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# **Recent developments in European social and environmental reporting and auditing practice – A critical evaluation and tentative prognosis**

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# **Recent developments in European social and environmental reporting and auditing practice – A critical evaluation and tentative prognosis**

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## **Abstract**

The past decade has witnessed a remarkable growth in the number of European companies reporting publicly on various aspects of their environmental and social performance. Whilst for many this has simply entailed providing fairly rudimentary, and generally qualitative, environmental and social performance information within the annual report, leading edge reporters have gone much further. For this latter group, predominantly, but not exclusively, large companies operating in 'sensitive' industrial sectors, the preferred means of dissemination has become the production on an annual basis of a substantial 'stand alone' report featuring copious quantitative, as well as qualitative, data. The reliability of such data is increasingly likely to be attested to by an external verifier.

The paper reviews two strands of this development. Firstly, environmental reports which initially appeared on the scene in significant numbers in the early 1990's, and secondly, 'sustainability' reports which evolved towards the end of that decade. Whilst due acknowledgement is made concerning the technical progress achieved in reporting, major reservations are expressed concerning the efficacy of these initiatives as a means of enhancing the public accountability of major corporations. A particular problem centres on the failure to 'close the reporting loop' in terms of introducing institutional reforms empowering stakeholders to utilise the information provided in order to hold corporate management accountable and thereby meaningfully influence decision making.

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## Introduction

The past decade has witnessed a remarkable growth in the number of European companies reporting publicly on various aspects of their environmental and social performance. Whilst for many this has simply entailed providing fairly rudimentary, and generally qualitative, environmental and social performance information within the annual report, leading edge reporters have gone much further. For this latter group, predominantly, but not exclusively, large companies operating in 'sensitive' industrial sectors, the preferred means of dissemination has become the production on an annual basis of a substantial 'stand alone' report featuring copious quantitative, as well as qualitative, data, the reliability of which is increasingly likely to be attested to by an external verifier. My task in the present paper is to attempt some critical evaluation of this latter phenomenon with a view to informing public policy debate. In doing so I draw on my own research experiences and, in particular, my participation as a judge and member of the shortlisting panel for the Association of Chartered Certified Accountants (ACCA) Environmental (later Sustainability) Reporting Awards scheme since its inception in 1991.

### SOCIAL AND ENVIRONMENTAL REPORTING AND AUDITING: AN EVALUATIVE FRAMEWORK AND BRIEF HISTORY

The evaluative framework I am operating within derives from the following, fairly widely cited, definition of social and environmental reporting and auditing as being: ".....the process of communicating the social and environmental effects of organisations' economic actions to particular interest groups within society and to society at large. As such, it involves extending the accountability of organisations (particularly companies) beyond the traditional role of providing a financial account to the owners of capital, in particular shareholders. Such an extension is predicated upon the assumption that companies do have wider responsibilities than simply to make money for their shareholders" (Gray et al, 1987, p ix).

Particularly noticeable in the above definition is the lack of any reference to the now seemingly ubiquitous 'business case' for a more environmentally and socially aware approach to corporate reporting practice. Companies going down this route may well find it efficacious in terms of reputation enhancement and risk management, with a consequent beneficial effect on the 'bottom line'. On the other hand they may not,

and for me this is of little concern. The whole *raison d'être* for social and environmental accounting lies in its potential to make certain aspects of corporate activity more transparent to external stakeholders, who may then be empowered to hold corporate management accountable for their actions insofar as they are affected by them. My standpoint is unashamedly normative and predicated on the notion that conventional accounting (including potentially much social and environmental accounting) practice, with its overriding focus on the interests of wealthy capital providers in, predominantly, western nations is fundamentally flawed and pernicious in its influence. In simple terms, accounting's preoccupation with financial performance as the sole yardstick of organisational success leads inevitably to its implication in the environmental destruction, social dislocation and exploitation of the weakest members of society consequent upon such a narrow interpretation of 'success'. Current corporate social and environmental reporting initiatives are therefore to be judged on the basis of whether they offer more emancipatory alternatives that may improve the situation in terms of delivering greater levels of organisational accountability.

Whilst social disclosure within the medium of corporate reports is far from being a recent phenomenon, and can indeed be traced back to the beginning of the twentieth century (see, for example, Guthrie and Parker, 1989), the issue first achieved real prominence in the 1970's. This was largely a natural consequence of the debate then raging concerning the role of the corporation in society at a time of rising societal expectations and emerging environmental awareness. More perceptive managements speedily grasped the public relations benefits of producing, at least rudimentary, social reports which attempted to convey a picture of corporate responsiveness to key societal concerns.

Within Western Europe, external social reporting initiatives in the 1970's exhibited an overriding emphasis on the enterprise-employee relationship, largely as a result of continuing debate at that time over the status of labour and its position in the enterprise. A notable exception to the general reporting pattern is, however, provided by the activities of a number of larger German companies, particularly those operating in the chemical and oil industries, whose published *socialbilanz* attempted to present the corporation's performance and results as they affected the total

societal environment. Prominent amongst these companies is Deutsche Shell whose 'goal directed' reporting, employing quantitative indicators to describe the attainment of wide ranging social objectives, and attempting to integrate such data with traditional financial reporting, has been (probably largely unwittingly) resurrected in the new wave of environmental and sustainability reporting initiatives of recent years.

