

The Role of Regulation in Social and Environmental Reporting in the UK

by

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Abstract

Over the last eight years, the UK government has reformed Social and Environmental Reporting (SER) regulations three times, introducing the Operating and Financial Review (2005), The Enhanced Business Review (2007) and the Strategic Report and Directors' Report (2013). These frequent changes and increasing stakeholder interest in SER regulation have resulted in a growing body of literature measuring firms' compliance with regulation. However, very little empirical research has been carried out analysing the impact of regulation on SER, and in particular, analysing the lobbying practices and attitudes of firms towards regulations governing social and environmental issues.

Thus, this research examines the role of regulation in social and environmental reporting in the UK, focusing on the development of and changes in the Operating and Financial Review (OFR) and the Enhanced Business Review (EBR). By examining the role of regulation as well as the practices and attitudes of firms towards SER regulation, the thesis evaluates their complementary effects. It is presented in three empirical chapters.

The first empirical chapter applies content analysis to documentary evidence, and employs in-depth interviews with key stakeholders, to examine the influence of lobbyists on government, in particular on the changes that occurred in the OFR and the EBR. Contrary to previous findings, the chapter finds that the Confederation of Business Industry (CBI) and the Friends of the Earth (FoE), contributed significantly to the changes that occurred in social and environmental regulations. In concluding that the government responded to pressure from lobbyists by reforming regulations, this thesis adds to the standard account of regulatory capture by showing that regulatory outcomes were a function, not just of lobbying, but also access to ex ante regulatory processes, creating a dynamic incrementalism in the regulatory framework.

The second empirical chapter explores the impact of the EBR on social and environmental Reporting on disclosures in firm's annual reports. To analyse the effect the introduction of the EBR had on the quantity and quality of SER, the chapter compares the SER levels of firms listed on the FTSE4Good and those not listed on the FTSE4Good; in particular to examine whether FTSE4Good listed firms *differ* from other firms in their reporting on social and environmental matters. The findings suggest that the EBR had a significant impact on firms SER, questioning the fears of cost and

competitiveness as articulated by the CBI's lobbying position against regulation. Furthermore, the chapter finds that whilst the FTSE4Good did not significantly differ in mandatory reporting levels from the Non-FTSE4Good, their engagement with voluntary reporting was higher. In light of the CBI's opposition to regulation and firm's increasing levels of SER, the chapter suggests that firms are increasingly using SER as a form of strategy in a bid to increase competitiveness in the SER field.

Finally, having suggested that firms are increasingly using SER as a form of strategy, the third empirical chapter explores this theory in detail. Using the Resource Based View it is argued that competitive dynamics explain firms' SER behaviour and that firms use SER to build their competitive position. It is postulated that firms pursue their competitive advantage, firstly, by using SER to create difficult to replicate assets and secondly, by adopting either a positive or negative attitude towards SER regulation depending on the quality of their SER assets. Thus, using interview evidence obtained from firms, it is found that firms either adopt a positive attitude towards regulation with the aim of standardising regulation to enable them to compete effectively, or alternatively adopt a negative attitude towards regulation with the aim of maintaining their competitive advantage in SER.

In summary, the thesis demonstrates that regulatory outcomes are a dynamic function of lobbying and previously enacted legislation, creating a path dependency in the evolution of control over firm behaviour. Firm level accounting disclosures reflect these outcomes, but also contain a significant element of voluntarism thereby increasing disclosure quality. The extent of disclosure and attitude to regulation are further strongly informed by the strategic posture of the organisation and the progressive empowerment of internal SER advocates that have emerged in response to the regulatory agenda.

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List of Abbreviations

ABI	Association of British Insurers
ACCA	Association of Chartered Certified Accountants
ASB	Accounting Standards Board
BR	Business Review
BIS	Department for Business, Innovation and Skills
CBI	Confederation of British Industry
CORE	Corporate Responsibility Coalition
CLR	Company Law Review
CSR	Corporate Social Responsibility
DTI	Department for Trade and Industry
EBR	Enhanced Business Review
FoE	Friends of the Earth
ICAEW	Institute of Chartered Accountants in England and Wales
NGO	Non-Governmental Organisation
OFR	Operating and Financial Review
PwC	PricewaterhouseCoopers
ROE	Return on Equity
SER	Social and Environmental Reporting
SRI	Sustainable and Responsible Investment
TJM	Trade Justice Movement
TUC	Trade Union Congress
TQnS	Total Quantity Score
TQIS	Total Quality Score

CHAPTER 1

Chapter 1. Introduction

1.1 Introduction

The regulation of social and environmental reporting (SER) has been a source of debate for over two decades. These debates are mainly focused on the implementation of streamlined regulation for SER, with one side calling for increased regulatory requirements and the other calling for reduced regulatory requirements. Over the last eight years, in seeking to improve and develop narrative reporting, the UK government has revised SER regulations three times: the Operating and Financial Review (OFR) (in 2005)¹, the Enhanced Business Review (EBR) (in 2007)² and most recently the Strategic Report and Directors' Report (in 2013). However in implementing these regulations, the UK government has been accused of taking sides, with Friends of the Earth (FoE), for example, criticising the government for inadequate regulations and being willing to be 'led by the nose' by the business lobby and ignoring public concerns.³

On the other hand, the Confederation of British Industry (CBI) argues that regulation imposes restrictions on firms and exposes them to unfair competition in the market. Indeed, Gallhofer and Haslam (1997) suggest that a voluntarist and market-based stance is likely to be advocated by businesses, an opinion which is resonant of the CBI's stance. Hence, the issue of SER regulation and lobbying has been brought to the fore by these debates and frequent regulatory changes. Consequently, a growing body of literature which examines the impact that lobbying has on regulatory outcomes, has emerged. Jupe (2000) and McLeay et al., (2000) are an example of these studies which

¹ An OFR is a balanced and comprehensive analysis of the development and performance of a company's business, including the main trends and factors underlying its performance and financial position during the year, together with the trends and factors that are likely to affect its performance in future years. The OFR must include information about environmental matters (including the impact of the business of the company on the environment), information about the company's employees, and information about social and community issues (The Companies Act 1985, Part 3).

² A Business Review is a fair review of the company's business within the reporting period. It must be a balanced and comprehensive analysis of the development and performance of the company, with a description of the principal risks. For reports relating to financial years beginning on or after 1 October 2007, the content requirements for a business review in the directors' report for quoted companies were extended significantly, to include information on environmental, employment, social and community issues and the main factors likely to affect the company's future business (the 'enhanced business review') (The Companies Act 2006, Section 417).

³ Macalister, T (2004). New rules for audits watered down by lobbyists. *The Guardian*, 26 November, p.21.

find that lobbyists exert a great level of relative power over the legislature. These studies further shed light on the influence lobbyists exert in regulatory processes. Several other studies have also examined the groups which are successful in exerting influence on the final enacted accounting standard (see for example, Kirsch and Day, 2001; Tutticci et al., 1994).

However, despite an increase of the literature on the impact of lobbying, few have examined the impact of lobbying on social and environmental accounting standards. Weetman et al., (1996) as well as Rowbottom and Schroeder (2014) have examined the impact of lobbying on the OFR, a form of narrative reporting. Nonetheless Weetman et al.'s study was carried out at a time when the OFR was non-mandatory, and Rowbottom and Schroeder's study failed to acknowledge the influence lobbyists exerted on the changes that occurred in the mandatory OFR. Hence, this thesis investigates the impact of lobbyists on the changes that occurred in the OFR and EBR, as well as the relationship between path dependence and the power of lobbyists. Furthermore, no empirical study to date has investigated the impact of lobbying and the lobbying processes which resulted in the changes that occurred in the EBR. Examining these aspects is important as the EBR was one of the longest standing SER regulations, and in analysing the lobbying practices and attitudes of firms towards these regulations, further evidence on path dependence in legislation is added to literature.

Likewise, previous studies have examined the annual reports of firms in order to measure firms' compliance with the EBR and measure the effectiveness of the EBR (see for example, Accounting Standards Board, 2009; Deloitte, 2009; Henriques, 2010; Tauringana and Mangena, 2009). Despite these studies, very little empirical research has been carried out analysing the impact of regulation on SER, in particular, analysing the attitudes of firms towards regulations governing social and environmental issues.

Although past research has examined the impact of regulation on firms' disclosures; these have produced conflicting results. For example Henriques and Sadowsky (1996), Owen et al., (2005) and Spence and Gray (2007) report a rise in firms' disclosures as a result of regulation. On the other hand, Tauringana and Mangena (2009), Henriques (2010) and a study by PricewaterhouseCoopers (2009), report very little or no impact on firms' disclosures as a result of regulation. Hence, in following the debate as articulated by the CBI on the costly nature and loss of competition, if regulation is made

mandatory, it is of interest to determine to what extent firms complied with the mandatory EBR as well as to determine whether the EBR had an impact on firms disclosure in the period after it was introduced.

Prior studies have also suggested that firms are increasingly using SER as a form of strategy (see for example Clulow et al., 2003; Falkenberg and Brunsæl, 2011; Vilanova et al., 2009). Other studies further suggest that regulation can be used as a form of competitive advantage (Barrett, 1991; Hart, 1995). However, little empirical research has been carried out on examining the strategic attitude of firms to SER and in particular their attitude to regulation. Therefore, the thesis will present further insight into the relationship between firms' strategic use of SER and their attitude towards regulation, in order to analyse the effect that regulation has on firms' behaviours towards SER.

The aim of the thesis is therefore to explore and investigate the role of regulation in SER, focusing on the OFR and the EBR, two important mandatory SER regulations. In so doing, this thesis examines the relationship between lobbying and the consequences it has on firms' attitudes towards SER and regulation. Specifically this thesis examines how firms reacted to the changes in the EBR and whether the business 'opposition' to regulation impacted on the quantity and quality of SER output. Further, this thesis controls for firms characteristics by testing if these characteristics contributed to disclosure levels. Finally this thesis discusses the concept of the strategic use of SER by firms and interviews firms to determine whether firms which portray a high strategic attitude to SER, exhibit a negative attitude towards regulation. It is hoped that the findings of this research will extend knowledge in core areas of accounting by adding to existing literature on SER, regulation and lobbying. In this regard, this thesis also hopes to portray how research can develop and contribute to effective SER regulations.

