

Stakeholder activism and corporate accountability

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Three questions:

- Has stakeholder activism had any demonstrable effect on the level and/or nature of corporate accountability?
- Has stakeholder activism had any demonstrable effect on corporate financial performance?
- What is the relationship between stakeholder activism and the wider regulatory environment?

Has stakeholder activism had any demonstrable effect on the level and/or nature of corporate accountability?

Need to situate accounting as a social and political practice, not as being “boring and dull and hence not worthy of further investigation” (Bebbington and Thomas 2007, 40). Often accountancy is seen as being socially neutral, but in reality many in the field, let alone outside it, are very aware of its wider significance – cf journals such as “Accounting, Organisations and Society”.

Social accounting has been around for some time – popular in the 1970s, politically unpopular in the 1980s, resurgent since the mid 1990s. Link to changes in nature of CSR more generally.

One strand of argument would suggest that social accounting is beneficial to corporations because it offers enhanced means of organisational risk governance, thereby improving the extent of corporate accountability. For instance Bebbington and Thomas (2007) argue that SEAAR (social and environmental accounting, auditing and reporting) makes social and environmental risks more apparent, and can challenge expert-based approaches to decision making: “the techniques of SEAAR can make risks more visible, and in so doing create a basis for the governance of those risks... In essence, new forms of accounting create a basis for new forms of accountability” (p 50).

Similarly organisations such as CORE (the Corporate Responsibility Coalition) campaign for mandatory reporting of social and environmental indicators of performance; an expanded duty of care on directors to include care for society and the environment; and foreign direct liability – enabling communities overseas to seek redress in UK courts. Underpinning this strategy is the view that activism can improve accountability. Other

examples would include the Global Reporting Initiative and AccountAbility's AA1000. The latter has three principles:

- Materiality – assurance provider has to state whether it has included sufficient information to enable stakeholders to make informed judgements.
- Completeness – assurance provider should evaluate the extent to which it can identify and understand material aspects of performance [a measure of the “degree of knowability”].
- Responsiveness – assurance provider has to evaluate whether it has responded to stakeholder concerns and adequately communicated those responses.

A contrary view would hold that current forms of reporting offer little opportunity to facilitate action by organisational stakeholders, as they are not really genuine exercises in accountability. For example Cooper and Owen (2007, 653) examined “whether stakeholders are able to enter into some form of purposeful communicative action with corporations [and] the potential for new corporate environmental and social disclosure initiatives to enhance stakeholder accountability via empowerment”. They analysed 15 reports short listed for the 2003 ACCA (Association of Chartered Certified Accountants) UK Sustainability Reporting Awards Scheme (ie leading edge companies).

Structures identified frequently included the incorporation of external organisations – eg BT has 15-member Stakeholder Advisory Panel (of whom 12 are external) and an Independent Advisory Panel (4 external members). The former meets twice annually to share insights into societal trends and expectations, the latter advises on the development of the company's external reporting procedures.

But how much real empowerment has taken place?

- External members are typically appointed by management not elected from those they are held to be “representing”.
- External members are typically playing a consultative not strategic role.
- The majority of reports examined conceived the relationship as being provision of assurance by the advisory group to corporate management, not to wider stakeholders – “the assurance provider is appointed by corporate management and, if they report to anyone, report to the same constituency” (p 657).

Conclusion (p 658): “the rhetoric within these reports provides very little to substantiate claims of enhanced accountability”.

Others in the social accounting field share this outlook: eg Gray (2001, 2006) argues that over thirty years, social accounting has failed to learn from the past, and that it is not sufficiently challenging. He identifies three approaches to social, environmental and sustainability reporting: managerialist, “business-as-(almost) usual”; triple bottom line, “there is a common ground”; and ecologically/eco-justice informed. He concludes that the former is prevalent.

Has stakeholder activism had any demonstrable effect upon corporate financial performance?

How to measure this relationship? At least three possible routes:

- Through statistical analysis of a range of companies.
- Through statistical analysis of investor/investment performance.
- Through firm-specific case-study research.

