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Non-Financial Reporting Regulation and Challenges in Sustainability Disclosure and Corporate Governance Practices

Abstract

This paper aims to investigate how the shift from voluntary to mandatory non-financial information started by the EU Directive 95/2014 may influence corporate practices. In particular, this research presents a paradigmatic case study to highlight relevant changes in reporting strategy and corporate governance adopted by an Italian listed company that never disclosed sustainability information before the transposition of the EU Directive into the Legislative Decree 254/2016. In this scenario, new obligations on non-financial reporting were not perceived as mere additional administrative duties and the non-financial statement became an opportunity to communicate company's paths toward sustainability, guaranteeing transparency and greater stakeholders' engagement. Our findings go beyond prior studies pointing out how organisations adopt strategic and tactical responses to the pressure stemming from the external environment. Additionally, it highlights the pivotal function played by the Internal Audit in setting up the direction of change. This research has theoretical and practical contributions for academic communities, policymakers and practitioners.

Keywords: sustainability, internal audit, EU Non-Financial Directive, governance, regulation, ESG reporting, case-study, stakeholders' engagement.

1. Introduction

An increasing amount of organisations are providing information on environmental, social and governance (ESG) aspects worldwide through sustainability and integrated reports (Dumay et al. 2016; de Villiers et al. 2017; de Villiers and Sharma 2018). Due to some issues on the quality of voluntarily reported information, the advent of EU Directive 2014/95 (The Directive), enforcing large companies to disclose non-financial and diversity information, aims to increase corporate accountability, transparency and comparability of information for stakeholders, among which investors and consumers are included.

The Directive assumes companies' conformity to ESG disclosure requirements in the light of positive legitimacy and/or economic gain. Thus, companies' behaviour is assumed to have changed to be compliant with the new regulation (La Torre et al. 2018). Nevertheless, inconsistencies between non-financial reporting talk and real Corporate Social Responsibility (CSR) performance may exist due to the symbolic adoption of new sustainability actions (Cho et al. 2015; Maglio et al. 2020; Michelon et al. 2015) and the decoupling phenomenon (Meyer and Rowan, 1977).

Aiming to investigate which company's reactions this external pressure for non-financial reporting generates (e.g. adaptation, 'window dressing' or just a 'tick-the-box' exercise in preparing reports), we combined institutional theory (Clemens and Douglas 2005; DiMaggio and Powell 1983) with

resource-dependence theory (Oliver 1991; 1997) to draft company's responses to external challenges as suggested by Sherer and Lee (2002).

Since research posits that sustainability-related regulation may even change a company's environmental strategy and its governance structure and foster multi-stakeholder dialogue (Ioannou and Serafeim, 2017), we focused on the role played by Board Members and the Internal Audit (IA), who have the power to inform them. Board members are those that can connect sustainability with core strategy and have a major impact on sustainability reporting quality according to the literature (Michelon and Parbonetti 2012). The IA plays an important role in sustaining the credibility of the information reported by companies, contributing to good corporate governance (CG) practices (Chartered Institute of Internal Auditors, 2015). Therefore, our RQ is "How does regulation on non-financial reporting affect company reporting strategy and governance practices?"

We proposed the single case study method to understand which corporate changes derive from the advent of the Directive and which aspects of reporting and corporate governance changed. The empirical analysis indicates that regulative pressures interact with normative and mimetic pressures leading to corporate changes that go beyond mere conformity to what laws prescribe. Additionally, the role of the IA went beyond its assurance function and became the internal actor guiding organisational adaptation toward sustainability.

The remainder of our paper is as follows: section 2 is the literature review, section 3 describes the case study method, section 4 presents our findings and discussion on the case study and section 5 presents conclusions and future research.

2. Literature Review: The rise of mandatory non-financial disclosure and its relation with corporate governance

Corporate reporting is a long-standing business practice evolved in the recent diffusion of sustainability and/or integrated reports (Mervelskemper and Streit 2017; Frías-Aceituno et al. 2014; Stacchezzini et al. 2016) providing information related to environmental, social and governance (ESG) aspects.

The disclosure of ESG aspects has mostly been a voluntary practice adopted by corporations in response to stakeholders' expectations and to gain legitimacy (Cho et al. 2012; Deegan 2002). However, several studies have highlighted how the quality of voluntarily reported information is quite poor, does not correspond to effective, responsible behaviour and is a symbolic management practice (Cho et al. 2015; Michelon et al. 2015). Therefore, both researchers and regulators have started to call for mandatory ESG reporting.

