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CONCEPTUAL REVIEW ON BUSINESS SUSTAINABILITY REPORTING

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ABSTRACT

Markets and companies are becoming competitive and sticking only to financial reporting does not no longer create a competitive edge. Therefore, companies have enhanced their commitment towards sustainability initiatives as well as the communication of sustainability related matters to the stakeholders. As a responsible corporate citizen it is essential to pay attention to the effects made by them on society, environment and economy. Subsequently, sustainability reporting is the systematic disclosure and communication of the company's compliance on environmental, social and governance goals. Even though sustainability reporting is a voluntarily practice, most of the companies are keen on communicating their sustainability initiatives to its stakeholders. It is because sustainability reporting subsequently assists the companies to establish a good corporate image among the stakeholders.

Introduction

Sustainability refers to the firm's ability to meet today's requirements without compromising the opportunity of the future generation to fulfill their requirements (World Commission on Environment and Development, 1987). The stakeholders rapidly demand the companies to provide transparent disclosure in a holistic manner covering the dimensions of economic, social and environmental affects is refereed as sustainability reporting (Logsdon & Lewellyn 2000; Rasche & Esser 2006). Thus, Sustainability reporting has become an integral part in decision making, accounting practices and reporting due to the increasing awareness and relevance to the society (Burritt and Schaltegger, 2010; Windolph, Schaltegger & Herzig, 2014). According to Dienes, Sassen and Fischer (2016), sustainability comprises of two objectives namely creating the compatibility of social and environmental management with the company's strategy and embedding social and environment information to sustainability reporting and corporate information. Therefore, most of the companies voluntarily publish information related to sustainability initiatives in order to meet the stakeholders' expectations.

Since all the required areas should be covered in sustainability reporting, the need for standardized frameworks are gaining the momentum. Thus, different frameworks such as Global Reporting Initiative, OECD Guidelines, ISO 26000, International Standard for Social Responsibility and many more have been introduced to maintain the consistency in reporting practices. When considering the available literature, it has illustrated both the negative and positive impact of sustainability reporting on corporate finance. Furthermore, the three dimensions of sustainability reporting which are economic, social and environmental are discussed. In line with that, this study focuses on understanding the implications for business organizations and financial management practice, development of sustainability reporting and its future directions and merits and demerits of the concept. According to Adams and Whelan (2009), sustainability reporting is influenced by maximization of shareholder wealth, regulation compliances and maintenance of corporate image. Thus, information provided related to sustainability should be audited irrespective of it is being published in paper or online (Adams & Frost, 2006; Maijala & Pohjola, 2006). With the growing importance of sustainability reporting many studies have been done about the drivers of sustainability, sustainability practices in different countries and industries.

Motivation of the Study

This paper attempts to review the empirical and theoretical arguments related to sustainability and its impact of business organizations and financial practices. Furthermore, the dimensions of sustainability will be discussed based on the previous literature. Finally, the future trends and research areas will be identified. Accordingly, paper follows a deductive approach to review the concepts and empirical contributions. Research tools include literature survey methods and journal articles, case studies, industry reports and theories were examined to organize the arguments and conclusions. Paper provides a discussion based on theoretical arguments and it concludes future research directions accordingly.

Literature Review

Development Over Time

Both the financial and non-financial aspects in reporting practices have been changed over the time and according to Cormier and Gordon (2001), there are instances where traditional financial reporting has been accompanied by social reports and environmental reports. In line with this trend, since 1990s the focus of reporting has moved towards comprehensive corporate social responsibility reports or sustainability reports. Furthermore, sustainability reporting is complimenting with non-financial reporting, triple bottom line reporting, corporate social responsibility reporting and also an integral element in integrated reporting which is a recent improvement in reporting which has combined the corporate performance of financial and non-financial indicators.

