially misstated.

Considering the extent of the engagement and the relative risks, no standard procedures were defined but some general indications were provided based on the desired assurance level:

- Reasonable Assurance:

- Understanding of the client and the processes;
 - Analysis of risk indicators such as business continuity, fraud, use of estimates;
 - Adequate evidence from procedures (testing of controls but more frequently substance procedures).
- Limited Assurance:
 - Understanding of the client and the processes;
 - Analytical procedures and interviews;
 - Although not normally expected, risk indicators such as those mentioned above may be present.

Among the various checks that must be carried out by the auditor, there are: inspections, observations, confirmations, recalculations, re-performances, analytical procedures, inquiries, tests of the operating effectiveness of controls, etc. This is a mix of control tests and substance tests that should investigate in-depth non-financial report in order to reach conclusions supported by sufficient and appropriate evidence.

STEP 4 – Forming the assurance conclusion and preparing the assurance statement¹¹⁰

This phase includes the redefinition of materiality (if necessary), the analysis of subsequent events, the preparation of a summary of the critical aspects detected, the obtainment of the final assurance statement signed by the auditor and any further communications with the governance bodies.

The practitioner shall form a conclusion stating whether the reported outcome of the measurement or evaluation of the underlying subject matter is free from material misstatement. In forming that conclusion, the practitioner shall consider:

- (a) The practitioner's conclusion regarding the sufficiency and appropriateness of evidence obtained; and
- (b) An evaluation of whether uncorrected misstatements are material, individually or in aggregate.

If the practitioner is unable to obtain sufficient appropriate evidence, a scope limitation exists and the practitioner shall express a qualified conclusion, disclaim a conclusion, or withdraw from the engagement. Withdrawal is possible under applicable laws or regulations, if appropriate.

¹¹⁰ AASB, ISAE 3000 Revised, par. 56 and ss.

The assurance statement shall contain a clear expression of the practitioner's conclusion that conveys the assurance obtained about the subject matter information. The practitioner's conclusion on the subject matter information shall be clearly separated from any emphasis of matter, findings, recommendations or similar information included in the assurance report. ISAE 3000 suggests using either a "short form" or a "long form" report for effective communication purposes with the intended users. The assurance practitioner can include additional information and explanations in a "long form" report. This type of information could add value to the assurance provided. In this sense, the assurance report could also act as a means for encouraging effective communication and dialogue with users.

Assurance standards - A1000AS

An assurance report in accordance with ISAE 3000 can only be issued by professional accountants, since the auditor must also comply with the IESBA Code of Ethics for Professional Accountants. Other assurance issuers may use assurance methodologies based on ISAE 3000 or on combined elements of ISAE 3000 and other standards, such as AccountAbility 1000 Assurance Standard (AA1000AS).

The AA1000AS was published for the first time in 2003, qualifying itself as the first sustainability assurance standard in the world. This standard, in its 2008 updated version, aims to evaluate and provide conclusive considerations on the adoption of the principles of Accountability 1000 and, where applicable, on the quality of the information communicated by organizations regarding their non-financial performance¹¹¹. Unlike ISAE 3000, the AA1000AS pays specific attention to whether the organization and its NFI reporting respond to stakeholder concerns. The external assurance statement prepared under this assurance standard has to be based on three principles: completeness, materiality and responsiveness. Inclusiveness is the founding principle and *"means fostering stakeholder participation in development and achieving a responsible and strategic response to sustainability"*¹¹². The principle of materiality pertains to the relevance of a theme for the company and its stakeholders. A theme is considered material when it is able to influence *"the decisions, actions and performances of an organization or its stakeholders"*¹¹³. The practitioner has to investigate how a company responds to the issues raised by its stakeholders and is accountable towards them¹¹⁴. According to the AA1000AS, there are two types of tasks related to the process of reviewing a NFI report:

¹¹¹ Accountability, AA1000AS. Pag. 8

¹¹² Accountability, AA1000 Accountability Principles Standard (APS), 2008. Pag. 12.

¹¹³ Accountability, AA1000 Accountability Principles Standard (APS), 2008. Pag. 14.

¹¹⁴ Accountability, AA1000 Accountability Principles Standard (APS), 2008. Pag. 16.

1. The principles of AccountAbility: the assurance provider will assess, in addition to the degree of adhesion of the organizations to the three Accountability Principles, the information communicated, and the systems and processes adopted by the company to guarantee the compliance with these principles. The assurance provider is not required to verify the reliability of the information communicated¹¹⁵.
2. The principles of AccountAbility and information on performance: the assurance provider will assess the nature and degree of adherence of an organization to the AA1000 principles, as specified in the first type of assurance. Moreover, the assurance provider will assess the reliability of specific non-financial performance information, as agreed among the parties with the purpose of assurance and selecting information based on materiality¹¹⁶. In this case, the review process can follow two paths depending on whether the result is provided at a *High level of assurance* or at a *Moderate level of assurance*. Given the diversity in nature of the reviewed topics, it is possible to provide a high level of Assurance for certain issues and a moderate one for others within the same assurance statement. In the case of a high level of verification, the verification procedures activated and the checks collected allow the assurance provider to judge the risk of error in his conclusions at a very low (but not zero). In the case of a moderate level of verification, the assurance provider obtains sufficient evidence to enable him to reduce the risk that his conclusion is incorrect, even if this risk is not as low as that of high level assurance. In any case the risk can not be equal to zero¹¹⁷.

This standard is used by different types of assurance providers. Organizations seeking to emphasize their commitment to the AA1000AS Principles, including their responsiveness to stakeholder views, often choose assurance based on AA1000AS. Unlike ISAE 3000, the standard is not supported by an external assurance framework and does not provide guidance on specific aspects of an assurance engagement such as engagement acceptance, measurement criteria, types of procedures to be performed, and types of conclusion to be provided.

Key elements of an assurance statement

Once the assurance engagement is completed, the practitioner will issue an assurance statement that may be disclosed as part of the sustainability reporting process. This document

¹¹⁵ Accountability, AA1000AS. Pag.9.

¹¹⁶ Accountability, AA1000AS. Pag.10.

¹¹⁷ Accountability, AA1000AS. Pag.11.

is drafted and signed by the assurance issuer. The form and content vary depending on the assurance scope, the assurance standard being used and, to some extent, on the assurance issuer preferences. Below two examples of assurance statement on NFI report are reported, the first according to ISAE 3000 (Revised) and the second according to AA1000AS principles.

Fig. 1: Example of assurance report according to ISAE 3000 (Revised)

Independent auditor's report on the consolidated non-financial statement

pursuant to article 3, paragraph 10, of Legislative Decree n° 254/2016 and article 5 of Consob Regulation n° 20267

To the Board of Directors of **ABC S.p.A.**

Pursuant to article 3, paragraph 10, of Legislative Decree n° 254 of 30 December 2016 (the "Decree") and article 5 of CONSOB Regulation n° 20267, we have performed a limited assurance engagement on the "Sustainability Report - Containing the Group non-financial disclosure" of **ABC S.p.A.** and its subsidiaries (hereafter the "Group") for the year ended 31 December 2017 prepared in accordance with article 4 of the Decree and approved by the Board of Directors on 15 March 2018 (hereafter the "NFS").

Responsibility of the directors and of the Board of Statutory Auditors for the NFS

Directors are responsible for the preparation of the NFS in accordance with article 3 and 4 of the Decree and with the "Global Reporting Initiative Sustainability Reporting Standards" defined in 2016 by the GRI - Global Reporting Initiative ("GRI Standards"), as laid down in paragraph "Reporting Methods, Principles and Criteria" of the NFS, identified by them as the reporting standard.

Directors are responsible, in the terms prescribed by law, for such internal control as management determines is necessary to enable the preparation of a NFS that is free from material misstatement, whether due to fraud or error.

Directors are responsible for identifying the content of the NFS, within the matters mentioned in article 3, paragraph 1, of the Decree, considering the activities and characteristics of the Group and to the extent necessary to ensure an understanding of the Group's activities, its performance, its results and related impacts.

Directors are responsible for defining the business and organisational model of the Group and, with reference to the matters identified and reported in the NFS, for the policies adopted by the Group and for the identification and management of risks generated and/or faced by the Group.

The Board of Statutory Auditors is responsible for overseeing, in the terms prescribed by law, compliance with the Decree.

Auditor's Independence and Quality Control

We are independent in accordance with the principles of ethics and independence set out in the Code of Ethics for Professional Accountants published by the International Ethics Standards Board for Accountants, which are based on the fundamental principles of integrity, objectivity, competence and professional diligence, confidentiality and professional behaviour. Our audit firm adopts International Standard on Quality Control 1 (ISQC Italy 1) and, accordingly, maintains an overall quality control system which includes processes and procedures for compliance with ethical and professional principles and with applicable laws and regulations.

Auditor's responsibilities

We are responsible for expressing a conclusion, on the basis of the work performed, regarding the compliance of the NFS with the Decree and with the GRI Standards. We conducted our engagement in accordance with International Standard on Assurance Engagements 3000 (Revised) – Assurance Engagements Other than Audits or Reviews of Historical Financial Information (hereafter “ISAE 3000 Revised”), issued by the International Auditing and Assurance Standards Board (IAASB) for limited assurance engagements. The standard requires that we plan and apply procedures in order to obtain limited assurance that the NFS is free of material misstatement. The procedures performed in a limited assurance engagement are less in scope than those performed in a reasonable assurance engagement in accordance with ISAE 3000 Revised, and, therefore, do not provide us with a sufficient level of assurance that we have become aware of all significant facts and circumstances that might be identified in a reasonable assurance engagement.

The procedures performed on the NFS were based on our professional judgement and consisted in interviews, primarily of company personnel responsible for the preparation of the information presented in the NFS, analyses of documents, recalculations and other procedures designed to obtain evidence considered useful.

In particular, we performed the following procedures:

- 1 Analysis of the relevant matters reported in the NFS relating to the activities and characteristics of the company, in order to assess the reasonableness of the selection process used, in accordance with article 3 of the Decree and the with the reporting standard adopted.
- 2 Analysis and assessment of the criteria used to identify the consolidation area, in order to assess their compliance with the Decree.
- 3 Comparison of the financial information reported in the NFS with the information reported in the Group's consolidated financial statements.
- 4 Understanding of the following matters:
 - business and organisational model of the Group, with reference to the management of the matters specified by article 3 of the Decree;
 - policies adopted by the Group with reference to the matters specified in article 3 of the Decree, actual results and related key performance indicators;
 - main risks, generated and/or faced by the Group, with reference to the matters specified in article 3 of the Decree.

With reference to those matters, we compared the information obtained with the information presented in the NFS and carried out the procedures described under point 5 a) below.

- 5 Understanding of the processes underlying the preparation, collection and management of the significant qualitative and quantitative information included in the NFS.

In particular, we held meetings and interviews with the management of **ABC S.p.A.** and with the personnel of (**specify what group's Companies are involved**) and we performed limited analyses of documentary evidence, to gather information about the processes and procedures for the collection, consolidation, processing and submission of the non-financial information to the function responsible for the preparation of the NFS.

Moreover, for material information, considering the activities and characteristics of the Group:

- At a group level:
 - a) with reference to the qualitative information included in the NFS, and in particular to the business model, the policies adopted and the main risks, we carried out interviews and acquired supporting documentation to verify their consistency with available evidence;
 - b) with reference to quantitative information, we performed analytical procedures as well as limited tests, in order to assess, on a sample basis, the accuracy of consolidation of the information.
- For the companies (**specify what group's Companies are involved**), which were selected on the basis of their activities, their contribution to the performance indicators at a consolidated level and their location, we carried out in depth analysis, during which we met local management and gathered supporting documentation regarding the correct application of the procedures and calculation methods used for the key performance indicators.

Conclusions

Based on the work performed, nothing has come to our attention that causes us to believe that the NFS of **ABC S.p.A.** as of 31 December 2017 has not been prepared, in all material respects, in compliance with articles 3 and 4 of the Decree and with the GRI Standards.

Other aspects

The comparative data presented in the NFS in relation to previous years has not been subjected to any procedures.

Place, Date

Auditing Firm

Signed by

Name, Surname

(Partner)

Signed by

Name, Surname

(Authorized signatory)

To summarize, information provided in an assurance statement according to ISAE 3000 (Revised) may include¹¹⁸:

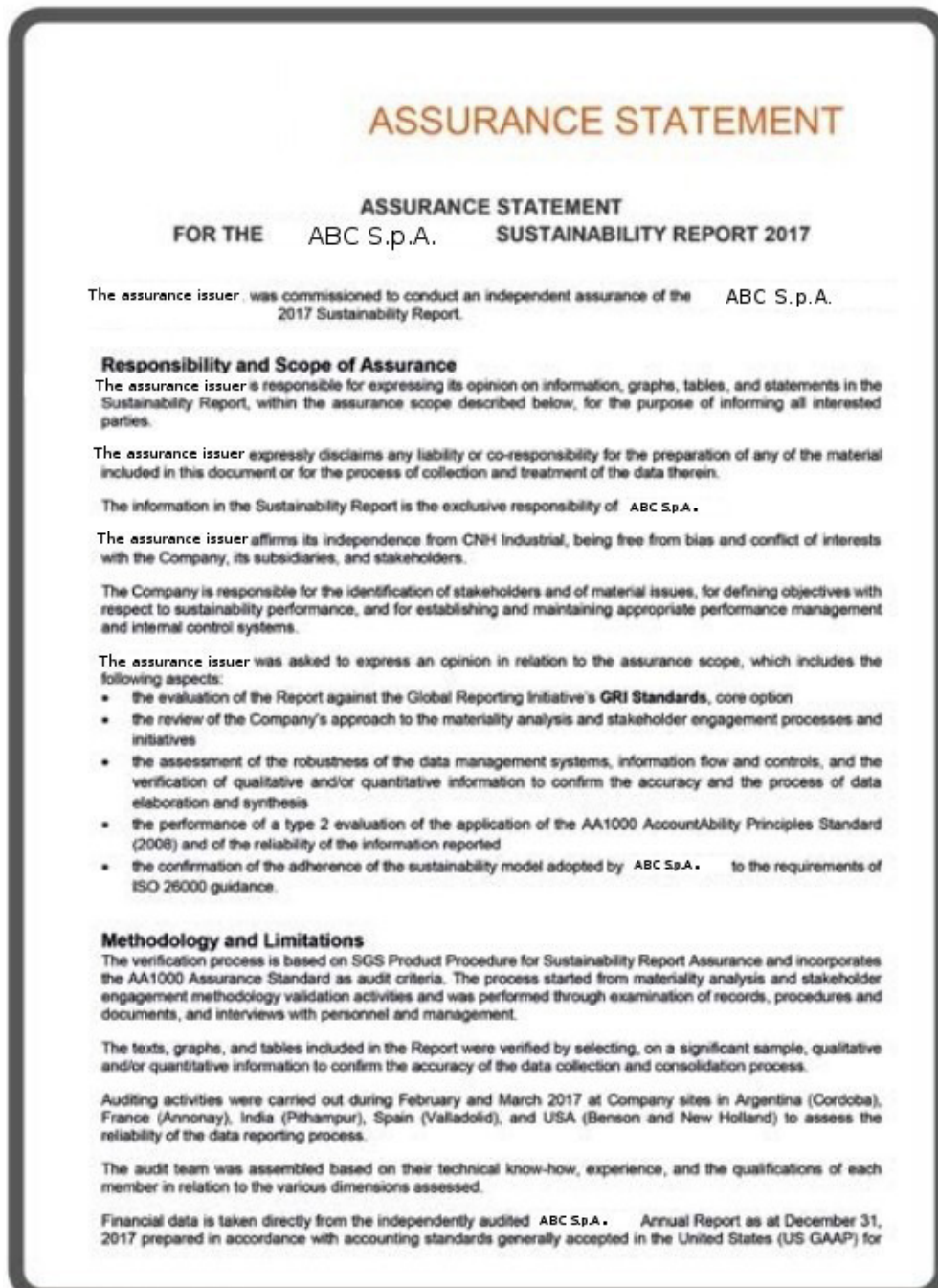
- Title: indicating that the report is an independent assurance statement and the regulation to which the statement is subject;

¹¹⁸ IAASB, ISAE 3000 (Revised). Par. 60.