The debate on the effectiveness of regulation compared to voluntary ESG reporting is retrieved in the studies of Gunningham (2007) and Stubbs and Higgins (2018). Chelli et al. (2018) found that legislation by the central government is more successful in making reporting credible than market mechanisms promoted by stock exchanges. On the contrary, Bebbington et al. (2012) showed that rules might not be perceived as binding if the regulation is incongruent with the prevailing informal norms. Both Luque-Vilchez and Larrinaga (2016) and Chauvey et al. (2015) argue that mandatory ESG disclosure does not lead to an improvement in information quality.

Governments and the EU have become aware of the inefficacy of voluntary reporting, resulting in unbalanced, inaccurate, inconsistent and incomparable information (EC 2013). As a result, many countries have begun to require mandatory reporting. The latest regulative intervention refers to

the Non-financial EU Directive, which amends the 'soft' obligations included in the previous directives (2003/51/EU and 2013/34/EU).

As reported by the Directive itself, the EU promotes companies' accountability and increase transparency that favours stakeholders' (mainly investors' and consumers') trust and consequently companies' access to their resources (Campra et al. 2020; Cohen et al. 2015). The EU assumes that companies conform to ESG disclosure requirements because this results in positive legitimacy and/or economic gain. Generating change in companies' behaviour is a consequence that is taken for granted (La Torre et al. 2018).

However, some authors have already raised some doubts. According to Stubbs and Higgins (2018) and Cooper and Owen (2007), there is little desire for accountability and regulatory reform among stakeholders other than investors. Therefore, companies may feel that ESG disclosure is not necessary or not legitimate, and this situation may increase the risk of 'window dressing' (i.e., the misuse of reporting as a public-relations exercise driven by marketing goals), generating inconsistencies between non-financial reporting talk and real CSR performance (La Torre et al., 2018). The symbolic adoption of new sustainability words while still relying on traditional policies and organisational routines is a sort of ritualistic compliance, already analysed in organisation studies and named decoupling (Meyer and Rowan 1977).

Since decoupling is usually linked to the company decision-makers' will to avoid implementing policies that conflict with their ideological beliefs, we might expect that the new ESG requirements are welcomed by family firms who have roots in the community, respect for employees and prefer a relational approach with partners and suppliers (McGuire et al. 2012; Cennamo et al. 2012). Although family firms report less information on their CSR duties than non-family firms do (Garcia-Torea et al. 2016a; Nekhili et al. 2017), they usually behave in a socially responsible manner as a means of generating reputation, prestige and potentially useful goodwill or resources (Dyer and Whetten 2006; Gomez-Mejia et al. 2007).

Quality of sustainability reporting and its coherence with actual practices is also strongly related to corporate governance. CG defines principles, rules and regulations affecting the way a company is directed, administered or controlled by managers in the interests of investors (Paape et al. 2003). CG is linked to CSR (Garcia-Torea et al. 2016b; Jamali et al. 2008; Kolk 2008; Kolk and Pinske 2010) as CG aims to create value for both shareholders and stakeholders (Mihret 2014). In this direction, the new provisions of the Directive are moving corporate behaviour toward greater dialogue with multiple stakeholders and introducing new structures of CG.

An under-investigated function that contributes to good CG practice is the IA that provides consultation and assurance to the evaluation of risk and control governance (Mahzana and Yan 2014; Melville 2003). It is a control mechanism that assists management and the board of directors in accomplishing corporate objectives (Mihret 2014). IA's responsibilities change in response to regulations and increased organisational environment complexity (Jones et al., 2017) as demonstrated by the fact that in some countries this role is more than a supervisor, but it is highly geared towards contributing to strategic management (Melville 2003).

When a company adopts the non-financial reporting perspective, either voluntarily or obliged by law, the IA needs to assume "a broad view across the organisation's systems and processes, and it should have a role in assuring the quality of information contained in the strategic and integrated reports" (Chartered Institute of Internal Auditors 2015). Thus, auditors could play a role in sustaining the credibility of the information reported. Additionally, the IA must provide a wide range of guarantees referring to processes for producing the non-financial report, risks identification and materiality of non-financial information (Page and Spira 2016).

Since "certain companies may not necessarily be 'responsible corporate citizens' but may instrumentally use 'greenwash' to favourably influence stakeholder perceptions" (Ackers 2015; Aras

and Crowther 2008), the credibility of corporate ESG disclosures is directly related to the level of assurance provided by IAs and other subjects that counter management information bias and possible errors (Holt 2012; Soh and Martinov-Bennie 2015). Therefore, the IA could be a key player in the company's change toward sustainability reporting.

3. Method

3.1 Case study research

We adopted the case study research (Yin 2014; Lys and Vincent 1995) as a qualitative approach to undertaking an in-depth investigation of a phenomenon in its real-life context. We proposed a paradigmatic case study (Cooper, Morgan 2008) because it helps better understand which changes occur after the new provisions, which aspects of reporting and corporate governance are subject to change and what is the role of the IA function. The paradigmatic case was adopted to analyse “actual practices, including the details of significant activities that may be ordinary, unusual or infrequent...and phenomena in which the context is crucial because the context affects the phenomena being studied” (Cooper, Morgan 2008).