The remainder of this chapter proceeds as follows. In section 1.2, a discussion on the scope of enquiry is presented. Section 1.3 then presents the research questions. Section 1.4 discusses the significance of the thesis with section 1.5 detailing the contribution of the thesis. Section 1.6 concludes with a structure of the thesis.

1.2 Scope of Enquiry

In analysing the role of regulation in SER in the UK, the thesis presents three empirical chapters. The first empirical chapter (chapter 4) examines the influence pressure groups exerted in the removal of the OFR and the implementation of the EBR, and details how particular groups were involved in opposed mandatory regulations. Previous empirical research has presented evidence showing that lobbying has an impact on the regulatory processes that occur. McLeay et al., (2000) for example, examined the impact of constituent lobbying activities on accounting regulators and find that the industry group exerted the greatest level of relative power over the legislature, with the proposals from the academics displaying the least likelihood of success. Similarly, Kirsch and Day (2001) with the use of interviews and comment letters, find that lobbying is multidirectional, and suggest a mutual agency concept; as the standard setter had been lobbied by external parties in support of their points of view, and had also lobbied some of those same parties to gain support for its points of view. Despite this interest in the impact of lobbying on regulation, previous studies have failed to examine the impact of lobbying on the removal of the OFR.

A recent study by Rowbottom and Schroeder (2014) analysed the processes that occurred in the removal of the OFR. They find that the Treasury was instrumental in the events which led to the removal of the OFR. However in presenting this evidence, Rowbottom and Schroeder (2014) fail to acknowledge the impact and the influence the CBI exerted by pressurising the government on mandatory regulation governing SER. Rowbottom and Schroeder further base their analyses and findings on a narrow set of evidence, limited to Treasury documents as provided by the Treasury. Thus it is to be expected that a narrow set of information as the basis of analysis results in a narrow set of findings on which conclusions are based. Hence this chapter in responding to the findings of Rowbottom and Schroeder (2014) adds to literature by providing further evidence of pressure group lobbying; provided in the form of interviews with key stakeholders as well as media and parliamentary documents.

Furthermore, in presenting evidence of pressure group lobbying, this thesis analyses the ideologies and mechanisms by which these pressure groups lobbied; further examining the relationship between these pressure groups and the regulators. In so doing, the role of regulation is examined in detail. Moreover in analysing the impact of lobbying in

regulatory processes, the thesis adds to the political economy of accounting theory by suggesting that organisations protect their self-interests and will seek to deflect regulatory burdens. Finally, the chapter adds to existing literature by examining how SER regulation is influenced by political ideology and how the effect of ideological power is framed by regulatory preferences.

The second empirical chapter analyses the impact of the EBR on firms' disclosure, in order to monitor SER performance and evaluate firm's compliance with EBR. In so doing, the chapter distinguishes between voluntary and mandatory regulations to fully investigate the impact the EBR had on firms' disclosures before and after its introduction. Prior studies have found evidence suggesting that the impact of the EBR is low. For example, Taurigana and Mangena (2009) examine the annual reports of media firms to determine the reporting of financial and non-financial key performance indicators in compliance with the EBR and find that in spite of an increase in reporting over a four year period, the general compliance with the statutory EBR remains low. Henriques (2010), also in surveying the annual reports of the FTSE100 firms, finds that the Business review does not appear to be serving its purpose of improving the quality of firms' SER. As it is important that the SER performance of firms is monitored, in order to evaluate their compliance with regulation, this chapter conducts a systematic comparison of the SER levels, of both quantity and quality, of the FTSE4Good and non-FTSE4Good firms. This comparison will shed light on whether the FTSE4Good firms indeed *differ* in reporting levels against their counterparts. The importance of controlling for firm's characteristics in analysing firms' performance is also a technique which has been employed in several previous studies (see for example, Cowen et al., 1987; Gray et al., 2001; Hackston and Milne, 1996; Ljubojevic et al., 2012; Roberts, 1992; Toms, 2002). The most common firm characteristics used are size, profitability, leverage, listing and industry sector. Hence, employing statistical tests, the chapter analyses the impact of firms' characteristics of size, profitability, industry category and CSR committee to determine whether these characteristics contributed to firms' SER levels.

The third empirical chapter examines the issue of the strategic use of SER and firms' attitudes to regulation. The use of SER as a form of strategy has been documented in previous studies. For example, Clulow et al., (2003), find that managers realise the importance of the strategic use of SER. Hence the intangible assets that a firm possesses

such as its employee skills, consumer trust and firm reputation are important in providing the firm with a sustainable competitive advantage. Vilanova et al., (2009) further find that CSR in the strategic management process can contribute to implement a successful strategy in the firm. In addition, previous studies suggest that regulation can be used as a form of competitive advantage. Barrett (1991) for example argues that some firms can influence the form of the regulations in such a way to enhance their competitive advantage. Hart (1995) also finds that raising barriers through the setting of rules, regulations, or standards, also has provided the basis for many successful competitive strategies. Despite these studies, literature has paid far too little attention to SER regulation and if, and how, it is used as a form of competitive advantage. In particular, the use of the EBR or the OFR as a form of competitive advantage has been ignored in the literature. Hence this chapter adds to literature by exploring the concept of SER as a form of strategy, and analyses firms' attitude to regulation. Through the lens of the resource based view, this chapter further seeks to explore the attitudes of firms to SER regulation and how it is used as a form of competitive advantage. As such, this chapter examines the argument as put forward by pressure groups opposing regulation and investigates the attitudes of firms to SER and regulation.

In summary, this thesis reviews the growth of SER regulation and examines the role of regulation in SER. It is predicted, that lobbying will have an impact on the changes that occur in regulation and that regulation will have an impact on firms' disclosure levels; notwithstanding firms' strategic behaviour towards SER.

1.3 Research Questions

Based on the previous discussion of the scope of enquiry, the objectives of this thesis are to examine the following research questions:

1. How did pressure group lobbying impact on the removal of the OFR and the implementation of the EBR?
2. What is the impact of the EBR on firms SER in annual reports?
3. Why do firms display a strategic attitude towards SER and regulation?

1.4 Significance of the Thesis

This study explores the role of regulation in SER by examining the impact of lobbying on regulatory processes and the impact of the EBR on firms' disclosures. By examining the impact of lobbying on the changes that occurred in the OFR and the EBR, this study presents new evidence on the influence exerted by the CBI in the process leading up to the removal of the OFR. Few empirical studies have examined the impact of lobbying on regulatory changes. In light of this situation, many questions have been left unanswered by literature. In particular, what remains unanswered is what the impact of lobbying was, on the changes that occurred in the EBR. This is important to know as the EBR has been, to date, one of the most longest standing regulations, governing SER in the UK. Furthermore, how the EBR impacted on the quantity and quality of firms SER has also been largely ignored, notwithstanding the lack of empirical literature on analysing firms' strategic attitudes towards SER and how regulation is influencing firm behaviour. This study therefore sheds light on the lobbying practices in SER regulation as well as on the practices and attitudes of firms towards regulation. This study is therefore significant for the following reasons:

First, contrary to previous findings by Rowbottom and Schroeder (2014), it provides evidence showing how the CBI was instrumental in pressuring the government and preventing the implementation of mandatory SER regulations. Furthermore, evidence is presented showing how although the CBI claim to be the 'Voice of Business', in reality, business voice is more nuanced reflecting a more differentiated stance on regulation than suggested by the CBI. Moreover further evidence is provided showing how the FoE and other NGOs contributed significantly in the changes which led to the implementation of the mandatory EBR. Hence the chapter is significant as it shows that the biggest influence on future regulation is past regulation and lobbying groups, highlighting the relationship between path dependence of legislation and the power of lobbyists.

Second, this study presents evidence on whether the EBR impacted on the levels of SER disclosures. Prior research provides conflicting evidence on the impact of regulation on firms' disclosures. Thus this thesis presents evidence on the impact of the EBR on firms SER disclosures. In addition a comparison is made between the SER disclosures of the

FTSE4Good and non-FTSE4Good firms to evaluate the differences in the quantity and quality of SER reporting between these two indices.

Thirdly, this research examines the strategic attitudes of firms to SER and in so doing, examines their attitudes towards regulation. Previous research highlights the increasing use of SER as a form of strategy (Vilanova et al., 2009) and find evidence suggesting that regulation can be used as a form of strategy (Barrett, 1991). Hence in examining firms' attitudes towards SER and regulation, this study presents evidence on the impact of SER regulation on firms' attitudes towards SER, as well as the effect the regulatory system has on firms.

Finally, as the debate on SER regulation continues and the U.K government is under continued pressure to improve SER regulation, this research enhances the literature by providing evidence and identifying key players and their involvement in the implementation of SER regulation. Overall, the research will discuss the influence that lobbyists have on legislation; thus adding to the current literature on lobbying by corporate bodies and pressure groups on accounting standards.

1.5 Contributions of the Thesis

In examining the role of regulation in SER, this thesis contributes to knowledge in empirical and theoretical aspects. To date, no research has examined the impact of lobbying on the EBR and how it impacted on firms attitudes towards SER regulation. Given the significant changes made to narrative reporting over the last eight years, and the intense lobbying and parliamentary debates that occurred during this period, it is important that policy makers and organisations, understand how regulation is impacting on narrative reporting requirement, as well as on firms attitudes to regulation. The findings of the first empirical chapter further show that the CBI was influential in pressurising the government to reduce mandatory regulation and in the events that led to the removal of the OFR, information previously not exposed. The thesis also presents evidence of how the ideologies and mechanisms of key organisations, helped influence their actions towards SER regulation. In examining the impact of lobbying, this thesis does not only rely on comment letters as data sources, but also uses interviews and documentary evidence. The chapter further contributes to literature by presenting evidence on how the CBI is not representative of all businesses, highlighting the

divergence of views in the business lobby. In sum, as lobbying remains relevant to current and future regulatory activities on narrative reporting, the thesis highlights the relationship between path dependence and the power of lobbyists, a contribution which is generalisable and could be of interest, not only to researchers considering SER, but also those beyond the SER field.