Whereas business experimentation with social reporting in the 1970's was certainly innovative, more so it has to be said on the other side of the Atlantic, the prevailing climate of voluntarism generally produced reports that were largely public relations driven and served to portray the reporting organisation in a favourable light<sup>i</sup>. A notable exception to this general pattern is, however, provided by the activities of the UK based independent research and lobbying organisation Social Audit Limited. Adopting an un-compromising stance of holding to public account the activities of powerful economic entities, Social Audit Limited conducted a number of critical exposés (audits) of the social and environmental performance of major commercial organisations, publishing the results in its journal *Social Audit Quarterly* (1973-6). Not only do these exercises provide a fund of ideas and tools for researchers (and reporters) today, but they also offer a yardstick by which modern corporate reporting initiatives may be judged in terms of the claims made by their exponents that they are informed by the ideals of transparency and accountability<sup>ii</sup>.

The dawning of the 1980's heralded pretty much the end of widespread experimentation and debate concerning social accounting as the 'New Right' policies of the Thatcher – Reagan era appeared increasingly to hold sway. Admittedly, the employment dimension continued to figure in much reporting practice, with, in the UK, employee consultation issues receiving widespread, if somewhat cursory, attention reflecting largely government initiated moves to weaken trade union influence. Similarly, community issues began to figure in UK corporate reports as the private sector gradually took over responsibilities for regional economic and social development abdicated by central government. However, here again disclosure was very sketchy, and certainly social and environmental issues in general became peripheral, at best, as far as much corporate reporting practice was concerned.

In sum, voluntary corporate social and environmental reporting initiatives prevalent in the 1970's appeared to lose all impetus during the 1980's, apparently reflecting fading public interest in such issues. For Roberts (1990) macro-economic factors, notably rising rates of unemployment consequent upon a slow down in economic growth, were instrumental in focusing attention on economic priorities and away from matters of corporate social performance. There were, however, exceptions to this general rule. Significantly, the public accountability pre-occupations of Social Audit Limited were carried forward by a number of UK Local Authorities which undertook plant closure social audits seeking to highlight the human and public financial cost of the run down of much traditional manufacturing activity in the early to mid eighties (see Harte and Owen, 1987). Of greater long term impact, however, was the tentative flowering of the social investment movement in Europe, with the UK leading the way in the launch of ethical investment funds offering investors the opportunity to invest in accordance with environmental and social, as opposed to exclusively financial, criteria. Despite such activity, and notwithstanding the dramatic growth in recent years of the ethical investment market (see, for example, Kreander, 2001), one would nevertheless have been hard pushed to predict at the end of the 1980's the seemingly inexorable rise in corporate environmental reporting activity which began in the early '90's and has continued to the present day.

### **The Rise of Environmental Reporting and Auditing**

There have been numerous surveys published over recent years of the extent of environmental reporting at a European and wider international level, and a full review is beyond the scope of this paper. A flavour of the growth in popularity of 'stand alone' environmental reports amongst larger companies may be conveyed, however, by referring briefly to the series of surveys published by KPMG on a triennial basis since 1993. Looking at reporting practice amongst the top 100 companies in eleven countries (including nine from Europe<sup>iii</sup>) over the four survey cycles the following pattern emerges;

Year of survey	Percentage of companies producing a corporate environmental report
1993	13%
1996	17%
1999	24%
2002	28%

(Source: KPMG International Survey of Corporate Sustainability Reporting, June 2002, p.12)

Traditionally, within Europe, German and Scandinavian companies have led the way in terms of numbers of reports published. However, in the latest (2002) KPMG survey the UK has taken the lead with 49% of top 100 companies producing separate environmental reports. Other major players are the Netherlands, Finland and Germany, all exhibiting around 30-40% reporting rates. Also worthy of mention is the significant rise in the number of French companies reporting, up from 4% in 1999 to 21% in 2002, possibly indicating an anticipation of the mandatory reporting requirements introduced from financial year 2002 onwards. Finally it should be noted that the incidence of reporting tends to be skewed between industry sectors, with utilities, chemicals and synthetics, forestry, pulp and paper, oil and gas, and transport traditionally exhibiting higher reporting rates<sup>iv</sup>.

That the practice of environmental reporting has grown amongst key market players throughout western Europe is perhaps not surprising in view of the wide variety of influences that have been brought to bear on the process from a myriad of sources. These have included<sup>v</sup>

- Supra-national bodies. Prominent here have been the United Nations Environment Programme (UNEP)/SustainAbility Engaging Stakeholders initiative launched in 1994, which has served to increasingly turn the spotlight on 'non-reporters', and the European Union's Eco-Management and Audit Scheme (EMAS) with its requirement for disclosure and verification.
- National Governments. Generally the focus has been on encouragement and development of voluntary reporting guidelines, such as the UK Government's DEFRA/DTI Environmental reporting Guidelines published in 2001. As noted earlier, however, France has recently opted for a legally mandated approach, following the earlier examples of Denmark, Norway, Sweden and the Netherlands

who have all provided some, generally limited, legal backing for environmental reporting. Focus tends to be placed, however, on the annual financial report, rather than a special purpose report, as the medium for disclosure.