The use of one case study can be subject to some critiques deriving from the generalisation of results. However, a case study is not based on statistical generalisation (Tsang 2014). It provides an analytical generalisation that derives from the observation of a specific phenomenon, aiming to determine theory understanding and explanations useful for other cases (Yin 2014). The following subsections define the research context, theoretical framework and the methods used for data collection and analysis.

3.2 The research context

The case study analysed was the “Biesse Group” (BG), a family firm (the founder and his family own 51% of ordinary share capital) located in the Marche Region of central-west Italy but with subsidiaries all over the world. The BG employs about 4000 people and is a leading company in the field of wood and glass processing, listed on the Milan Stock exchange.

The company was chosen for investigation because it elicits insight for a better theoretical understanding as implied by paradigmatic case study type. Biesse’s reaction provides evidence that integrates existing theory, namely suggesting possible heterogeneity and not conformity in companies’ response to regulation.

Biesse was chosen because it never communicated social and environmental information before Legislative Decree 254/2016 (the law that enacted the Directive in Italy), despite being a large and multinational organisation. Moreover, the company appeared somehow unusual to the researchers because it decided to entrust the preparation of the sustainability report to the IA. On the contrary, as emerged in previous research by one of the authors (Aureli et al. 2017), Italian listed companies usually have a dedicated CSR office (51%), associate CSR to a communication activity (in 22% the Investor Relation function is responsible for CSR) or appoint the CFO to take care of it (14%). Finally, the complex process of collecting and assembling ESG data from international subsidiaries triggered by the IA made this case a relevant setting for investigation.

3.3 Theoretical framework

The adoption and disclosure of socio-environmental practices have been investigated from the perspective of the institutional theory and legitimacy theory (Deegan 2007; Fernando and Lawrence 2014; Archel et al. 2009).

Institutional theory (DiMaggio and Powell 1983; Meyer and Rowan 1977; Scott 1987) explains organisational behaviour as shaped by institutions, i.e., by symbolic systems made up of regulative, normative and cultural-cognitive elements (or pillars), perceived as external and coercive (Durkheim 1982), that provide meaning to social action (Scott 1995). According to Di Maggio and Powell (1983), institutions affect organisations through three types of mechanisms or pressures: coercive, normative and mimetic. Coercive pressures refer to laws, norms and sanctions issued by governments and authorities. Normative pressures refer to values, conventions and social expectations mainly expressed by dominant professions, academic institutions and powerful bodies. Lastly, mimetic pressures imply a company's imitation of procedures and/or structures of other closer organisations as there is a shared cultural framework on the right behaviour to follow (i.e., it is legitimate), or it is believed that the imitated behaviour has technical value. The underlying idea is that companies conform to these external pressures to achieve legitimacy and not for an economic rationale (Oliver 1991; Lukka 2007).

However, structural and organisational conformity (i.e., isomorphism) to external pressures is not the only possible answer. Two studies of companies' reaction to mandatory sustainability reporting reveal diverse strategies, ranging from dismissal to concealment (Criado et al. 2008; Doshi et al. 2013). Critics of the institutional view argue that it is too deterministic (Greenwood and Hinings 1996). A company's reaction may vary depending on organisational actors' power and interest, and historical, social, and political factors (Collier 2001). Moreover, organisational change depends on how constituents' demands that generate pressure for conformity are accepted, adopted and internalised within the company. If they contrast with company routines and culture, organisational actors may generate inertia. Vice versa, internal actors guide organisational adaptation (Burns e Scapens 2000; Tsamenyi et al. 2006). Institutional theory alone neglects internal organisational dynamics, which may lead companies to the symbolic adaptation to external pressures (Moll et al. 2006) or the manipulation of external constituencies' beliefs and values (Archel et al. 2009).

Clemens and Douglas (2005) suggest linking the institutional view to strategic choice because the two theories have greater predictive power when used together (Sherer and Lee 2002). Similarly, Oliver (1991; 1997) incorporated the resource-dependence theory with the institutional theory demonstrating that organisational responses might be proactive or even strategic, depending on various contingencies in the organisation and the environment. She identifies five types of strategic responses: acquiescence (obeying rules and institutional models), compromise (balancing or negotiating with the expectations of multiple stakeholders), avoidance (changing domain or loosening institutional attachment), defiance (ignoring or contesting rules and values), and manipulation (shaping values or dominating constituents). Responses will depend on the ability and willingness of the firm to select an appropriate response. The author identifies five elements that may anticipate companies' responses: cause (why these pressures are being exerted), constituents (who is exerting them), content (what these pressures are), control (how or by what means they are exerted), and context (where they occur).

