

Non-Financial Risk Disclosure: Evidence from the Reporting Practices of Listed European Companies

Research Objective and Methodology

Phase II of the research project titled “*Fostering sustainability mindset: How non-financial disclosure and corporate risk assessment may drive ESG value creation*” (prot. nr. 2022CTBNRN, which received funding from the European Union Next-GenerationEU - National Recovery and Resilience Plan (NRRP) – MISSION 4 COMPONENT 2, INVESTIMENT 1.1 *Fondo per il Programma Nazionale di Ricerca e Progetti di Rilevante Interesse Nazionale* (PRIN) – CUP N. H53D23002380006) was dedicated to an empirical analysis of listed European companies’ non-financial risk reporting practices. The objective of this examination was to assess the impact of the Non-Financial Reporting Directive (NFRD) (Directive 2014/95/EU) on the volume and quality of the non-financial risk information disclosed by firms within the scope of such Directive.

Our analysis focused on the companies included within the STOXX Europe 600 index, which gathers the 600 largest European companies by market capitalisation. Data were collected by inspecting the content of the top 300 non-financial firms’ annual reports covering the 2016, 2017, 2019, and 2023 accounting periods. A comparison between the contents of non-financial risk disclosures in the 2016 and 2017 reports allowed us to evaluate the immediate impact of the NFRD, while extending the examination to the 2019 and 2023 periods enabled us to uncover and highlight any longer-term effects of such Directive. Findings from past research indeed suggest that formal legislative acts such as the NFRD yield benefits over a longer timeframe that are not detectable when adopting a short-term perspective (Traxler *et al.*, 2023). Furthermore, inspecting non-financial risk disclosures found in 2023 annual reports allowed us to assess the current state of non-financial risk reporting practices in anticipation of the 2025 reports, which will be the first ones prepared in

compliance with the requirements of the Corporate Sustainability Reporting Directive (Directive 2022/2464/EU).

To examine and evaluate non-financial risk information in terms of quality and quantity, a quantitative content analysis was performed. This empirical research tool consists in computing the number of sentences devoted to the specific issue under examination and assessing them along a given set of dimensions (see Agostini & Costa, 2017; Costa & Agostini, 2016). To appraise the quantity of non-financial risk disclosure, the number of sentences related to non-financial risks was collected for each annual report considered (in both absolute and relative terms, i.e., in relation to the total number of sentences found in a report), as well as the number of pages dedicated to the discussion of such risks. To assess the quality of non-financial risk information, on the other hand, these sentences were examined according to the category of risks which they address (i.e., environmental, social and employee-related, human rights, or anti-corruption and bribery risks, as envisaged by the NFRD), the temporal orientation of the disclosed information, the disclosure tone used in the sentence (i.e., positive if the sentence addresses an opportunity, negative if it addresses a risk, and neutral if addresses neither of the previous aspects), and the completeness of the disclosed information. Data on the number of tables and pictures related to non-financial risks found in annual reports were also collected to evaluate the intensity with which companies take advantage of visual forms of reporting.

Some Preliminary Results

Our data shows that, since the introduction of the NFRD, the volume of non-financial risk information found in corporate annual reports has more than doubled; this finding is more pronounced when a longer timeframe is considered (3-5 years). Indeed, while a relatively modest increase in the quantity of non-financial risk information can be observed immediately after the entry into force of the Directive, a comparison between the volume of such information found in the 2016 reports and the 2023 ones provides evidence of a tremendous rise in the quantity of non-financial risk disclosure.



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This outcome supports Traxler *et al.* (2023)'s assumption that formal legislations are prone to generating observable effects in both the short and long term. Such a result may also be partially ascribed to growing stakeholder pressures for a higher volume of sustainability disclosure in corporate reports.

Concerning the various categories of risks addressed by the NFRD, firms primarily discuss risks related to the environment (e.g., climate change, water consumption, and biodiversity) and their employees or wider society (e.g., health and safety at work and personnel recruitment and retention); such information makes up roughly 60% of all non-financial risk disclosures found in annual reports. Conversely, risks regarding human rights and anti-corruption and bribery receive noticeably less coverage. As far as the temporal reference of disclosure is concerned, most risk-related sentences are past- and present-oriented, with little room left for forward-looking risk information; companies therefore currently fail to address the future implications of risks and how they may impact value creation. Finally, non-financial risk information tends to be disclosed vaguely, with few details on how the risks under examination could affect the company or the environment/society, and on how the company is managing or intends to manage the consequences of these risks. In most cases, firms additionally forgo providing numerical estimates on the impacts of non-financial risks (e.g., in the form of the amount of resources that the company would need to employ to face the consequences of a negative risk event).

References

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