- Addressee: The intended audience for the assurance statement (e.g. stakeholders, the board of directors, etc.);
- Introduction: a general overview of the information contained in the NFI report such as the specific regulation to which the report is subject, which disclosures are covered by the assurance verification process and what is the subject matter, the reporting year of reference, the subject in charge of the verification, and the level of assurance engagement (the assurance of NFI report is always a limited assurance);
- A statement to identify the responsibilities of the management and of the Supervisory Board and the selected reporting criteria: the responsibility for the preparation and presentation of the non-financial statement in accordance with the general accepted principles is solely of the management, with the supervision of those in charge of the governance. Auditor's responsibility is to express an opinion on the NFI report. This paragraph also identifies criteria and methodologies used by the reporter when preparing the NFI report (e.g. GRI G4 Guidelines, GRI Standards, <IR> Framework, etc.);
- A statement to underline the compliance with auditor's principles and standards: a declaration on the respect of the principles of independence and of the other ethical principles established by the International Code of Ethics and used in the assurance process. There is also a reference to the International Standard on Quality Control 1 (ISQC 1);
- A statement to identify the responsibilities of the auditor: this paragraph identifies the standard(s) used by the auditor to perform the assurance engagement (e.g. ISAE 3000, AA1000AS, or national and sector standards) and summarizes the actions and procedures taken to check the accuracy, plausibility and relevance of the NFI covered by the assurance. If necessary, there could be also a comment on any noteworthy limitations on either the scope of the information assured or on the assurance activities, such as the unavailability of some data, or changes in the data gathering systems;
- Conclusion: a statement indicating whether the assured information is fairly presented, free of material misstatements and reported in accordance with reporting criteria. A focus on the possible types of auditor's opinions is provided below.
- Other aspects: a statement indicating some additional material aspects.
- Signature and date: a formal sign-off by the auditor responsible for the assurance.

The second example of assurance statement analyzed is the one issued according to AA1000AS principles. This standard is used by the non-accounting providers, for this reason a company which follows the Italian legislation could not be assured with a report as reported below.

Fig. 2: Example of assurance report according to AA1000AS



US Securities and Exchange Commission (SEC) reporting purposes. The US GAAP financial results are included in the Annual Report on Form 20-F.

Assurance Opinion

On the basis of the verification work performed, we are satisfied that the information contained in the ABC S.p.A. 2017 Sustainability Report is accurate, balanced, and reliable, representing a relevant summary of the activities carried out by ABC S.p.A. in 2017 and an essential tool in communicating with stakeholders.

The assurance issuer confirms that the information included in the Report provides a material and complete representation of the Company's sustainability performance.

The verification process confirmed that the Report was prepared based on rigorous processes.

With regards to the level of adherence to the AA1000 Principles (Inclusivity, Materiality, and Correspondence), and to the approach of the Company to the materiality analysis and stakeholder engagement processes and initiatives, the Audit team provides the following opinion:

- the Creating Shared Value (CSV) approach adopted by CNH Industrial reflects its commitment to the most relevant UN Sustainable Development Goals for the Company, in line with the global megatrends, the material topics, and the long-term targets identified
- the Materiality Matrix has been further enhanced by surveying additional stakeholders. Customers were the focus in 2017, and 177 interviews were conducted with Agricultural Equipment, Commercial Vehicles, and Powertrain customers
- regarding environment and energy management, the integration of a new criterion based on carbon pricing into the evaluation and prioritization of energy efficiency projects was welcomed.

In the 2017 Sustainability Report, the Company has included more indicators than specified by the minimum requirements of the core option.

Furthermore, we confirm that the sustainability model – integrated into the Company's business model – is in line with the requirements of ISO 26000 guidance.

Statement of conclusion

On the basis of the verification performed, we are satisfied that the information contained in the 2017 Sustainability Report is accurate and reliable, and provides stakeholders a fair and balanced representation of the activities of ABC S.p.A.

With reference to the GRI Standards, the organization satisfies the principles for defining report content and the principles for ensuring the quality of reported information.

We confirm that the Report is aligned with the requirements of the Global Reporting Initiative's **GRI Standards: core option**.

Place, Date

Name, Surname

Business Manager



To summarize, information provided in an assurance statement according to AA1000AS may include:

- Title: indicating the object of the document and the parties between which the engagement was performed;
- Responsibility and scope of assurance: the responsibility for the preparation and presentation of the NFI report is solely of the management, with the supervision of

those in charged of the governance. The assurance issuer's responsibility is to express an opinion on the NFI report. The assurance scope includes the evaluation of the report against the choosen reporting principle (GRI Standards), the verification on the accuracy of management and control systems and the performance of a *type 2* evaluation of the AA1000APS and of the reliability of the information reported.

- Methodology and limitations: summarizing the actions and procedures taken to check the accuracy, plausibility and relevance of the NFI covered by the assurance. If necessary, there could be also a comment on any noteworthy limitations on either the scope of the information assured or on the assurance activities.
- Assurance opinion: containing some consideration about the Creating Share Value approach, the adherence to SDGs, the materiality assessment process and other suggestions.
- Statement of conclusion: a statement indicating whether the assured information is accurate and reliable, and provides stakeholders a fair and balanced representation of the activities of the company.
- Signature and date: a formal sign-off by the assurance business manager responsible for the issued assurance statement.

From this comparison is possible to notice that the content of the assurance statement is very similar both in the case of the use of ISAE 3000 and the use of AA1000AS. The AA1000AS, unlike the ISAE 3000, also provides observations and recommendations to be included in the assurance statement and aimed at improving the quality of reports, processes and information management systems. Instead, the assurance statements usually issued by the auditor do not contain recommendations and comments on company processes. Moreover, they are often characterized by a limited assurance and therefore expressed in a negative form. Assurance statements prepared by non-accounting providers often contain additional comments, are characterized by a reasonable or high assurance, and therefore are expressed in a positive form. The reason why advice and recommendations are not present in the assurance statements issued by an auditor seems to be the fear of a lesion, in the eyes of the stakeholders, of the principle of independence of the auditor. For example, an auditor who provides suggestions for the improvement of the report might appear to be interested in providing also other services as well. On the contrary, it can be argued that the provision of recommendations could be useful in order to inform third parties about what can be introduced or improved in the audited reports. Other differences found in the non-accounting

assurance statement are a greater innovation and a greater focus on the stakeholders-users of the statement compared to those issued by an auditor¹¹⁹.

In practice, when carrying out assurance engagements on NFI reports practitioners sometimes report under both ISAE 3000 and AA1000AS for practical reasons. Since AA1000AS is widely known and recognised by clients in the area of corporate responsibility, some practitioners might find it helpful to refer to this standard. Practitioners use ISAE 3000 because it provides a framework by which the engagement can be carried out. Other providers of external assurance reports might, however, only use AA1000AS or may follow no particular framework or standard when performing an assurance engagement in this area. This lack of a common assurance standard and process results in a number of different reports and conclusions being given on non-financial statements. This lack of consistency in external assurance statements might create some difficulties for stakeholders when making comparison.

Despite the differences between the two assurance standards, in both cases the most relevant part of the auditor's report for stakeholders is the auditor's opinion on the corporate statements¹²⁰. An *unmodified opinion* of the auditor effectively states the auditor believes the statements present a true and fair view, and are in accordance with accounting standards and relevant legislation. This is sometimes also called an “unqualified” or a “clean” audit opinion. Unmodified auditor's reports are the most common in the analysis of non-financial statement issued by listed companies¹²¹. This is in part because management usually addresses most of the problems or adjustments that auditors discover before the non-financial statements are issued. An unmodified review report effectively states the reviewer did not become aware of anything that suggested the financial statements do not present a true and fair view in accordance with accounting standards. In some circumstances, the auditor will include additional wording in the report to give users additional information that is fundamental to understanding the non-financial statements, or it is material for their decisions. It is important to note that an emphasis of matter or other matter paragraph is not considered a qualification, limitation or adverse conclusion.

A *modified opinion* of the auditor is issued when the auditor believes the financial statements contain a material misstatement, or when the auditor is unable to obtain enough evidence to form an opinion. “Material misstatements” are intended those misstatements that are

¹¹⁹ Tarquinio L., 2018. Pag. 113 and ss.

¹²⁰ IAASB, ISAE 3000 (Revised). Par. 63 and ss.

¹²¹ See the analysis performed in the last chapter of this Thesis.

significant enough to affect the decisions made by the users of the financial statements. This can be both in terms of quantitative or qualitative significance of misstatements.

Regarding the detection of material misstatements, it is necessary to underline that the auditor also considers the possibility that material misstatements could be the result of fraudulent activities, but this does not mean that the audit has the primary aim to investigate and discover frauds.

When an auditor expresses a modified opinion, he also has to carry out an in-depth analysis on the reasons. Depending on his judgement and on the types of misstatement, the auditor shall express a *qualified opinion*, an *adverse opinion* or a *disclaimer opinion*. The criteria to evaluate his opinion are:

- the nature of the matter giving rise to the modification, that is, whether the statement is materially misstated or, in the case of inability to obtain sufficient appropriate audit evidence, may be materially misstated; and
- the auditor's judgement about the pervasiveness of the effects or possible effects of the matter on the statement. Pervasive misstatements on the statement are those that, in the auditor's judgement:
 - are not confined to specific elements of the statement;
 - if confined, they represent or could represent a substantial proportion of the statement; or
 - in relation to disclosures, they are fundamental to users' understanding of the statement.

Following these criteria, the auditor shall express a qualified opinion when:

1. The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in aggregate, are material, but not pervasive, to the statement; or
2. The auditor is unable to obtain sufficient appropriate audit evidence on which to base his opinion. However, the auditor concludes that any possible effects of undetected misstatements on the statement could be material but not pervasive.

An example of qualified opinion is when the auditor has a different view on the valuation of an asset than that applied by the management in the financial statements, but the rest of the financial statements are found to be free of material misstatements.

The auditor shall express an adverse opinion when, having obtained sufficient appropriate audit evidence, he concludes that misstatements, individually or in aggregate, are both material and pervasive to the statement. An example of adverse opinion is when the auditor

believes that the management has applied an inappropriate reporting framework when preparing the statements as a whole.

The auditor shall disclaim an opinion when he is unable to obtain sufficient appropriate audit evidence on which to base his opinion. For this reason, the auditor concludes that the possible effects on the statements of undetected misstatements, if any, could be both material and pervasive. Moreover, the auditor shall disclaim an opinion when, in extremely rare circumstances involving multiple uncertainties, he concludes that, notwithstanding having obtained sufficient appropriate audit evidence regarding each of the individual uncertainties, it is not possible to form an opinion on the statements due to the potential interaction of the uncertainties and their possible cumulative effect on the statements. An example of disclaimer of opinion is when the company's reporting information system is damaged and key data is lost, meaning adequate evidence is not available to support the disclosures in the statements.

Once explained the importance and the types of opinion that can be read in the audit report conclusion, it is necessary to make some general considerations about the auditor responsibility. First of all the auditor's report is intended to increase the degree of confidence users have in the information stated in corporate statements, it is not about the state of the company itself or whether it is a safe investment. An unmodified auditor's report means investors or other stakeholders can make an assessment of the company based on its financial and non-financial statements with a higher degree of confidence that the information is materially correct and unbiased. Auditors also perform a role in assessing the appropriateness of the going concern assumption used by the management in preparing the statements. The meaning of going concern assumption is that a company will continue to stay in business for the foreseeable future and it is adopted unless evidence indicates otherwise. The auditor performs his job to assess this assumption as part of the audit, but this cannot be taken as a conclusion of the solvency or the financial health of the company. The auditor's focus in this assessment is whether the company can continue as a going concern for a 12-month period from the date of signing the auditor's report.

The going concern assumption involves judgements about events taking place in the future, which are inherently uncertain. Where there is a significant uncertainty in the company's ability to continue as a going concern, and this has been disclosed by management in the financial statements, the auditor includes in the auditor's report an emphasis of matter paragraph to underline this issue. Ultimately, if the auditor does not agree with the management's assumptions in regard to going concern, the result would be a modified opinion.

3.3 PRACTICE-RELATED CONSIDERATIONS FOR THE AUDITOR

Despite the existence of guidance, such as ISAE 3000 and AA1000AS, there are a number of additional challenges and issues for practitioners to consider when they perform an assurance engagement on NFI. As a general overview, the following critical issues could be mentioned.

Skills – experience, training and additional specialist knowledge

Practitioners' auditing experience can be valuable when carrying out assurance engagements on non-financial information. They use professional judgement and are familiar with assessing materiality, understanding the business and obtaining sufficient appropriate audit evidence. ISAE 3000 addresses certain quality aspects of external assurance such as the need for appropriate specialist knowledge and specific skills to be available in the assurance team. For example, practitioners have expertise in performing quantitative assessment of information but they are less likely to have experience of performing assurance engagements on qualitative information. Furthermore, it is unlikely that practitioners will have an in depth expert technical knowledge, for this reason practitioners will consider to use the work of experts. These skills can, however, be developed and the use of multi-disciplinary teams and frameworks can help practitioners to meet these needs¹²².

Define the scope of assurance engagement

In some instances, the scope is defined by regulatory requirements or by a specific standard. However, defining the scope for the majority of assurance engagements is quite complex. The scope of the assurance engagement has shifted from focusing only on the company's KPIs to a broader set of NFI. The increased scope introduces a number of challenges for assurance practitioners that may have to deal with a scope for the assurance engagement that differs from the scope used for reporting purposes by the company.

Moreover, there is considerable flexibility in determining the scope. For example, limited or reasonable assurance can be provided on a selection of KPIs, a full NFI report, or a combination of limited assurance on some KPIs and reasonable assurance on other part of the NFI report. Given this flexibility, clients and others stakeholders have difficulty in understanding the scope of the assurance engagement. The scope of the assurance engagement is sometimes not clear enough in the assurance statements. Also, clients and users often do not have a sufficient understanding of the roles and responsibilities of the assurance practitioner.

¹²² ICAEW Audit and Assurance Faculty, Assurance of non-financial information: Existing practice and issues, 2008. Pag.18.

Asses the subject matter and suitable criteria

ISAE 3000 requires the assurance practitioner to assess whether the underlying subject matter is appropriate for the specific assurance engagement. This means that the subject matter must be identifiable and capable of consistent evaluation and measurement.