According to this theoretical framework, companies may ignore rules and the EU objective of a similarly high level of transparency can be at risk. Therefore, more research on the impact of non-financial obligations is necessary.

3.4 Case study design and data analysis

The primary step in our paradigmatic case study design was to define a research protocol to ensure reliability (Yin 2014). Our research protocol permits us to determine focal elements of the analysis, including the identification of people in the company to interview, the length of interviews and the questions. We conducted semi-structured interviews (Qu and Dumay 2011) with two auditors of the IA function, one of the Independent members of the board of directors (BoD) and one of the Executive Member of the BoD. Field interviews are indicated by Oliver (1991) as a tool for identifying institutional antecedents. We organized two rounds of questions at one year distance. Questions mainly explored three aspects:

- the role of the people interviewed;
- the company's vision, mission, objectives and strategy;
- the perceived external pressures toward the adoption and reporting of CSR practices and
- the activities and procedures started when the legislation came into force and role that corporate governance is expected to play.

Additionally, we explored the 2017 and 2018 Biesse Sustainability Reports, their Industry Plan, the latest annual report and *Corporate Journal*, the BG's official magazine addressed to the corporate world, in which a new section on non-financial information has been recently added. The table below provides a detailed list of the documents collected and people interviewed (Tab. I).

Table I. Sources used for developing the study

Source	BG	Code
Documents		
	Annual Report 2017	A1
	Sustainability Report 2017	A2
	Sustainability Report 2018	A3
	Industrial Plan (2018-2020)	A4
	Corporate Journal	A5
Interviews		
	Internal Auditor 1	B1
	Internal Auditor 2	B2
	Independent Member of BoD	B3
	Executive Member of BoD	B4

The data analysis was developed through the support of institutional theory (Scott 1987) as a theoretical framework. All data and results were discussed among the authors to guarantee investigator triangulation and with the interviewees to achieve validation of the results (Yin 2014). However, the analytical approach based on narrative analysis and qualitative data collection draws on an interpretivist approach (Crane 1999), which is considered appropriate for studying evolving organisational practices (Higgins et al. 2014) and new reporting practices (Stubbs and Higgins 2014).

4. Findings and Discussion

4.1. Company's orientation toward sustainability before the Directive

BG never disclosed ESG information in a structured manner before the introduction of the Legislative Decree N. 254/2016: *"The word sustainability had never been used in the company before the Decree"* (B2). Several initiatives were present but isolated and related to specific policies (e.g., safety policies). The company has always been concerned about the social impacts of its activities, in particular regarding new investment projects because *"Biesse cannot disregard the territory in which it operates and the people they work with"* (B3).

All four divisions of Biesse have their headquarters and main production plants in the same province (Pesaro), where 60% of the total workforce is employed (A1; A3) and from which several talents are hired. *"Employees and their families are important...because they allow the company to innovate...they form part of the Biesse family"* (A2). Good relations with employees and trade unions are considered fundamental to excel. There is also a sort of socio-emotional attachment (Gomez-Mejia et al. 2007) to employees as demonstrated by the latest corporate celebration for all employees and their families that was organized for the company founder's 80th birthday. *"It was a way to thank all those who, with their work, dedication and commitment, have made the Group a major global player"* (A2). Moreover, *"the Group listens to the requests of local organisations, like sport and cultural associations, charities and not-for-profit organisations and collaborates with them in support of local communities"* (A3). As suggested by Marquis and Battilana (2009) and Greenwood et al. (2010), when a firm's headquarters and its nearby factories are embedded in local communities, they are especially motivated to preserve constructive relationships with such communities, and the case of Biesse seems to confirm this attitude.

The company Board conceived the new reporting obligation as *"an opportunity to enhance the social-environmental sensitivity and company care for the local community that has historically characterised the group; in other terms, it was an opportunity to put things into place that already existed"* (B2). In the past, the company never felt the need to disclose a sustainability report because they consider the production processes "clean", not capable to harm the environment: *"the company never had problems, not even in our foreign subsidiaries as we adopt Italian production standards. Thus, the company never felt the need to justify its actions"* (B1). Document search revealed that no NGOs or eco-friendly organisations have ever raised issues in newspapers or other contexts. As one interviewee said: *"Biesse operates in a sector characterised by a low, critical environmental impact and this avoids criticisms raised by NGOs and citizens. Thus we do not have stakeholders' pressures like other companies"*. A similar situation applies to BG's competitors who do not prepare a sustainability report.