The second empirical chapter examines the annual reports of firms', pre and post EBR to determine the effectiveness of the EBR on firms SER. In so doing, the chapter distinguishes between the voluntary and mandatory aspects of the EBR, an aspect which previous studies fail to employ. Moreover no empirical study has systematically conducted a comparison of the SER levels (quantity and quality) between the FTSE4Good and non-FTSE4Good firms. This thesis therefore contributes to literature by analysing the impact of regulation and examining the annual reports of these two indices. The findings suggest that the EBR had a significant impact on firms SER, questioning the fears of cost and competitiveness as articulated by the CBI's lobbying position against regulation.

The third empirical chapter explores firms' strategic use of SER, by analysing interview evidence. It finds that firms either adopt a positive attitude towards regulation with the aim of standardising regulation to enable them to compete effectively, or alternatively adopt a negative attitude towards regulation with the aim of maintaining their competitive advantage in SER. In light of the CBI's opposition to regulation and firm's increasing levels of SER, the chapter suggests that firms are increasingly using SER as a form of strategy in a bid to increase competitiveness in the SER field. As the role of regulation and how firms react to regulation has been largely ignored in literature, this chapter contributes to literature by showing that regulation has an impact on firms' general attitudes.

Overall, this thesis shows that regulatory outcomes are a dynamic function of lobbying and previously enacted legislation, creating a path dependency⁴ in the evolution of control over firm behaviour. Firm level accounting disclosures reflect these outcomes,

⁴ Generally interpreted, path dependence means that current and future actions or decisions are influenced by previous actions or decisions. Hathaway (2001) further argues that history influences the pattern and process of legal change. Hence it is impossible to understand the law as it is today without understanding the law as it was in the past (p. 602).

although these contain a significant element of voluntarism thereby increasing disclosure quality. In addition, the extent of disclosure and attitude to regulation are strongly informed by the strategic position of the organisation and the progressive empowerment of internal SER advocates that have emerged in response to the regulatory agenda.

In concluding that the government responded to pressure from lobbyists by reforming regulations, this thesis adds to the standard account of regulatory capture by showing that outcomes were a function, not just of lobbying, but also access to ex ante regulatory processes, creating a dynamic incrementalism in the regulatory framework. In addition, in showing that pressure groups were influential in the changes that occurred in the removal of the OFR and the implementation of the EBR, this thesis adds to the political economy of accounting theory – that organisations protect their self-interests and will seek to deflect further regulatory burdens.

1.6 Structure of the Thesis

This thesis consists of seven chapters. Chapter 1 introduces the research, the scope of enquiry for this thesis, and presents the research questions. The significance of the study and the contribution of the thesis are also presented and discussed. The chapter ends by outlining the structure of the thesis.

Chapter 2, the literature review, introduces the concepts of SER and regulation, further discussing the theories associated with these two concepts. Previous literature examining the effect of regulation on social and environmental disclosure, is also presented in Chapter 2, showing how lobbying is an integral part in regulatory processes. This chapter also discusses the conflicting evidence found, on the impact of regulation on SER.

Chapter 3 covers the Data and Research Methods. It presents the research methods, and methodology, used to analyse the data. In so doing, the chapter illustrates how the thesis combines the use of literature, content analysis and interview study research methodologies in achieving the aim of the research. More detailed information on the data sources and data analysis are presented and discussed in Chapters 4 to 6.

The first empirical chapter, Chapter 4, examines the influence pressure groups exerted in the changes that occurred in the removal of the OFR and implementation of the EBR. In addition, the chapter discusses the issue of lobbying and strategic SER, in order to examine how businesses are increasingly using SER as a form of strategy while at the same time opposing mandatory regulation in a bid to ensure continued competitiveness in the SER field. The chapter then examines the relationship between the government and the pressure groups involved, and in so doing, highlights the congruence of ideologies and mechanisms, as displayed during the regulatory processes.

The second empirical chapter, Chapter 5, examines the effects the EBR had on the quantity and quality of firms SER. In particular the chapter distinguishes between voluntary and mandatory SER to present a detailed examination of the impact of the EBR. Statistical tests on firms' disclosures are employed in order to investigate the effect of firms' characteristics on SER disclosure. This chapter is the first study which systematically conducts a comparison of the SER levels (quantity and quality) of two indices, the FTSE4Good and the non-FTSE4Good.

Finally, the third empirical chapter, Chapter 6, examines whether firms are using SER as a form of strategy. In addition the impact of regulation on firms' strategic attitudes towards SER and towards regulation is explored. Moreover the issue of whether firms are using SER regulation as a form of competitive advantage is examined in this chapter.

Chapter 7 concludes this thesis. This chapter presents a summary of the findings, and their significance, of the thesis. Furthermore, the chapter outlines the policy implications of the research as well as directions for further research.

CHAPTER 2

Chapter 2 . Literature Review

2.1 Introduction

The regulation of Social and Environmental Reporting (SER) has been a source of debate by researchers, firms, NGO's and policy makers, for over two decades (Gallhofer and Haslam, 1997; Hart, 2010; Polishchuk, 2009; Rivoli and Waddock, 2011; Vogel, 2005). In this regard, previous research (see for example, Friedman and Miles; 2001; Owen, 2004; Prout 2006; Solomon, 2007) has investigated and highlighted the importance of regulation. Additionally, reports by a number of Non-Governmental Organisations (NGOs) detail their desire for firms to be made more accountable in reporting on their social and environmental issues. However there are other organisations such as the Confederation of British Industry (CBI), which argue that SER regulation interferes with the efficiency of the market, and the London Stock Exchange (LSE), stating that increased transparency requirements open the main market companies to unfair competition; forcing them to expose their business strategies in ways that competitors that are off the main market are not required to. Furthermore, an increasing number of studies have examined firms' compliance with regulation governing SER (see for example, Accounting Standards Board, 2009; Deloitte, 2009; Henriques, 2010; Tauringana and Mangena, 2009). However despite this long-running debate and studies investigating firms' compliance with SER regulation, the impact of lobbying and attitudes of firms towards SER regulation, remains largely ignored.

This chapter discusses previous research carried out on SER and regulation in order to inform the empirical studies in this thesis, which are, to examine the impact of lobbying on the changes that occurred in SER regulation, to examine the impact of regulation in firms annual reports, and finally, to examine the strategic attitudes of firms to SER and regulation.

The aims of this chapter are therefore:

1. To critically examine work done to date on SER, regulation and lobbying, in particular identifying gaps in previous empirical literature, in order to justify the research questions.

2. To present a summary of existing work on social environmental reporting and regulation, including the different ways in which these works have been studied, as well as the different ways these concepts have been defined.
3. To discuss the various theoretical approaches applied and evaluate their usefulness.
4. To assess the methodologies and methods that have been employed to study SER and regulation in order to evaluate the relative strengths and weaknesses of the literature.

Following the introduction, Section, 2.2, discusses the definitions and perceptions of SER, Regulation and competitive advantage, highlighting their use within the SER literature. Section 2.3 presents and discusses the theories underpinning the concept of SER, Regulation and competitive advantage. Following that, Section 2.4 then presents previous empirical evidence on lobbying and regulation, the impact of regulation on SER and, a discussion on the relationship between SER and Competitive advantage. Then, Section 2.5 identifies the gaps in the literature and shows how these gaps have provided a basis for this thesis. Finally, Section 2.6 concludes with a summary of this chapter and introduction of the next chapter, Data and Research Methods.

2.2 The Definitions and Perceptions of SER, Regulation and Competitive Advantage

2.2.1 Defining SER

The concept of social and environmental reporting has evolved from corporate social responsibility (CSR), which is defined by the Department of Business Innovation & Skills (BIS) as ‘...*how companies address the social, environmental and economic impacts of their operations and so help to meet our sustainable development goals*’⁵. Waddock and Bodwell (2004) also define CSR as ways in which a company’s operating practices (policies, processes, and procedures) affect its stakeholders and the natural environment. Rivoli and Waddock (2011) however, argue that there is no generally accepted definition of CSR as responsible corporate practice shifts over time. Therefore accepted corporate activities at one point could be considered irresponsible at another

⁵ Department for Business, Innovation and Skills (2010) Corporate Responsibility. Available from <<http://webarchive.nationalarchives.gov.uk/20100402205747/bis.gov.uk/policies/business-sectors/low-carbon-business-opportunities/corporate-responsibility>> [Accessed 20 June 2012].

point in time, thus a ratcheting quality. Nevertheless, researchers also define CSR more as a theory or a concept, whereas businesses and society groups interpret it as a more practical, localised, oriented set of actions often directed towards sustainability and affected by their stakeholders' content. As SER describes only the social and environmental aspects of company narrative reporting, omitting economic aspects, this thesis focuses only on SER, though references are sometimes made to the mention of CSR in other studies. SER is therefore the process of organisations communicating their social and environmental actions to stakeholders, through various forms of media such as annual reports, websites and separate social and environmental statements. SER also '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, p9).

Gray et al., (1995) further summarise social and environmental disclosures into four broad categories; employment, environment, community and customers. Adam's (2002) also suggests that due to the heightened interest in the demand for the provision of non-financial information, social and environmental information should contain the basic information which are; matters relating to the environment, employees, consumers or products and community. Hackston and Milne (1996) however include another dimension, and their creation of a checklist of categories for SER (social disclosure in their study) includes the broad headings of Environment, Energy, Employee, Products and Community Involvement. Campbell and Slack, (2008, p. 3) also posit that the typical contents of social and environmental disclosures should include information on human resources, communities, environmental resource consumption and environmental impact. In addition, the Accounting Standards Board (ASB) and Department for Trade and Industry, suggest that information to be presented by companies in relation to SER should include inclusion of community information, environmental information, employee information and customer information. Consequently, as in it in line with the aims of this research, this thesis adopts the four broad categories as posited by Gray et al., (1995) which are employment, environment, community and customers; supported by the requirements as contained within the Companies Act 2006 Chapter 5, Section 417 (5b); *Contents of Directors' Report:*

Business Review; which states that quoted companies should report on information about environmental matters, employees, and social and community issues.

In exploring the concept of SER further, the next subsection discusses stakeholder perceptions and motivations of SER, as it informs how firms perceive and why firms engage in SER, regardless of regulatory requirements.