In comparison with financial information, standardized measurement for non-financial information, in particular for qualitative information, are not usually available.

This has potential implications for practitioners, which include:

- the subject matter can be evaluated from different viewpoints and it might not be possible to establish consistent measurement criteria that are acceptable to all interested parties; and
- the subject matter is fundamentally of a subjective nature, for instance the company's vision for the future, and hence it is impossible to identify suitable criteria.

Where different viewpoints exist to evaluate the subject matter, interested parties may not be able to agree on the criteria. In such circumstances, practitioners consider whether the chosen criteria are relevant to the needs of the intended users. Practitioners include a reference to the criteria used in the external assurance report in order to communicate the basis of the assurance conclusion and they may also attempt to have the intended users or the engagement party acknowledge that the specified criteria are suitable for the intended users' purposes. Where there are concerns that the subject matter may be fundamentally subjective, practitioners need to consider whether they can accept the engagement. It should be noted that practitioners' own judgements or personal experiences do not qualify as suitable criteria. However, there may be other services that practitioners can offer that might be helpful for the company and the intended users, for example, an advisory service.

Moreover, while in financial reporting the management assessment of internal controls and its external examination has become part of standard audit practice, the procedures over the preparation of non-financial information are comparatively less formalised. Internal controls related to non-financial business activities and operations are not always well monitored or documented and may not be as robust as those related to financial reporting.

Assessment of materiality

Another practical consideration for practitioners is that of materiality. Materiality helps practitioners determine the nature, timing, and extent of work procedures needed to arrive at a conclusion. However, identifying material issues can be challenging when performing an

assurance engagement on non-financial information. Materiality needs to be assessed based on the factors that might influence the decisions of users of the information.

When users have been defined and consulted by the responsible party (the preparer of information), practitioners are more likely to understand and assess the factors that might influence their decisions. If no consultation has taken place or there are too many users, then practitioners will need to use their professional judgement to determine what will affect the users' decision making and whether they have enough information to be able to reach a conclusion¹²³.

Identifying and understanding the intended users

ISAE 3000 emphasises the importance of understanding who the intended users are and their needs. However, defining and managing users might be difficult.

Given its nature, the non-financial statement has a plurality of stakeholders and that may result for example, from different types of performance indicators addressed to the various stakeholders. However, it is clear that the assurance report will be addressed to the corporate body that requested it and to which the auditor is professionally responsible.

Professional standards

There is a lack of consistent standards or guidance being used for external assurance on non-financial information. In this regard, ISAE 3000 is a standard that can be applied to all assurance engagements, but it presumes that the issuer of the external assurance report has to be a practitioner, a professional accountant in public practice and not a non-accounting provider. Moreover, ISAE 3000 leaves a lot of scope for professional judgement in determining the nature, timing and extent of the procedures to be conducted. This results in variations between assurance engagements. Also, the depth and nature of limited assurance procedures is a challenge that requires continuous discussion within the engagement team and beyond. Equally, clients and report users often have difficulty in understanding the difference between limited and reasonable assurance. In addition, there are some subject matter specific assurance standards available. It is sometimes unclear which ISAE 3000 requirements apply on top of a subject matter specific standard requirements.

There are also different legal and regulatory considerations to take into account, as for example those of the Legislative Decree 254/2016. Moreover, given the growing need to support the credibility and trust of emerging forms of external reporting such as <IR> Framework, new ad hoc assurance standard or an integration of the existing standards are

¹²³ ICAEW Audit and Assurance Faculty, Assurance of non-financial information: Existing practice and issues, 2008. Pag. 19.

expected. In this regard, a focus on the need of assurance standards for <IR> framework is provided below.

3.4 ASSURANCE ON AN INTEGRATED REPORT

Integrated reporting, as already explained in the previous chapter, is a new reporting framework based on the integration of financial and non-financial information into a single report. The assurance is not currently requested by the IR framework, but it is emphasized that the reliability of the information contained in the integrated report could be improved in the presence of effective systems of control and internal reporting, involvement of the stakeholders and in the presence of an independent third-party verification¹²⁴. It has also been observed that, in the absence of a suitable system to strengthen the credibility of these reports, there is the risk that they are perceived as nothing more than marketing or greenwash documents.

Nowadays, a standard or guidance specific to integrated assurance has not yet been approved. The need to support the credibility and trust of emerging forms of external reporting led the IAASB Integrated Reporting Working Group to publish a discussion paper entitled: *Supporting Credibility and Trust in Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements*, in August 2016.

The document states that ISAE 3000 Revised is the basic standard for assurance engagements of new forms of reporting. It should also be noted that, since the integrated reporting is only at an initial phase of development, it is considered too early to develop a standard that can support the assurance of these documents¹²⁵. Also the International Integrated Reporting Council (IIRC) became aware of the topic and in July 2015 published a summary of the feedback received from the public consultation that took place a year earlier¹²⁶. From the various feedback received, the importance of assurance emerges with the aim of improving the credibility of the IR and supporting the trust of the stakeholders in relation to the report. Moreover, additional difficulties are recognized in the assurance of an IR, due to the fact that it is a principles-based framework, and that there is a wide and different subject matter. The subject matter of an <IR> report has in fact an orientation towards the future and it is based on interconnections between different types of *capitals*, financial and non-financial. From the consultation with the stakeholders, different positions emerged regarding the standards to be used and the object of the assurance. Some stakeholders pointed out that to develop the

¹²⁴ IIRC, The International Framework. Pag. 21

¹²⁵ IAASB, Integrated Reporting Working Group, *Supporting Credibility and Trust in Emerging Forms of External Reporting: Ten Key Challenges for Assurance Engagements*, 2015. Pag. 8.

¹²⁶ IIRC, *Assurance on <IR>. Overview of feedback and call to action*, July 2015.

assurance of IR it was necessary to introduce innovations, while others did not exclude that the already existing frameworks and standards could be used also for IR¹²⁷. The stakeholders consultation highlighted therefore differences in views on the subject of the assurance, which could be the whole <IR> process or only some of its elements, the whole <IR> report or only some specific information. While some users of the integrated report might have been more interested in obtaining assurance on certain pieces of information rather than the integrated report as a whole, some assurance practitioners were concerned that an assurance approach on a specified data would have been contrary to the holistic approach inherent in the framework. For the same reason, separate assurances on components such as financial, sustainability and operational matters undermine the concepts of <IR> and, in particular, the aspects of connectivity of information.

On the other hand, greater uniformity of views is found on the principles that should characterize the assurance process (independence, professional skepticism, rigorous and structured verification procedures, relations with the other control systems present in the company, etc.) as well as in relation to the opportunity for the assurance of IR to form multidisciplinary teams with a combination of different skills and abilities.

In more detail, the first critical aspects for the standardization of the <IR> assurance engagement is the nature of some elements present in the IR framework. Reference is made to some guiding principles of IR, such as the materiality, the connectivity of information and the future orientation of the given information. Another element of criticality in terms of assurance is the presence in the report of numerous qualitative data expressed in narrative form and, in general, a combination of qualitative and quantitative data. In this regard, the IAASB currently provides frameworks and standards for the audit of financial information and for the assurance of non-financial information, while indications on the assurance of forward-looking information or those provided in a narrative way are less widespread.

Moreover, the actual disclosures within integrated reports will likely vary significantly from one organization to another, as each organization will report only the information relevant to itself within the guiding principles and content elements of the framework. Such level of flexibility requires an increased level of judgement by both the preparer in assessing what is to be included in the integrated report, and by the assurance practitioner in assessing the integrated report's completeness.

For these reasons, the need for reflections and research to be developed on these issues is therefore widely supported. Although the financial statement audit model can be an important part of the integrated reporting framework, it is necessary to integrate this consolidated

¹²⁷ IIRC, Assurance on <IR>. *Overview of feedback and call to action*. Pag. 14.

verification approach with new forms of assurance, which can be described as a combined assurance framework. This new assurance model has to focus on the validity, accuracy and completeness of financial and non-financial disclosed information and on the interpretation of financial and non-financial indicators that explain how an organization is generating sustainable returns in the short and especially in the long term.

CH. 4

ANALYSIS OF ITALIAN LISTED COMPANIES' NFI REPORTS

This chapter analyses the changing landscape of corporate reporting and assurance regarding 2018 NFI disclosure of Italian listed companies.

Although for some decades environmental and social issues have influenced companies' strategic management, as well as production choices and innovation processes, the transition from voluntary reporting to a mandatory one appears to be one of the most significant changes in the field of non-financial disclosure.

With the Directive 2014/95/EU, the European Commission aims to promote the transparency of corporate information and the creation of long-term value.

In order to achieve these objectives the role of the Regulatory and Supervisory Authority of the financial market (CONSOB) is also important. In the Italian context, in 2018 the verification of the fulfilment of the transparency obligations deriving from Legislative Decree n. 254/2016 which implemented the Directive in the Italian regulatory context has been requested.

Even if regulators and standard setters are doing their part, companies remain the real protagonists in this corporate reporting journey. They need to realise that nowadays providing only financial information is not enough because stakeholders need to see the full picture of their activities.

Companies need to consider transparency as a must and no more as an option. These recent developments are the reasons why further analysis on the disclosure of non financial issues are needed.

The purpose of the analysis in the following is to provide a general picture of the trends that are emerging in the first year implementation of the mandatory reporting requirements on NFI. Both the trends followed by companies to comply with the requirements and those followed by auditors in the assurance engagement of NFI report are analysed in more detail.

The results of the analysis outline a complex and heterogeneous scenario, whose interpretation makes it possible to identify the main elements of the development process undertaken by Italian companies.

An analysis of a specific case study is also presented in order to identify some general best reporting practices and to understand how a company can concretely fulfil both the requirement of reporting and the legislative standards.

4.1 METHODOLOGY

Sample selection

The research is focused on the analysis of the NFI reports published by the listed companies in the Italian Stock Exchange *Borsa Italiana*.

Starting points of this research are the provisions of the Italian legislative Decree n. 254/2016 that implemented the EU Directive 2014/95/EU. The Decree entered into force on January 1, 2017, and it is mandatory for public interest entities (PIEs) that fall within the dimensional parameters set by art. 2 of the Decree. The companies obliged by the Decree are those with more than 500 employees on average during the financial year 2017 who have also passed one of the two following parameters in their consolidated financial statements: €20 million of total assets from the balance sheet, or €40 million from revenues net sales. According to the Integrated Governance Conference of the CONSOB, listed companies issuing shares in regulated Italian markets, the companies issuing securities other than shares and that have Italy as a member state of origin and other widespread issuers qualifying as PIEs are considered obliged subjects. For the purpose of this analysis, the sample consists only of the Italian listed company in Borsa Italiana categorized under the FTSE MIB, FITSE MID CAP and FTSE SMALL CAP index at the date of November 15, 2018.

For a general overview, in its conference the CONSOB states that as of June, 2018 there were only a few NFI reports issued by PIEs that quote securities other than shares and which have Italy as a member state of origin (6 NFI reports). The same document identifies 48 other diffused issuers qualifying as PIEs. According to the last list of NFI reports published by CONSOB on August 31, 2018¹²⁸ all 48 diffused issuers have published a NFI report pursuant to the Decree. Given the total of 226 Italian listed companies in Borsa Italiana as of November 15, 2018¹²⁹, it is considered appropriate to exclude from the sample of this analysis the following companies:

- Olidata S.p.A. and Gruppo Waste Italia since they both are in composition with creditors in order to avoid bankruptcy (concordato preventivo);
- Trevi S.p.A. because in debt restructuring;
- Cnh Industrial N.V., Exor N.V., Ferrari N.V., FCAGroup, STMicroelectronics N.V., Tenaris S.A., IVS Group, and D'Amico International Shipping S.A. since they are

¹²⁸ CONSOB, *Elenco dei soggetti che hanno pubblicato al DNF alla data del 31 Agosto 2018*, 31/08/2018.

¹²⁹ Source of the sample: www.borsaitaliana.it

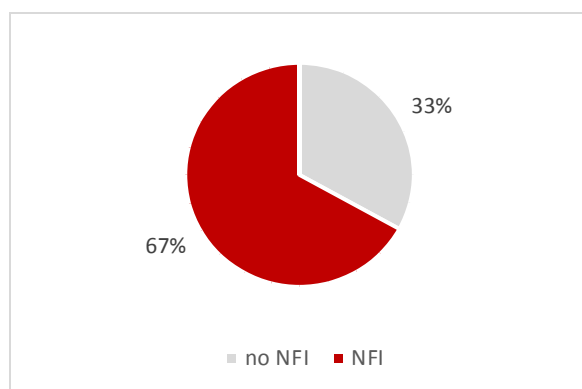
foreign companies not subject to Italian legislation on the disclosure of non-financial information¹³⁰.

Subtracting these companies, the total number of companies that composed the sample of this analysis is equal to 215 listed companies in Italian regulated market. Out of these 215 companies, 144 published a NFI report in 2018 pursuant to the Decree¹³¹ (67%).

Data collection

All the documents consulted for this analysis were downloaded from authorized document storage platforms, in particular *emarket storage* and *IINFO*, or downloaded from company websites¹³². The specific NFI report's sections taken into consideration for the analysis are the paragraph *Methodological Note* and the assurance report of each NFI report. When no NFI report was available, the Financial Statements were analysed.

Graph. 1: Companies that published a DNF pursuant the Decree during the year 2018.



Sources: personal elaboration with the data collected.

Before analysing the trends followed by the companies that have drawn up the NFI report, it is appropriate to focus on the 71 companies (33%) that did not published a NFI report pursuant to the Decree. Out of these 71 companies:

- 8 companies availed of the exemption provided for by art. 6 of the Decree (a company is not subject to the obligation to draw up the NFI report, in a separate or consolidated form, if it is included in the consolidated NFI report of another parent company subject to the same obligations);
- 58 companies have not published a NFI report, not even on a voluntary basis, because they don't exceed the dimensional requirements imposed by the Decree. Out of these

¹³⁰ See Appendix 1.

¹³¹ See Appendix 2.

¹³² Last consultation date of all the websites: November 15, 2018.

companies, 16 companies expressly indicated in a specific section of the Financial Statements the exemption from the legal obligation and 42 companies did not specify anything about in the Financial Statements. For these last companies specific checks were carried out on the dimensional data obtained from the Financial Statements (average number of employees of the group, revenues or total assets of the balance sheet). All the 42 companies were not exceeding the dimensional limits of the Decree.

- 2 companies have explicitly indicated in the Financial Statements that, although they were obliged subjects, they were not able to provide non-financial data for the year 2017 and that they will align with the requests of the Decree starting from the year 2018 (Aeroporto Marconi di Bologna S.p.A., Carel Industries S.p.A.). No further explanations were provided by these companies;
- 1 company expressly stated in the Financial Statements that, although it was an obliged subject, it will prepare the NFI report starting from 2018 as the present 2016/2017 financial year started before the application date indicated in the legislation of January 1, 2017 (Mittel SpA - it changes the closing date of the financial year from September, 30 to December, 31 of each year, so the financial year at 31/12/17 lasted 15 months, from October 1, 2016 to December 31, 2017);
- 2 companies, although they were obliged subjects, have published a Sustainability Report without any reference to the Decree and without any explanation in the Financial Statements (Juventus F. C. S.p.A., Coima Res S.p.A.);

In regards to the 144 companies that have published a NFI report in 2018, they are divided by sector as follows:

Table 1: Companies published a NFI report in 2018 divided by sector.

| Sectors | Percentage % | Number of Companies |
|--------------------|--------------|---------------------|
| Oil & Gas | 3% | 5 |
| Basic Materials | 2% | 3 |
| Industrials | 29% | 42 |
| Consumer Goods | 22% | 32 |
| Health Care | 2% | 3 |
| Consumer Services | 11% | 16 |
| Telecommunications | 1% | 1 |
| Utilities | 7% | 10 |
| Financials | 17% | 24 |
| Technology | 6% | 8 |
| Total | 100% | 144 |

Source: company list by sector in Borsa Italiana.