However, in the Chinese and Indian subsidiaries, there were already social activities in place before the Directive came into force. Since 2013, a CSR manager has been in charge in the Indian factory, due to local government regulations (the Indian Companies Act, Section 135), prescribing a mandatory CSR spend 2% of average net profits for all companies meeting specified financial thresholds in terms of turnover and net profit. The subsidiary was thus required to create a committee to allocate and audit the money for different CSR purposes and issue an annual report on the various CSR activities to be published on the company website. Currently, such initiatives are included in the BG sustainability report (A2; A3). Also, in both China and India factories, BG implemented the lean production and kaizen philosophy, aimed at reducing waste and minimising the consumption of resources.

According to Doshi et al. (2013), different organisational responses may emerge inside complex organisations on an international scale—such as BG—due to different institutional pressures faced by its units and depending on local embeddedness and organisational size. In the case of the BG, local embeddedness and the concentration of factories in one specific area of Italy drove the organisation toward “implicit” CSR strategies in favour of local communities but did not affect ESG reporting. The Indian unit indeed started disclosing ESG information because of mandatory obligations, independently from the parent company.

The first impression is that BG’s approach towards ESG reporting has been reactive, i.e., a reaction to the legislation (a coercive pressure) that introduced a challenge (table II). As B1 says: “*The law talks about strategies, objectives, budgets, so company documents, like the industrial plan, must now include these issues. Before the decree, there were only two slides on sustainability*”. The company had to introduce some changes, but it also intends to “*set up the necessary steps to develop a sustainability strategy, which is currently in its infancy, in the future*” (B1).

The coercive pressure exercised by the law did not occur in a void. It interacted with normative mechanisms linked to pre-existing company values stemming from the controlling family and shared by the top management. BG was willing to prepare an ad hoc report because sustainability is in line with top management’s and company owners’ sensitivity towards the local territory as found in many other family businesses in Italy and abroad (Del Baldo 2012; Nekhili et al. 2017; Gomez-Mejia et al. 2007).

Table II. Pressures on reporting ESG information

	Coercive	Normative	Mimetic
Reporting or not	Country legislation in India: obligation for a CSR manager and CSR report New EU legislation: BG has to report on ESG aspects.	Expectations and beliefs of BG’s ownership and management: alignment between the informal sustainability orientation of the family business, the business model and values-set shared by the top management.	BG direct competitors (SCM in Italy and Homag in Germany) do not issue an ESG report.

4.2. The preparation and use of the sustainability report

BG’s board charged the Chief Internal Auditor with guiding the company in the process of internal reflection and change required by the new provision. The choice of the IA refers to the wider cultural belief of its autonomy and professionalism and was linked to the will of the family controlling the board to appoint a guaranteed figure such as the IA.

The IA had to take several choices because the Italian law does not set reporting criteria: national and international standards or frameworks can be chosen, nor does the law impose the creation of ad hoc committees within the board or procedures inside organisations. “*We started looking at what listed and unlisted companies that manufacture similar goods disclose about ESG aspects... We also had meetings with accountancy and auditing firms. In the end, we perceived that preparing a sustainability report according to GRI standards was the best solution (B1)*.” So, analysis of other

companies' behaviour and discussions with the auditing community and an external consulting company (i.e., normative influence) induced the choice of the IA and the board on how to become compliant with the new regulation (Table III). Another interviewee confirms this: *"We opted for GRI standards because suggested by the external consultant and adopted by other companies that manufacture machine tools"* (B2). Preference for the GRI framework is actually large widespread (EY 2016).

Table III. Pressure affecting the structure of ESG reporting

	Coercive	Normative	Mimetic
How companies report ESG information	The Board entrusted the IA to guide the preparation of the report.	Consultants and normative rules stemming from the professional audit culture led the company to opt for GRI guidelines.	BG perceived sustainability reporting as the best practice to dialogue with stakeholders.

Evidence indicate that BG did not make the minimum effort to obey the regulation (e.g. including ESG data in the management report following an Italian reporting standard) but it started a more challenging and extensive project: drafting a sustainability report according to international standards, whose implementation solicits for strategic development (a sort of over implementation compared to law provisions). *"With our first sustainability report we responded to a legal obligation, but more importantly, we have triggered an internal and external process of active reflection on the issues of sustainability. This first step allowed us to define a new sustainability journey and objectives related to the short and long term"* (B3).

Moreover, BG understood the potential benefits of using a specific report to communicate that it cares about society and the environment. One interviewee said: *"The importance of sustainability aspects is going to grow as investors are more and more interested. We used to present our annual report and discuss financial data with investors, but now, we can arrange ad hoc meetings with Social Responsible Investment funds"* (B1).

Looking at the content of the sustainability report (A2), it emerges that the preferred interlocutors are investors, customers and employees. This is confirmed by the interviews. *"We were already excellent at communicating our financial data and technical projects ... now we can tell investors our policies of gas emissions reduction and environmental protection"* (B2). The report is mailed to some very important customers *"so having a formalised sustainability strategy and communicating it can become an element of competitiveness"* (B1). In addition, the report provides a more comprehensive picture of BG to employees, *"allowing to attract young talents"* (B3).