- **Business Organisations.** Initial work undertaken by the International Chamber of Commerce (1991) in developing its Business Charter for Sustainable Development has been carried forward in recent years by the World Business Council for Sustainable Development. Additionally, business groupings at various national levels, notably the Confederation of Business Industry in the UK, have been proactive in drawing up reporting guidelines.
- **Industry Associations.** Perhaps best known here, certainly in Europe, are the European Chemical Industry Council's (CEFIC) Responsible Care Programme's reporting guidelines.
- **The Accounting Profession.** The umbrella organisation for the European accountancy profession, the Fédération des Experts Comptables Européens (FEE) has been particularly active in developing both guidelines for providing assurance on environmental reports and a conceptual framework to underpin such reporting. Additionally, international accounting firms have been heavily involved in verification and consultancy work, whilst national professional bodies have actively promoted research into environmental (and social) accounting issues. Prominent amongst the latter has been the UK Association of Chartered Certified Accountants (ACCA) which, amongst many initiatives, launched an Environmental Reporting Awards Scheme in 1991. The scheme has grown over the years to encompass the sustainability and social reporting, in addition to environmental reporting, dimensions and has also given rise to the launch of a European Awards Scheme (EERA) in 1996 which now draws on contributions from accountancy bodies in fifteen European countries<sup>vi</sup>.

Significantly, increased incidence of environmental reporting has been accompanied by a discernible improvement in the quality of reports produced. Early disclosure initiatives largely consisted of providing sketchy, generally qualitative, information within the annual financial report, or the production of a separate 'green glossy'

amounting to little more than a crude publication relations exercise. As Adams et al (1995) put it in their study of disclosure practices in 150 of the largest European companies;

“.....the typical company provides purely discursive information, describing only some of its activities in some sectors (often only for domestic operations) with no information on external benchmarks or plans and fails to place information provided in any context” (p24).

A sense of continual improvement from such a low base level is, however, clearly conveyed by the successive annual reports of the judging panels for the ACCA UK and European reporting awards schemes. Here, for example, we find reference to improvement in structure and content, with fewer blatant public relations exercises, a willingness to convey bad, as well as good, news, continual improvements in the reporting of performance against stated quantified targets, an increased prevalence of verification statements and the steady development of industry wide performance indicators enabling intra-sectoral comparisons to be made.

Notwithstanding the absence of definitive regulatory guidance, a coherent and comprehensive reporting framework has also steadily emerged. One can now expect the typical stand alone report<sup>vii</sup> to feature:

- **An organisational profile** presenting an overview of the organisation in terms of size, markets served and key environmental impacts.
- **Evidence of board level commitment**, generally comprising a statement from the organisation’s CEO which explains in broad terms the environmental management strategy being pursued.
- **A (definitive) environmental policy statement** committing the organisation to pursue specific goals and objectives in terms of managing, measuring and reporting environmental performance. The policy statement is used as a basis for generating comprehensive and detailed targets against which performance may be measured.
- **Targets and achievements** addressing key issues concerning, for example, natural resource and energy usage, waste generation and emissions to air and water.

- **Performance and compliance data** employing physical and financial measures in order to demonstrate progress towards achieving stated performance targets. Increasingly, physical data is set in context via benchmarking against statutory limits or industrial averages, and normalised data (i.e. presented in terms of quantities per unit of product etc.) employed to give an indication of efficiency and performance improvement. Financial data predominantly comprises selective investment figures and cost savings achieved through the establishment of more efficient environmental management procedures, although leading edge companies are increasingly employing activity based costing techniques to capture and disclose more fully environmental expenditure.
- **Environmental Management Systems** are described which pinpoint responsibility for managing various aspects of environmental performance. One can also expect to find here information on internal environmental audit procedures and progress towards certification standards such as ISO or EMAS.
- **An independent Verification Statement.** Whilst initially verification centred mainly on systems compliance recent practice has addressed more complex issues such as completeness of reporting and acceptability of performance, whilst also offering recommendations in terms of systems improvement, performance and disclosure practice.
- **Site level data** is provided for organisations operating from multiple sites. Generally, this comprises brief summarised qualitative and quantitative data (e.g. physical indicators, key actions undertaken, serious incidents and detail on the environmental management system employed). Transparency of local operations is often heightened by specifically naming a management contact on site.

### **Leading Edge Environmental Reporting Practice: A Critique**

As the above, of necessity brief, overview indicates, corporate environmental reporting practice amongst its leading edge exponents has made considerable strides in terms of rigour and completeness over the past decade. It is however now appropriate to strike a somewhat cautionary note.

At the outset it must be stressed that the reporting practice I have been describing is a minority pursuit even amongst the largest (top 100) companies in all European countries. Far too many significant players in environmentally sensitive industries continue to supply, at best, brief and rudimentary information as part of their financial

reporting package. Outside of the top 100, amongst 'second tier' companies and SME's environmental reporting is largely conspicuous by its absence<sup>viii</sup>.

