CONNECTIVITY AND ANNUAL REPORT: A MODEL OF ANALYSIS

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Abstract

Stakeholder information on sustainability is becoming increasingly important at the international level. Following the issuance of international sustainability standards by the International Sustainability Standards Board, ISSB (IFRS Sustainability Standards), and European Sustainability Reporting Standards (ESRS) by the European Financial Reporting Advisory Group (EFRAG), there is a focus on how these standards relate to financial standards (IFRS). Greater attention is being given to their connectivity, recognizing that sustainability information often complements and anticipates the effects of financial information in the medium to long term.

Studies refer to connectivity in information (reports) to mean the connection of information on strategy, business model, risks, and opportunities to metrics and targets and financial statements information via adherence to the principles of coherence, complementarity, and consistency of data, assumptions, and qualitative information (EFRAG Secretariat, 2024).

The document that encompasses sustainability and financial information is the annual report, which includes various documents such as the sustainability report and the financial statements. The benefits of appropriate connectivity between the documents comprising the annual report are numerous for both the company and stakeholders. Connectivity means coherence of information across documents,

reconciliation of values reported, complementarity of information, creation of links between documents, and coordinated analysis of the same topic from various perspectives.

Well-structured and implemented connectivity can thus lead to more effective corporate communication, making the company's value-creation communication more understandable and complete. From this perspective, connectivity should help avoid duplication or information gaps, reducing greenwashing situations. Reconciling sustainability and financial information should provide significant contributions in this regard.

Thus, there is a need for an appropriate conceptual framework to structure how connectivity should be achieved. This provides a tool for researchers and stakeholders to evaluate connectivity and for companies to improve their external communication.

The objective of this research is to propose a model that defines the parameters to evaluate the degree of connectivity in the information provided by companies concerning sustainability and financial information.

Currently, there is a lack of contributions in this area. Existing studies are limited and primarily focused on more specific aspects. Current research is more focused on analyzing connectivity concerning environmental risks in financial statements.

In a study, EFRAG Secretariat (2023) highlighted that investments and commitments related to environmental issues are often not reflected in financial statements, and sustainability information is challenging to reconcile with financial information. Forvis Mazars (2024) examined the financial statements of 72 companies, noting that about one-third discuss the impacts of environmental issues on financial items, but only a minority reference their contributions to carbon neutrality in financial statements.

Given the need for a study that systematically analyzes connectivity, a model is proposed that applies to public information provided by a sample of listed companies, starting from ESRS standards and extending to IFRS standards. The aim is to verify areas of commonality between the required information and different presentation methods, as well as where ESRS-required information impacts or could impact financial information.

The starting point for the content analysis is the information required by the ESRS and the three possible types of links identified between this information and financial information: direct link, where sustainability information is also quantitatively presented in financial statements; indirect link, where connecting information is only partially provided in financial statements; and other forms of link, such as the potential impacts of environmental variables on the business. Identifying possible types of links, the study will assign a score to evaluate the usefulness or complexity this link creates for stakeholders.

It will also highlight areas most impacted by voluntary connectivity today to preview which IFRS might require greater attention and possibly some modifications in the future.

The complexity of the research arises from the numerous areas impacted by connectivity: from business models to strategies, from the valuation of tangible and intangible assets in terms of amortization and impairment to revenue segmentation, from the presentation of human capital data to the respect for human rights, to governance.

When the ESRS standards come into force, the model can be tested on the annual reports of companies. In any case, this theoretical model is designed to evaluate whether financial statement readers can objectively assess the level of connectivity by companies and thus derive the greatest possible benefit from the presented environmental, social, and governance (ESG) data.

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