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June 21, 2011 (Tuesday)   55th EOQ Congress

CONCURRENT SESSIONS   **Tuesday 13:30 – 17:30**
KEMPINSKI HOTEL CORVINUS   **Erzsébet tér 7-8, Budapest V.**

SALON REGIOMONTANUS   **Tuesday 15:30 – 17:30**

**15.2. CORPORATE SOCIAL RESPONSIBILITY AND SUSTAINABLE
DEVELOPMENT I.**

Session Chair: *Györgyi Nyikos, Ministry of National Development, Hungary*

16.25   CSR as a Concept with Special Regard to Core Business
Erzsébet Szegedi, Hungarian National Committee for EOQ, Hungary

Szegedi, Erzsébet (Hungary)

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CSR as a Concept With Special Regard to Core Business

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1.   Background

In the fall of 2001, the European Commission published a green paper, entitled „Promoting a European Framework for Corporate Social Responsibility".[1] The green paper's purpose is to promote CSR, both within the member states and internationally. The green paper stated that EU member governments should „focus on putting the proper regulatory or legislative framework in place in order to define a level playing field on the basis of which socially responsible practices can be developed".

The European Commission also published in March 2006 a Communication on CSR entitled „Implementing the Partnership for Growth and Jobs: Making Europe a pole of excellence on CSR". The Communication underlines the potential of CSR to contribute to sustainable development and to the European Growth and Jobs Strategy.[2]

The European Parliament welcomed the Commission Communication's objective to link CSR to the economic, social and environmental aims of the Lisbon Agenda and the trend for larger companies to publish voluntary social and environmental reports in recent years. The Parliament also reminded the Commission to bring forward a proposal on the annual accounts of types of companies which includes requirements for social and environmental reporting alongside financial reporting.

It is also noteworthy that EU-based trans-national companies, multinational enterprises (MNE) with production facilities in third countries have to abide by core ILO standards, social and environmental agreements to achieve worldwide balance between economic growth and environmental standards.

Voluntary activity or regulated by law?

The definition of CSR was formulated in 2001 by European Commission as „CSR is a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis." [3]

This definition has two implications:

1. CSR relates to what enterprises can do in the social and environmental fields over and above what they are required to do by law.

2. Defining CSR as a voluntary concept does not mean that its boundaries are fixed once and for all – regulation and CSR while being mutually exclusive are dynamic and evolving.

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1 COM(2001) 366.

2 COM(2006) 136.

3 COM(2001) 366.

EU has several regulating instruments with implications for all Member States regarding reporting on sustainability information. These instruments are directly in force in all Member States that have to comply with their obligations under the regulation. In turn, the regulations refer to voluntary and mandatory systems with elements of reporting on sustainability information:

- Accounts Modernisation Directive,

- European Pollutant Release and Transfer Register (PRTR),

- Integrated Pollution Prevention and Control Directive (IPPC),

- EU Eco-Management and Audit Scheme (EMAS),

- EU Emission Trading System (ETS).

The EU Accounts Modernisation Directive (2003/51) amended the Accounting Directives and stipulates that from reporting year 2005 onward, European companies must provide a Business Review including non-financial, environmental and social performance indicators, to the extent necessary for an understanding of a company's development, performance or position.

2. Focus on core business, strategic CSR

CSR is an investment that can pay off in the longer term. It can bring advantages, for example in terms of staff retention and recruitment, staff development and motivation, customer loyalty and reduced expenditure on energy. It can increasingly be a source of innovation and it can facilitate access to and sharing of information.

By managing CSR in a more strategic and conscious manner, enterprises can better reap these advantages. CSR is about continuous improvement and should be seen as part of the modern model of business excellence.

Michael E. Porter and Mark R. Kramer proposed a fundamentally new way to look at the relationship between business and society that does not treat corporate growth and social welfare as a zero-sum game. They introduced a framework that individual companies can use to identify the social consequences of their actions; to discover opportunities to benefit society and themselves by strengthening the competitive context in which they operate; to determine which CSR initiatives they should address; and to find the most effective ways of doing so. Perceiving social responsibility as an opportunity rather than as damage control or a PR campaign requires dramatically different thinking[4]

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[4] PORTER, Michael E. – KRAMER, Mark R.: Strategy and Society: The Link Between Competitive Advantage and Corporate Social Responsibility, Harward Business Review, Dec 01, 2006

Stakeholders and their needs

It can be of interest to approach the activities related to CSR from a not too frequently studied point of view: from that of their influence on the stakeholders of the company's core business.: how CSR activities are in line with the company's core business and strategy. Some company activities, e.g. sponsorship, charity not being part of core business, will in this respect be disregarded.