As shown in the table above, the major part of the sample is constituted by companies belonging to the non-financial sectors while only 17% are companies operating in financial sectors. More in detail, the predominant non-financial sectors are *Industrials* and *Consumer Goods*. Moreover, compared to the total sample of companies that have published a NFI report, 31 companies are from the FTSE MIB index (22%).

Regarding the reporting experience of the companies analysed, a research conducted in July 2018 by Università Cattolica del Sacro Cuore in Milan showed that for 62% of the companies analysed¹³³ the *2017 NFI Report* was the first experience in reporting on sustainability issues. Focusing on the FTSE MIB segment, in its 2018 Integrated Governance Conference the CONSOB reports that out of the 31 companies currently in the index that published a NFI report, in 2016 24 companies had published a NFI disclosure in the form of sustainability reports (16 cases) or in the form of integrated reports (8 cases, of which 4 accompanied by an ad hoc sustainability report) and the remain 7 companies had not submitted NFI report for the year 2016 not even on a voluntary basis.

With the entrance into force of the Decree, for the financial year 2017 all the companies in the FTSE MIB index fall into the obligation to draw up a NFI report, with the exception of two companies (Fincobank and Unipolsai Assicurazioni) for which the obligations are met by the listed parent company.

4.2 IDENTIFIED TRENDS

Type of document adopted

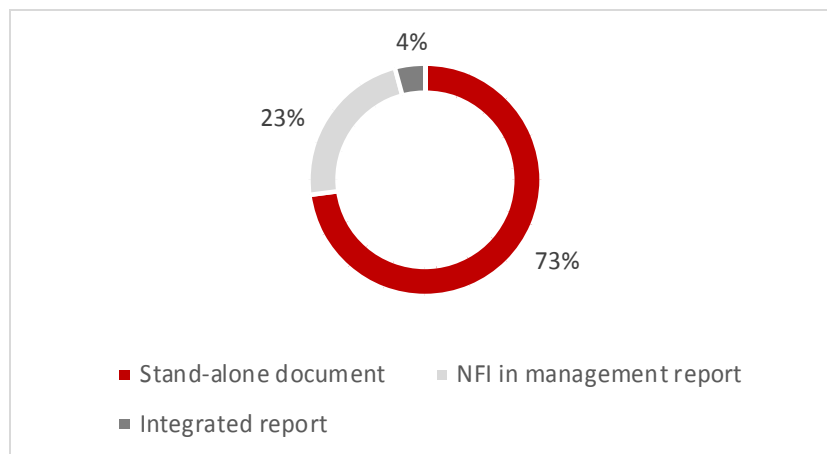
Pursuant to Article 5 of the Decree, the NFI report may be included in a specific section of the management report or may constitute a separate report. In both the cases, the information related section has to be clearly identifiable and titled with the words “*Non-financial information report pursuant the legislative Decree 254/2016*”. Whatever the choice of where placing the non-financial information, the main objective of the company must remain the usability of the information reported.

The 144 NFI reports analysed are divided according to the type of document adopted as follows: 105 companies have published a stand-alone document, 33 companies have entered the NFI in a specific section of the management report and 6 companies have prepared an Integrated Report.

¹³³ ALTIS – Università Cattolica del Sacro Cuore di Milano, DNF: le prime risposte all'obbligo di rendicontazione, July, 2018. The sample of NFI reports analysed is composed by 138 NFI report published by Italian listed companies as of July, 2018.

In particular, the companies that have drawn up an integrated financial statements according to the IR framework are: A2A, Assicurazioni Generali, Atlantia, Pirelli & C., Unicredit, Unipol Gruppo Finanziario.

Graph. 2: NFI report divided by type of document adopted.



Source: personal elaboration of the data.

Focusing on the FTSE MIB segment, we can see that the percentage distribution of the collocation of the DNF reflects that of the whole sample analysed, specifically the 61% of FTSE Mib companies published a stand-alone report, 20% entered the NFI within the management report, and 19% drew an integrated report.

Moreover, the average number of pages of a NFI report issued by the companies belonging to the FITSE MIB is 93 pages, with a variance between the average length of the DNF included in the management report (average of 35 pages) and that of the stand-alone documents (average of 127 pages). Therefore, the collocation of the document has influenced the length of the report. It is important to underline that the length of the document does not necessarily indicate the completeness or the good quality of the information reported.

Reporting Standards adopted by companies

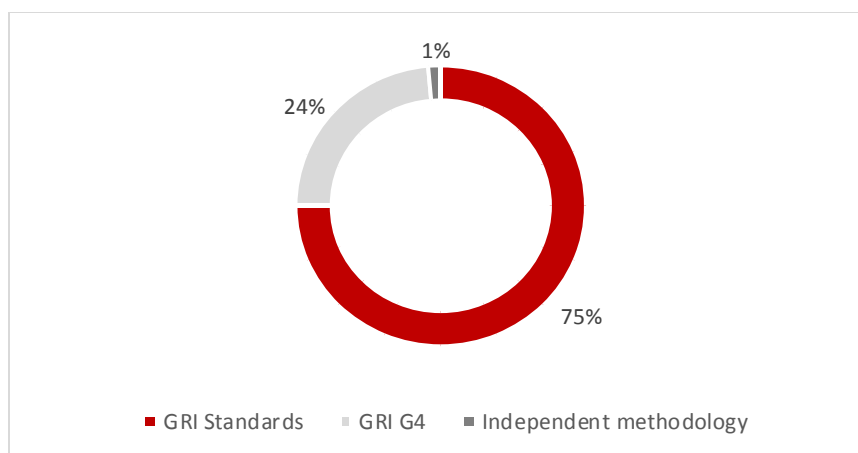
According to the provisions of art. 3.3 of the Decree, the information that constitutes the DNF must be provided *"according to the methodologies and principles provided by the reporting standard used as a reference or by the autonomous reporting methodology used for drafting the report"*.

Almost all the companies analysed referred to the reporting guidelines of the Global Reporting Initiative (GRI), choosing mainly the 2016 GRI Standards (they will definitively replace G4 guidelines for 2018 reporting year), while 2 companies decided to adopt an

independent reporting methodology. The CONSOB has specified that, although expressly expected by the Decree, with *"adoption of autonomous methodologies"* it should be understood exclusively the possibility to combine one or more of *"standards emanating from authoritative supranational, international or national organizations"*. In these two specific cases, both companies have explicitly indicated in the methodological note to adopt an autonomous reporting methodology taking reference to the GRI guidelines.

In combination with the GRI Guidelines, also the European Guidelines on non-financial reporting 2017/C215/01 was explicitly mentioned in the methodological note of 15 companies as a model for reporting non-financial information.

Graph. 3: Reporting Standards adopted by companies in NFI report.



Source: personal elaboration of the data.

The adoption by all companies of the GRI Framework as reporting standard can represent a first step towards the comparability of the information and performances reported, and towards the definition of a common language to integrate the sustainability issues in the company strategies.

According to Università Cattolica survey, the most reported GRI indicators for the economic sector concerned the established acts of corruption and the actions taken, for the environmental sphere energy consumption within the organization and the emissions of greenhouse gases. In the social sphere the indicators were the total number of hirings and turnover rates for age groups, gender and employee categories and the composition of the governing bodies and the division of employees by category with respect to gender, groups and membership to minority groups. Instead the indicators that most frequently have not been fully reported by the companies that therefore reported some omissions, concern the

environmental waste, the selection of new suppliers according to environmental and social criteria, the rates of accident/illness/absenteeism and training hours for employees.

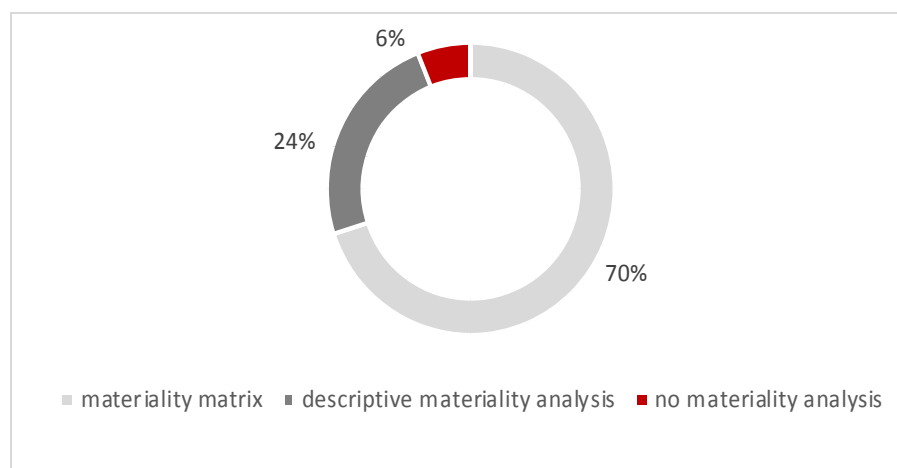
Materiality Analysis

As expressly required by the GRI guidelines, most companies have described their materiality analysis process within the NFI report. The principle of materiality is a key principle in defining the content of non-financial information, and provides that the relevant topics to be included in NFI report are those that can reasonably be considered important to reflect the economic, environmental and social impacts of business activity, or influence stakeholders' decisions.

In relation to the modalities of representation of the material themes, the GRI proposes a representation through a materiality matrix. The use of a materiality matrix is not mandatory, but is an effective graphic solution to represent the prioritization of the issues both with respect to the impact of the company and to the expectations of the stakeholders.

According to the July 2018 survey conducted by Università Cattolica del Sacro Cuore, 70% of the companies analysed carried out a materiality analysis reporting a materiality matrix, 24% described their materiality process without any materiality matrix and only 6% did not mention any materiality analysis.

Graph. 4: materiality analysis process



Source: ALTIS – Università Cattolica del Sacro Cuore di Milano, July, 2018.

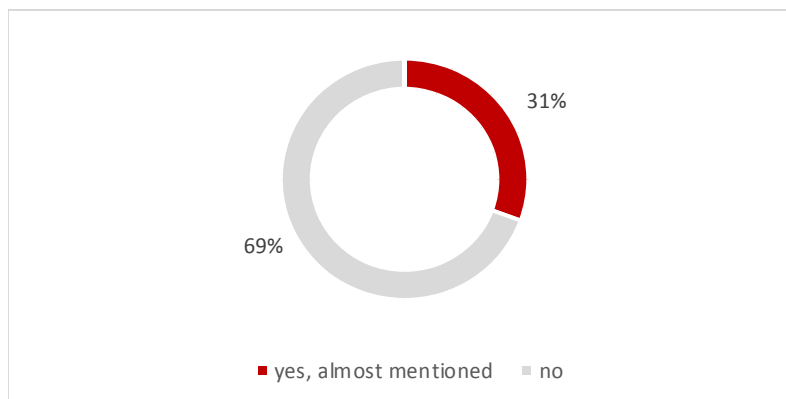
From this data, it seems that the analysis of materiality is a process not yet fully structured or formalized within specific company procedures that clearly define methods of analysis and subjects involved, both internally and externally to the organization.

Adherence to the Sustainable Development Goals (SDGs)

On September 25, 2015, the United Nations approved the 2030 Agenda for Sustainable Development which contains 17 Sustainable Development Goals (SDGs). The 2030 Agenda represents an action plan aimed at guaranteeing an inclusive and sustainable development, capable of favouring the coordination and collaboration among public, private and civil society entities. In this context, the private sector certainly plays a fundamental role. As stated in the 2030 Agenda, companies are called *"to use their creativity and their innovation, in order to find a solution to the challenges of sustainable development"*, also considering that *"the private entrepreneurial activity, the investments and innovation are the main drivers of productivity, inclusive economic growth and job creation"*¹³⁴.

The 17 SDGs can concretely support companies to integrate sustainability practices into their medium and long-term strategies, effectively contributing to the achievement of global objectives. It is therefore suggested that companies refer to the SDGs in order to define and communicate their sustainability objectives and the results achieved through the reduction of the negative impacts and the maximization of positive ones for the benefit of people and for the protection of the planet. In the analysed sample, 44 companies (31%) refer to or at least mention, the SDGs within their NFI report, in the methodological note section or with a dedicated section.

Graph. 5: Companies' disclosures of SDGs in their NFI report.



Source: personal elaboration of the data.

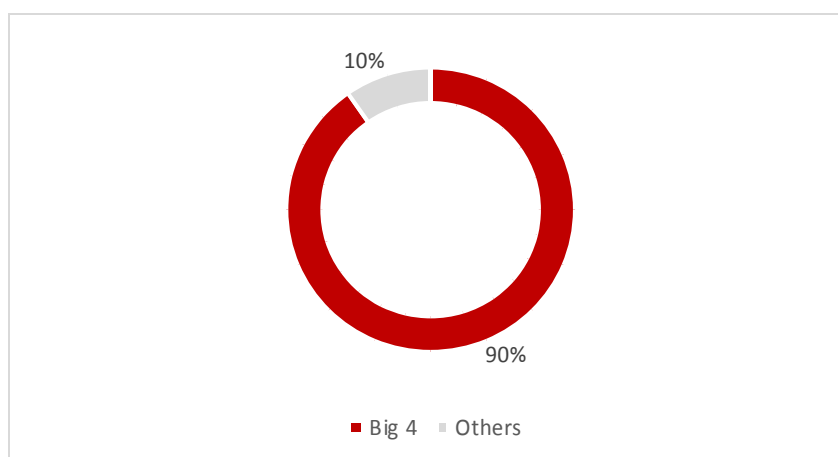
More in detail, in the FITSE MIB segment 20 companies (65%) at least mention the SDGs in their NFI report and 11 companies (35%) do not take SDGs into consideration within the NFI report.

¹³⁴ United Nations, *Transforming our world: The 2030 Agenda for Sustainable Development*, 2015. Pag. 34

Assurance statement on NFI

As expressly required by the Decree, all assurance reports are issued by certified auditing firms. In particular, 130 companies (90%) of the sample engaged a *Big 4* auditing firm.

Graph. 6: Providers engaged for the NFI assurance process.



Source: personal elaboration of the data.

The assurance standards of reference for the assurance process are ISAE 3000 (Revised) and the International Standard on Quality Control 1 (ISQC 1). Within the assurance reports the AA1000APS has been mentioned in only two cases (Enel Group and Be Group) as a principle to support the company reporting process.

Moreover, in 17 assurance reports specific GRI Sector Disclosures were also mentioned. It can be deduced that in the Italian context only ISAE 3000 is used as standard assurance, while both GRI guidelines and AA1000APS are used by companies as reference frameworks for corporate reporting. The detailed list of GRI Sector Disclosures is reported in the table below.