In the second round of interviews, the company's awareness of the importance of communicating CSR strategies in a structured manner became more evident. *"Now, the situation is different for two main reasons: 1) there are several leading customers, like Ikea, who exert pressure, asking us to certify the sustainability of the supply chain and even medium-sized customers are starting to approach the issue of sustainability; 2) there are more traditional investors (not necessarily SRI funds) who ask 'how green are you?'"* (B2). So, while BG mainly conformed to the law in the first

year, during the second year it matured the idea of ESG reporting as a tool to acquire eligible external tangible and intangible resources (financial resources, talents and reputation). This indicates that there is not a unique permanent corporate response to external pressures. In BG, a mix of typologies among the responses identified by Oliver (1991) coexist and changed over time (Table IV).

Table IV. Mixed and changing BG response

Strategies	Tactics	First Year NF implementation	Second Year NF implementation
Acquiesce			
Imitate	Mimicking institutional models	Yes/no	No
Comply	Obeying rules and accepting norms	Yes (in Italy and India)	Not only (“over-implementation” of the law provision)
Compromise			
Balance	Balancing the expectations of multiple constituents	No	Yes - stakeholders engagement based on questionnaires and interviews aimed at understanding and balancing constituents’ expectations
Bargain	Negotiating with institutional stakeholders	No	Yes - starting negotiating with some institutional investors and clients’ specific requests and provisions
Manipulate			
Control	Dominating institutional constituents and processes	No	Yes BG started to make specific efforts to influence external constituents strengthening communication tools (i.e., the Corporate Journal) and participating in national and international competitions (i.e., Best Performance Award 2018; Deloitte “Best Managed Companies”)

During the two years of observation, BG shifted from passive (acquiesce) to increasingly active responses (manipulation) to institutional pressures. “Avoid” and “defy” strategies are missing as BG welcomed ESG reporting and had no reasons to adopt these two responses.

In the first phase, acquiesce manifested through a conformity tactic (it fulfilled the regulatory obligation) and a mimetic behaviour emerged in defining the format and content of reporting (following what other companies do). However, the strategy was not of “pure” acquiesce because the IA launched new processes and communication activities that led to a strategy of compromise in the second year. This is signalled by the IA’s goal to *“balance and negotiate stakeholders’ expectations when defining the prioritisation of their requirements in terms of decision-making”* (B3). In particular, the IA activated multiple initiatives to address the expectations of constituents by refining the materiality matrix and helped other functions to negotiate with external requests (e.g. the production department in negotiating with some customers’ requests).

More recently, BG seems to be oriented towards a manipulation strategy based on extensive communication with external subjects and participation to some competitions for “the best

performing company” awards. In this case, manipulation is not an attempt to change stakeholders’ expectation. It cannot be considered a form of decoupling because these initiatives aim to generate new strategic opportunities for the well-being of the organisation and the socio-economic context where it is embedded (McGuire et al. 2012; Garcia-Torea et al. 2016a; Nekhili et al. 2017).