Even amongst leading edge reporters a number of problem areas remain. Recent ACCA and EERA judges reports, for example, draw attention to reporters not making clear their strategic priorities and thereby failing to prioritise targets, with the result that a mass of often over-aggregated data is produced which is difficult for the reader to navigate his, or her, way through. Additional problems typically identified are that links to financial reporting are often unclear and explanations of performance variations lacking, with more attention needing to be paid to trend analysis thereby enabling some interpretation of performance improvement or deterioration.

Of course, it may be argued that weaknesses such as those outlined above are only to be expected at this stage of development of environmental reporting and, judging by the experience of recent years, improvement can be confidently anticipated. However, certain problem areas appear to be somewhat more intractable. Prominent amongst these is the vexed issue of report verification. Reference has already been made to the fact that verifiers have recently shown more willingness to address issues such as completeness of reporting and acceptability of performance in contrast to their earlier virtually exclusive focus on systems compliance issues<sup>ix</sup>. However, a fundamental issue remains concerning the independence of the verification process. Put simply, verifiers are appointed by corporate management and effectively report their findings to corporate management. A clear contrast can be drawn here with the financial audit process where, at least as far as legal theory is concerned, auditors are appointed by shareholders and report to the same constituency on management stewardship of funds invested.

The issue of verifier independence is, in fact symptomatic of a much deeper problem. This is the prevailing confusion as to the stakeholder groups the company is seeking to communicate with via the environmental reporting process, and, equally fundamentally, how such groups are to be able to use the information provided, and verified, in order to hold management accountable for their actions. Little real thought seems to have gone into the corporate governance ramifications of environmental reporting, save possibly for the Turnbull Report's (1999) reference to issues of risk

management together with some vague notions of enlightened self interest. The latter pre-occupation is neatly summarised in the 1992 report of the ICAEW's Environment Research Group which suggests that:

“A company will be wise to ensure that appropriate information is provided to all those groups – whether they are groups with which it has direct contract, or in society generally - which are in a position to take action, in the light of their perception of a company's environmental performance, that may directly or indirectly affect the company's present or future position” (p12).

Unfortunately, as Tricker (1983) has so cogently argued, such global concepts of general accountability to a wide amorphous set of “stakeholders” are likely to amount to little more than a “mirage of responsiveness to meet pseudo demands”. (P35)

Clearly, there is a need to prioritise particular stakeholder interests within the environmental reporting exercise and direct reports more specifically towards the information requirements of the selected stakeholder group(s). Should, for example, shareholders be identified as the primary constituency for environmental reports, reporting weaknesses identified earlier, such as a failure to identify strategic priorities and lack of integration with the financial report in terms of clearly identifying the “bottom line” implications of the company's environmental management strategy, must be urgently addressed. Indeed, serious reservations can be expressed as to the efficiency of a separate environmental report for communicating with the shareholder group whose primary focus is always likely to be the annual financial report.

Even a casual reading of the overwhelming majority of environmental reports produced over recent years does, however, suggest that shareholders are not the only, or indeed primary, stakeholder group of concern. Clearly there is an apparent desire expressed, at least implicitly if not always sufficiently explicitly, to address a much wider audience. This observation gives rise to the identification of the most fundamental problem area with the initial wave of environmental reporting exercises – namely a tendency to privilege the physical environmental dimension to the almost complete exclusion of the social.

Given that companies going down the environmental reporting route invariably claim to be committed to pursuing **sustainable** business practices in response to the

agenda laid down in the Brundtland Report (World Commission on Environment and Development, 1987), omission of any consideration of the social dimension is unfortunate in the extreme<sup>x</sup>. As will be recalled, the Brundtland Report was at pains to stress that the environment cannot be considered in isolation from human actions, ambitions and needs, and clearly underlined that, "... links between poverty, inequality and environmental degradation formed a major theme in our analysis and recommendations" (p xii). In other words, excluding any consideration of the social dimension, or in the Brundtland Report's parlance, issues of eco-justice, in terms of both inter and intra generational equity, results in attention being focussed on merely the symptoms, not the causes, of environmental problems.

Crucially, for stakeholders other than shareholders their assessment of the sustainability, or otherwise, of business performance is highly likely to be informed by social as well as purely environmental concerns. For example, introducing provision of secure employment as one simple measure of intra generational equity can dramatically alter perceptions derived from looking at single dimensional (physical) environmental reports as to a company's contribution to sustainability. The case of the privatised utilities in the UK in the early 1990's provides an instructive example here. Companies drawn from the water, power and telecommunications industries were very much at the forefront of innovative environmental reporting practice, and indeed figured prominently in shortlists of leading reporters in the early years of the ACCA's awards scheme. At the same time, as Shaoul (1998) and Williams and Haslam (1995) for example graphically illustrate, these organisations were busily engaged in shedding labour in order to finance increased dividend payouts to shareholders. Ironically it would appear that what amounts to human wastage here resulted from the same 'efficiency' motive that drove environmental performance. It is indeed difficult to class any societal structure arising from such a process as 'sustainable' however successfully eco efficiency objectives have been pursued.