The **main stakeholders** of CSR can be identified as follows:

- **Owners** of the company (with a widening of owners' circle, especially in case of public companies, and with the internationalization of companies, a growing number of people are involved) – a special importance in this respect is to be attributed to making profits, this being the main element of the company's responsibility towards its owners.

- **Employees, workers and their families** – the level and volume of the company's core business is of special importance not as a source of profits here, but as an activity producing ample quantity and quality of sources that make it possible to employ a staff which will be satisfied with their working conditions and salaries, offering at the same time a reasonable stability of employment. The well managed CSR towards this stakeholder group is at the same time the basis of ensuring employee's loyalty and it is an important means of PR as well.

- **Employee's organizations** (including trade ones) – fulfilling their expectations and occasionally their explicit demands can be essential for ensuring a continuous efficiency and productivity of the company; sources for meeting demands are also produced by the company's core activities.

- **The state** – this field of responsibility is not too frequently referred to, though taxing, as well as traceable use of state and international loans and subsidies can be indispensable conditions of future work.

- **The law** – it is the very interest of each company to keep the law; obeying the rules is inevitable e.g. in the fields of technology employed, the quality standards, the environment, the responsibilities towards consumers, business partners, in the distribution of products, product warranties etc.

- **The population** – it is obvious that companies must refrain from disturbing the community of their siege (garbage, poisonous materials, sound effects, etc.); but there are also other important aspects of this type of responsibility: helping the population, serving their interests, non-production investments, social establishments, etc.

- **Natural environment** – the part of environmental protection connected to the core business is the technology employed, the „cleanness" of it; a clean technology is, by the way, usually less expensive for the company in the long run.

- **Public opinion –** the public opinion is formed to a significant extent by the above fields of company responsibility, which are, this way, also parts of the company PR. The core business, on the other hand, is responsible for the product image, too, this way also shaping the opinions on the company. As it profoundly influences the results of the company, forming the public opinion is one of the most important activities of CSR.

At last, those two very important fields of CSR, which are the basic topics of the present lecture (and, consequently, will be discussed in more details):

- **Consumers, end users, customers, buyers**
  - quality and prices, prices and values,
  - true statements, ethics of sales and advertisements, warranties, settlement of claims,
  - quality, quantity and reliability of (product, availability, etc,) information, fair treatment.

- **Suppliers**
  - their treatment as stakeholders, keeping suppliers for long periods, mutually satisfactory prices,
  - ensuring stable qualities, proper quantities,
  - deliveries in time, stable raw material and parts sources – stable and regularly repeated orders,
  - winner-winner game.

If we combine these stakeholders needs with Porter's Value Chain (1985) and take into consideration its improved version prepared by Michael E. Porter and Mark R. Kramer (2006), we will have a good approach to understand the whole concept and spirit behind CSR, being one of the most important aspects of company management recently.
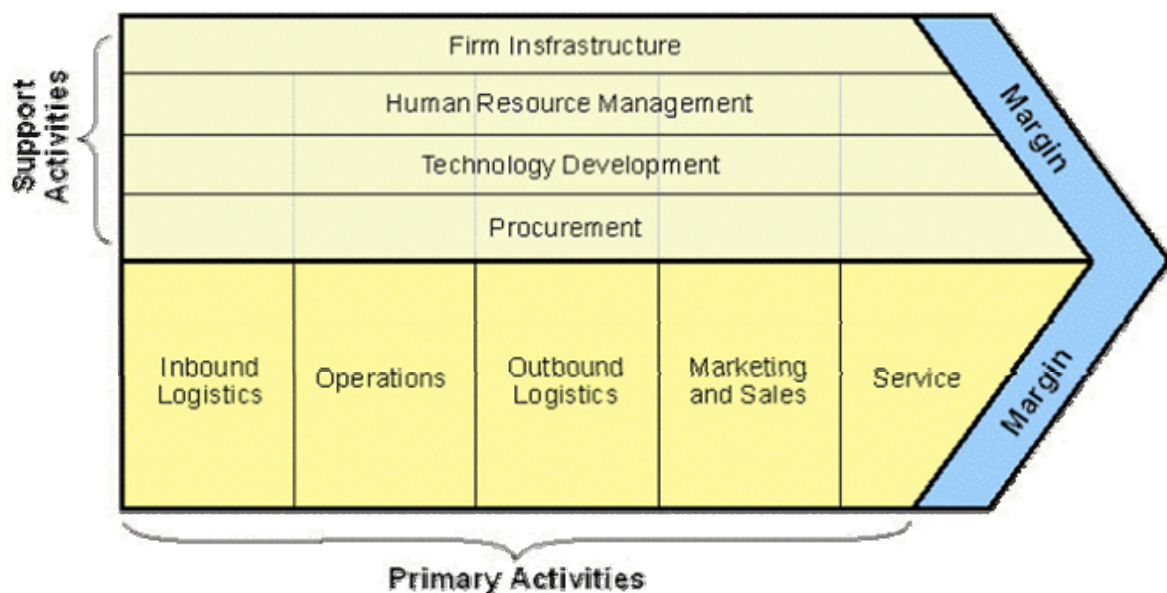
Source: Michael E. Porter (1985)

