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Sustainability Reporting in Stakeholder Value Creation: A Framework

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Abstract

Business organizations enter into a mutual social contract when operating in the business environment, since they consume the resources on behalf of the society. Hence, the manner in which the businesses interact with its environment and society has come under the scrutiny. As a result, organizations have become obliged to behave in a socially and environmentally responsible manner. Following the notions of Stakeholder theory, this study argues that any organization has a diverse set of parties who holds legitimate interest on the business and its operations and thus they are required to fulfil the information needs of the diverse stakeholders. In order to fulfil the largest aspects of information requirements of the users, organizations tend to report on the broader economic, social and environmental aspects related to the organizations, i.e. "Sustainability Reporting". This study aims to examine the factors influencing sustainability reporting practices and develops a framework to explain the ways in which sustainability reporting contributes to generate value to the stakeholders in an organization. The proposed framework reflects the findings of the research, which has been developed in reference to the empirical research conducted in the field of Sustainability Reporting for the period of year 2001-2011. The proposed theoretical framework is viewed as a contribution to the literature relating to Sustainability reporting. Moreover, further research could be conducted based on this framework to identify the practical implication.

Keywords: *corporate social responsibility; stakeholder theory; sustainability reporting*

1. Introduction

Business organizations in the corporate world operate with the aim to fulfil their ultimate objective of maximizing the shareholders' wealth. This aim focuses prominently on the shareholders attached to the business organization. Shareholders can be defined as a prominent figure that drives an organization providing the funds, by sacrificing their current consumption and undertaking risks of the uncertainty for the capital investment and a satisfactory return. Yet, shareholders alone are not the only party, which contributes to a business organization. Hence, other stakeholder groups hold a legitimate interest in the business organizations aside from the shareholders.

According to the stakeholder theory, all persons or groups with legitimate interest participating in an enterprise do so to obtain benefits and there is no prima facie priority of one set of interests and benefits over another (Donaldson & Preston, 1995). According to this Shareholder, business partners, society and the environment prominently form the basis of a business's stakeholders. Further to this point, Rajapakse (2003) mentions that in the Brundtland Report the stakeholders are broadly divided into, humanity and nature, which can be considered as another aspect of the stakeholders.

According to Hill and Jones (1992), firms can be seen as a collection of contracts that has been developed between the resource holders of the organization. This has an implication on the organizational behaviour, the structure of the management and the organizational strategy. In other words, business organizations enter into mutual social contract, when operating in the business environment as they consume the economic resources on behalf of the society. The diverse base of the stakeholders consists of variety of parties that may have a direct or an indirect influence on the business organization. The point to be noted in this regard is that the different parties would hold different interests and hence lead the organization to a conflict of interests in objective fulfilment. As a result the organizations have been influenced to embed a broader perspective to the business which would lead the organizations to shift their priorities focusing solely on profit motive to an ethical perspective. This requires the businesses to recognize and incorporate the interests of the most influential parties to their corporate agenda. Hence, in order to fulfil the larger aspects of information requirements of the users, organizations tend to report on the broader economic, social and environmental aspects related to the organizations, i.e. "Sustainability reporting".

Research Problem

This paper mainly focuses to address "To what extent do the Sustainability reporting practices contribute in stakeholder value creation?" Mainly the factors that directly influences on the development of Sustainability reporting will be identified and how each of these factors leads to value creation for the stakeholders is identified by developing a framework, to address the research problem.

Significance of the research

The research mainly focuses upon identifying the possibility of developing a link between Sustainability reporting and stakeholder value creation, based on the empirical literature. In addition, contributes a framework that establishes a link between these two variables. Hence, the proposed framework is a contribution to the literature on Sustainability reporting.