The overriding problem with the environmental reporting initiatives we have been discussing lies in their virtually exclusive focus as the eco efficiency dimension of sustainability. Implicit is an assumption that environmental challenges can be met within a 'business as usual' scenario without the necessity of fundamentally re-examining basic social and economic values and life styles. Such a view fails to take

on board the complexity of sustainability as a concept within which the eco justice dimension, with its concern with issues on inter and intra generational equity, is central. It is also this latter dimension that is often of primary importance to the stakeholder groups which the reporting exercise purports to address. Provision of secure employment was used as a fairly simple illustration in this context, although many other examples, perhaps most notably community impact issues within both developed and developing countries, could equally well have been employed.

In addition to stakeholder information needs not being met, mention has also been made of the fact that corporate governance mechanisms have not evolved so that stakeholders can effectively use information provided, or highlight information not provided, with a view to influencing corporate decision making. In essence, stakeholders within the environmental reporting process, unlike shareholders within the financial reporting process, appear largely disenfranchised and therefore unable to hold corporate management accountable in any meaningful sense. Interestingly, a new wave of corporate sustainability reporting which arose in the late 1990's, and appeared as largely a natural extension of earlier environmental reporting initiatives, appears, at least on the surface, to address both the problems of information deficiency and stakeholder exclusion. It is to a consideration of these new initiatives in 'sustainability' reporting that we now turn our attention.

### **The Move Towards Sustainability Reporting**

In addition to the predominantly eco-efficiency centred environmental reporting initiatives appearing from the early 1990's onwards an alternative, more socially rounded reporting somewhat reminiscent of the German *socialbilanz* of the 1970s, has also recently begun to emerge. Pioneering this development were avowedly 'values based' organisations, most notably Bodyshop and the Co-operative Bank, whose initial forays into what became initially termed social and ethical accounting, auditing and reporting (SEEAR) were taken up by more mainstream companies in the latter part of the 1990's. Significantly, at the forefront of this movement have been companies who some years previously were equally pro-active in the early years of the environmental reporting revolution. Prominent examples here are the oil giants Shell and BP Amoco and privatised utility conglomerates such as BT and United Utilities. KPMG's (2002) survey referred to earlier gives an indication of the

growth of this phenomenon in noting that amongst their top 100 samples by 2002 approximately one third had incorporated social (and economic) issues into what had previously been a purely environmental report. Indeed, the scale of change has been such that the ACCA was led to introduce a sustainability reporting category into its long running UK awards scheme in 2001.

Whilst terminology applied to these reporting initiatives varies greatly, with report titles ranging, for example, through 'Social and Environmental', 'Partnership' and Corporate Responsibility in addition to 'Sustainability', the initiatives have broadly two themes in common. Firstly, some attempt is made to address the economic, environmental and social dimensions within the confines of one report, a process for which Elkington (1997) memorably coined the phrase 'triple bottom line reporting', and, secondly, a commitment expressed to involve stakeholders directly in the reporting process. The latter dimension is clearly evidenced, for example, in reports such as BAA's. 'Towards Sustainability' (1998/99) where it is noted that "This report... is part of our commitment to stakeholder dialogue and our internal drive for continuous improvement' and a reference in United Utilities (2002) 'Social and Environmental Performance Report' to the development of "...a stakeholder interest map to capture the key interests of our audiences".

Significantly, as was the case for environmental reporting, sustainability reporting initiatives have been accompanied by the appearance of a range of standards and guidelines designed to secure the quality of reports produced<sup>xi</sup>. Particularly prominent amongst these are the Global Reporting Initiative's Sustainability Reporting Guidelines (GRI, 2002) and the Institute of Social and Ethical Accountability's (ISEA) Foundation Standard AA1000, originally launched in 1999 and undergoing review at the time of writing.

Originally convened by the Coalition for Environmentally Responsible Economies (CERES) in partnership with the United Nations Environment Programme (UNEP), the GRI has evolved into a multi-stakeholder international initiative incorporating the active participation of corporations, NGO's consultancies, trade unions and accountancy bodies amongst other interest groups. Its overriding aim is unequivocally stated as being to enhance "the quality, rigour and utility of

sustainability reporting” (GRI, 2002, pi). To this end, the Guidelines offer a comprehensive set of reporting principles and structured report content that incorporates performance indicators for the economic, environmental and social performance dimensions. Whilst the environmental; indicators, which are able to draw on extant practice, are not surprisingly the most highly developed, the social indicators prescribed are by no means insignificant. These latter address the key areas of labour practices and decent work, human rights, society (including issues such as community impact and bribery and corruption); and product responsibility and certainly present a demanding agenda for reporting companies to follow. Equally significantly, the central importance of stakeholder dialogue in informing the reporting process is made quite clear.

“A primary goal of reporting is to contribute to an ongoing stakeholder dialogue. Reports alone provide little value if they fail to inform stakeholders or support a dialogue that influences the decisions and behaviour of both the reporting organisation and its stakeholders” (GRI, 2002, p.9).