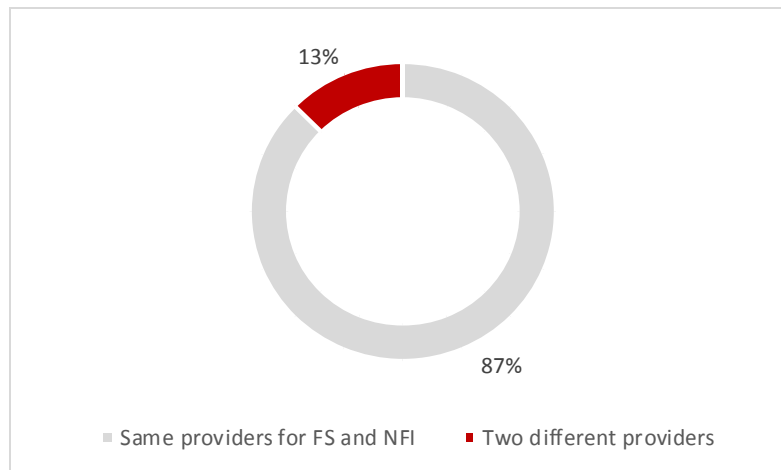
Tab. 2: List of additional Sector Disclosures mentioned in NFI assurance reports.

| Sector Disclosures | Number of Companies |
|----------------------------------|----------------------------|
| Financial Services | 7 |
| Construction & Real Estate | 1 |
| Electric Utilities | 4 |
| Media | 1 |
| Airport Operators | 1 |
| Food Processing | 2 |
| Accident reporting UNI 7249/2007 | 1 |
| Total | 17 |

Source: personal elaboration of the data.

Moreover, it is possible to distinguish between the companies that engage the same auditing firm both for the audit of Financial Statements and for the assurance of NFI reports and those companies that decide to engage two different auditing firms. According to this analysis, only 18 companies (13%) decide to engage two different auditing firms for the Financial Statement and the NFI reports respectively.

Graph. 7: Providers engaged for both the assurance of FS and NFI report or not.



Source: personal elaboration of the data.

Moreover, with the implementation of the Directive 2014/95/EU, Italy has provided for the mandatory verification of conformity of the NFI report, as explained in chapter 3 of this Thesis. In particular, pursuant to art. 3, paragraph 10 of the Decree states:

- the person in charge of carrying out the statutory auditing of the financial statements verifies the preparation and publication of the NFI report by the Board of Directors;
- the same person charged with carrying out the statutory audit of the financial statements, or other subject authorized to carry out the audit, issue a certificate of compliance of the information provided in the NFI report with respect to the requirements of the Decree and to the principles and methodologies required by the same. Moreover, the conclusion requested by the auditor could be provided in the form of limited assurance or in the form of reasonable assurance. The conclusion is expressed in a positive form as a consequence of reasonable assurance engagement, and in a negative form as a consequence of a limited assurance engagement. The type of assurance performed by the auditor depends by the scope and the extent of the audit procedures performed.

Within the two different types of conclusions indicated by ISAE 3000 Revised for the preparation of assurance reports, in the assurance of NFI reports a limited assurance is favoured.

In fact, in all 144 NFI reports analysed the auditor carried out a limited assurance engagement "on the NFI report drawn up pursuant to art. 3, paragraph 10, of Legislative Decree 30 December 2016 no. 254 of the art. 5 of Consob Regulation no. 20267".

In one case the company drew up a NFI report expressly pursuant to the Decree but with an assurance report on the Sustainability Report and not pursuant to the Decree (B. Mediolanum).

The totality of limited assurance engagement is due to the fact that the NFI report, in accordance with the requirements of the Decree, is characterized by the presence of a high number of qualitative information deriving from companies' information systems and internal control often not fully integrated or incomplete, which do not allow the auditor to conduct the engagement with the necessary and adequate level of extension required by a reasonable assurance.

Given the limited assurance level of all the analysed NFI reports, for all the 144 NFI reports analysed the auditor expresses an opinion without any relevant aspect on the information disclosed. In one case (Astaldi S.p.A) the auditor reports an *Emphasis of matter* that highlights significant doubts about the Directors' assumption of business continuity.

Fig. 1: Emphasis of matter paragraph of Astaldi S.p.A. NFI assurance report.

Astaldi S.p.A.
Relazione della società di revisione
31 dicembre 2017

Richiamo di informativa

Richiamiamo l'attenzione a quanto descritto nel paragrafo "Rischi collegati alla struttura finanziaria" incluso nella sezione "Gestione del rischio" della DNF in merito ad eventi e circostanze che indicano l'esistenza di una incertezza significativa che può far sorgere significativi dubbi sulla capacità della Società di continuare ad operare come un'entità in funzionamento e alle ragioni in base alle quali gli amministratori hanno ritenuto appropriato l'utilizzo del presupposto della continuità aziendale nella redazione del bilancio d'esercizio e consolidato per l'esercizio chiuso al 31 dicembre 2017 da cui sono stati estratti i dati e le informazioni alla base degli indicatori finanziari inclusi nella DNF del Gruppo Astaldi.

Source: Astaldi S.p.A. NFI report.

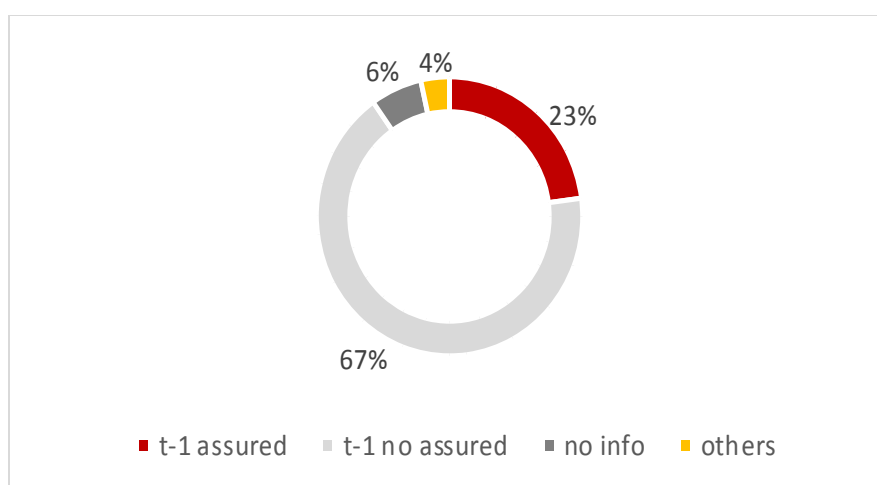
With regard to the paragraph *Other aspects*, in most assurance reports it is highlighted whether the information from previous years compared to the current year data has been

verified according to ISAE 3000 or not; in only 9 cases no information regarding the comparative data is reported in the assurance report.

Moreover, in 3 cases it is specified that the data carried as comparison for the year 2016 have been verified while those related to the year 2015 had not (CIR S.p.A, Cofide S.p.A, Gedi Gruppo Editore).

In one case it is expressly indicated that the data of previous years are shown only in a qualitative and non-satisfactory way (Mediobanca Group) and in one case no data are available for previous years because the group was established in 2017 (Banco Group BPM).

Graph. 8: Assurance of previous years data reported as comparison in NFI reports.



Source: personal elaboration of the data.

4.3 RESULTS

In its first year of the implementation, the solutions used by companies to comply with the Decree results in a heterogeneous picture without an univocal solution under various aspects. The main results of this research can be summarized as follows:

- Many listed companies were excluded from the scope of application of the Decree according to the dimensional requirements, in particular the average number of employees was below the threshold dictated by the Decree. The threshold of 500 employees in fact proved to be high for many listed companies in Borsa Italiana (58 issuers, about 1/4 of the list are sub-threshold). Moreover, the checks on listed issuers that did not draw up the NFI report were laborious especially because few issuers provided an explicit motivation for the lack of a NFI report (for example due to the failure to exceed the dimensional thresholds, the option of exemption from obligation

as subsidiaries of issuers who have drawn up the consolidated NFI report, or the closing dates of the financial year subsequent to 31/12).

- Most of the NFI reports have been drafted in an ad hoc document; the 6 companies that published an integrated report were the same ones that prepared an integrated report last year. According to the latest list of the entities that have published a NFI report provided by CONSOB¹³⁵, only one company (Acque Venete SpA) has published a NFI report pursuant to the Decree on a voluntary basis. Although they are not required to fulfil the obligations, there are also many companies that publish non-financial information on a voluntary basis in other formats, such as sustainability reports or dedicated paragraphs in the management report.
- All the NFI reports have been drawn up on the basis of the GRI (Global Reporting Initiative) guidelines, mainly in accordance with the 2016 GRI Standards. Only 2 companies have adopted an independent reporting methodology for the disclosure of non-financial information. With reference to the GRI guidelines, only a limited percentage of companies (6%) did not report any materiality analysis to identify the issues to be reported¹³⁶;
- A little more than 1/6 of all companies listed on the Italian Stock Exchange refers to or at least mentions the United Nations Sustainable Development Goals; 20 of the companies that refer to the SDGs are part of the FITSE Mib index.
- All the assurance engagements were performed by auditing firms, mostly from the Big 4 auditing firms. In 18 cases, the auditor who verified the NFI report is not the same person in charge of auditing the company's Financial Statements.
- All the assurance reports issued by the auditors are in the form of limited assurance and end up with an *unmodified opinion* by the auditor. Only in 1 case the assurance report includes an *Emphasis of matter* paragraph;
- Most of the comparative data referring to previous years and reported in the NFI report 2017 has not been verified by an auditor. In 9 cases, no information is available in the assurance report issued by the auditing firm with regard to the comparative data.

¹³⁵ CONSOB, as of 31/08/18.

¹³⁶ According to Università Cattolica of Milano survey in July, 2018.

4.4 CASE STUDY: ANALYSIS OF ENI NFI REPORT

In addition to the previous general analysis, it is useful for the purpose of this Thesis to briefly explain a specific non-financial report as a case study. This reported example is not a qualitative analysis on the correctness or trustworthiness of the information published in the report, but it is a road map helpful to explain how a company can concretely implement the non-financial reporting frameworks complying also with the legislative requirements.

The choice of the company to take into analysis is based on the competition conducted annually by FRPI (Federazione Relazioni Pubbliche Italiana) with the collaboration of Borsa Italiana and Università Bocconi, that rewards the most virtuous companies in the reporting activity since 1954. According to the 2018 list¹³⁷, the winner of the “Oscar di Bilancio 2018” for the category *Big listed companies* is Eni Group. In the light of this result, in the following paragraph Eni NFI report is analysed.

Following the trends identified in the general analysis, the first issue to take into consideration is the type of document used by the company to disclose its non-financial information.











ENI has chosen to include the NFI report in the management report within a specific section easily identifiable. More specifically, the NFI report provides an integrated overview on the issues required by the Decree thanks to the information published in this specific section, but also through numerous references to other sections of the management report, or other corporate documents (for example the report on corporate governance and ownership structures), if the information is already contained by in the documents mentioned above or for further information. In continuity with the previous years, Eni has also published a sustainability report on a voluntary basis, with the aim of deepening some issues and illustrating the main sustainability initiatives undertaken during the year. In its NFI report, Eni articulates the disclosure on three integrated business levers: *Path to decarbonisation*, *Operating model* and *Cooperation model*. In the first section, the information on the climate is reported on the basis of the thematic areas subject to the recommendation of the Task Force on Climate-related Financial Disclosures (TCFD). Eni is in fact the only company in the Oil & Gas sector to be part of the Task Force of the Financial Stability Board, which at the end of June 2017, published some recommendations of voluntary nature to promote an effective disclosure of the financial implications linked to climate change. The reporting of this information meets the requirements of *art. 3.2* paragraph *a* and *b* of the Decree. The second integrated business lever of Eni is called Operating Model. In this section the report shows all

¹³⁷ The analysis was carried out on a sample of 120 of companies and entities, divided into 7 categories including those of *Large Listed Companies*. The results were based on the analysis of the documents that make up the company's financial statements, therefore both the financial statements and the non-financial reporting documents prepared in compliance with the law.

the NFI required by *art. 3.2* paragraph *c, d, e* of the Decree relating to the following areas: environment, personnel, respect for human rights and the fight against active and passive corruption. The third and last section of Eni NFI report included in the Cooperation Model, in which it is possible to find the information required by *art. 3.2* paragraph *d* related to the local communities. These three sections include all the information expressly requested by the Decree, concerning both the social/environmental areas considered relevant by the legislator, and the relative impact of the company's activities in relation to the aforementioned areas. Furthermore, according to the legislator, the information relating to the aforementioned areas must also be organized on the basis of company strategies (thus referring to the company model, the policies applied and the results achieved), and to the main risks deriving from company activities. These requirements, expressly mentioned in the *art. 3.1* paragraph *a, b, c*, are transversally reported in Eni's report with an indication of these requirements for each of its three integrated business levers. Given the triple division of the report according to the business levers, in its introduction Eni reports a table that links the information content required by the Decree and its positioning within the various corporate documents. The Decree provides for the possibility that the NFI report, when included in the management report, limits itself to indicating the other sections of the report or other documents and where to find the requested information, thus assuming the role of an orientation map used to find information among multiple documents. This explains the reduced number of pages that make up Eni's NFI report: only 24 pages compared to the average of 93 pages as reported in the general analysis. The legislator's choice to permit the references to other documents for the information required by the Decree is due not only to simplify the reporting for companies, but it is also useful to avoid unnecessary duplication of documentation or unnecessary full-bodied reports.