Perceptions and Motivations of SER

Perceptions

A firm's behaviour towards SER could be attributed to a lot of factors. This includes internal factors such as the firm's culture or external factors such as pressure from stakeholders. Whichever way a firm views SER shapes their attitude and perceptions towards it. However much of the literature of perceptions of SER has tended to focus on the perceptions of corporations, and by so doing fail to involve other key players, such as regulators and NGOs.

SER is viewed as a temporal process; and represents the ongoing tension gap between social expectations expressed legally or through norms and company behaviour (Rivoli and Waddock, 2011). Business organisations are embedded in different national systems and will therefore experience divergent degrees of internal and external pressures to engage in social responsibility initiatives (Aguilera et al., 2007). A socially responsible company may thus takes steps in the interests of its stakeholders that are not dictated by direct commercial needs and market requirements (Baron, 2001).

Polishchuk, (2009) however argues that when a company takes the interests of its stakeholders into account of its activities, they inadvertently contradict the classical concept of a private company as a tool for creating and multiplying profits for their shareholders. The management of a company is therefore accountable only to the shareholders and must be guided in its activities solely by their interests. Polishchuk's argument highlights Friedman's (1970) view that the social responsibility of business is to increase its profits. Polishchuk's (2009) view is however narrow-focused, as it relates to private companies only, thereby limiting its scope and application. Karnani (2011) also posits that companies do not have a social responsibility, but have a fiduciary duty to their shareholders to maximize profits while conforming to the laws and norms of society, therefore CSR activities are negatively related to profits. Companies therefore

talk a lot about CSR but do very little, derisively referred to as ‘greenwashing’ which might result in delaying effective regulation. To this end, Gallhofer and Haslam (1997) argue that “green accounting” should be open, accountable and properly subject to a democratic process, to reduce the possibilities or opportunities for firms to engage in green washing. However Karnani, (2011) argues some companies are ahead of the curve in implementing socially desirable activities before required to do so by law. Moreover, companies’ responses to changing social expectations, in particular, their serious implementation of CSR initiatives into their strategic goals, have the potential not only to change their corporate culture but also to impart true social change (Aguilera et al., 2007). In addition, variance in viewpoints often exists within management on issues such as ecological responses (Bansal & Roth, 2000) or ethics programs (Weaver et al., 1999) and management will incorporate CSR in their organisational strategies only when doing so is clearly associated with greater economic opportunities, as in the case of green marketing (Smith, 1990). Thus it is reasonable to state that the perception that a firm has of SER is likely to shape their attitude towards it. Furthermore, an aspect influencing firms’ attitude towards SER is the issue of what motivates firms to report. This is discussed next.

Motivations

The reasons why an organisation might report is hardly known but the literature suggests a number of reasons why companies engage in SER. Owen (2004) for example posits that managerial motivations for making social and environmental disclosures has developed in the CSR research agenda for over a decade and have been investigated more directly through interviews.

CSR is driven more by an *intrinsic* motivation than by an *extrinsic* motivation (Graafland and van de Ven, 2006). Several theories have been further proposed for these motivations; including the legitimacy theory which is where a company reports to legitimise their actions within society. How corporations maintain their legitimacy, perhaps through social disclosure, is influenced by management perceptions of the threats to legitimacy (Deegan et al, 2000). This reactive approach is demonstrated in the many empirical studies finding that companies publish more environmental information in reaction to increased environmental exposures or some environmental event (see for example Deegan and Rankin, 1996; Patten, 1992). Also, previous research examining the relation between environmental disclosures and environmental performance often

indicate a reactive approach. An example of a reactive social change is when Royal Dutch Shell re-evaluated its operating principles and issued its first social report following a public outcry against Shell's operations within the Ogoni Community in Nigeria (Aguilera et al., 2007).

Gray (2003) further identifies some possible reasons for company engagement with SER which includes: educate stakeholders; explain the organisation's achievements; indicate to potential regulators that legislation is unnecessary; persuade stakeholders that the organisation is "walking the talk"; counter environmentalists claims; legitimate the industry; express the personal commitment by the board; signal to financial stakeholders that environmental risk is managed sensibly and provide an external focus for the environmental management systems. Curran (2005) also posits that the main motivational factors include profit, image and reputation, altruism, consumer demand, government policy and economic climate. Other reasons include the issue of competitiveness (Porter and Kramer, 2006), where companies in a bid to stay in the market, report on their Social and Environmental Issues (SEI) to portray a sense of responsibility and hence seek favour with this same market; as well as the business case (Unerman & O'Dwyer, 2007), which emphasises the benefits of reporting and regulatory reasons. SER is also widely viewed as a form of symbol (Buhr, 1998, Patten, 1992).

The use of CSR as a strategic tool has also been discussed in the literature. Polishchuk (2009) for example suggests that CSR is dictated by strategic considerations: to elicit a favourable response for the company from stakeholders or to prevent a threat from them to business. Baron (2001) also argues that a firm motivated only by profits may adopt a practice labelled CSR because it increases the demand for its products (Baron, 2001, p. 9). Thus, Baron concludes that, this strategic CSR is simply a profit maximisation strategy motivated by self-interest and not by a conception of CSR.

In summary, motivational factors for engaging in SER, as identified in previous literature include:

- The desire to comply with legal requirements. This would not be a major motivation in a great deal of countries given the lack of requirements in relation

to social and environmental disclosures and associated verifications (Deegan, 2000).

- ‘Economic rationality’ considerations – that is, there might be business advantages in appearing to do ‘the right thing’ and this might be a key motivation rather than any acceptance of any social responsibilities of business (Friedman, 1962).
- A belief in an accountability or responsibility to report – that is, there could be a view held by managers that people have an inalienable right to information that should be satisfied (Hasnas, 1998; Donaldson and Preston, 1995; Freeman and Reed, 1983) regardless of the associated costs.
- A desire to comply with borrowing requirements. Increasingly, lending institutions are requiring, as part of their own risk management policies, borrowers to periodically provide various items of information about their social and environmental policies and performance (Deegan, 2002).
- To comply with community expectations; reflective of a view that compliance with the ‘community licence to operate’ (or ‘social contract’) is dependent upon providing certain accounts of social and environmental performance (Deegan, 2002).
- A result of certain threats to the organisation’s legitimacy. For example, reporting might be a response to negative media attention, particular environmental or social incidents, or perhaps as a result of poor rating being given by particular ratings agencies (see Deegan et al., 2000, 2002; Patten, 1992).
- To manage particular (powerful) stakeholder groups (see Ullman, 1985; Roberts, 1992; Evan and Freeman, 1988; Neu et al., 1998).
- To attract investment funds. Internationally, “ethical investment funds” are becoming an increasing part of the capital market; for example, the FTSE4Good Index and the Dow Jones Sustainability Group Index. People responsible for rating particular organisations for the purpose of inclusion or non-inclusion within the funds’ investment portfolio utilise information from a number of sources, including information being released by the organisations themselves (Deegan, 2002).

- To forestall efforts to introduce more onerous disclosure regulations. Evidence shows that one of the reasons that the Australian Minerals Industry introduced its code of environmental conduct, which requires external environmental reporting, was a fear that government might take the matter further and instigate the development of regulation (Deegan and Blomquist, 2001).
- To win particular reporting awards. There are a number of environmental, social, and sustainability reporting awards being offered within numerous countries throughout the world, with possibly the most well-known ones being those offered by the Association of Chartered Certified Accountants. Many organisations put a great deal of effort into winning these awards, and receiving the associated positive publicity such awards generate. Winning an award might in turn have positive implications for the reputation of the company (Deegan and Carrol, 1993).

Thus it is seen that there are diverse factors which motivate firms to engage in SER. As is seen later in Chapter 6, the reasons why firms' report, are similar and include strategic, legal and stakeholder reasons.

In summary, the above section has discussed the perceptions and motivations of SER. The next section, 2.2.2, discusses the concept of regulation.

2.2.2 Defining Regulation

Regulation is the act of controlling or governing conduct in certain activities. It is 'a set of formal and informal rules that govern the behaviour of private individuals, businesses and public organisations... It is used by governments to influence choices, decisions and preferences in a way which helps deliver economic, social and environmental objectives that are in the public interest' (Business, Enterprise and Regulatory Reform (BERR), 2008). Regulation can take many forms: legal restrictions promulgated by a government authority, self-regulation, social regulation (e.g. norms), co-regulation, and market regulation.

The process of governmental regulation begins after legislation is passed in parliament. These regulations are enforced by agencies appointed by government and they could be destroyed by governments be it through sheer pressure or for the fact that the regulation,

given evidence, is no longer useful. This process of destroying regulation is termed as deregulation with in some cases, governments choosing to deregulate to give businesses greater freedom. A mainly political process, regulation is normally caused by social demand although occasionally it stems from political demand.

Regulations on business can benefit a range of stakeholders, including corporate and financial institutions, interest groups, employees, customers, and the general public. Of course, such regulations impose costs as well as benefits. These costs— including capital and other compliance costs as well as an increased risk of litigation or of civil or criminal penalties—typically fall most heavily on the businesses being regulated (Dixon et al., 2006). Regulation has a major role to play in society, hence the need for corporate companies to adhere to legislative requirements. The compliance with regulation is therefore an essential component of corporate issues. (Gray, 1995; Deegan, 1996; Deegan and Gordon, 2002; Miles. et. al, 2002). In order to highlight the perceptions surrounding regulation, the next section discusses the importance and desirability of regulation, as well as government’s role in managing regulation.

The Importance and Desirability of Regulation

Legislation has been facilitated by Corporate Responsibility (Rivoli and Waddock, 2011). History also suggests that regulation and other social and political forces have been much more effective than CSR at shaping firm behaviour. In fact, social reformers have long exposed (negative) corporate practices as means of mobilising political support for new legislation or regulation aimed at curbing them (Reich, 2008). Gallhofer et al., (2011), for example, posit the need for the development of a body of international law that would recognise business obligations to protect human rights. Aguilera et al., (2007) also argue that the laws governments pass to encourage CSR are uniquely powerful because they can achieve broader coverage than voluntary initiatives, such as the UN Global Compact (substantive human rights standards) or the Global Reporting Initiative (social, economic, and environmental disclosure format). An output of the desirability of regulation is the Climate Change Act of 2008, which following extensive consultation was implemented and is now being adhered to by the UK.s largest companies.