With membership mainly drawn from the corporate sector, consultancy organisations and leading professional accountancy firms, ISEA represents a similar multi-stakeholder initiative avowedly committed to ‘strengthening the social responsibility and ethical behaviour of the business community and non-profit organisations’. Unlike the GRI initiative, ISEA’s Foundation Standard AA1000 doesn’t directly concern itself with prescribing reporting formats, but rather with specifying the internal processes organisations should employ to secure reporting quality. Significantly, the standard clearly notes that, “Engagement with stakeholders is at the heart of AA1000” (ISEA, 1999, p.7). Underpinning the standard’s approach to stakeholder engagement is the fundamental principle of ‘inclusivity’. Put simply, this entails the reflection of the aspirations and needs of all stakeholder groups at all points of the process, from issue identification through performance measurement and reporting to the final feedback stage at the conclusion of the cycle. Most fundamentally, attention is also drawn to the necessity for reporting organisations to define governance procedures in order to secure the inclusion of stakeholders centrally in the process.

Taken together, the GRI and ISEA initiatives, along with the growing practical response from economically significant corporates, seem to hold out the promise of

significantly enhanced transparency in terms of social and environmental performance and predicate a meaningful extension of accountability to stakeholders. Indeed, the approach advocated and followed appears, at least on the surface, to draw inspiration from the pioneering efforts of Social Audit Ltd. referred to earlier. There is, however, one fundamental difference.

The motivations underpinning Social Audit Ltd's work are clearly underlined by Charles Medawar, one of the leading figures in the organisation;

"We have, in fact, a democratic bias. We believe that corporate power should be exercised to the greatest possible extent with the consent and understanding of ordinary people. We believe that people should be encouraged and allowed to share responsibility, but that, at present, they are not and are imposed upon instead. The question of secrecy and accountability is fundamental here" (Medawar, 1976, p.390, emphasis added).

The radical edge of this earlier social accounting and auditing movement is noted by Geddes (1992) who suggests that it represents nothing less than a fundamental assault on prevailing market-based economic orthodoxy. Not surprisingly, companies didn't buy into this vision and Social Audit Ltd's activities were carried out with a distinct absence of corporate co-operation. By stark contrast, the impetus for the new wave of reporting activity has come from companies themselves, seemingly persuaded by the 'business case' for going down such a route.

It is indeed most noticeable how keen advocates of the new reporting initiatives are to persuade companies how beneficial the process can be. SustainAbility's (1999) *Social Reporting Report* (1999), for example, draws attention to benefits in terms of identification of weaknesses in management control of high risk activities, and enhanced stability enabling the organisation to mitigate against unexpected shocks. For their part Gonella et al (1998) note that;

"A stakeholder-based company is one that in many respects is most fit to take advantage of the technological and regulatory changes that underpin and enable the globalisation of trade, production and marketing" (p.15).

Gonella et al further acknowledge that the process "has a strong emphasis on being useful in managing the organisation as well as increasing transparency and accountability" (p.81). Interviews conducted with a sample of leading corporate

players, representatives of major professional accounting firms, consultants and representatives of NGO's by Owen et al (2001) largely confirm suspicions that a 'managerial turn' is coming to dominate the reporting process. In particular, corporate responses suggested that commitment to stakeholder engagement is largely confined to managing stakeholder expectations and balancing competing interests, whilst leaving much scope for the exercise of managerial discretion. Certainly, there was very little in the way of anticipation of any need to radically overhaul corporate governance mechanisms in order to incorporate systematic reporting cycles.

In essence, as Owen et al (2000) note, the new wave of sustainability reporting is inextricably bound up with a process of stakeholder management that has effectively displaced any meaningful moves towards expanding corporate accountability towards stakeholders. Swift (2001) illustrates this point further in noting that corporations are engaging in stakeholder dialogue and utilising information gleaned for the purpose of self reporting on their trustworthiness simply as part of a reputation building process. Crucially, there are no links to **rights** to information built in, so what are we witnessing is a 'soft' form of accountability at best, with power differentials between the organisation and its stakeholders remaining unaltered.

Lacking in the current voluntaristic reporting climate is any acknowledgement that substantial elements of largely unaccountable power have to be wrested from narrowly conceived corporate interests if any meaningful extension of accountability to stakeholders is to be achieved<sup>xii</sup>. As Frank (2001) so cogently puts it;

"What we must have are not more focus groups or a new place where people can express themselves... but some countervailing power, some force that resists the imperatives of profit in the name of economic democracy" (pxvii).

Equally amongst advocates of sustainability reporting there seems little appreciation of the fact that stakeholder conflict, rather than harmony, permeates much economic activity (see Shaoul, 1998), and that such conflict is invariably resolved in favour of the economically powerful shareholder group. As Jones (1999) points out in drawing attention to the continual downsizing of even profitable firms at the bestest of the all-powerful capital markets, we have a situation where an unresistable combination of external financial hegemony and internal bureaucratic control procedures conspire to

prevent organisations from being socially responsible in anything but an instrumental sense.

Against such a background, stakeholder dialogue and engagement processes however well meaning are highly unlikely to pose any real threat to the economic 'imperatives' of globalisation which pay scant heed to the interests of employees, consumers and communities<sup>xiii</sup>. Essentially, in the absence of any meaningful reform to corporate governance processes, designed to pass over real elements of power to stakeholder groups other than capital providers, we are left with simply a corporate led dialogue (or monologue?) agenda. The overwhelming advantage enjoyed by corporate interests in terms of the financial and expert power they are able to bring to the process indicates that this can hardly be otherwise. The control the corporate constituency is able to exert is likely to be all the more complete as they are well represented in the workings of influential bodies such as ISEA and the GRI, a situation that contrasts starkly with the very independence from such interests that characterised the work of Social Audit Ltd.