An example of the first approach would be Clark et al (2008). They analysed social and environmental resolutions brought by the Interfaith Centre for Corporate Responsibility in the USA from 2001 to 2004, and related the volume of these to a) Credit Suisse Holt database on corporate financial performance and b) Innovest database on corporate environmental performance. ICCR includes religious organisations, foundations, charities and some pension funds, with an asset base of \$120bn in 2005. Partner organisations seek investment decisions favouring long-term welfare, elimination of sweatshops, end to debt obligations of poorest countries, and reversal of global warming. US regulatory context limits resolutions to shareholder meetings: SEC rules prohibit anything concerned with “ordinary management”, and re-submission in subsequent years is not allowed if it fails to reach threshold level of support on previous occasion.

Key findings:

- Resolutions were spread across range of companies, with only a few targeted by multiple resolutions.
- Firms at lowest range of financial performance range attracted the most resolutions, so that social investors were acting like mainstream investors.
- Based on impact in year after a resolution was submitted, resolutions had a neutral impact on environmental performance.

Hence: “the corporation is not always responsive to social activist shareholder resolutions”.

But:

- Is a simple count of the number resolutions submitted adequate here? What about their content, impact, etc?
- Innovest database utilises interviews with corporate executives (in part) under four headings – profit opportunity, risk improvement, management performance, environmental strategy. Many of these are long term yet methodology related resolution to change in index in subsequent year.

Further, few companies actually collect metrics to demonstrate the value of CSR to corporate reputation – in other words they don’t know/cannot show how CSR influences any aspect of their external image, let alone financial performance. Oft-proclaimed benefits of CSR include consumer preference, investment openings, employee motivation, enhanced innovation, and reputational risk reduction. Yet few firms have developed metrics to assess the consequences of CSR upon their core businesses. One

study of the top 150 companies in the FTSE4Good concluded that only 20 of these (mostly extractive, telecommunications and to a lesser extent utilities firms) were able to evaluate how their CSR objectives and statements affected other aspects of business performance (Knox et al 2005). Exception here = BT, which claims to know that CSR activities account for at least 25 per cent of the dimensions that drive customer satisfaction and the company's reputation (WEF 2004).

Some CSR practitioners are acutely aware that the process of defining new ways of measuring (and thereby managing) corporate social and environmental responsibility is at one and the same time a methodological challenge and a political issue. This interviewee for example reflected as follows:

From my point of view responsibility is to do with the assessment of impact but a lot of the social stuff seems to me to be ill thought through. The point about responsibility is about boundaries, it's about what is fair and equitable. Something I have been looking at is what is responsibility and what is a burden and I don't think anyone has got into that space. What is a brand? What is trust? How do you quantify that? We don't have the tools to do that yet.

Equally, it is instructive to ask what corporate managers think they are seeking to achieve with corporate responsibility programmes. For example McKinsey (2007) surveyed 721 corporate executives world wide. In response to the question "In addition to the social benefits of your company's corporate philanthropy programmes, which, if any, of the following business goals does your company try to reach with these programmes" (multiple answers possible):

- Enhance corporate reputation and/or brand – 70%
- Build employee and/or leadership capabilities/skills – 44%
- Improve employee recruitment and/or retention – 42%
- Differentiate company from competitors – 38%
- Manage current and/or future risk – 19%
- Build knowledge about potential new products/markets – 16%
- None – 12%

Survey also found that companies are addressing issues through CR programmes that are different to those expected to influence the business the most over the next five years. Key issues for future = environmental concern, including climate change; health care/benefits for employees; data security. Key issues for CR programmes = education, community, economic development. Assessment of effectiveness of CR – "To what extent are your CR programmes effective in meeting overall social goals?":

- Extremely/very – 20%
- Somewhat – 47%
- Slightly/not at all – 23%
- Don't know – 10%

Second approach would explore investment performance. Key question here would be nature of the relationship between financial investment community and the companies in which it invests. Clark and Hebb (2004) analysed two cases: UK Universities

Superannuation Scheme (USS) and California Public Employees Retirement Scheme (CalPERS), concluding that financial investors were driving higher standards of corporate responsibility. There is however much evidence to the contrary on this point. For instance a World Economic Forum report:

“Even where there is a growing belief that social and environmental issues do, should or could count, the fact is that most analysts and fund managers do not take such factors adequately into account. This fact is rooted in short term horizons dominating today’s financial markets, and associated approaches to valuation and profit-taking, and reflects a continued resistance to mainstreaming responsible investment.” (WEF 2005, 16).