Moreover, the laws and policies that governments enact send a strong signal about the importance of a subject, a signal that, with regard to SER, is amplified by the business

culture, consumers' interests, institutional investors' actions, the corporate governance regime, to name a few (Aguilera et al., 2007). For example, some UK companies have adopted the practice of awarding schemes for employees' engagement with community matters.

The importance of regulation which is at the forefront of business agenda, and government agenda, shows the strong interlink between regulation, businesses and society, bolstering the importance and contribution of this study. Regulation therefore has an important role to play in protecting both society and the environment. It is argued that regulation emerges out of a force to maintain self-regulation by the profession versus a desire by government to intervene directly in times of crisis (Byington and Sutton, 1991). Nevertheless, better regulation brings in better benefits and everyone needs to get the balance right as considerable damage to the environment could be caused by even a few people acting in a self-interested way (BERR, 2009).

Spence and Gray (2007) also state that in the absence of any regulatory requirements and as long as the discourse of social information is non-mandatory, companies are highly likely to report external social information for legitimacy purposes. To prevent companies from using social information as an image-making tool, a way forward could be through regulatory codes of conduct, whereby regulations or recommendations concerning ethical and social issues related to different stakeholder groups are explicitly outlined for companies.

Arguments on Regulation

The subject of regulation has however been one of the most contentious, with critics such as the CBI arguing that regulations interfere with the efficiency of the market, and advocates arguing that well designed regulations not only make markets more efficient but also help ensure that market outcomes are more equitable (Stiglitz, 2009). Where there is lack of regulation, companies are highly likely to report less or none at all. For example, EIRIS recent report in August 2009 identified that only a third of the world's largest companies produced reports on how they are tackling climate change. Companies seem to refuse or fear to tackle information which seems hard to confront, rather concentrating on reporting easy ones like health and safety etcetera, whilst others have complained of the extra cost of providing SER in their annual reports.

Further research into regulation have identified that there are issues surrounding government regulation, which pose some problems. One of these is that regulation in itself is unable to cover every aspect in detail of a corporation's operations. This leads to burdensome legal processes bogged down in interpretations of the law and debatable grey areas (Sacconi, 2004). This situation has further given rise to the business case for SER, which is that companies would benefit from voluntarily being social responsible. The business case is increasingly being promoted by the government and corporations as justification for self-regulation (Hart, 2010). The idea of self-regulation within legislative parameters can be interpreted as a move away from state responsibility and as a form of deregulation (Murray, 2004). ‘Regulating self-regulation’ (Bluff et al., 2004, p. 4) has always meant more emphasis on persuasion, such as collaboration, training and education, than on development or enforcement of any existing regulations (Nichols and Tucker, 2000; Walters, 2005).

A recent example of deregulation by the UK government is the introduction on the 1st September 2010 of a ‘One in –one out rule, to be effective for all regulation beginning on or after 1st January 2011. With this rule, which applies to government departments only, BIS states that if the government needs to bring in new legislation, one which will impose a direct cost on businesses and voluntary organisations, the department will have to remove or modify an existing regulation of equal cost. This is the current view taken by the UK government whose stance is that ‘unnecessary red tape can stifle growth, so reducing it is critical to making the UK the best place to start and grow a business’⁶.

Reliance on the business case in the argument for self-regulation is however seen as problematic (Hart, 2010). The business case, it is argued, is flawed because of its instrumentality in the context of a global discourse and economy. Therefore the reliance on the business case to justify self-regulation for equality and safety in the workplace, for example, is problematic (Hart, 2010). Also the business case clearly has ‘greater salience for some organisations than others and one should not be surprised to see inaction as well as action’ (Dickens, 1994, p.11). The rationale for the business case in

⁶ Department for Business Innovation and Skills. (2010). Reducing the impact of regulation on business. Available from: <<https://www.gov.uk/government/policies/reducing-the-impact-of-regulation-on-business/supporting-pages/operating-a-one-in-two-out-rule-for-business-regulation>>. [Accessed 10 January 2012].

simple terms is that CSR will, either directly or indirectly, result in a corporation's improved financial performance, thus inciting them to voluntarily behave ethically, leading eventually to positive social and environmental change. However, Vogel (2005) pointed out that a firm is more likely to be punished for misdeeds rather than for excellent CSR performance, so that companies are likely to perform within a narrow range around a regulatory norm or, in a few cases, such as child labour, a civil norm. Cragg (2005) identified the potentially serious consequences of relying on the instrumentality of the business case in a self-regulatory context, arguing:

... self-regulation based on voluntary standards of conduct is not simply bound to be ineffective; it is also profoundly deceptive. By advocating self-regulation as an effective alternative to regulation by democratic institutions, corporations are moving the task of setting standards from the public arena, where motivations and principles are subject to public scrutiny and debate, to private control, where the dominant and dominating motivation is governed by private (financial) interest (p. 15).

Empirical research has also shown that 'regulating self-regulation' is most successful in companies "... that have a "natural interest" in safety matters, due to the high risk in the production process or the social "visibility" of the company' (Aalders and Wilthagen, 1997). However, asking companies to voluntarily sacrifice profits to increase public welfare will not work. A more effective solution is to rely on government regulation and pressure from other social and political organizations (Karnani, 2011). Thus, the tendency for individual managers not to improve social and environmental standards until their industry acts collectively, because their relational motives within the industry are stronger than their instrumental motives to use CSR for competitive advantage in the market, should be understood as a market failure and a rationale for government regulation (Aguilera et al., 2007).

Path Dependence in Legislation and Policy

One further aspect relating to regulation is the issue of path dependency, in particular how path dependence is used by a group or organisation to advance its cause. Path dependency is often said to make the strongest claim with regards to how policies are implemented. Previous studies provide evidence of how path dependency is used within institutions. Dimitrakopoulos (2001) for example finds that the UK, France and Greece

parliaments have all used familiar mechanisms and procedures in reacting to the challenges stemming from the process of European integration; underpinned by a limited amount of innovation.

Further studies have also highlighted the importance of path dependence in legislation and policy (see for example, Levin et al., 2007), with Hathaway (2001) arguing that it is impossible to understand the law as it is today without understanding the law as it has been in the past. However not all path dependence processes result in increasing returns or positive outcomes. (Gains et al., 2005) for example, find that some established institutional patterns reasserted themselves in the process of implementation, but that increasing returns are not as great as some theorists of path dependency would suggest. Page (2006) also argues that the focus on increasing returns and positive externalities is misplaced and scholars searching for evidence of path dependence should instead be looking for evidence of negative externalities. Nevertheless, within the field of regulation or law, the issue of path dependence is recognised, as evidence suggests that history plays an important role in legal development (Hathaway, 2001).

Hence, in line with previous studies, this thesis examines the impact of path dependence in the regulatory changes that occurred, in particular examining how the FoE was able to draw upon the tenets of old regulation to propagate their cause and effectively lobby the government.

Government's Role in Managing Regulation

The role of government is to introduce regulation that obliges firms to reduce the negative externalities, or impose tax on firms with the revenue utilized to reduce the negative impact. In such conditions, government plays its role and as long as companies comply with government regulation, such negative externalities can be reduced. The basic assumption is that the government in performing its duties is solely for the sake of public interest (according to the public interest theory); however, various empirical studies find that government officials take action not only for public interest, but also for personal or group interest (according to the interest group theory). The existence of this personal or group interest may result in the failure of government's role to provide public service, including in reducing the negative externalities of company's activities.

To this end, CSR plays its role to substitute government failure in performing its duties (Besley and Ghatak, 2007). Without being required by the government, a company implementing CSR strives to reduce its negative externalities and increase its positive externalities. Government action, both enacting laws and enforcing them, is nevertheless an important factor influencing firms to implement CSR initiatives and so become agents of social change (Aguilera et al., 2007).

Governments' interests in establishing competitive business environments, promoting social cohesion, and fostering collective responsibility for the betterment of society will lead them to push firms to engage in social change through CSR (Aguilera et al., 2007). In recent years, the UK government has been committed, through the BIS department, to creating a stable economy, with lower taxation and less regulation. In return, the government asks for the commitment, creativity and innovation of businesses to help grow the economy and tackle the wider challenges that face Britain (BERR, 2009).

The effectiveness of government regulation however depends on the complexity and scale of the tasks that are being implemented and the ability of regulatory authorities to perform their functions effectively. The more complex and numerous the tasks requiring regulation and the greater the doubts regarding the government's ability to accomplish them, the more grounds there are for relying on CSR (Polishchuk, 2009). Equally important is the government's ability to effectively manage regulatory powers, including selecting regulatory instruments in a timely and accurate manner and applying them professionally. This requires experience and qualifications, transparency and accountability for decision making by the regulatory authorities, an impartial and effective dispute-resolution system, and so on. It is further important that regulatory powers are distributed among the levels of government. For example the UK government has devolved responsibilities to several departments to implement legislation.

The government, may thus be viewed with good reason as "one of the chief and vigilant stakeholders". However, specific features of CSR can be explained on the basis of the structure of the country's economy, the way government authority and finance are organised, the state of society and the established institutional regime (Polishchuk, 2009). A change in political party can also bring about a change in regulation. For example, the Coalition government on assuming power announced, in 2010, their

intention to reintroduce the OFR, the regulation that was repealed by the Labour government 5 years earlier. Hence, it is to be expected that the government's role in managing regulation is one that is carried out in the public interest, however the government occasionally allows external influence in the form of lobbyists, to help it manage this role; further putting into question their reliability and core role in developing regulation. This is an issue which is discussed further in Chapter 4.

Having discussed previous studies on the concept of regulation, it is seen that regulation is increasingly being recognised as an important aspect in society, regardless of arguments for the business case and self-regulation.

2.2.3 Defining Competitive Advantage

Grant (1991), states that a firm's competitive advantage is determined by its ability to organise its resources and capabilities to produce greater performance. However, a more explicit definition of competitive advantage is given by Barney (1991); 'a firm is said to have a competitive advantage when it is implementing a value creating strategy not simultaneously being implemented by any current or potential competitors' (p. 102). Furthermore, Hofer and Schendel (1978) describe competitive advantage as 'the unique position an organisation develops vis-a-vis its competitors through its patterns of resource deployments' (p. 25). Firms therefore gain a competitive advantage when they implement strategies that exploit their resource strengths, respond to environmental opportunities, and neutralise weaknesses. The competitive advantage is then held by the firm while it is difficult for competitors to duplicate the successful approach (Branco and Rodrigues, 2006; Reed and DeFillippi, 1990).