The history of sustainability reporting is going back to environmental reporting which was done by the companies in the chemical industry which faced issues in their reputation and tobacco companies which wanted to attract investors despite of the growing popularity in ethical investing. One of the prominent addition to sustainability reporting is the Global Reporting Initiative which is established in year 2000 and a frequently practiced adapted framework up until now. It has been developed based on the concept of triple bottom line operationalized by Elkington (1997) covering the three sustainability measurements of economic, social and environment is such a standardized framework. In addition, the Organization for Economic Co-operation and Development has OECD Guidelines for multinational enterprises and the International Organization for Standardization has ISO 26000 and International Standard for social responsibility to report the sustainability practices of corporates. Furthermore, The United Nations Global Compact is in the process of implementing another framework for sustainability reporting.

According to Dyllick and Hockerts (2002), sustainability is defined as a systems level concept rather than an organizational level concept. However, majority of the organizations are still performing their businesses in an unsustainable manner and a drastic redesigning in the business strategies and processes is very much needed (Brown, 2001; Gray 2010). In the Sri Lankan context organizations in the bank, finance and insurance sector engage in the sustainability reporting the most, followed by manufacturing and hotel and travel sector. However, irrespective of the sector majority prepared non GRI reports (SheConsults, 2015).

Implications for Business Organizations and Financial Management Practices

The companies are compelled to engage in sustainability reporting since not only being successful in terms of sustainability indicators are not enough, but also reporting those in a systematically is essential since it acts as one of the main communication tools between the company and the stakeholders. Furthermore, according to previous study corporate sustainability has expanded the bottom line to triple bottom line by incorporating social and environmental indicators to the organization's strategies (Dixon-Fowler, Slater, Johnson, Ellstrand & Romi, 2013).

However, as stated by Breiki and Nobanee (2019), implementation of corporate sustainability is done with a financial cost to the company. Thus, it is essential to achieve proper financial management to ensure future sustainability. Subsequently, studies done by Presber (2011), companies which do not disclose sufficient information regarding environmental performance are gaining the unnecessary attention of social pressure groups. Subsequently, many organizations have incorporated sustainability initiatives in their annual reports.

As stated by Shah (2011), there are two theories namely value creating and value destroying which elaborates the impact of sustainability on the financial management of a company. Value creation theory demonstrates that firm's risk can be alleviated by fulfilling social and environmental responsibilities whereas value destroying theory explains that the focus given on profitability is reduced at the expense of pleasing the stakeholders instead of shareholders. Similarly, trade-off theory also illustrates that there is a negative relationship between the engagement in sustainability activities and the profitability, since it deviates the scare resources from the most profitable activities of the company (Endrikat, Guenther & Hoppe, 2014).

In contrary, the positive relationship is also explained in theories such as resource based view theory and stakeholder theory. According to resource based view, if the company can strategically exploit its unique capabilities, the company can achieve competitive advantages and better financial performance subsequently (Haffar & Searcy, 2017). Similarly, the stakeholder theory suggests that financial performances are accelerated by fulfilling the stakeholders needs such as society at large and environment (Chernev & Blair, 2015).

Furthermore, auditors play a vital role in sustainability reporting since it is essential to verify the accuracy of the claims related to firm's sustainability initiatives. However as stated by Lindström (2019), auditing the sustainable reports are more than just a profession, since it is about the future of the planet. Therefore, it is essential to assure the materiality of the information provided in these reports while guaranteeing the accuracy of the content.

Merits & Demerits of Sustainability Reporting

There are many reasons behind the fact that organizations engage in sustainability reporting. However, the main reason is intended as to be perceived as transparent and accountable. Thus, the companies are able to improve the corporate image and the reputation among the stakeholders' mind since the sustainability reports act as a key mechanism in communication. Thus, it leads to investor and consumer confidence. Similarly, Morsing and Schultz (2006) stated that way of communicating the company's activities indicates the strategic direction the company takes toward its stakeholders. Thus, it will assist the company to clearly covey the corporate strategies such as efforts and standards followed to the internal and external stakeholders while maintaining the consistency in the messages. On the other hand, sustainability reporting enables an organization to track the progress against the goals set for the betterment of the avenues in sustainability while enhancing the awareness of the broad environmental and social issues. Subsequently sustainability reporting leads to reputational benefits, cost saving and new business opportunities.