4.3. The role of the IA

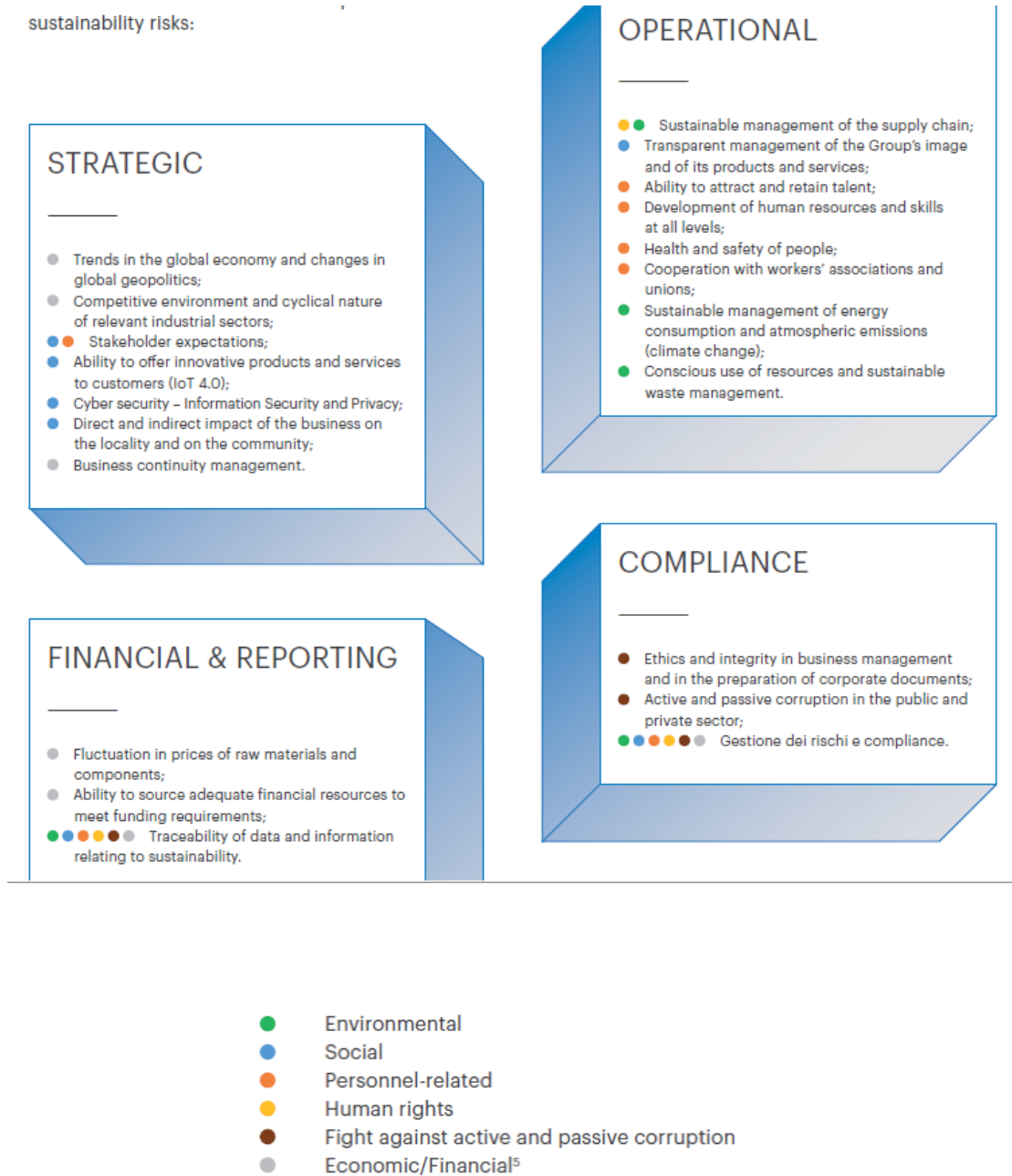
The key role of the IA emerges from the following words: *“The IA function had a leading and “structural” role because it kept control of the whole implementing process, since its inception and during all phases: from ESG reporting methodology identification (in collaboration with the consulting firm) to its sharing among departments and units (in collaboration with the CFO), stakeholder mapping (with corporate managers), information gathering (with the support of various corporate departments), and the drafting of the sustainability report”* (B2). The marketing and communication departments played a complementary role. *“The marketing office is most actively engaged in conveying CSR outside the Group, while the IA function disseminates CSR within the company. Moreover, the IA is in charge of verifying the reliability of quantitative and qualitative ESG data collected from organisational units”* (B1).

The first and most time-consuming activity of the IA was the organisation of internal meetings with managers to explain the concept of sustainability and create the materiality matrix based on their perceptions. During this phase, the IA served as the “facilitator” of the whole process. As B2 says: *“The internal auditor had a technical and very supportive role. All functions participated in the drafting of the materiality matrix, although some functions were more active than others (B1). Managers did not hinder the process because “we jointly decided what to put in the sustainability report. We aimed to mirror what the company does in the document. The attempt to transform the report into a marketing tool that emphasised our product innovation was stopped”* (B1).

After the publication of the 2017 sustainability reports, two initiatives were launched by the IA to improve the materiality matrix (this is also reported in A3), strengthen stakeholder engagement and assess possible gaps affecting the first sustainability report. *“A questionnaire was sent by e-mail to more than a hundred external stakeholders to ask which aspects or issues of sustainability they consider most relevant and what they would like to know about Biesse. Then, 35 company managers were interviewed to refine the materiality matrix”* (B2). Involvement of Biesse managers is held as necessary because *“sustainability themes cover many areas and they directly or indirectly impact all company functions”* (B3). Both the questionnaire and interviews allowed the IA to actively sensitize the control and risk committee and the board of directors to reflect on how CSR should be integrated into the three-year strategic plan.

The second key activity performed by the IA was the creation of the first map of company risks related to sustainability, which started being included in the Enterprise Risk Management process. *“Biesse already adopted an ERM model in 2012. Starting from 2017, the management and monitoring of risks linked to sustainability became an integral part of the business strategy and the Group’s approach to sustainability”* (B1), which led to the preparation of a box (Figure I), where stakeholders can find the relationship between identified risk factors and areas of sustainability.

Figure I-Sustainability risks in BG



In the same year, BG also adopted an Anti-corruption Code of Conduct (B1) to strengthen the group's commitment to counter corruption, which is one of the key matters for which the Directive requires disclosure. This Code is in addition to the previous Code of Conduct introduced in 2010 and sets the rules of business conduct that all employees must observe to ensure compliance with anti-corruption regulations in force.