Supply chain

Supply Chain is the interrelated collection of processes and associated resources that starts with the acquirement of raw material and extends to the delivery of end items to the customer. It includes suppliers, manufacturers, logistics service providers, warehouses, distributors, wholesalers and all other entities that lead up to delivery to the final customer. In a wider perspective it may also include the suppliers to the vendors and the customers of the immediate customers. The supply chain is often restricted and extends from purchasing the finished goods from the manufacturing facilities to supplying the immediate customer.

As part of CSR activities you should think of the following issues:

Procurement:

- recycling,
- conservation of raw materials,
- procurement practices
- bribery,
- child labour.

Inbound logistics:

- transportation impacts,
- emission,
- logging roads.

Operation:

- emission and waste,
- biodiversity and ecological impact,
- energy and water usage,
- hazardous materials,
- worker safety.

Outbound logistics:

- packaging use and disposal,
- transportation impacts.

Marketing and sales:

- responsible advertising and marketing,
  - advertising to children,
- pricing practices
  - price discrimination among customers,
  - anticompetitive pricing practices,
  - pricing policy to the poor
- dealing with customer complaints,

- anti-corruption measures,

- ethical practice, ethics and consumer rights,

- imposing social and environmental requirements on suppliers,

- support of local suppliers,

- timely payment of bills,

- customer retention and satisfaction,

- product safety,

- quality of product/service,

- disclosure of information,

- labelling and packaging,

- fair pricing,

- marketing and advertising

- after-sales service and consumer education,

- transparency of criteria for selecting business partners,

- working and living conditions and human rights issues in developing countries where you may source raw materials.

All the above mentioned issues should be managed when planning companies' activities, communicating with different stakeholders and preparing sustainability or CSR report.

3. Reporting as a tool for communicating with stakeholders

Many initiatives have already been taken in the context of transparency and the call for openness by business. Over the last couple of years there has been an increase in the number and variety of external ratings, rankings and indices that seek to measure corporate sustainability performance and provide information to stakeholders on the performance of companies. Different stakeholders are increasingly relying on these ratings to help inform their decisions (to invest, purchase, work etc.).

3.1 How to measure ESG performance?

Advocates of the triple bottom line argue that since an organization's long term viability is dependent on sustaining "profitability" over all three dimensions, they should be measured, reported, and assessed on a periodic basis, in a manner conceptually similar to the current financial reporting model.

Further, stakeholder groups, such as socially responsible investors, non-governmental organizations, green consumers, and governmental regulators and agencies are increasingly calling for information related to the social and environmental dimensions.

Companies have a hard time defining which topics to include in reporting and setting up appropriate stakeholder processes to define the most relevant topics.

The sustainability information should be placed on the same level as financial information. A move towards integrated reports can contribute to the creation of a sustainable society where shareholders and other stakeholders consider each others' interests.

Especially smaller companies have trouble with data collection and the choice of performance indicators. However, because of the growing number of firms that report, the availability of reporting knowledge and possibilities to learn from others is growing.

Reporting frameworks such as the GRI also try to solve (part of) this obstacle by defining the issues to report on and the indicators that can be used.