To support the argument that firms use CSR as a form of strategy to achieve and or maintain a competitive advantage, a framework has been developed, based on an extensive review of literature. This framework shows some of the main resources and capabilities used by firms in their social and environmental endeavours.

Table 2.1 Resources and Capabilities: A Conceptual Framework.

Form of asset	Level of imitability	Assumptions	Selected authors
Resource Capability (R/C)			
Employees / Personnel / Managers (R)	Fairly easy to replicate	Personnel are mobile and their competitive advantage has the potential of being short-lived.	(Clulow et al., 2003; Smart and Wolfe, 2000)
Technology (e.g. creating websites; online reports)	Fairly easy to replicate	Technology is regarded as valuable but not a rare asset and therefore is not a factor in achieving a competitive advantage	(Barney, 1991; Clulow et al., 2003)
Information processing systems			
Technological knowhow (R)			
Accreditation / Certification (R)	Moderately difficult to replicate	Environmental awards, denoting public recognition of strong environmental performance, result in a significant, positive change in the market valuation.	(Deegan and Carroll, 1993; Klassen and McLaughlin, 1996)
CSR Committee, Specially created CSR Department (R)	Moderately difficult to replicate	CSR should not just be apparent explicitly, for example, in organisational activities, reports, strategies, and mission statements, but is implicitly present in the organisation through employee attitudes, behaviours, <i>decision-making</i> and organisational culture.	(Hackston and Milne, 1996; Hart, 1995; Jones and Bartlett, 2009; McWilliams and Siegel, 2001; Porter and Kramer, 2006; Russo and Fouts, 1997)
Employee skills / Managerial Judgement / Intellectual property / Mature CSR Systems (R)	Moderately difficult to replicate	Tacit knowledge and specialist skills of employees are difficult to imitate. The value of the firm is embodied both in the firm and in the knowledge and skills of the employees. It is the talents and modus operandi of the individual staff members combined with the firm's investment approach that create the key capabilities producing the firm's competitive advantage.	(Castanias and Helfat, 1991; Clulow et al., 2003; Grant, 1996; 1996 McEvily and Chakravarthy, 2002)
Intellectual Property Rights; Trade Secrets and Contracts (R)	Very Difficult to replicate	Contracts, in the form of agency agreements, license agreements, and property leases can constitute one of the most important resource categories of some businesses.	Hall (1992)
Creating Value (C)	Fairly easy to replicate	Strategy is the art of creating value. Strategic CSR occurs when a company adds a social dimension to its value proposition and makes a social impact integral to the overall strategy; to improve its efficiency and effectiveness.	Porter and Kramer (2006)
Benchmarking (C)	Fairly easy to replicate	A firm will always be looking at its competitors in order to keep up with trends. Firms also collaborate with competitors and peers and other groups; NGO's, Government	Falkenberg and Brunsæl (2011)

Form of asset	Level of imitability	Assumptions	Selected authors
Risk / issues management (C)	Fairly easy to replicate	agencies. Risk / issues management can be used by a firm to enhance its CSR activities.	(Kytte and Ruggie, 2005; Litz, 1996)
Verification (C)	Fairly easy to replicate	As auditing is not legally required and developing an applied CSR auditing procedure will be a challenging task engagement in auditing / verification by a firm, could be viewed as building a positive image.	Morimoto et al. (2005)
Engagement in CSR (C)	Fairly easy to replicate	Social issue participation, although valuable to the firm, does not generate a competitive advantage because it is largely a transactional investment which can easily be duplicated by competing firms.	Hillman and Keim (2001)
Sponsorship (C)	Fairly easy to replicate	Firm's use of Proactive policies such as sponsorship, could be seen as image enhancing strategies.	(Amis et al., 1997; Fahy et al., 2004)
Firm's culture and history; Unique organisational culture or R&D (C)	Moderately difficult to replicate	Culture can be a valuable, rare, and imperfectly imitable resource, and can be a source of sustainable competitive advantage. Also, a unique organizational infrastructure is a strategic asset.	(Barney, 1991; Clulow et al., 2003; Dierickx and Cool, 1989; Hall, 1992)
Stakeholder relationships Networks (C)	Moderately difficult to replicate	Stakeholder perception is important. Firms engage in CSR to manage particular (perhaps powerful) stakeholder groups. Stakeholder relations are inimitable and non-substitutable, and should therefore be seen as a source of competitive advantage.	(Bhattacharya and Sen, 2004; Brammer and Pavelin, 2004; Hillman and Keim, 2001; Post et al., 2002; Roberts, 1992; Ullmann, 1985)
Political Acumen (C)	Moderately difficult to replicate	Political strategy or political skills, for example a firm's influence on sector regulation, can be difficult to imitate.	(Mahon and McGowan, 1998; Russo and Fouts, 1997)
Reputation (C)	Very Difficult to replicate	Reputation is an accepted and valued intangible asset. CSR can help build and improve an organisations reputation. Reputation and client trust are also 'time-path-dependent'.	(Branco and Rodrigues, 2006; Falkenberg and Brunsæl, Kostopoulos et al., 2002; Vilanova et al., 2009)
Trust (C)	Very Difficult to replicate	A firm's strategy aimed at the development of and commitment to trust. Firm integrity (including honesty) builds barriers to duplication because this asset cannot easily be replicated by rivals.	(Amit and Schoemaker, 1993; Barney and Hansen, 1994; Jones, 1995; Katsoulakos and Katsoulacos, 2007; Moldaschl and Fischer, 2004)

Table 2.1 shows that there is a level of agreement in the literature on the assumptions made on the imitability of resources and capabilities; further suggesting that these resources and capabilities are used as a form of strategy to enhance firms competitiveness in CSR. In summary, by developing this framework, the thesis seeks to expand on previous RBV studies by applying this resource-based model of SER and competitive advantage, to examine the issue of firms' strategic use of SER, discussed in Chapter 6.

In the next section the theories used by previous studies and employed in this research are discussed.

2.3 Theories of SER, Regulation and the Resource Based View

2.3.1 Theories of SER

Numerous studies have attempted to place the empirical investigation of social disclosure into three broad groups of theories, including decision-usefulness studies; (which overlaps with) economic theory studies; and social and political theory studies (Gray et al., 1995a).

Decision-usefulness studies present the view that, companies disclose social information because traditional user groups, such as investors, creditors and shareholders, find it useful in making investment decisions (Blacconiere and Patten, 1994; Dierkes and Antal, 1985; Milne and Chan, 1999). Decision usefulness studies can be distinguished by two different aspects, namely the "ranking" studies in which analysts, bankers etc are asked to rank various accounting data in order of perceived importance (see Belkaoui 1984; Benjamin and Stanga, 1977) and secondly the investigation of information effects on share price behaviour (Aupperle, 1984; Richardson and Welker, 2001; Shane and Spicer, 1983; Spicer, 1978, Ullman, 1985). The use of the decision-usefulness studies is however limited. Gray et al. (1995) for example, argue that there is a negative view of the decision-usefulness theory, in that the term "usefulness" is ambiguous. CSR is not necessarily motivated by a concern for the needs, wants and whims of financial participants. Thus, there is a discrepancy between corporate non-financial motives and the financial information needs of financial stakeholders. Consequently, it is not appropriate for this study, which examines the role of regulation in SER, to be linked to the decision-usefulness theory,

as the focus of this study is not on how “useful” user groups find social information, but rather focuses on the impact of regulation on social and environmental reporting.

Economic theory studies are informed by Agency theory and Positive accounting theory (see for example, Belkaoui and Karpik, 1989; Ness and Mirza, 1991; Deegan and Hallam, 1991; Milne, 2002). For example, while Deegan and Hallam (1991) suggest that the value-added statement is produced in Australia to reduce political cost (agency cost), Milne (2002) did not find similar evidence for social disclosure. In this regard, there is a debate over the sophistication of economic agency and positive accounting theory, and consequently, the use of economic theory to explain SER issues has generated much doubt. Furthermore, economic theory studies are seen to have relatively little impact on the economic aspect of CSR. Their principal tenets firstly avoid any concern with what “should be” and secondly run entirely counter to principal concerns of CSR which is motivated primarily by market failures and desire to change current practice (Gray et al., 1995). In addition, these theories mainly explain voluntary financial reporting and fail to provide detailed guidelines on the measurement and reporting of social and environmental activities. Moreover, economic theory studies revolve around issues including classical and modern equilibrium theory, cooperative and non-cooperative game theory, macroeconomics, intertemporal economics (including dynamical systems), public economics amongst several others and hence have no direct link to SER.

As a result of the limited power of the decision-usefulness studies and the economic theory studies therefore, numerous studies now use social theories (see for example, Bichta, 2003; Deegan et al., 2000; Donaldson and Preston, 1995; Mobus, 2005; Moerman and Van Der Laan, 2005; Owen et al., 2005) or political theories (see for example, Buhr, 1998; Garriga and Melé, 2004; Gray et al., 1995b; Tinker and Gray, 2003) to interpret social disclosure. Social theories include the Legitimacy theory and Stakeholder theory, whilst political theories include the Political Economy theory.

Legitimacy theory rests on the concept that organisations have contracts with society and fulfilling these contracts, legitimates the organisations and their actions. Where an organisation is successful in meeting such contracts, this leads to congruence between the organisation and society (Guthrie & Parker, 1990; Brown & Deegan, 1998 and Cormier & Gordon, 2001). Cormier & Gordon’s (2001) also posit that the legitimacy

theory leads to the conclusion that the risk faced by a firm in capital markets will affect its reporting strategies. Hence, an organisation can attempt through communication, to become identified with symbols, values, or institutions, which have a strong base of social legitimacy.