Tab. 3: Table of content references

| AREAS OF THE ITALIAN LEGISLATIVE DECREE 254/2016 | PARAGRAPHS INCLUDED IN THE NFI | THEMES AND FOCUSES IN THE INTEGRATED ANNUAL REPORT (IAR) AND IN OTHER 2017 DOCUMENTS |
|---------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| COMPANY MANAGEMENT MODEL AND GOVERNANCE <i>Art. 3.1, paragraph a)</i> | <ul style="list-style-type: none"> • Path to Decarbonization, pp. 94-97 • Operating Model, pp. 98-105 • Cooperation Model, p. 106 | <p>IAR</p> <ul style="list-style-type: none"> ● Business Model, pp. 18-19 ● Governance, pp. 28-31 ● Key sustainability issues and stakeholders' perspective, pp. 15-17 <hr/> <p>CGR</p> <ul style="list-style-type: none"> ▶ Responsible and sustainable approach, pp. 9-11 ▶ Corporate Governance Model, pp. 11-15 ● Board of Directors: Composition pp. 36-41 and Board induction, pp. 56-57 ▶ Board Committees, pp. 57-66 ▶ Board of Statutory Auditors, pp. 67-75 ▶ Model 231, pp. 102-103 |
| POLICIES <i>Art. 3.1, paragraph b)</i> | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 | <p>CGR</p> <ul style="list-style-type: none"> ▶ Eni Regulatory System, pp. 90-112 |
| RISK MANAGEMENT MODEL <i>Art. 3.1, paragraph c)</i> | <ul style="list-style-type: none"> - | <p>IAR</p> <ul style="list-style-type: none"> ● Integrated Risk Management pp. 24-25; Targets, risks and treatment measures, pp. 26-27; Political Considerations, pp. 81-82; Risks associated with the exploration and production of oil and natural gas, pp. 78-81; Safety, security, environmental and other operational risks, pp. 77-78; Risks related to legal proceedings and compliance with anti-corruption legislation, pp. 86-87; Risks related to climate change, pp. 85-86. |

| | AREAS OF THE ITALIAN LEGISLATIVE DECREE 254/2016 | PARAGRAPHS INCLUDED IN THE NFI | THEMES AND FOCUSES IN THE INTEGRATED ANNUAL REPORT (IAR) AND IN OTHER 2017 DOCUMENTS |
|------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|  PATH TO DECARBONIZATION |  CLIMATE CHANGE Art. 3.2, paragraph a) Art. 3.2, paragraph b) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Path to decarbonization (governance, risk management and strategy), pp. 94-97 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 ● Integrated Risk Management, pp. 24-27; Safety, security, environmental and other operational risks, pp. 77-78; Risks related to climate change, pp. 85-86 ▶ Scenario and strategy, pp. 20-23 <hr/> CGR <ul style="list-style-type: none"> ▶ Responsible and sustainable approach, pp. 9-11 |
|  OPERATING MODEL |  PEOPLE Art. 3.2, paragraph d) Art. 3.2, paragraph c) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • People (employment, diversity, development, training, health), pp. 98-100 • Safety, p. 100 | IAR <ul style="list-style-type: none"> ● Key sustainability issues and stakeholders' perspective, pp. 15-17 ● Business model, pp. 18-19 ● Integrated Risk Management pp. 24-27; Risk factors and uncertainties: Risks associated with the exploration and production of oil and natural gas, pp. 78-81; Safety, security, environmental and other operational risks, pp. 77-78; ● Governance, pp. 28-31 (Remuneration Policy, p. 31) |
| |  RESPECT FOR THE ENVIRONMENT Art. 3.2, paragraph a, b, c) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Respect for the environment (circular economy, water, oil spills, biodiversity), pp. 101-102 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 ● Integrated Risk Management, pp. 24-27; Risks associated with the exploration and production of oil and natural gas, pp. 78-81; Safety, security, environmental and other operational risks, pp. 77-78 |
| |  HUMAN RIGHTS Art. 3.2, paragraph e) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Human rights (security, training, whistleblowing), pp. 103-104 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 <hr/> CGR <ul style="list-style-type: none"> ▶ Responsible and sustainable approach, pp. 9-11 |
| |  SUPPLIERS Art. 3.1, paragraph c) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Suppliers, p. 104 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 |
| |  TRANSPARENCY AND ANTI-CORRUPTION Art. 3.2, paragraph f) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Trasparenza and Anti-Corruption, p. 105 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 ● Integrated Risk Management, pp. 24-27; Risk related to legal proceedings and compliance with anti-corruption legislation, pp. 86-87 <hr/> CGR <ul style="list-style-type: none"> ▶ Principles and values. The Code of Ethics, p. 8; Anti-corruption Compliance Programme, pp. 104-106 |
|  COOPERATION MODEL |  LOCAL COMMUNITIES Art. 3.2, paragraph d) | <ul style="list-style-type: none"> • Eni's main regulatory instruments, p. 93 • Cooperation model, p. 106 | IAR <ul style="list-style-type: none"> ● Business model, pp. 18-19 ● Integrated Risk Management, pp. 24-27; Political considerations, pp. 81-82; Risks associated with the exploration and production of oil and natural gas, pp. 78-81 |

IAR Integrated Annual Report.
CGR Corporate Governance Report.

● Sections / paragraphs containing the information required by the Italian Legislative Decree 254/2016.
 ▶ Sections / paragraphs to which reference is made for further details.

Source: Eni 2017 annual financial report, pag. 106 and 107.

Therefore, in terms of content Eni reports on all the areas expressly requested by the Decree. The level of details of information is based on the materiality process previously conducted by Eni. This aims to extrapolate the information that must be provided in the NFI report in

order to ensure the understanding of the business activity, its performance, its results and its impact, according to a criterion of importance in consideration of the activities and characteristics of the company. The materiality process of Eni is explained later in this paragraph.

The second trend analysed concerns the reporting standards taken into reference by the company in reporting its NFI. In the case of Eni, the report has been drawn up according to the GRI Standards, recognized by the Decree as guidelines issued by an authoritative international body able to fulfil the non-financial reporting obligations¹³⁸. The first aspect to consider in the light of the chosen reference standards, is the principle of materiality of information.

In the context of the GRI principles, it is stated that *"the relevant themes and indicators are those that can reasonably be considered important in reflecting the economic, environmental and social impacts of the organization, or that influence the decisions of the stakeholders and therefore deserve to be included in the report. Materiality corresponds to the threshold beyond which a topic or indicator becomes sufficiently important to be included in the report."*¹³⁹

In the specific case of Eni, the materiality process is explained in a specific initial section of the annual financial report, and, therefore, it is not included into the non-financial report.

For Eni the determination of the materiality sustainability issues takes place on annual basis through a process of identification and prioritization, which is divided into 3 main phases:

1- Analysis of the sustainability scenario: Analysis of the context in which Eni operates, highlighting the emerging sustainability issues, the relevant issues and progress with respect to the objectives set. This scenario analysis is presented and detailed to the Sustainability and Scenarios Committee and approved by Eni Board of Directors.

2- Results of the Risk Assessment: Identifying the main risks for Eni, including those with potential environmental impacts, on health and safety, social and reputational, fields.

3- Stakeholder perspective: process that identifies the priority themes for the various company stakeholders, defined according to the GRI Standards and Accountability AA1000 principles.

In this regard, the materiality analysis in perspective of the company's stakeholders is provided in the following table:

¹³⁸ Art. 1, lett. f) del dl. n. 254/2016

¹³⁹ Sustainability Reporting Guidelines G4.

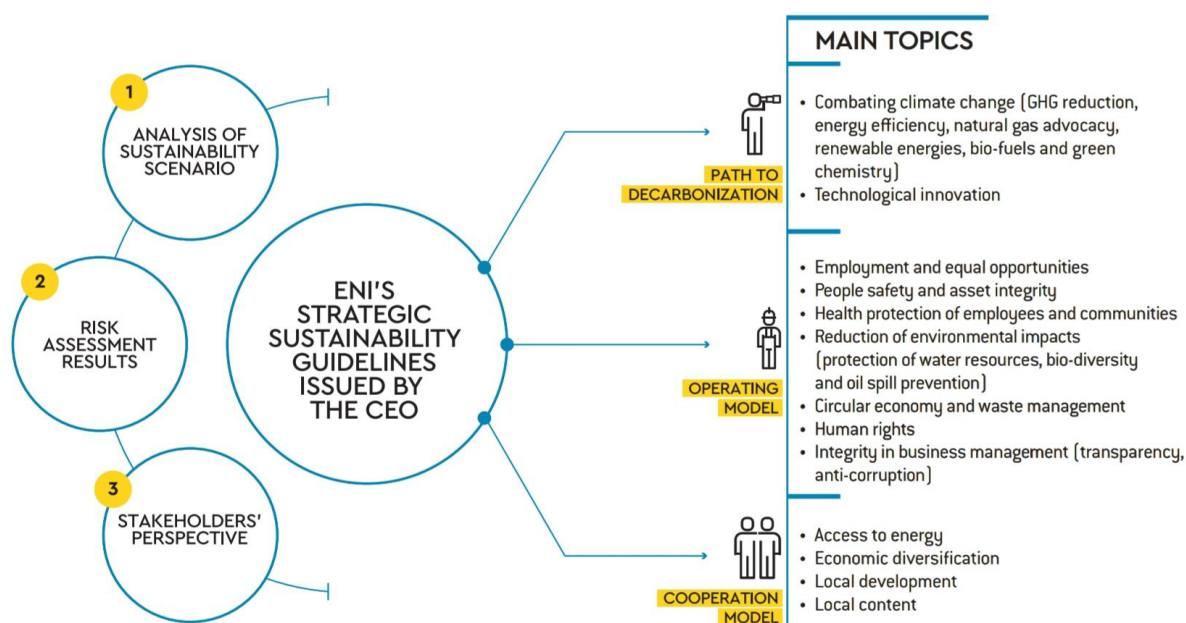
Tab. 4: Eni Materiality analysis in a stakeholders' perspective.

| Key issues | PEOPLE AND NATIONAL AND INTERNATIONAL TRADE UNIONS | LOCAL COMMUNITIES & COMMUNITY BASED ORGANIZATIONS | CONTRACTORS, SUPPLIERS AND COMMERCIAL PARTNERS | FINANCIAL COMMUNITY | CUSTOMERS AND CONSUMERS | DOMESTIC, EUROPEAN AND INTERNATIONAL INSTITUTIONS | UNIVERSITIES AND RESEARCH CENTRES | VOLUNTARY PARTICIPATION IN ORGANIZATIONS AND CATEGORY ASSOCIATIONS | ORGANIZATIONS OF INTERNATIONAL AND NATIONAL ADVOCACY |
|----------------------------------------------------|----------------------------------------------------|---------------------------------------------------|------------------------------------------------|---------------------|-------------------------|---------------------------------------------------|-----------------------------------|--------------------------------------------------------------------|------------------------------------------------------|
| Health and safety in the workplace | ● | | ● | ● | ● | ● | | ● | ● |
| Climate change and energy efficiency | ● | | ● | ● | ● | ● | ● | ● | ● |
| Management of environmental impacts | | ● | ● | ● | ● | ● | ● | ● | ● |
| Protection of human rights | | ● | ● | ● | | ● | | ● | ● |
| Integrity and transparency | ● | | ● | ● | ● | ● | | ● | ● |
| Fairness and transparency of commercial policies | | | ● | | ● | | | | |
| Challenges for development | | | | | | ● | ● | ● | |
| Relations with the community and local development | | ● | ● | ● | ● | ● | | ● | ● |
| Economic and financial value creation | | | ● | ● | ● | ● | | | |
| Sustainable management of the supply chain | | | ● | ● | ● | | | ● | ● |
| Asset integrity and emergency management | | | ● | ● | | ● | | | ● |
| Corporate governance | | | | ● | ● | ● | | ● | |
| Risks and vulnerabilities in the energy sector | | | | ● | ● | ● | | | |
| Organizational environment and welfare | ● | | | ● | | ● | | ● | |
| Response capacity to the consumers needs | | | | | ● | | | | |

Source: Eni 2017 Annual financial report, pag. 16,17.

The issues emerging from the three phases of the materiality process are the basis for defining Eni's strategic guidelines for sustainability. These guidelines are issued by the CEO for all the business lines, and are the basis to define the four-year strategic plan and managerial objectives are defined. They identify the relevant sustainability issues, which determine the company's ability to create value in the short, medium and long term. These themes are presented below according to the three levers of Eni's business model:

Fig. 2: Scheme of Eni's materiality assessment process.



Source: Eni 2017 annual financial report, pag. 15.

The next step to complete the reporting process of NFI is to link the material themes identified by Eni with the related performance indicators developed by the chosen reporting framework, i.e. the GRI Standards. These Key Performance Indicators, selected according to items identified as the most relevant, are collected on annual basis and relate to the 2015-2017 period. They concern Eni SpA and its consolidated subsidiaries. The detection of the information and data is structured to ensure comparability of data across several years. This data refers only to consolidated companies based on the line-by-line method. The indicators shown are those foreseen by the *Core Standard approach* of the GRI Standards. There are in fact two possible “in accordance” criteria options both focused on material aspects:

- Core: for each identified material aspect the organization should disclose the General Standard Disclosures and at least one topic-specific indicator.

- Comprehensive: for each identified material aspect, the organization should disclose the General Standard Disclosures and all indicators related to the material aspect.

The minimum information required to disclose are those needed to understand the nature of the organization, its material topic and related impacts, and how these are managed. For this reason, the company has to meet the minimum criteria both for Core or Comprehensive approaches in order to claim that the report has been prepared in accordance with the GRI Standards.

Tab. 5: GRI Required Criteria for Core and Comprehensive Approach.

| Required criteria | Core option | Comprehensive option |
|--------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Use the correct claim (statement of use) in any published materials with disclosures based on the GRI Standards | Include the following statement: 'This report has been prepared in accordance with the GRI Standards: Core option' | Include the following statement: 'This report has been prepared in accordance with the GRI Standards: Comprehensive option' |
| Use GRI 101: Foundation to follow the basic process for preparing a sustainability report | Comply with all requirements in Section 2 of GRI 101: Foundation ("Using the GRI Standards for sustainability reporting") | [Same as for Core] |
| Use GRI 102: General Disclosures to report contextual information about the organization | Comply with all reporting requirements for the following disclosures from GRI 102: General Disclosures: <ul style="list-style-type: none"> • Disclosures 102-1 to 102-13 (Organizational profile) • Disclosure 102-14 (Strategy) • Disclosure 102-16 (Ethics and integrity) • Disclosure 102-18 (Governance) • Disclosures 102-40 to 102-44 (Stakeholder engagement) • Disclosures 102-45 to 102-56 (Reporting practice) | Comply with all reporting requirements for all disclosures from GRI 102: General Disclosures Reasons for omission are only permitted for the following disclosures: Disclosure 102-17 (Ethics and integrity), and Disclosures 102-19 to 102-39 (Governance). See clause 3.2 for more information |
| Use GRI 103: Management Approach to report the management approach and the topic Boundary for all material topics ⁵ | For each material topic, comply with all reporting requirements from GRI 103: Management Approach Reasons for omission are only permitted for Disclosures 103-2 and 103-3 (see clause 3.2) | [Same as for Core] |
| Use the topic-specific GRI Standards (series 200, 300, 400) to report on material topics | For each material topic covered by a topic-specific GRI Standard: <ul style="list-style-type: none"> • comply with all reporting requirements in the 'Management approach disclosures' section • comply with all reporting requirements for at least one topic-specific disclosure For each material topic not covered by a GRI Standard, it is recommended to report other appropriate disclosures for that topic (see clause 2.5.3) Reasons for omission are permitted for all topic-specific disclosures (see clause 3.2) | For each material topic covered by a topic-specific GRI Standard: <ul style="list-style-type: none"> • comply with all reporting requirements in the 'Management approach disclosures' section • comply with all reporting requirements for all topic-specific disclosures For each material topic not covered by a GRI Standard, it is recommended to report other appropriate disclosures for that topic (see clause 2.5.3) Reasons for omission are permitted for all topic-specific disclosures (see clause 3.2) |

Source: GRI Standards 101 Foundation, pag. 23

As required by the GRI Standards, at the end of its NFI report Eni reports a *GRI Content Index* which lists all the GRI indicators related to the information reported. In detail, the first section of the indicators concerns the General Standards (GRI 101-102-103), while the second part concerns specific standard disclosures, i.e. the indicators of information on topics considered relevant for the company. For the latter, it is necessary to make a correlation between the themes identified as relevant by the company and the corresponding indicators. At the end of the report in fact, Eni clarifies this correlation with a specific summary table:

Tab. 6: Correlation table between the key sustainability issues and GRI Standards

| | KEY SUSTAINABILITY ISSUES | GRI STANDARDS | INSIDE | OUTSIDE AND LIMITATIONS |
|----------------------------------|---------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|------------------------------------------------------------------|
| PATH TO DECARBONIZATION | Climate change | GRI 201 Economic Performance GRI 305 Emissions | ✓ | Suppliers and customers (RNES ¹ ; RNEC ²) |
| | | GRI 302 Energy | ✓ | |
| | Innovation | - | ✓ | |
| OPERATING MODEL | Employment and diversity | GRI 401 Employment GRI 404 Training and Education GRI 405 Diversity of governance bodies and employees GRI 202 Market presence | ✓ | |
| | Occupational health and local communities health | GRI 403 Occupational H&S | ✓ | |
| | Safety and asset integrity | GRI 403 Occupational H&S | ✓ | Suppliers |
| | Circular economy and waste | GRI 306 Effluents and Waste | ✓ | |
| | | GRI 303 Water | ✓ | |
| | Environment | GRI 306 Effluents and Waste | ✓ | |
| | | GRI 304 Biodiversity | ✓ | |
| | | GRI 307: Environmental compliance | ✓ | |
| | Human Rights | GRI 412 Human Rights Assessment GRI 410 Security Practices GRI 406 Non-Discrimination GRI 414 Supplier Social Assessment | ✓ | Local security forces; Suppliers (RNES ¹) |
| Integrity in business management | GRI 205 Anti-corruption | ✓ | Suppliers (RPES ³) | |
| COOPERATION MODEL | Access to energy, economic diversification, Local development | GRI 203 Indirect Economic Impacts GRI 413 Local Communities | ✓ | |
| | Local content | GRI 204 Procurement Practices | ✓ | Suppliers (RNES ¹) |

Source: Eni 2017 annual financial report, pag. 123

All relevant topics have been linked to at least one performance indicator as required by the Core approach. It is possible to find an omission for the topic *Technological Innovation*, to which only an explanation of the management approach corresponds (general indicators 103-1, 103-2, 103-3), but not a specific performance indicator. Moreover, for 3 of the indicators identified as relevant, Eni expressly underlines an omission. In particular it is reported that even if their materiality is recognized, the information required by those indicators are not

currently available, and Eni undertakes to cover the indicator in the coming years. The list of Eni GRI indicators is reported in the Appendix III of this chapter.