Typical indicators regarding ESG issues

Environment

The measures a company can take to mitigate its negative impact on the environment:

- energy efficiency measures,
- increase energy or water conservation,
- less use of pollutants,
- protecting the natural environment,
- maintain biodiversity,
- reduce air and water pollution,
- reduce use of hazardous chemicals,
- reduce waste generation and hazardous waste.

Social issues

How a company treats its **employees.** It includes issues such as:

- recruitment,
- equal opportunity employment,
- work-force diversity and discrimination,
- safe working conditions,
- compensation policies, wages, performance evaluation, motivation system,
- staff training and development;
- health and safety,
- recognition of trade unions,
- human rights issues,
- employee satisfaction;
- he work/life balance (flexible hours, balancing family and work).

The relations between the company and the citizens and **communities** that may be affected by its operations. It includes issues such as:

- human rights, social integration, ethnic tolerance and social cohesion

- dialogue and partnership with potentially affected communities,

- active contribution to community wellbeing, for instance through employee volunteering schemes,

- concentrate on any company supported,

- volunteer activities by owners or employees,

- charitable donations or sponsorships and ways in which the company promotes economic regeneration,

- community healthcare or education,

- quality of life (sports/culture),

- the local infrastructure, security.

3.2 Lessons learned about reporting

The number of companies disclosing information on their ESG performance has grown very significantly in recent years. According to statistics, the global reporting output per year increased from almost zero in 1992 to an expected 4,000 reports in 2010. Despite the financial crisis and the following recession the growth rate of sustainability reporting has slowed only marginally during 2009. This number of 4,000 reports reflects only the number of reports from the larger companies that are „officially" registered.[5]

A growing number of companies use a standardized scheme (framework or guidelines) for reporting. The two most widely used reporting schemes are the G3 Guidelines of the Global Reporting Initiative (GRI) and the United Nations Global Compact Communication on Progress (UNGC COP).

Besides the increasing voluntary uptake of companies to start reporting, legislation and regulation are expected to contribute to this growth as well. In Denmark for example, it is now mandatory for the largest companies to report on CSR in their annual reports, affecting around 1,100 companies.

Due to the lack of mandatory standards, businesses freely pick and choose which characteristics they measure, derive their own metrics and standards for these characteristics, and produce a report that reveals precisely what they wish to disclose.

The depth and quality of this disclosure varies however. Issues relating to reporting social aspects of corporate responsibility generally lag behind the reporting of environmental issues, in terms of both timing and quality.

Especially when competitors are not reporting, companies hesitate providing sensitive information.

A number of leading companies have developed innovative practices for effective ESG disclosure.

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[5] http://www.corporateregister.com

Regulation of assurance is necessary; the status of sustainability KPIs and information should be aligned with the status of financial information and reporting. KPIs that are reported in the annual report should also be subject to an appropriate level of assurance. This will improve the quality of the information and provide investors with confidence in relation to completeness and reliability of disclosures made.

<u>SMEs</u>

CSR as practiced in SMEs is usually less formal and more intuitive than in larger companies. It is often closely tied to the personal and ethical values of the SME owner-manager. As a general rule, the smaller the enterprise the greater the relative importance of personal and ethical values as a driver for CSR. A large proportion of SMEs have always done things that could today be called CSR, even if they do not know or use the term themselves.

CSR in SMEs is less formal and more intuitive than in larger enterprises, but that does not make it less valuable.

The fact that SMEs are an extremely diverse group (size, history, sector, ownership, and so on) calls for a range of different approaches and strategies to encourage the uptake of CSR.

SMEs from the same cluster or sector often face common social and environmental issues. Addressing these issues collectively can reduce the costs of action and result in improvements that an individual SME acting alone cannot achieve.

Large companies may provide guidance to SMEs on how to improve their CSR reporting. A best practice for it can be that the official Spanish Credit Institute partnered with a regional savings bank (Caja Navarra) to promote reporting among SMEs. A simple electronic tool for producing a standardised CSR report was provided to the clients of Caja Navarra. More than 1,100 SMEs prepared their first CSR report as a result of the initiative in 2009.

3.3 Guidelines, standards

Reporting process is a very good opportunity to improve communication with stakeholders.

In case you want to improve your CSR activities in your core business, you should apply different guidelines and standards and look for best practices.