2. Review of Literature

Stakeholder Theory

A stakeholder group is "any identifiable group or individual who can affect the achievement of an organization's objectives, or is affected by the achievement of an organization's objectives" (Freeman, 1983, as cited in Rajapakse, 2003). This group has a legitimate claim on the organization. This legitimacy is established based on an exchange relationship. The stakeholder group of any organization would include common parties such as, investors, potential investors, management, employees, trade unions suppliers, customers, government. These parties supply the firm with critical resources for their operations and in exchange, each party expects its interests to be fulfilled by the firm (March & Simon, 1958, as cited in Charles & Jones, 1992) these stakeholders differ from one another based on the stake they hold in the respective firms. The management of a firm plays a unique role as they play a vital part in coordinating and managing relationships with all the stakeholders (Charles & Jones, 1992). The agency theory explains the relationship between the shareholders of the organization and the management, who plays the role of an agent. Recent studies in the field of stakeholder theory linked with the CSR activities of a business organization highlighted that the stakeholders have the ability to influence the corporate decisions and the business strategies. CSR could be simply described as the policies or actions that will reflect a company's interest in the social related issues.

According to Roberts (1992) larger firms tend to exert higher level of influence and power in the society as a result they are obliged to utilize the resources in an economical manner to meeting the social goals as well. This is a gradually developed understanding in the corporate world and the society and stakeholders considering a broader scope that has drawn the attention of variety parties. Moreover, many researchers have been conducted in relation to this, with the attempt to identify relationships that may prevail in CSR and sustainability reporting and the operation of the businesses. In addition, there has been findings that supports this argument and the establishment of a positive as well as a negative relationship between the two variables in consideration.

Corporate Social Responsibility (CSR)

From an ethical perspective, the organizations have been influenced to recognize the value of the social responsibilities in addition to their prime objective of wealth maximization. The concept which developed as a result of the ethical perspective of the business organizations is known to be Corporate Social Responsibility (CSR). CSR can be described as a company's commitment to behave socially and environmentally responsible while striving for its economic goals. CSR includes the company's relations with all its stakeholders, from market-related stakeholders (customers, share owners, suppliers), to internal (e.g. employees, board of directors) or societal stakeholders (e.g. government, NGOs). It is assumed that the variety of the stakeholders and their concerns lead to corporate responsibility including economic, environmental and social aspects. (Zink & Steimle, 2008).

Sustainability Reporting

Sustainability reporting is the incorporation of the environmental, societal and economical aspects of an organization to the reporting and communication to the interested parties. The most solid reason for the initiation of such reporting is due to the stakeholder pressure and coercive pressures upon the organizations. This reporting is mainly used as a communicating mode to the wider stakeholder base of the organization.

Sustainability reporting is still in its initial stage of development. In most countries, this practice is adopted on a voluntary basis. Haider (2010) observes the historical development of Corporate Social and Environmental Reporting (CSER) and concludes that the development of CSER is following a slow process which begins 'with employee reporting and then moves on to social reporting, environmental reporting, triple bottom line reporting and eventually, and ideally, sustainability reporting'. Similar to their developed counterparts, corporations in developing countries are also making CSER, although low in volume. This explains the situation in countries such as Sri Lanka related to the Sustainability reporting practices. Yet, since the publication of the first separate environmental reports in 1989, the number of companies that has started to publish information on its environmental, social or sustainability policies and/or impacts has increased substantially (Kolk, 2004).

With the gradual development in the Sustainability Reporting by the businesses, there has been shift from the voluntary nature of reporting to mandatory. For this purpose, various regulatory bodies have developed frameworks and regulations related to the reporting. According to the assessment done by the Corporate Registrar (2009 it has been evident that the corporations has elevated beyond the external and regulatory pressure and has reached the realization that they have to move beyond including a sustainability report/ statement in the annual report. Hence there is a trend of shifting towards an integrated reporting approach, which combines the performance and the purpose of a business.