The third trend identified concerns the reference to the SDGs listed by the United Nations within the 2030 Agenda. In the specific case of Eni, within the non-financial report and in general within the annual financial report, there is no reference to the SDGs. However, the analysis of the SDGs and the related connection with the material themes are widely explained in the sustainability report, which is divided into the three main sections corresponding to the integrated business lines of Eni.

Fig. 3: Eni SDGs according to the integrated business lines.



Source: *Eni For 2017*, Sustainability report, pag. 13.

The fourth and last trend to be analysed concerns the assurance of the NFI report. Although according to the GRI Standards the assurance of NFI report is only recommended and not compulsorily, the Italian legislator specifically requires that a statutory auditor must perform a consistency check of whether the document has been prepared. Also he needs to perform an assurance engagement at least at a limited level according to the international standard ISAE 3000 (Revised). The sustainability report, being a voluntary document and not included among those required by law, it is not subject to external assurance obligations. In the specific case of Eni, the non-financial report and the sustainability report were both subjected to a limited assurance by an auditing firm. The company responsible for revising the non-financial

documents was the same one that carried out the audit of the financial statements. Regarding the assurance of the NFI report of Eni, the auditor issued a conclusion without remarks and underlined in the specific paragraph *Other Aspects* the data related to previous years and used as a comparison to the reporting year. This data was voluntarily submitted to a limited examination in accordance with ISAE 3000 with conclusions without remarks.

Summarizing, it is possible to state that Eni has correctly reported the information required according to the chosen reporting standard, giving an explanation for any omission diligently underlined in the report (comply or explain principle). Eni has correctly complied to the obligations of the non-financial report in regard of the form, the contents and the external assurance. The only aspect to be improved concerns the materiality assessment process. Although Eni performed a detail assessment, it did not report the sustainability issues using a materiality matrix from which the reader could understand the prioritization from the point of view of both the company and the stakeholders together.

A further personal consideration can be made in the light of the analysis carried out. Even though Eni's non-financial reporting format complies with the requirements and standards, the choice of high use of references to other sections or other corporate documents was not practical but dispersive as far as the usability of information. In order to have a complete picture on a specific topic was in fact it necessary to look for the information in different sections of different corporate documents.

Moreover, part of the information, although of integrative nature, were published in the sustainability report, which represents a voluntary document separated from the financial statements.

4.5 FURTHER DEVELOPMENTS: WHAT IS NEXT?

The last paragraph of this chapter is dedicated to a list of general considerations concerning the issues previously analysed. Given the current situation of the NFI disclosure, it is possible to suppose some developments in regard to the regulation, the reporting standards used by companies, and the role of auditor in the sustainability reporting process.

- Regulation: generally in this field it is possible to underline the companies need of flexibility and with no additional requirements and legal burdens. Moreover, given the aim of the legislator to achieve the highest level of homogeneity and comparability among companies, an expansion of the requirements to a large category of companies can be expected in the next years. In fact, as explained in the general analysis, only a

limited number of companies fulfil the criteria to be considered Entity of Public Interest (EIPs).

- Reporting standards: given that the regulation leaves companies the freedom of choice on the standards to be used in reporting NFI, the current trend among the various reporting frameworks is that of convergence towards shared principles and practices. Moreover, from the European consultations on the *Directive on non-financial information disclosure and diversity information* it seems that both companies and investors consider more useful and suitable to report on an integrated basis, preparing an homogenous report with both financial and non-financial information together. For these reasons, it is possible that in the near future a share integrated reporting standard will develop to simplify the companies reporting as well as to implement the comparability between companies. Regarding the reporting standards, it is useful to focus on the principle of materiality of information.

The analysis of materiality should be reviewed on a regular basis to ensure that the information published in the report continue to be relevant. Such reviews should be more frequent in companies belonging to dynamic and innovative sectors, and may be less frequent in more stable circumstances. Therefore, in the following years of publication of the non-financial disclosure, it will be interesting to check how many companies will update their materiality analysis. In addition, working on the definition and application of the principle of materiality the length of reports could also be reduced, avoiding duplication of information.

A further principle of GRI to follow in defining the content of non-financial disclosure is represented by the stakeholder inclusiveness, i.e. the involvement of identified stakeholders aimed at responding to their expectations and interests. Also the EC guidelines emphasize the importance that companies maintain relationships with their relevant stakeholders, since the expectations of the stakeholders represent the fundamental element to be taken into account in the identification of the relevant aspects to be included in the NFI report. The involvement of the stakeholders also stems the possible self-referentiality that could result from an analysis of materiality with the only involvement of the company's management. Therefore, in updating the materiality matrix, it will be also interesting to note how many companies will declare to have carried out stakeholder engagement activities and in what modalities.

- Auditor engagement: currently the required level of assurance of non-financial information is that of limited assurance. In the next years it will be interesting to observe if the companies want to move to the form of reasonable assurance, at least on

some types of particularly relevant information, in order to further increase the reliability of this information.

- Application for companies other than big listed companies: the previous considerations are true for the non-financial reporting conducted by the big listed companies, but what about small and medium enterprises? While larger companies are seen as the key users of sustainability measures, it should not be assumed that these measures are not being embraced by smaller businesses. SMEs in fact are closely involved into local communities and for this reason are highly interested in maintaining a positive community image or, in a legitimacy theory view, in maintaining their license to operate. Therefore, for SMEs the main advantages in reporting NFI are to improve their reputation and to achieve a competitive advantage in respect to other local competitors. However, small businesses differ from big corporations in a variety of ways including the amount of resources available, strategies, drivers, importance of managerial values, level of involvement and stakeholder prioritization. All those factors impact the different ways in which NFI reporting is perceived and practised by SMEs in contrast with large companies. Also the personal values of the owner-manager affect the sustainability strategy of the firm, since small business are characterized by the absence of the separation between ownership and management. Moreover, issues more relevant to the firm and primarily stakeholders have priority in the sustainability activities of SMEs. Therefore, employee-direct programs and local community involvement are the most frequent practised sustainability activities. These considerations result usually in a non-systematic, non-formalized and internally oriented non-financial disclosure in SMEs. In regard to the reporting activity, the high number of available reporting frameworks is a problem especially for the accountants of SMEs since they lack the expertise and resources to evaluate the frameworks' suitability. In addition, another challenge is of ensuring proportionality of both reporting and assurance standards on non-financial information. The existing set of standards and guidance for non-financial reporting and assurance are in fact not sufficiently scalable to be capable of cost effective use by SMEs. Hence, guidance on how such standards can be best applied in a proportional manner is welcome. In regard to the demand for assurance on non-financial information, while in the case of larger companies will be primarily driven by external users, for SMEs any demand is more likely to come from internal users such as business owners, customers and the providers of finance. Presently there is little

demand amongst SMEs for assurance. This is due to the lack of awareness and understanding of benefits firms could gain in assure their disclosures, making the trade-off between benefits and costs for assurance less attractive for SMEs¹⁴⁰.

¹⁴⁰ GRI, *Ready to report? Introducing sustainability reporting for SMEs*, 2014. p. 5 and following.

APPENDIX

Appendix I: Foreign companies

8 companies listed in Borsa Italiana are foreign companies, not subjected to the Italian legislation on the disclosure of non-financial information. A brief analysis has been conducted also on those companies, with the following results:

- 5 companies have the Netherlands as state of origin: according to Dutch law, auditors have to check the presence of the statement and has to perform a consistency check of disclosures. The identification of material misstatements and the auditor conclusions are part of the review of the management report. The NFI in fact has to be presented in the annual management report, an additional ad hoc Sustainability Report can be prepared on a voluntary basis. 4 of these Dutch companies have also prepared an ad hoc Sustainability Report, in 3 cases assured by an accounting-provider (engagement based on ISAE 3000) and in one case assured by a non-accounting provider (engagement based on AA1000APS, type II evaluation). One company decided to disclose NFI only in its Financial Statements.
- 3 companies have Luxembourg as state of origin: according to Luxembourg law, the auditor has to check only the presence of the statement. The NFI shall be presented in the management report or in a separate report published alongside the management report. In 1 case the company requested an auditor verification according to ISAE 3000 of its Sustainability Report on a voluntary basis, in another case the NFI was disclosed in an ad hoc Sustainability Report with no assurance report, and in one another case the company decided to disclose its NFI only in the Financial Statements.

Tab 1: List of Foreign listed companies in Borsa Italiana

| FOREIGN LISTED COMPANIES in B.I. | STATE OF ORIGIN | NFI DISCLOSURE | ASSURANCE |
|-----------------------------------------|------------------------|-----------------------|----------------------------------------|
| CNH INDUSTRIAL N.V. | The Netherlands | Ad hoc SR | Assurance of a non-accounting provider |
| D'AMICO INTERN. SHIPPING S.A. | Luxembourg | Only in FS | Assurance of management report |
| EXOR N.V. | The Netherlands | Only in FS | Assurance of management report |
| FCA GROUP | The Netherlands | Ad hoc SR | Assurance of an accounting provider |
| | | | Assurance of an accounting |

| | | | |
|--------------------------|-----------------|-----------|-------------------------------------|
| FERRARI N.V. | The Netherlands | Ad hoc SR | provider |
| IVS GROUP | Luxembourg | Ad hoc SR | Assurance of an accounting provider |
| STMICROELECTRONIC S N.V. | The Netherlands | Ad hoc SR | Assurance of an accounting provider |
| TENARIS S.A. | Luxembourg | Ad hoc SR | No assurance on SR |

Source: personal elaboration of the data.

Appendix II: List of companies that published a NFI report in 2018 taken into analysis in this Thesis

| | | | | | |
|----|-----------------------------|----|-------------------------|-----|-----------------------|
| 1 | A2A SPA | 49 | DATALOGIC SPA | 97 | MONRIF SPA |
| 2 | ACEA SPA | 50 | DAVIDE CAMPARI SPA | 98 | NICE SPA |
| 3 | AEFFE SPA | 51 | DE LONGHI SPA | 99 | OPENJOBMETIS SPA |
| 4 | AMPLIFON SPA | 52 | DIASORIN SPA | 100 | OVS SPA |
| 5 | ANSALDO STS SPA | 53 | DOBANK SPA | 101 | PANARIAGROUP I.C. SPA |
| 6 | AQUAFIL SPA | 54 | EDISON SPA | 102 | PARMALAT SPA |
| 7 | A. MONDADORI ED. SPA | 55 | EL.EN. SPA | 103 | PIAGGIO & C. SPA |
| 8 | ASCOPIAVE SPA | 56 | ELICA SPA | 104 | PININFARINA SPA |
| 9 | ASS. GENERALI SPA | 57 | EMAK SPA | 105 | PIQUADRO SPA |
| 10 | ASTALDI SPA | 58 | ENAV SPA | 106 | PIRELLI & C. SPA |
| 11 | ASTM SPA | 59 | ENEL SPA | 107 | POSTE ITALIANE SPA |
| 12 | ATLANTIA SPA | 60 | ENI SPA | 108 | PRIMA INDUSTRIE SPA |
| 13 | AUTOGRILL SPA | 61 | ERG SPA | 109 | PRYSMIAN SPA |
| 14 | AVIO SPA | 62 | ESPRINET SPA | 110 | RAI WAY SPA |
| 15 | AZIMUT HOLDING SPA | 63 | EXPRIVIA SPA | 111 | RATTI SPA |
| 16 | B. CARIGE SPA | 64 | F.I.L.A. SPA | 112 | RCS MEDIAGROUP SPA |
| 17 | B. GENERALI SPA | 65 | FIERA MIALNO SPA | 113 | RECORDATI SPA |
| 18 | B. IFIS SPA | 66 | FINCANTIERI SPA | 114 | RENO DE MEDICI SPA |
| 19 | B. INTERMOBILIARE SPA | 67 | FNM SPA | 115 | REPLY SPA |
| 20 | B. MEDIOLANUM SPA | 68 | GAMENET GROUP SPA | 116 | SABAF SPA |
| 21 | B. MPS SPA | 69 | GEDI GRUPPO ED. SPA | 117 | SAES GETTERS SPA |
| 22 | B. POP. DI SONDRIO S.C.P.A. | 70 | GEFRAN SPA | 118 | SAFILO GROUP SPA |
| 23 | BANCO BPM SPA | 71 | GEOX SPA | 119 | SAIPEM SPA |
| 24 | B. DI DESIO E BRIANZA SPA | 72 | GRUPPO C. RICCHETTI SPA | 120 | SALINI IMPREGILO SPA |
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| 26 | BE SPA | 74 | HERA SPA | 122 | SARAS SPA |
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Appendix III: Eni GRI Content Index