### **A Tentative Prognosis**

Over the past decade, environmental reporting, and more recently sustainability reporting, has become firmly established practice for a sizeable minority of the largest companies throughout Europe. The network of institutional support and encouragement for the process from government, industry, professional and pressure groups, together with the first forays into legislative requirement in some parts of Europe, suggests that the current reporting wave will not meet the same fate as the earlier 1970's initiatives. One can also confidently predict a rise in the proportion of companies progressing from purely environmental reporting into a more rounded sustainability approach incorporating the social and economic dimensions. The key question is, however, whether or not this reporting development heralds an era of significantly extended levels of corporate accountability to stakeholder groups other than capital providers?

Turning first to the longer established environmental reporting domain, which is likely to remain populated by companies outside the 'top tier' for some time to come, such an extension of accountability is severely limited. Certainly, the degree of rigour now

brought to the process by leading edge exponents has achieved significantly increased levels of transparency in terms of the (physical) environmental ramifications of corporate activity. Indeed, for profit seeking shareholders, one could argue that the potential for enhanced accountability is offered, should reports do more to clearly indicate strategic priorities (and related targets) in terms of managing environmental risk and spell out the 'bottom line' implications of the strategies pursued. For other stakeholders however, save perhaps for ammunition being supplied for pressure group activity, it is far more difficult to establish much of a case in accountability terms. This is for two significant reasons. Firstly, in excluding the social dimension reports fail to address key sustainability issues of concern to non-financial stakeholders. Secondly, there is a complete failure to close the reporting loop in terms of establishing appropriate institutional mechanisms for stakeholders to use information gleaned from the reporting exercise in influencing corporate decision making.

For its part, sustainability reporting with its commitment to incorporating the social dimension into the reporting domain offers much in terms of transparency with respect to issues of key stakeholder concern. Clearly, at this early stage of development a great deal remains to be done as regards the quality and robustness of data disclosure in the social (and economic) spheres. In drawing attention to this issue, the ACCA UK Sustainability Reporting Awards judges report (2002) notes that, "Undoubtedly the new version of the GRI sustainability report guidelines... will aid the advancement of economic and social reporting" (p.32). Certainly, the take up rate for GRI, particularly on the part of major multinationals across the globe, is encouraging with currently some 140 companies actively using the guidelines in preparing sustainability reports<sup>xiv</sup>.

As noted earlier, the GRI Guidelines present a challenging agenda for would be reporters with reports prepared on this basis certainly achieving a high level of transparency. Significant progress is already being made by leading edge reporters in terms of communicating employment and community impact data, with websites being used most effectively to convey detailed quantitative information. However, huge problems remain to be overcome. Most notably, as the ACCA judges report observes, organisations have to consider how growth in profitability, based on the

'business as usual' scenario that currently holds sway, can be reconciled with the pursuit of sustainable development in a world that is subject to significant ecological (and one might add, social) stress.

A further sensitive issue, just as was the case with environmental reports, concerns the process of verification. At the current time two verification models exist. The first is broadly based on a fact checking exercise, often restricted in scope, and the second intertwines a consultancy role with the audit function in offering direction on overall strategy, thereby raising serious concerns over independence (see *Ethical Performance*, Vol. 4, No. 5, 2002 p.1). Clearly, much further thought needs to go into developing a verification process combining independence and rigour with the provision of information that is both intelligible and useful to stakeholders. The cost of such an exercise would be a far from trivial matter, of course, should there be any desire to match the degree of rigour (theoretically) brought to the annual financial audit exercise. Most fundamentally, the question again arises as to how useful a verification exercise can be that purports to be conducted on behalf of stakeholder groups largely excluded within existing governance arrangements from using the information provided in order to influence corporate decision making.

The essential point, as Owen et al (1997) drawing on earlier work by Power (1994) have stressed, is that administrative reform in the shape of developing new reporting systems, in isolation can do little to achieve real social change. Rather, it must be accompanied by institutional reform designed to empower stakeholders by instituting more participatory reforms of corporate governance. In the absence of such reform, sustainability reporting, however well intentioned its practitioners may be, is highly unlikely to elicit much in the way of stakeholder involvement and hence lose much of its purpose<sup>xv</sup>. Surprisingly, for some leading commentators reform is a fairly unproblematic issue. Elkington (2001), for example, in claiming that we stand on the threshold of a new era of stakeholder capitalism, simply suggests that successful companies, "...will have to focus growing attention on business eco-systems of which they are part, seeking to co-evolve with a much wider array of stakeholders...." (p. 23) and, "... business will increasingly find itself with no option but to co-evolve global governance systems appropriate to the 21<sup>st</sup> century" (p.21). Unfortunately, information gleaned from current reporting exercises, strongly suggests Elkington's

optimism to be somewhat misplaced. Stakeholder dialogue processes appear to be very much one way, company controlled exercises designed simply to canvas stakeholder views on various aspects of performance. It is indeed difficult to see how such initiatives can amount to anything more than sound market research or (the largely discredited) 1980's vintage joint consultation exercises. Certainly, they fall far short of ISEA's vision of reformed governance procedures designed to secure the inclusion of stakeholders centrally in the reporting, and more importantly decision-making, process referred to earlier<sup>xvi</sup>. Quite bluntly, reports produced in these circumstances amount to little more than fashion statements rather than offering a means of enhancing public accountability.