Currently the governments have taken up a role of creating the business organizations through regulations. In addition, these legislations are covering a wider scope ensuring to cover most of the activities of the business organizations. Aside from the legislative pressure, since as a norm most of the businesses are in the process of incorporating sustainability reporting, this has created a peer pressure on the other companies operating in the industry. As certain researchers have found that, the stakeholders could, while rewarding the corporations that do not disclose will be punished in a social perspective.

Global Reporting Initiatives (GRI)

GRI reporting framework is widely used among the business organizations. GRI framework operates with the purpose of supporting companies in producing sustainability reports that integrate social, environmental and economic impacts of business. The GRI intends to establish their guidelines as an internationally accepted framework that promotes comparable sustainability reporting. The current version of the guidelines (GRI-G3) was published in 2006, which has been updated to the GRI-G3. This guides the businesses by providing a common platform for Sustainability Reporting.

GRI guidelines are compatible with the principles of the United Nation Global Compact. To indicate that a report is GRI-based the companies are expected to self-declare to which extent the report covers the GRI Reporting Framework. According to the Corporate Register, (2009), over 2000companies are in the process of adopting the GRI to their reporting , with the intention of making reporting more open and accountable, and provide a universal framework for disclosure.

3. Methodology

The research will employ a qualitative research paradigm as it is concerned with qualitative phenomenon of sustainability reporting, to uncover and explore the previously specified research problem. Further, the research takes a deductive approach, as it studies an already established concept of Sustainability reporting. Empirical data relating to this field for the duration of year 2000 -2011 is reviewed to generate knowledge in the relevant subject area.

The research design employed is a descriptive study of the subject area. Also critically analyse the data gathered in order to recognize relationships among the factors that leads to the development of Sustainability reporting and how this is been used to generate value to the stakeholders. This relationship analysis will be used to develop the framework, which is the outcome of the paper.

Data analysis

As the research is considering the literature available for the duration of 2001-2011, data reduction plays a crucial role in the analysis. This will allow eliminating the excess information and focusing the research towards the mentioned research problem. The rational for the selection of the mentioned period is that a significant increase in the reporting could be observed after the year of 2001. For example, reporting has increased from approximately around 1000 reports in 2001 to approximately over 3000 reports in 2008 (Corporate registrar, 2009).

The reduced or summarized data will be analyzed to establish a relationship between how business could create value to the stakeholders through Sustainability reporting. The findings are displayed in a conceptual framework linking to the theoretical aspects gathered from the literature review. The proposed framework will facilitate to convey the findings of the research in a simple and an understandable manner.

4. Findings

It is evident through the existing literature and the facts discussed earlier in this paper, that business organizations are under the scrutiny of many pressures from its internal and external environments. These normative pressures can be broadly categorized into 3 as, internal stakeholders, external stakeholders and regulatory frameworks. The internal stakeholders include parties such as the employees, trade unions. The external stakeholders of an organization are diverse as well as their expectations. External stakeholders create social and cultural pressures to an organization. Social pressures arise mainly with the increased awareness of the customers, as result of the high emphasis and concern over the climate changes. This has led the society to closely monitor the activities of the business organizations to ensure that the negative impacts of their operations are maintained at a minimum level. These social pressures arise in clusters, in the form of pressure groups.

As a result of the internal and external stakeholders' pressures, regulatory pressures are been developed. The regulatory frameworks are an external stakeholder, yet it is separately identified as it plays a major role in the external environment. In addition, the regulatory frameworks are mostly of mandatory nature and needs to be adhered to without a choice. Hence, this pressure has prevailed constantly on the organization. These regulatory frameworks lead to the initiation of reporting frameworks such as the GRI framework discussed earlier and regulations. GRI has

These reporting and regulatory frameworks have influenced the nature of reporting relating to the social, economic and the environmental aspects of the organizations. Namely, these can be identified as the impact on the content, confirmations and the disclosures.

Considering the content aspect of the reporting, according to Kolk (2004) the field of sustainability reporting follows a gradual development path. Business firms initially produced pure environmental reports. And gradually, a clear tendency can be observed in environmental reporting broadening into the inclusion of the societal and at times also financial issues related to the business operations to the reports.