One of the constraints in sustainability reporting is to what extent the data related to environmental, social and corporate governance practices and its impacts must be revealed. Thus, as a solution for this the United States applies the materiality principle to determine the vitality of disclosing sustainability related information. Thus, materiality would be high, if the specific information would significantly alter the currently available information acquired by the stakeholders. In addition, disclosing sustainability related information might create an unnecessary influence of the pressure groups on the organization while it tarnishes the corporate reputation and impose legal implications upon the shortcomings in sustainability reports (Kolk, 2004). Furthermore, if the competitors are not engage in sustainability reporting, the companies are not ready to incur an extra cost. In addition, like reporting financial reporting, sustainability reporting lacks in the ability to gather consistent and accurate data and choose the most suitable indictors. However, the stakeholders have a responsibility to create an urge among the companies to engage in sustainability reporting since it will be beneficial for the society in large in the long run.

Future Directions and Development of Sustainability Reporting

In order to accelerate the sustainability reporting requirements, different professional bodies have introduced sustainability reporting frameworks. However, the mandatory guidelines are still evolving due to the differences in the industries, company size, country etc. affect the sustainability practices of an organization. The International Chamber of Commerce (2015) has identified 8 key areas which needs to be improved in sustainability reporting. They are indispensable part of corporate sustainability which is meant by disclosing the relevant information related to sustainability, flexibility in reporting based on the company's nature, reduce the number of reporting frameworks to enhance harmonization, third party service to verify the accuracy of reporting, being relevant to local context while matching the global standards, internal and external consultations to improve the engagement with the stakeholders, continuous improvement and exceling integrated reporting.

According to the Global Reporting Initiative (2015), climate change, human rights, wealth inequality, data and technology are the key five trends were identified as the trends in 2025. In relation to climate change it is advised to follow the Paris Agreement and expected to link to Intended Nationally Determined Contributions. Furthermore, the companies are expected to utilize sustainable energy models to efficient production and distribution. As per the human rights the companies are expected to disclose the initiatives taken to preserve the human rights since the investors, rating agencies and the regulators are more concerned about those matters. In terms of wealth management, increasing the wage rates of labourers and excelling the share of value of small and medium scale producers while eliminating the gender inequalities has been discussed. Finally, data and technology has been perceived as a challenge as well as an opportunity when engaging in corporate sustainability. The opportunities are associated with the availability of wider platforms to disclose sustainability initiatives, ability to embed sustainability related key performance indicators to the performance management systems, ease of monitoring and providing feedbacks whereas challenges are associated with the lack of availability of sensitive and confidential data and the need for holistic analytical tools to understand data comprehensively.

Conclusion and Future Research Directions

Even though sustainability reporting is a voluntarily practice, most of the companies are keen on communicating their sustainability initiatives to its stakeholders. With the growing trend of sustainability reporting, different frameworks such as Global Reporting Initiative, OECD Guidelines, ISO 26000, International Standard for social responsibility and etc. have been introduced to maintain the consistency in reporting practices. In addition, the role of external auditors has been recognized vital since it is essential to assure the accuracy as well as the materiality of reporting. There are theories which explain the positive effects as well as the negative effects of sustainability reporting. Thus, the company should be able to strategically exploit its unique capabilities, to achieve competitive advantages and better financial performance subsequently. Furthermore, there have been discussions on incorporating climate change, human rights, wealth inequality, data and technology into sustainability reporting.

In this paper, theories related to the positive impact and negative impact of sustainability were identified from different perspectives. However, future research should seek to clarify the significance of each of these theories on sustainability reporting. Thus, it will help the companies to design their sustainability initiatives in a way of satisfying the stakeholders. Furthermore, the different frameworks should be evaluated to identify the best framework of sustainability reporting since there is a diversified range of available frameworks.

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