Looked at from a UK context, I must confess to much pessimism concerning the likelihood of institutional reform. The long drawn out deliberations of the UK Company Law Review Steering Group have resulted in a White Paper (cm 5553, Modernising Company Law, July 2002) which simply concludes that;

"...the basic goal for directors should be the success of the company in the collective best interests of shareholders, but the directors should also recognise, **as the circumstances require**, the company's need to foster relationships with its employees, customers and suppliers, its need to maintain its business reputation, and its need to consider the company's impact on the community and the working environment" (s.3.3. emphasis added).

Whilst for economically significant companies some provision is made for publication of environmental and social information in a (to be legally required) Operating and Financial Review Statement this is subject to relevance and materiality considerations<sup>xvii</sup>. Significantly, the White Paper notes that, "It will, of course, be for directors to decide precisely what information is material to their particular business" (s.4.33).

For the UK then, voluntarism prevails and a meaningful extension of corporate accountability to stakeholders is off the agenda. Of course, for a number of countries in mainland Europe, a more pluralistic route in corporate governance matters has been followed in post war years. It remains to be seen whether progress along these lines is continued and social and environmental reporting thereby established as a truly worthwhile exercise. However, here again, the climate of voluntarism

underpinning corporate social responsibility issues subscribed to by the European Union gives little cause for real optimism. At the present time we simply appear to be drowning in a sea of stakeholder rhetoric which, in the current political and economic climate, leads us up a blind alley as far as extending corporate accountability is concerned. Reference was made earlier to a recent significant growth in the ethical investment market. Given the absolute primacy awarded to the interests of financial capital by European legislatures it can be argued that, for those seeking to promote the cause of corporate accountability, focussing attention on the operations of the capital markets, in particular the unaccountable power wielded by institutional fund managers, offers more hope of success than engaging in corporate controlled stakeholder dialogue processes.

## Notes

<sup>1</sup> Significantly, in a European context, the only legally mandated social reporting introduced in the 1970's the requirement for larger French companies to produce an annual social balance sheet (*bilan social*), confined itself to matters appertaining to employment issues.

<sup>2</sup> See Gray et al, 1996 chapter 9 for a fuller analysis of the work of Social Audit Ltd.

<sup>3</sup> The European participants are Belgium, Denmark, Finland, France, Germany, Netherlands, Norway, Sweden and the UK, with the other countries represented being the USA and Australia.

<sup>4</sup> Interestingly, communication and media companies also figured strongly in 2002 with a 46% reporting rate.

<sup>5</sup> For a fuller discussion of these, and other, initiatives see Gray and Bebbington (2001).

<sup>6</sup> For further information on the UK and European awards schemes, including copies of judges reports, go to [www.accaglobal.com/sustainability](http://www.accaglobal.com/sustainability).

<sup>7</sup> Other reporting formats worthy of mention are EMAS reports which tend to be light on detail and relate only to individual sites and eco (or mass) balance reports. The latter are very much confined to Austrian, German and Swiss companies, and whilst scoring highly on the completeness criterion in their identification of physical qualities of inputs, outputs (products and waste) and leakages and emissions from the production process, pose distinct problems in terms of comprehension.

<sup>8</sup> For an empirical study and discussion of this issue in a UK context see Jackson et al (2000).

<sup>9</sup> For a more detailed critique of these early verification exercises see Ball et al (2000).

<sup>10</sup> For a fuller elaboration of the following analysis see Owen (1995).

<sup>11</sup> For a comprehensive description of the major social sustainability standards, see Henriques and Raynard (2001).

<sup>12</sup> The issues touched upon here are considered in more depth in Owen et al (2001).

<sup>13</sup> Prominent amongst these processes are questionnaire surveys, interviews, focus groups and public meeting.

<sup>14</sup> This figure is per a list updated on 5<sup>th</sup> August 2002 accessible at [www.globalreporting.org/GRI Guidelines/reporters.htm](http://www.globalreporting.org/GRI%20Guidelines/reporters.htm)

<sup>15</sup> See, for example, the experiences of BT (*Ethical Performance*, Vol. 1 No. 9, 2000, p.8) and BAT (*Ethical performance* Vol. 4, No. 4, 2002, p.8)

<sup>16</sup> A very rare example of a company beginning to address the corporate governance issues of stakeholder based reporting is provided by the UK lottery operator, Camelot. Here, an advisory panel, consisting of individuals with professional expertise in stakeholder concerns, oversees the reporting process and advises on strategic matters. The panel is chaired by a non-executive director thereby providing a link to board level decision making.

<sup>17</sup> On the criteria adopted this would cover about 1000 companies (i.e. less than 0.1 per cent of registered companies) responsible for about a quarter of corporate economic activity in the UK (cm5553, s 4.37).

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