As further stated by Kolk (2004), by 2002 the percentage of the pure environmental reports published by the largest 250 multinationals has declined to 71% (from 98% in 1999). The remaining 29%, of the reports have been categorized as Sustainability reports, which have incorporated the social, economic and the environmental information. Yet the percentage of the social and the financial information of these reports have been limited to less than 15% of the entire report. According to Kolk (2004), even though the content of the reporting has been subject to major changes throughout the years, majority of the Sustainability reports still tend to focus upon a selected and limited scope. Hence, with the guidance of the regulatory and reporting frameworks the content of the sustainability reports has widened over time.

Further, in current practice related to the Sustainability reporting of the firms emphasizes upon the third party audits and confirmations of the sustainability reports produced by the businesses. The GRI framework mainly provides a validation to the external confirmations/ assurances in the categorization of the reports according to their assessment levels. Hence, the business organizations have reached the understanding that the external assurance provides a competitive edge to the business through the Sustainability report and aids in stakeholder value creation.

In addition, the disclosure of the information is also been guided by the reporting frameworks. For example, the GRI framework facilitates the organizations to self-declare according to the Application Levels C, B or A based on the extent of the information disclosures related to the environmental, social and the economical aspects of the business.

Hence, based on the nature of reporting in the aspects of content, assurance/confirmations and disclosures, enables the measurement of the environmental, social and the economical/ financial prospects of a business. Both the nature of the reporting and the measurement of Sustainability currently take a strategic perspective in the business organizations.

The strategic perspective appears through the embedding of the sustainability concept to the corporate's core strategy with the view of reducing the corporate risk and corporate engagement which leads the business to focus on the developing a more innovative approach. As the corporations are pressured by the stakeholders to provide a more comprehensive and clear picture of the sustainability engagements of the business, which has led the organizations to relate these activities to the core strategy. Hence, the business entities are producing integrated reports that would allow the stakeholders to link the financial performance of the organization to their social and environmental movements. Corporations have realized the importance of the sustainability from a strategic view rather than a marketing view.

As the business organizations were openly criticized for its "green washing" behaviour under the sustainability aspect, where the society held a general perception that businesses use sustainability and its reporting as a marketing tool for image building. Hence, the business organizations have changed its approach on sustainability reporting to be more of a strategic action. There is a lot of involvement from the top level of the organization on the sustainability department, taking responsibility. This has elevated the importance of sustainability within the organizational settings. In addition, with the enhancement of the information provision to the wider stakeholder groups of the organizations, stakeholder value creation takes place in the form of economical value and social value. The reporting allows the stakeholders to make informed decisions and at the same time businesses incorporate the stakeholder interests to their business strategy. This could be seen as giving prominence to the needs and demands of the stakeholders, by making them an important element in the corporate agenda.

The findings of the research are summarized upon the proposed framework. This framework provides a concise understanding on how the business organizations create value to the broader stakeholder group with the use of Sustainability Reports.

5. Conclusion

In conclusion, the research paper observed the business organization's involvement in Sustainability reporting practices and the manner in which the businesses integrate Sustainability reporting to the core strategy. This leads to the development in the reporting itself in terms of content, disclosure and assurance. With the inclusion of the wider stakeholder interests in to the corporate agenda, not only the organizations are evidently generating value to the stakeholder, but with the use of the Sustainability reporting, create a competitive edge against the competitors.