Interview evidence with CSR consultancies supports this view:

“The investment community hasn’t actually got around to talking about what I would describe as the pluses of CSR. So they don’t look at what a company is doing in exploiting its CSR credentials. The level of understanding in the City [of London] doesn’t go so far. The push in the investment community if there is any at all is coming from the buy-side. What it hasn’t percolated into at all is the sale side of the brokerage houses and people writing investment notes. Because they are short term in what they produce, they have no interest in CSR.”

So: how does stakeholder activism affect investment performance and investor preference? UNEPFI (2007) survey of work on this subject – reviewed both academic and broker studies. Distinguished:

- First generation - negative screening, excluding sectors based on ethical criteria.
- Second generation – positive screening – best-in-class approach, selecting top performers within permitted sectors.
- Contemporary belief that ESG can enhance investment performance. UNEPFI Asset Management WG established 2003 to understand how ESG factors affect investment value, and techniques for their integration into investment processes.

Covered 20 academic studies (eg “is it better to be naughty or nice?” “saint or sinner?”): half reported a positive relationship between ESG factors and portfolio performance, seven a neutral effect and three a negative association. Goal of most of these studies was to compare conventional with SRI fund-management strategies. Also covered 10 broker reports, mostly thematic, largely concerned with impacts of climate change. Seven of these found a neutral relationship, three a positive. Concluded (p 8) that “more rigorous qualitative ESG research is vital to improve the comparability of ESG criteria with traditional financial criteria” and that “the short-term mindset of many in the financial world is highly incompatible with the long-term horizon necessary to integrate ESG factors more effectively and for investors to act more responsibly”.

Nature of ESG in the studies reviewed here:

- Environmental = sustainability (just two cases).
- Social = focus on the impact of screening out “sin” stocks
- Governance = corporate practices mostly, extent of shareholder activism to a limited extent.

Overall: even in own terms, limited evidence of activism influencing investment performance and investor preference.

Third approach would take up on recommendations of UNEPFI – firm-specific case-study research. This would also need to acknowledge the significance of the CSR consultancy industry. Twenty firms interviewed – see Sadler and Lloyd (2007). It is possible to identify a niche business sector engaged with the promotion of corporate responsibility. Earlier survey (Fernandez Young et al 2003) identified 84 CSR business consultancies in the UK, most of which were formed in the last two decades, and 60 per cent of which had been founded in the previous decade. A smaller cluster established in the 1970s was largely dedicated to environmental issues. The sector ranges from small businesses, often sole consultants, to dedicated branches of much larger firms such as accountants PriceWaterhouse Cooper. Hughes (2006) focused in particular upon the emergence of new ethical trading consultancies now working with the UK food and clothing industries, and explored some of the training practices that have been developed. In so doing, she argued, ethical consultancies were capitalising on the dilemmas of ethical trade, yet it was difficult to envisage how they might escape from this paradox.

Such issues are less of a problem from the outset for the majority of consultancies in the CSR sector more generally, for they emphasise their own profitability over ethics. Together, firms in the CSR consultancy sector offer a bewildering array of services such as sustainable supply chain management, communications strategies, reputational risk management, and legal compliance. A complex network of inter-relationships exists between these consultancies in a field where there are relatively few formal qualifications. Credentials from past business experience are important, but there is little definition of the necessary skill-base, so that CSR consultancy is an activity that is difficult to regulate and/or legislate for. It is an emergent grouping of business practices built on a developing understanding of appropriate forms of corporate behaviour.

Those engaged within this sector see it as an industry in its own right; a clearly-discernible and growing community of practitioners, as described by this interviewee:

“It is quite crowded and it is quite big, which is a good thing. It is growing all the time. You have got a whole range now of consultancies, think tanks, non-profit organisations across Europe, all of whose role is to advance CSR. Some of them are industry clubs, some of them are specialist consulting firms. So there is a whole range of people engaged in this *and it has actually become quite a big industry*, and it has got its own online magazines and so forth. But I think there is a risk that because it is a growth area, it is like the dot-com boom as it was ten years ago, although unlike that I don’t think this one is going to burst. The CSR industry is growing but we have to be careful that we don’t just have a CSR community that talks to itself. The challenge is to mainstream CSR and that means getting people who aren’t in the CSR community into it, and I think the CSR community has had varied success in doing that (emphasis added).”