| DISCLOSURE | INDICATOR DESCRIPTION | SECTION AND/OR PAGE NUMBER |
|-------------------------------|----------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------|
| Organizational profile | | |
| 102-1 | Name of the organization | Integrated Annual Report 2017, p. 1 |
| 102-2 | Activities, brands, products, and services | Integrated Annual Report 2017, pp. 4-5 |
| 102-3 | Location of headquarters | Integrated Annual Report 2017, inside back cover |
| 102-4 | Location of operations | Integrated Annual Report 2017, pp. 4-5 |
| 102-5 | Ownership and legal form | https://www.eni.com/en_IT/company/governance/shareholders.page |
| 102-6 | Markets served | Integrated Annual Report 2017, pp. 4-5 |
| 102-7 | Scale of the organization | Integrated Annual Report 2017, pp. 12-13 |
| 102-8 | Information on employees and other workers | NFI, pp. 99-100 |
| 102-9 | Supply chain | NFI, p. 104 |
| 102-10 | Significant changes to the organization and its supply chain | Integrated Annual Report 2017, p. 61 |
| 102-11 | Precautionary Principle or approach | Integrated Annual Report 2017, pp. 24-27 |
| 102-12 | External initiatives | Integrated Annual Report 2017, p. 17 |
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| Strategy | | |
| 102-14 | Statement from senior decision-maker | Integrated Annual Report 2017, pp. 6-9 |
| 102-15 | Key impacts, risks, and opportunities | Integrated Annual Report 2017, pp. 24-27, 75-89 |
| Ethics and integrity | | |
| 102-16 | Values, principles, standards, and norms of behavior | Integrated Annual Report 2017, pp. 18-19; 31 NFI, p. 93 |
| Governance | | |
| 102-18 | Governance structure | Integrated Annual Report 2017, pp. 28-31 |
| Stakeholder engagement | | |
| 102-40 | List of stakeholder groups | Integrated Annual Report 2017, pp. 15-17 |
| 102-41 | Collective bargaining agreements | NFI, pp. 99-100 |
| 102-42 | Identifying and selecting stakeholders | Integrated Annual Report 2017, pp. 15-17 |
| 102-43 | Approach to stakeholder engagement | Integrated Annual Report 2017, pp. 15-17 |
| 102-44 | Key topics and concerns raised | Integrated Annual Report 2017, pp. 15-17 |
| Reporting practice | | |
| 102-45 | Entities included in the consolidated financial statements | NFI, pp. 107-108 |
| 102-46 | Defining report content and topic Boundaries | Integrated Annual Report 2017, p. 15 NFI, p. 108 |
| 102-47 | List of material topics | Integrated Annual Report 2017, p. 15 NFI, p. 108 |
| 102-48 | Restatements of information | NFI, p. 107 |
| 102-49 | Changes in reporting | NFI, p. 107 |
| 102-50 | Reporting period | NFI, p. 107 |
| 102-51 | Date of most recent report | First NFI under the Decree 254/2016 Eni for: https://www.eni.com/en_IT/documentations.page |
| 102-52 | Reporting cycle | NFI, p. 107 |
| 102-53 | Contact point for questions regarding the report | Integrated Annual Report 2017, inside back cover |
| 102-54 / 102-55 | Claims of reporting in accordance with the GRI Standards and content index | NFI, pp. 107-110 |
| 102-56 | External assurance | NFI, p. 111 |
| Governance | | |
| 103-1 | Explanation of the material topic and its Boundary | Integrated Annual Report 2017, pp. 15-19 |
| 103-2 | The management approach and its components | NFI, pp. 107-108 |
| 103-3 | Evaluation of the management approach | NFI, pp. 107-108 |

Specific standard disclosures

| DISCLOSURE | INDICATOR DESCRIPTION | SECTION AND/OR PAGE NUMBER | OMISSION |
|--------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| CATEGORY: ECONOMIC METRICS AND COMMENTS | | | |
| Economic performance - DMA (103-1; 103-2; 103-3) | | NFI, pp. 94-97; 108 | |
| 201-2 | Financial implications and other risks and opportunities due to climate change | Integrated Annual Report 2017, pp. 85-86 NFI, pp. 94-97 | |
| Market presence - DMA (103-1; 103-2; 103-3) | | NFI, pp. 98-100; 108 | |
| 202-2 | Proportion of senior management hired from the local community | NFI, p. 100 | |
| Indirect economic impacts - DMA (103-1; 103-2; 103-3) | | NFI, pp. 106; 108 | |
| 203-1 | Infrastructure investments and services supported | NFI, p. 106 | |
| Procurement practices - DMA (103-1; 103-2; 103-3) | | NFI, pp. 106; 108 | |
| 204-1 | Proportion of spending on local suppliers | NFI, p. 106 | Some information related to this indicator are not currently available. Eni intends to elaborate a new methodologies to cover all the requirements in the future. |
| Anti-corruption - DMA (103-1; 103-2; 103-3) | | NFI, pp. 105; 108 | |
| 205-2 | Communication and training about anti-corruption policies and procedures | NFI, p. 105 | |
| CATEGORY: ENVIRONMENTAL METRICS AND COMMENTS | | | |
| Energy - DMA (103-1; 103-2; 103-3) | | NFI, pp. 94-97; 108 | |
| 302-3 | Energy intensity | NFI, pp. 96-97; 107 | |
| Water - DMA (103-1; 103-2; 103-3) | | NFI, pp. 101-102; 108 | |
| 303-1 | Water withdrawal by source | NFI, pp. 101-102 | |
| Biodiversity - DMA (103-1; 103-2; 103-3) | | NFI, pp. 101-102; 108 | |
| 304-1 | Operational sites owned, leased, managed in, or adjacent to, protected areas and areas of high biodiversity value outside protected areas | NFI, pp. 101-102 | Some information related to this indicator are not currently available. Eni intends to collect the necessary data to cover all the requirements in the future. |
| Emissions - DMA (103-1; 103-2; 103-3) | | NFI, pp. 94-97; 108 | |
| 305-1 | Direct (Scope 1) GHG emissions | NFI, pp. 94-97 | |
| 305-4 | GHG emissions intensity | NFI, pp. 94-97; 107 | |
| Effluents and waste - DMA (103-1; 103-2; 103-3) | | NFI, pp. 101-102; 108 | |
| 306-2 | Waste by type and disposal method | NFI, pp. 101-102 | |
| Environmental Compliance - DMA (103-1; 103-2; 103-3) | | NFI, pp. 101-102; 108 | |
| 307-1 | Environmental compliance | Relazione Finanziaria Annuale 2017, pp. 180-183 | |
| CATEGORY: SOCIAL METRICS AND COMMENTS | | | |
| Employment - DMA (103-1; 103-2; 103-3) | | NFI, pp. 98-100; 108 | |
| 401-1 | New employee hires and employee turnover | NFI, pp. 98-100 | |
| Occupational health and safety - DMA (103-1; 103-2; 103-3) | | NFI, pp. 98-100; 108 | |
| 403-2 | Types of injury and rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities | NFI, pp. 98-100; 107 | Some information related to this indicator are not currently available. Eni intends to collect the necessary data to cover all the requirements in the future. |
| Training and education - DMA (103-1; 103-2; 103-3) | | NFI, pp. 98-100; 108 | |
| 404-1 | Average hours of training per year per employee | NFI, pp. 98-100 | |
| Diversity and equal opportunity - DMA (103-1; 103-2; 103-3) | | NFI, pp. 98-100; 108 | |
| 405-1 | Diversity of governance bodies and employees | NFI, pp. 98-100 | |
| Non-discrimination - DMA (103-1; 103-2; 103-3) | | NFI, pp. 103-104; 108 | |
| 406-1 | Incidents of discrimination and corrective actions taken | NFI, pp. 103-104 | |
| Security practices - DMA (103-1; 103-2; 103-3) | | NFI, pp. 103-104; 108 | |
| 410-1 | Security personnel trained in human rights policies or procedures | NFI, pp. 103-104 | |
| Human rights assessment - DMA (103-1; 103-2; 103-3) | | NFI, pp. 103-104; 108 | |
| 412-2 | Employee training on human rights policies or procedures | NFI, pp. 103-104 | |
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| 413-1 | Operations with local community engagement, impact assessments, and development programs | NFI, p. 106 | |
| Supplier social assessment - DMA (103-1; 103-2; 103-3) | | NFI, pp. 104; 108 | |
| 414-1 | New suppliers that were screened using social criteria | NFI, p. 104 | |
| CATEGORY: INNOVATION | | | |
| Innovation - DMA (103-1; 103-2; 103-3) | | NFI, pp. 94-97; 108 | |

CONCLUSIONS

After the presentation of the main characteristics of the sustainability reporting and assurance processes, in this Thesis an empirical analysis of the non-financial information (NFI) reports published in 2018 by listed companies in the Italian Stock Exchange *Borsa Italiana* was conducted.

The purpose of the analysis was to provide a general picture of the trends that were emerging in the first-year implementation of the European Directive *on non-financial and diversity information by certain large undertakings and groups* (2014/95/EU) in the Italian context, focusing especially on the role of the auditor within the NFI reporting process.

Despite the existence of conflicting opinions on the issue, in the last years the demand of sustainability information by the general public and especially by the company's shareholders is growing. Even if their decision making process is based mainly on the corporate financial information, shareholders are developing the awareness that this information alone is no more sufficient to get a comprehensive understanding of a company reality, especially in the long term. Thus, NFI play an important role in changing the corporate reporting landscape, pushing towards an increasingly integrated form of corporate reporting. Based on these initial considerations, the results of the analysis performed show that the solutions used by companies to comply with the reporting and legislative requirements are heterogeneous without a univocal solution under various aspects. More in detail, the main results obtained can be summarized as follows.

Many listed companies were excluded from the scope of application of the Directive according to the dimensional requirements, especially the requested average number of 500 employees during the financial year. The majority of the companies affected by the requirements decided to disclose NFI in a stand-alone document (73%) while a minority of companies reported this information within the management report or followed an integrated reporting. Above all the reports analysed have been drawn up on the basis of the Global Reporting Initiative (GRI) guidelines. In addition, a little more than 1/6 of all companies analysed refers to or at least mentions the globally accepted SDGs (31%). Despite the high freedom of choice left by the legislator, the companies affected by the Directive could not avoid the publication of the mandatory requested information. Thus, how companies have approached to this new regulation? The general impression was that companies have intended the new legislation as a further legal burden, rather than as an opportunity to communicate with shareholders and to gain competitive advantage over competitors. Companies have in

fact fulfilled the minimum requirements following a compilative rather than substantive approach, basing the disclosed information on the previous years' sustainability reports rather than developing a new reporting process and methodology.

The reason why companies perceive the disclosure of the NFI report as a regulatory obligations rather than as an additional instrument at their disposal, is due to the marginal importance of NFI within the decision making process of the companies' shareholders in comparison with that given to corporate financial information. Despite the growing interest on the topic in fact, nowadays shareholders take into consideration NFI for their decision in a not entirely effective way.

The only partial standardization of NFI reporting practices and the intrinsic subjective nature of this type of information broadly contributes to their limited use and usefulness, especially in the general understanding and comparability of the information published by companies. Conscious of the aforementioned difficulties, companies have to approach the NFI reporting with a different perspective rather than that of a mere regulatory compliance. Companies should think to their NFI disclosure in a strategic perspective, disclosing material and reliable information and taking advantage of the benefits that could result from a substantial reporting as that of financial information.

The opportunities deriving from this change in perspective are various, as for example the possibility to communicate with shareholders on material issues other than the financial ones, or the positive publicity deriving from a conscious management of the sustainability issues through which a company could earn a competitive advantage, especially in sectors highly sensitive to sustainability issues. Given the not-numerical nature of this information, one of the biggest obstacles in NFI's development path is the lack of credibility of the shareholders on this type of information.

For this reason the role of the External Auditor in the NFI reporting process was analyzed, believing that his verification could help to minimize the uncertainty about any possible information and credibility gaps presented in the NFI reports.

From a normative point of view, the statutory auditor has to check at least the presence of the required information, either in the management report or in a separate document. In addition, the Italian legislator decides to straighten the control requesting a verification of the auditor also on the content of the NFI report. Given the nature of NFI and the poorly standardized practice of the reporting, all the assurance engagements performed by auditors in the first year implementation of the Directive were in the form of *limited assurance*. This is due to the fact

that the NFI report is characterized by the presence of a high number of qualitative information deriving from companies' information systems and internal control often not fully integrated or incomplete, which do not allow the auditor to conduct the engagement with the necessary and adequate level of extension required by a *reasonable assurance*. However, the scope of the auditor is to provide a professional opinion which shows that based on the work performed, nothing has come to its attention that causes to believe that the NFI report of the company has not been prepared, in all material respects, in compliance with the normative and the reporting standards. Despite the lowest level of assurance in respect to a reasonable one, the presence of an assurance statement remain an important tool to enhance the degree of confidence of the shareholders about the trustworthiness and correctness of the information disclosed in the report. Through the presence of the statement in fact, the readers of corporate documents could be reassure against “green washing” reports and eco-marketing campaigns, which include little in the way of substance. In the next years it will be interesting to observe if companies want to move to the form of reasonable assurance of their NFI at least on some types of particularly relevant information in order to further increase the reliability of this information.

Despite the mandatory presence of the assurance statement on NFI report, some limits could be identify especially in respect to the standards used as reference in the assurance of this information. In this regard, the main standards used for the assurance of NFI were explained, in particular the ISAE 3000 (Revised) and the AA1000 Assurance Standards. The first is based on an accounting perspective and it is used exclusively by the statutory certified auditors or auditing firms. The second is based on a non-accounting perspective and it is used by experts on the topic. For the purposes of this Thesis, it is important to underline that in the Italian context the legislation explicitly requests that the subject in charge of the verification has to be not a mere independent subject with certified professionalism, but a statutory auditor, subject to the ISAE 3000 Standard. Despite this requirement, it has been considered appropriate to make a brief analysis also of the AA1000 Assurance Standard, both for its global diffusion, and for the possibility to find a reference to both standards jointly within the assurance statement. The results of the analysis performed show that all the assurance statements analyzed were issued by auditing firms, mostly from the *Big 4* auditing firms (90%). The problem concerning the assurance standards refer to the absence of an ad hoc standard specific for NFI to be followed by the auditor in its assurance engagement. Both ISAE 3000 (Revised) and AA1000AS are in fact assurance standards for *information other*

than the financial one, to be intended as a residual comprehensive category of information instead of a specific and detailed information to be assured.

In order to better understand how a company can concretely fulfill both the reporting and the assurance requirements, at the end of the analysis a specific case study was briefly explained. According to the FRPI (Federazione Relazioni Pubbliche Italiana) annual competition, the winner of the “Oscar di Bilancio 2018” for the category *Big listed companies* was Eni Group. For the purposes of the analysis, Eni's NFI reporting process and format was explained, pointing out both the identified good practices and the limitations of its reporting methodology. Despite its award, Eni's NFI report presents some gaps both in terms of form and content, in particular concerning the continuous references to other parts of financial statements or other corporate documents within the NFI report, and the not in-depth process of materiality and stakeholder engagement performed by the company.

Concluding, although some steps have been taken, the path towards the standardization of NFI reporting and assurance processes seems to remain long and upward, with a significative difference in comparison with that of financial information. Even if regulators and standard setters are doing their part, companies remain the real protagonists in this corporate reporting journey. They need to realise that nowadays providing only financial information is not enough to give shareholders the full picture of their activities. NFI report is the way in which companies meet the demand of transparency from shareholders, and NFI assurance statement is the instrument used by companies to improve the reliability and credibility of their NFI reports. Nowadays, companies have to consider transparency on sustainability issues as a must and no more as an option.

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