The applicability of the Legitimacy theory in this study is however limited as does not adequately explain the role of regulation in SER. In particular, the theory is unable to explain why firms engaged in lobbying to increase/reduce SER regulation, nor does it satisfactorily explain why firms are strategically using SER as a form of strategy. This is due to the theory's focus on organisations fulfilling a contract with society, a focus which does not lend credence to the aims of this research. In addition, the legitimacy theory suffers from problems that include apparent conceptual overlap with political economy theory and institutional theory, lack of specificity, uncertain ability to anticipate and explain managerial behaviour and a suspicion that it still privileges financial stakeholders in its analysis (Parker, 2005, p. 846). Consequently, having determined that legitimacy theory is not best placed to explain the dynamics of SER regulation, this thesis adopts the Stakeholder theory and the Political Economy Theory, as they provide a sufficient lens for understanding the regulation of SER in the UK. These are discussed next.

Stakeholder Theory

The notion of the Stakeholder theory has evolved from a Stockholder perception. The Stockholder perception implied that managers have a duty to Stockholders, however this perception has progressed to a more contemporary view that managers now have a duty to stakeholders, encompassing a firm's owners, management, suppliers, customers, employees and the local community as a whole. Stakeholder theory is seen from the perspective of the management of the organisation who are concerned strategically with the continued success of the company. Thus the corporations' continued existence requires the support of the stakeholders and their approval must be sought and the activities of the corporation adjusted, to gain that approval. The Stakeholder theory accounts for the diversity of stakeholder interests and their competition for firm resources. When the owners have stakeholder wealth-maximizing interests, they will act to ensure the wellbeing of the different groups engaged in a relationship with the firm (Donaldson & Preston, 1995; Freeman, 1984; Jones, 1995). The more powerful the stakeholders, the more the company must adapt (Gray et al., 1995) and if stakeholder

interests are not in balance, the firm's survival could be in jeopardy (Bichta, 2003), to the extent that for example when wages are too high and product quality is too low, customers may leave, suppliers could suffer and owners could start selling stock and bonds, depressing stock price and making it difficult to raise capital at favourable prices.

Stakeholder theory analysts have argued that people, or groups with genuine interests in a firm, participate in the day to day running of the firm to obtain benefits and that there is "no prima facie priority of one set of interests and benefits over another" (Donaldson and Preston, 1995). Freeman (1984) however argues that there are attempts by companies to ascertain which groups are stakeholders in a corporation and thus deserve management attention. In other words, it attempts to address the 'principle or who or what really counts'. Stakeholders could also be categorised according to the way in which the company sees them, that is how important the stakeholders are to their operations (Smallman, 2004). Even with the classification, directors (as agents) attempting to serve too many principals, may fail to satisfy those with a genuine claim on the organisation. The Stakeholder engagement is such an important facet of company survival such that the United Nations Environment Programme (UNEP) has a manual, The Stakeholder Engagement Manual, which provides comprehensive information on how a company can undertake a rigorous stakeholder engagement process. The Global Reporting Initiative (GRI) also provides comprehensive guidance on stakeholder engagement. Bichta (2003) further propagates the acceptance of two stakeholder management principles, which serve as the foundation for articulating the stakeholder theory. These principles are the principle of corporate legitimacy and the stakeholder fiduciary principle. With the principle of corporate legitimacy, there is a redefinition of the purpose of the firm in line with the principles of corporate rights and effects, whilst the stakeholder fiduciary principle defines the duty of management to recognise the claims of the stakeholders.

The Stakeholder theory thus highlights the very purpose of a business, that is to serve as a vehicle for coordinating stakeholder interests and to meet the claim of each one of the group of shareholders, who are affected by corporations actions (Hoffman, Frederick 1995). For example, Solomon (2007) finds that companies did not view the proposed mandatory OFR as 'greenwash' but as a vehicle that would increase stakeholder confidence, as processes underlying the proposed OFR would be audited. The

importance of a social contract between companies and their stakeholders which most likely include regulators, therefore serves to show why a company has to adhere to regulatory guidelines in order to please their stakeholders.

There is also evidence to suggest that the Business Review and the Operating Financial Review (OFR) were mainly intended for shareholders. The Institute for Chartered Accountants of England and Wales (ICAEW) for example, highlights the importance of shareholders as the primary audience, stating ‘The business review is intended to allow shareholders to make an informed assessment of the performance and prospects of the company, and not as a repository for detailed information on corporate social responsibility and other issues that might be of interest to wider stakeholder groups’⁷. Owen, Shaw and Cooper’s (2005), survey also indicated that the intended audience for the OFR was shareholders. This survey of a ranking of perceived audiences by FTSE350 companies showed that nearly 80% of respondents thought that shareholders were of high importance and that they are perceived to be the most important audience for the OFR. Furthermore, Section 417 (2) of the Companies Act 2006, specifically states ‘The purpose of the business review is to inform members of the company and help them assess how directors have performed their duty under section 172’; essentially endorsing shareholders as the primary audience. Thus, it is reasonable to argue based on the above evidence that SER allows firms to give information to stakeholders that the firm believes is of importance to these stakeholders.

Equally important to the discussion on Stakeholder theory is the relationship between the stakeholder theory and competitive advantage. There is evidence to suggest that firms that attend to the needs of their stakeholders enjoy competitive advantages that are not available to other firms. The reason for this is that these firms have a better understanding of their primary stakeholders' utility functions, which in turn provides them with an enhanced ability to recognise value-creating opportunities (Harrison et al., 2007). Furthermore, competitive advantages occurring as a result of a good stakeholder management approach, are sustainable as they are associated with path dependence and causal ambiguity (Harrison et al., 2010).

⁷ Institute for Chartered Accountants of England and Wales (ICAEW) (2009). Enhanced Business Review. Available from <<http://www.icaew.com/en/technical/legal-and-regulatory/modernising-uk-company-law/enhanced-business-review>> [Accessed 12 October 2013].

Hillman and Keim (2001) further suggest that longer-term relationships with primary stakeholders are not easily copied, hence these relationships can give the firm a strategic competitive advantage. Other studies also argue that maintaining a good relationship with stakeholders, could result in a competitive advantage for a firm (see for example, Clulow et al., 2003; Deloitte, 2012; Hall, 1993; Jones and Bartlett, 2009, p. 7; McWilliams and Siegel, 2001). Thus, firms which acknowledge and endeavour to improve and maintain their stakeholder relations are at a greater advantage of achieving and sustaining a competitive advantage, relative to competitors.

Political Economy Theory

The Political economy theory is another theoretical concept that has been used to interpret SER. It is based on the argument that there are conflicting political, social and economic motivations within society (Gray et al., 1996), and suggests that SER is driven chiefly by socio-political concerns. Several studies attempt to interpret social disclosure (or non-disclosure) using the Political Economy theory (Adams et al, 1995; Adams and Harte, 1998; Adler and Milne, 1997; Buhr, 1998; Gray et al., 1995; Lim and Tsutsui, 2012), with the crucial point arising out of these studies being that political situations play a large role in the provision of social and environmental information by firms, as well as in the provision of regulation by governments.

The Political Economy theory also has a very long historical tradition. Zald (1970) for example defines it as 'The study of the interplay of power, the goals of power wielders and the productive exchange system' (p.223). Hence, as a framework, political economy does not concentrate exclusively on market exchanges, rather it first of all analyses exchanges in whatever institutional framework they occur and, second, analyses the relationships between social institutions such as government, law and property rights, each fortified by power and the economy, that is the system of producing and exchanging goods and services (Jackson, 1982, p.74).

Puxty (1986) further theorises that under the political economy theory, interests are in constant conflict and reflect the amount of power organisations wield. Thus, SER simply reflects the values and views of the corporation rather than wider social values (Adams et al., 1995), emphasising the inter-relationship between political and economic forces in society (Cooper and Sherer, 1984). The political economy further suggests that a number of different individuals, institutions and organisations, seek to preserve their

own self-interests, and therefore attempt to operate within the system through various relationships with others (see for example, Dahl, 1982, 1986). Therefore, 'Powerful organizational structures not only dictate, through their standard operating procedures, how things are to be done; they also impose beliefs about what *can* be done.' (Hancher and Moran, 1989, p. 288)

Moreover, Cooper and Sherer (1984) argue that power and conflict in society should be recognised in accounting, as power is widely diffused and society is composed of individuals whose preferences are to predominate in social classes. Thus, in recognising that social value is contested, the political economy of accounting highlights that accounting reports operate in specific interests. Actors, whether they are individuals or organisations, therefore have the right to pursue their own goals and self-interests (Clark, 1991). These rights, however, are moderated by the social environment in which they exist (Gray et al., 1996).

The political economy explanation of SER is however dominated by radical critical theorists' explanation of social responsibility. These theorists are mainly concerned with the socio-political and capitalistic economic system, and the power that exists within its structure (Adams et al., 1995ab; Cooper and Sherer, 1984; Tilt, 1994, Tinker and Gray, 2003). A conclusion is therefore drawn to the viewpoint that society consists of interests and ensures that the structure of such a society is reproduced.

An insight into the removal of the OFR by documents released by the Treasury Department in 2005, suggested that the repeal of the OFR was prompted when a fund manager from Hermes, met a senior official at the Treasury's enterprise unit and suggested that if the government wanted a quick win, they should get rid of the OFR - a good deregulatory measure which will be welcome in the city.⁸ In this regard, regulation or 'deregulation' is supplied to interest groups who provide benefits (e.g., votes, political contributions) to elected officials (Posner, 1974, p. 336). In addition, UK SER does appear to offer a plausible reflection of changes in the political economy of Britain (Gray et al., 1995). For example, the political agenda of the government in power at the time plays a huge part in the regulations implemented. Furthermore, together with the

⁸ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

governments deregulation process as well as decreasing costs with technological improvements, some large multinational companies have greater economic and social power than some governments (Garriga and Mele, 2004). In short, accounting standards are inherently political (Perry and Nölke, 2006).

2.3.2 Theories of Regulation

Several theories have been proposed for describing the issue of regulation, although these theories have tended to concentrate on the literature involving economics and finance. As a result, relatively few studies have attempted to apply regulatory theories to explain the regulation of social and environmental reporting. Four major theories of regulation have however been proposed by Croley (1998). These are: Public choice theory, Neo-pluralist theory, Civic republican theory and Public interest theory.