It is also an industry with specific strengths and weaknesses, even (in the account below) with defined skill shortages as it continues to grow:

“Yes, CSR is almost still a club, you have got a core of say fifty or sixty UK businesses that are really switched on and pro-active. You have got small niche consultancies that do some pretty brilliant and amazing things. You have got the interest in the PWCs, the KPMGs, the Ernst and Youngs and the Arthur D Littles and whatever, and then you have other people. You go to the accountability conferences and often it is the same small group of people but it has grown. There is probably a shortage of real talent at the moment. There are people who say that they can do it but there aren't that many who have a lot of experience because it is all so new.”

In these ways therefore, those engaged in the sector clearly see it as a new business field with its own (developing) rules of behaviour.

Good example of case study research = Gouldson et al (2007). Studied six companies, three in UK and three in Sweden. Explored changing approach to environmental risk communication in cases where firms had deliberately entered into dialogue with stakeholders, seeking to create a more open and inclusive approach. Driver was perceived lack of legitimacy (cases included Huntsman Petro-Chemicals Teesside, BP Grangemouth, Swedish nuclear waste company SKB). Issues:

- Management concern that broader public did not share its own “objective” understanding of the scientific evidence.
- Which groups to engage with? Management faced with diverse range of groups.
- How to engage – directly or through the media?

Suggest “j-curve” effect – trust actually diminished at first as company opened-up, then improved beyond initial start point once shared understanding had been established. [question that remains is how to assess the financial effects of this strategy]

What is the relationship between stakeholder activism and the wider regulatory environment?

UK context: debate over Operating and Financial Review (OFR). Proposed in 2002 White Paper “Modernising Company Law”. Two elements:

- “Compulsory” – statements on business, financial position, fair projection of future prospects and events
- “Duty to consider” – additional information necessary to assess corporate performance. Key issue was “materiality” – OFR WG on Materiality reported 2003 supporting broad view, including (eg) effects of environmental change on profitability. Consultation produced 79 responses – business groups argued the proposal unduly extended scope of accountability to wider stakeholders.

DTI draft regulation produced 2004, emphasising primacy of director's judgements and subordinating social and environmental dimensions of performance to financial ones. But in November 2005 Chancellor Gordon Brown, in speech to CBI, announced abolition of OFR, citing “burden of regulation” on business. (FoE took legal action citing lack of consultation – out-of-court settlement, brief consultation, same outcome.)

How to interpret this moment of regulatory review? Cooper and Owen (2007) suggest it shows separation of administrative from institutional reform, concluding (p 664) “It is quite impossible to envisage stakeholder accountability being established in a situation where company directors acknowledge enforceable duties only to shareholders”.

Alternative view: Power (2007). Even though mandatory OFR was abolished, we should not assume a simple binary divide between mandatory and voluntary reporting. Wider corporate governance debates are leading instead:

“the abolition of the OFR as a legal requirement is relatively trivial. The OFR was the outcome of an institutional process, a process that did not stop on 28th November 2005, and in which various transnational organisations have contributed to the increasing normalisation and internalisation of environmental issues.” (p 91)

His conclusion is that narrative reporting has become part of reputational risk management, and that a key concern then becomes whether this results in corporations becoming pre-occupied with how they appear.

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Stakeholder activism and corporate accountability

Has stakeholder activism affected corporate accountability?

- Accounting as a social practice; the return of social accounting
- Social accounting leads to new forms of accountability?
- But how much real empowerment has taken place...?

Has stakeholder activism affected corporate financial performance?

- Analysis of a range of companies – impact of shareholder resolutions on financial and environmental performance.
 - Few companies collect metrics to demonstrate the value of CSR to reputation
 - McKinsey survey – why do firms adopt CR programmes?
- Analysis of investment performance
 - Relationship between investment community and accountability – direction of causation?
 - UNEPFI review – evidence inconclusive
- Firm-specific case study research
 - Significance of CSR consultancy sector
 - Environmental risk management through new communicative strategies

Stakeholder activism and the wider regulatory environment

- UK Operating and Financial Review: mandatory and voluntary reporting