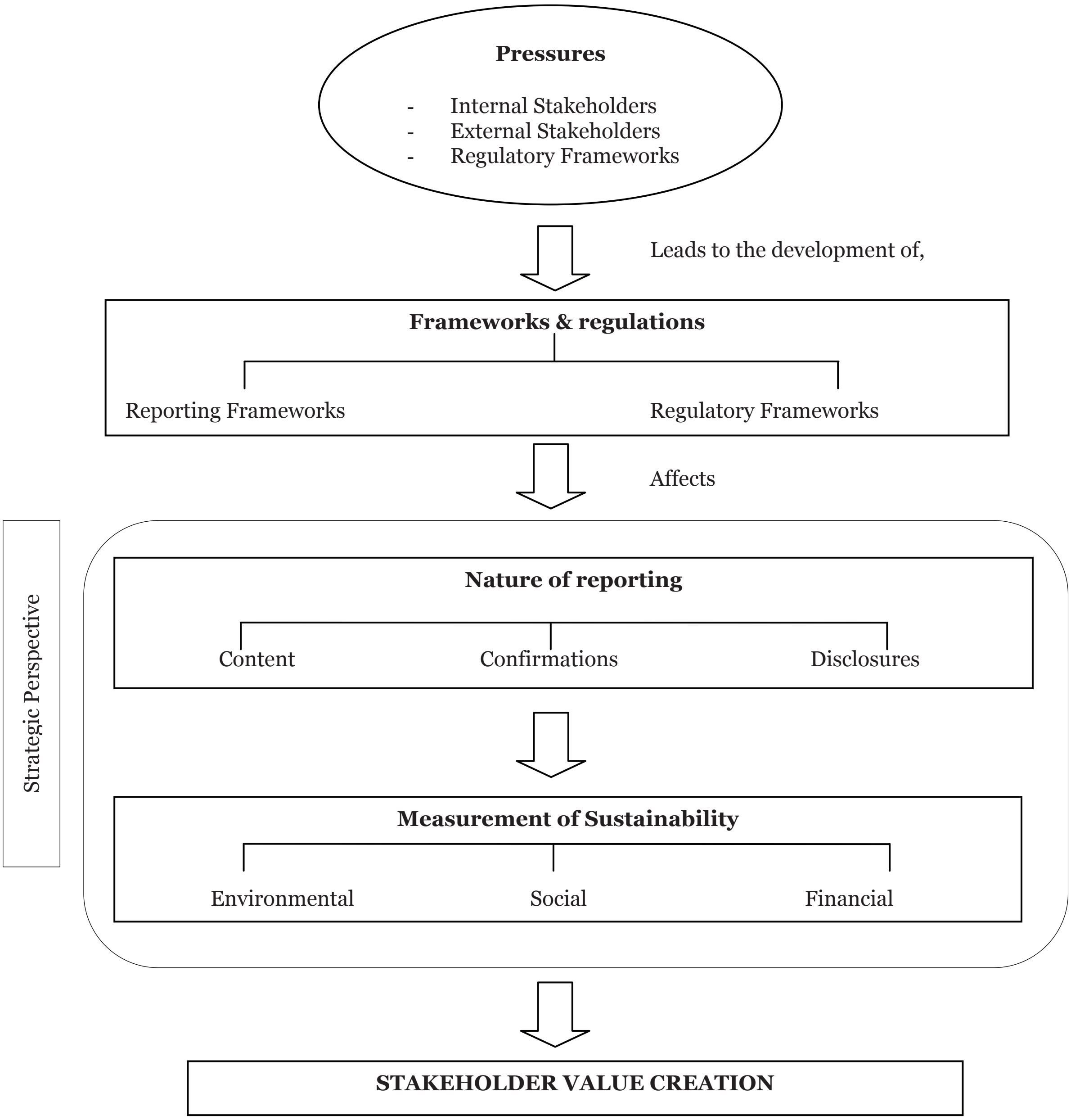

Figure 1: Proposed Framework to analyse the value creation to the Stakeholders

Future Research Areas

This research has been conducted based upon the empirical researches that have been conducted on Sustainability Reporting. In addition, the research contributes the proposed framework to the literature linking Sustainability reporting to stakeholder value creation. Future research can be carried out on a field research level, which goes beyond the simple explanatory level and reach to the level of gathering evidence to evaluate the proposed framework.

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