To carry out all previous activities, the structure of the IA function had to be strengthened. A new office (within the IA function) with dedicated personnel was created to manage all procedures related to the preparation of the sustainability report. This office is in charge of managing compliance and entrusting the supervision of sustainability issues to the Control and Risk Committee. There isn't a Sustainability Committee within the board. The IA periodically met the Risk and Control Committee to submit technical proposals, which were then approved by the board.

Lastly, the IA is also the subject that guarantees the reliability of data, as it supervises the company's internal processes that “verify” data together with the statutory auditing company (as reported in the sustainability report itself -B1). The IA defines the procedures to collect quantitative and qualitative ESG data from all 39 companies of the Group and performs specific checkings).

From the second year of reporting, the IA experienced a very proactive role, updating and simplifying the language of the GRI guidelines whose technicalities created difficulties for the operators in the data collection phase. Also, the IA designed projects and procedures tailored to specific functions aimed at increasing the reliability and timeliness of collection (B1) like the adoption of new software to track the training hours for all 4000 employees.

The IA did not act as an inspector, but added value through active support in management processes as described by Melville (2003). The IA aligns with traditional expectations stemming from the audit profession and academia (Ackers 2015; Holt 2012) because it contributed to the reliability of ESG information and contributed to anticorruption policies (Cardoni et al., 2020). However, it also had a supporting and teaching role, providing technical advice and favouring discussions within the company (Sarens and De Beelde 2006). It was the promoter of some important new procedures concerning the preparation of the sustainability report, contributed to homogenising different “languages” adopted in different units sparse throughout the world and launched some activities of stakeholder engagement that prompt the company to shift from a passive to a more proactive response towards pressures for ESG reporting.

Using the sustainability report to describe BS did not disturb the existing culture and routines. As the CEO declared in the Sustainability report (A1): *“We started an internal and external process of reflection on the themes of sustainability taking a current picture of our organisation.”* In organisational terms, constituents’ demands were accepted and internalised within the organisation as it was and the IA acted as the guide toward change instead of generating inertia (Burns and Scapens 2000; Tsamenyi et al. 2006).

5. Conclusions, limitations and future research

Our paper analyses how a company that never disclosed ESG information reacted to the advent of the EU Directive 95/2014 in terms of reporting strategy and corporate governance practices.

Firstly, we discovered that the company's reaction is connected to different pressures and not only to what exercised by the legislative force. When in line with existing organisational values and practices shared by BG’s top management, different constituents’ demands (regulation, employees, local communities, investors, competitors, other listed companies, auditing profession and the family ownership) for sustainability are accepted and this may lead to a multiplicity of responses to external pressures. Thus, our findings go beyond prior studies by contrasting the idea of a unique response (i.e., legislation may not generate uniformity in companies' behaviour) and confirm the benefits of using institutional and resource dependence theories together as they help to identify a range of strategic and tactical responses to the institutional environment.

Thanks to the longitudinal observation, we found that the “cause” of BG's behaviour changed from pressures linked to the legitimacy, social and cultural conditions in the first year, to reasons of efficiency or economic conditions in the second year of the application. Also, the "constituents" exercising pressures changed through time: first, the State and practitioners guided the adoption of ESG reporting, then other stakeholders like investors defined the direction of change. In terms of requirements the organisation has to conform to (“content”), we emphasise the consistency with organisational goals while concerning the way institutional pressures are exerted (“control”), we found that legal enforcement linked to the legislation was integrated by professional norms. Finally,

referring to the environmental context within which institutional pressures were exerted, we retrieved uncertainty and interconnectedness as relevant factors.

A second important result stemming from the case study is that a legislative requirement can become an opportunity. Despite being novel in sustainability reporting, BG complied with the law and continued to develop internal processes to improve its relations with external subjects that hold key resources. BG achieved greater strategical awareness deriving from the process of setting the sustainability report in place.

Lastly, the case study indicates that the IA function may emerge as a key implementing actor of sustainability culture despite the absence of regulations and common beliefs that attribute to IA such a role. The IA figure is usually associated to the assurance of reports, while our case study suggests that the advent of regulation started an unanticipated change in the IA function even if there were not many external pressures toward this option. Thus, institutional theory should integrate the analysis of internal organisational dynamics to better predict company behaviour.

The limitations of this paper derive from the analysis of one case study, as a result, we suggest referring to an analytic generalisation of the results (Yin 2014). Future research might, therefore, extend the analysis to other Italian and international companies to establish a real understanding of the impact of regulation on non-financial reporting and company governance practices. Thus, we set in motion a call for academic communities to verify the ESG rules that have emerged from the case study analysis in the international scenario.

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