As mentioned earlier the two most widely used reporting schemes are the G3 Guidelines of the Global Reporting Initiative (GRI) and the United Nations Global Compact Communication on Progress (UNGC COP). GRI is especially used by large European companies.

The **Global Reporting Initiative (GRI)** is a network-based organization that pioneered the world's most widely used sustainability reporting framework. GRI is committed to the Framework's continuous improvement and application worldwide. GRI's core goals include the mainstreaming of disclosure on environmental, social and governance performance.[6] Sustainability reports based on the GRI Framework can be used to demonstrate organizational commitment to sustainable development, to compare organizational performance over time, and to measure organizational performance with respect to laws, norms, standards and voluntary initiatives. GRI promotes a standardized approach to reporting to stimulate demand for sustainability information.

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[6] http://www.globalreporting.org/AboutGRI/WhatIsGRI

In March 2011 GRI released G3.1 Guidelines, an update and completion of the third generation (G3) Guidelines. The GRI Guidelines set out Reporting Principles and Performance Indicators for economic, environmental, and social information. A Sector Supplement contains integrated commentary and new Performance Indicators for the sector, ensuring that sustainability reports cover the sector's key issues.

The G4 Sustainability Reporting Guidelines are the fourth generation of Guidelines from GRI. The project is part of GRI's commitment to continuous development of its Guidelines. G4 is planned to be published in 2013. It will be developed using GRI's multi-stakeholder international consultation process.

GRI Sector Supplements are tailored versions of the GRI Guidelines. Sector Supplements help to make sustainability reports more relevant, and easier to produce, and also capture the relevant issues essential to sustainability reporting in a specific sector.

AccountAbility's AA1000 series are principles-based standards to help organisations become more accountable, responsible and sustainable. They address issues affecting governance, business models and organizational strategy, as well as providing operational guidance on sustainability assurance and stakeholder engagement.[7]

- AA1000APS provides a framework for an organisation to identify, prioritise and respond to its sustainability challenges.
- AA1000AS provides a methodology for assurance practitioners to evaluate the nature and extent to which an organisation adheres to the AccountAbility Principles.
- AA1000SES provides a framework to help organisations ensure stakeholder engagement processes are purpose driven, robust and deliver results.

ISO 26000:2010 is intended to assist organizations in contributing to sustainable development. It is intended to encourage them to go beyond legal compliance, recognizing that compliance with law is a fundamental duty of any organization and an essential part of their social responsibility. It is intended to promote common understanding in the field of social responsibility, and to complement other instruments and initiatives for social responsibility.[8]

3.4   Best practices

If you are looking for best practices on a global perspective, you should visit the website of top companies for each of the 19 Supersectors. This could be a valuable list if you want to compare the leaders in your sector in regards to their actions, movement towards sustainability.

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[7] http://www.accountability.org/standards/index.html

[8] http://www.iso.org/iso/catalogue_detail?csnumber=42546

The 2010-2011 Supersector leaders in sustainbility are[9]:

Company name	Supersector
Air France – KLM	Travel & Leisure
AkzoHobel	Chemicals
ANZ Banking Group	Banks
BMW	Automobiles & Parts
EDP Energias de Portugal	Utilities
GPT Group	Real Estate
Investimentos Itau	Financial Services
Lotte Shopping	Retail
Nokia	Technology
Pearson	Media
Philips Electronics	Personal & Household Goods
Roche	Health Care
Sasol	Oil & Gas
Siam Cement	Construction & Materials
Swiss Re	Insurance
Telefonica	Telecommunications
TNT	Industrial Goods & Services
Unilever	Food & Beverage
Xstrata	Basic Resources

Summary

CSR is culturally specific, it varies according to the nature of social dialogue, and the degree to which certain social and environmental issues are regulated by law. It is useful to have a common understanding at EU level about the importance of CSR, but ultimately the practice of CSR has to be adapted to the particular circumstances of different nations and regions.

CSR needs to be kept practical and results oriented, providing solutions to real problems faced by an enterprise, a locality or a sector. This will contribute to the positive evolution of European business culture in a way that will enhance Europe's competitiveness.

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[9]   http://amillaminute.wordpress.com/2010/09/13/dow-jones-sustainability-index-review-2010-effective-sept-202010/ (published: 20 Sept 2010)