The Public choice theory argues for increased reliance on markets rather than on government regulation, whilst the Neo-pluralist theory takes group interests as central to determining regulatory outcomes. Furthermore, the Civic republican theory holds that regulatory decision making involves the identification of shared regulatory values, whilst the Public interest theory highlights that regulatory outcomes ameliorate market failures and vindicate the citizenry's interest. This study however, in examining the role of regulation in SER, rejects the Public choice theory, the Neo-pluralist theory, and the Civic republican theory and adopts the Public interest theory, arguing that the Public interest theory is appropriate for explaining the events which led to the implementation of the Enhanced Business Review (EBR). Reasons for rejecting the applicability of these theories are discussed next.

First, the Public Choice Theory which argues for increased reliance on markets, rather than on government regulation, is not resonant of the lobbying practices and the dynamics of SER regulation, as it focuses on the reliance on markets rather than government regulation – which is what this study addresses. Second, the Neo-Pluralist theory which takes group interests as central to determining regulatory outcomes, fails to confront the problem of collective action, nor does it explain how interest groups overcome a problem (Croley, 1998). In addition, the theory has little to say about how groups purportedly representing the average voter emerge, whether they are truly representative, and whether their resources are sufficient to allow them to impede rent

seeking by other interest groups (Croley, 1998, p. 65). Hence this theory is not appropriate in explaining how group interests and in particular pressure groups, contributed to the lobbying practices which resulted in the changes leading to the removal of the OFR and the implementation of the EBR.

Third, the Civic Republican theory which holds that regulatory decision making involves the identification of shared regulatory values, does not adequately capture the lobbying practices and the changes which occurred leading to the removal of the OFR and implementation of the EBR. This theory, also does not fully explain why and how interested parties emerge to engage in regulatory deliberation (Croley, 1998), which is not useful to this study as the study aims to examine how certain pressure groups emerged to lobby for/against the changes which occurred during the OFR and the EBR periods. In short, neither the Public Choice theory nor the Neo-Pluralist theory, or the Civic Republican theory are deemed entirely suitable to appropriately explain the dynamics of SER regulation in the UK. Furthermore, these theories are not useful to explain the attitudes of firms towards SER or firms strategic attitudes towards regulation.

Thus, having discussed why the Civic Republican, Neo-Pluralist and Public Choice regulatory theories were rejected, the Public interest theory which proposes that regulation is supplied in response to the demand from the public for the correction of inefficient practices is deemed suitable, to explain the events which led to the implementation of the EBR. Further reasons why this theory is suitable and its relevance to this study is explained in the next section.

Public Interest Theory

Pigou (1932), who first developed this theory, argued that regulation is supplied in response to the demand from the public for the correction of inefficient or inequitable market practices. Bozeman (2002) also posits that regulation is used when public values are not realised by other means, be it through the market or through governments. Croley (1998) further argues that the public interest theory is dominated by three types of actors, which are the regulator, the citizenry at large and special interests groups, organised subsets of the population who are especially sensitive to particular regulatory policies. These actors have especially strong preferences about what constitutes desirable regulatory outcomes in particular areas. The first actors, members of the

public usually seek what they consider desirable regulatory policies, with special interest groups, the second actors, also seeking desirable regulatory policies. The latter however do so more actively than the public, for example, pressure groups actively setting up organisations to propagate their cause (FoE, World Wildlife Fund for Nature - WWF, and Corporate Responsibility Coalition - CORE amongst several others). Then, regulators, the third actors, have goals which are self-regarding, and pursue more general interests, that are the prolonged enjoyment of holding their positions and to preserve their positions both for the current personal benefits and for the expected personal benefits they will receive upon leaving those positions as a consequence of having held them. In seeking this end, regulators pursue more general interests that are policies enjoying broad public support. An example of this is the actions of the newly elected Labour Government which in 1997 signed the social chapter of the Maastricht Treaty of 1992, essentially introducing a minimum wage and publishing its proposals on industrial relations in the White Paper – Fairness at Work.⁹ Furthermore, Levine and Forrence's (1990) view the public interest account of regulation as 'the necessary exercise of collective power through government in order to cure "market failures", to protect the public from such evils as monopoly behaviours, ... or the effects of externalities'(p. 168). In short, Pigou's (1932) view of the supply and demand of regulation is reminiscent of the demand for greater transparency, through public campaigns, legal challenges and pressure group lobbying.

Another theory, the Regulatory Capture Theory, which indicates that public interests are pushed to the background in favour of governments' special interest (Stigler, 1971; Huntington, 1952; Levine & Forrence, 1990; Laffont & Tirole, 1991), is also used in this study, to explain the impact of lobbying in the changes leading to the removal of the OFR and the implementation of the EBR. This is discussed next.

Regulatory Capture Theory

Another theory closely associated with the issue of regulation is the Regulatory Capture Theory. Regulatory capture is a term used to refer to situations in which a government regulatory agency created to act in the public interest, instead acts in favour of the commercial or special interest that dominate in the industry or sector it is charged with

⁹Department of Trade and Industry (1998), Fairness at Work, 21 May, Cm 3968.

regulating. Put simply regulatory capture is the capture of regulators by the regulated.¹⁰ Hence, those who will benefit from regulation will lobby the state to enact a favourable law (Richardson and Kilfoyle, 2008).

Stigler (1971) further argues that the government has ‘legal’ coercive power and therefore has monopoly control of the ‘supply’ of regulation. Regulation is therefore an economic good, which is subject to the forces of supply and demand. This demand for regulation arises due to the notion that regulation can result in wealth transfers, in other words the capture theory predicting that regulated firms will earn higher rates on return (on average) than non-regulated firms. However, Posner (1974) identifies a problem with Stigler’s approach, arguing that there is a fundamental distinction between number of firms and number of voters which Stigler failed to recognise. Stigler emphasized that small firms in a regulated industry, possess high political strength, hence a larger influence. Yet, large groups could attract favourable regulation by vote-seeking politicians (Posner, 1974). Moreover, Posner (1974) argues that ‘Regulation is not about the public interest at all, but is a process, by which interest groups seek to promote their private interest....Over time, regulatory agencies come to be dominated by the industries regulated’ (p. 336). In effect, regulation is implemented on the insistence of a ‘selfish’ few who seek to ensure that the regulation introduced will suit their needs. Again, the current regulatory environment shows that regulation could be influenced by particular interest groups, notably corporations, supported by the vast amount of money firms devote to lobbying their interests, (Barth et al., 2014; Henriques, 2007). Their aim is to lobby government in order to protect their interests and those of their members. Further, the decision of legislators to grant regulation is based on the likelihood that the votes gained from the lobbying group will be greater than the votes lost from the group harmed by the regulation (Richardson and Kilfoyle, 2008).

Corporations may thus escape or preclude constraints through ‘regulatory capture’, the hijacking of the regulatory process, so that ‘what regulators decide and/or perform is what industry prefers’ (Mitnick 2011, p. 35) Alternatively, they may use indirect tactics, such as ideological capture: the ‘symbolic and rhetorical alignment’ of corporate activities with broader social discourses, framing business activities so as to make them

¹⁰ MacMahon, G. (2002) *Regulatory Capture: Causes and Effects*
www.iipe.org/conference2002/papers/McMahon.pdf

“acceptable” to regulators and civil society and thus paving the way for full-fledged regulatory capture (Lippmann 2005, p. 119). In this regard, firms which are successful in hijacking the regulatory process are more likely to achieve a competitive advantage over competitor firms. Furthermore, rooted in the economic assumption that people operate to maximize their self-interest and do so in a rational manner, Stigler (1971, p. 3) also proposed that regulation exists primarily to benefit those who are subject to the regulation, in a sense highlighting regulatory capture.

In sum, what emerges from the general regulatory deliberations however is that, as with the public interest theory, the regulatory capture theory does not explicitly consider the relationships among actors in the governmental process nor the mechanisms by which the acts of regulators are made to conform to the desires of organised subgroups. This thesis thus seeks to discuss the relationships between the actors and in so doing explore the mechanisms by which these actors propagate their cause; contributing to literature.

2.3.3 The Resource Based View (RBV)

This research also employs the Resource Based View (RBV) of the firm to argue that firms are using SER as a form of strategy. The RBV theory holds that only resources that are Valuable, Rare, Inimitable and Non-Substitutable (VRIN) are capable of producing and sustaining competitive advantage which contributes to superior performance. Furthermore, RBV places emphasis on the importance of particular intangible resources such as reputation, culture, and trust, as they are difficult to imitate and substitute and are important foundations for a firm’s success (Branco and Rodrigues, 2006). The RBV which proposes that companies report by utilising their resources and capabilities¹¹ to maintain a competitive advantage in the market, is also increasingly being used to explain firms’ Social and Environmental Reporting (SER) behaviour (see for example, Branco and Rodrigues, 2006; Carmeli, 2001; Clulow et al., 2003; Hall, 1992; Hart, 1995; Katsoulakos and Katsoulacos, 2007; Sandhu et al., 2012).

The Relationship between RBV and SER

From the RBV perspective, valuable, costly-to-copy firm resources and capabilities provide the key sources of sustainable competitive advantage (Hart, 1995). There are

¹¹ Please see Figure 2.2 for a detailed list of resources and capabilities and their assumptions as identified by previous literature.

two key features that distinguish a capability from a resource (Kostopoulos et al., 2002). First a capability is firm specific since it is embedded in the organisation and its processes, whilst an ordinary resource is not. Secondly, the primary purpose of a capability is to enhance the effectiveness and productivity of resources that a firm possesses in order to accomplish its targets. While resources are the source of a firm's capabilities, capabilities are the main source of its competitive advantage (Grant, 1991). Engaging in CSR has also been identified as a capability which provides the firm with a competitive advantage (Hart, 1995; Sandhu et al., 2012).

Hart (1995), was one of the first to apply the RBV framework to explain why firms engage in environmental responsibility, arguing that the firm's relationship to the natural environment encompasses three interconnected strategies (pollution prevention, product stewardship, and sustainable development). Hart further states that because these three environmental strategies are rooted in costly-to-copy resources and capabilities, such an external orientation could enhance competitive advantage, differentiating the firm's position through the effects of a good reputation.

Consequently, a firm's resources and capabilities together form its distinctive competencies. These competencies enable innovation, efficiency, quality, and customer responsiveness, all of which can be leveraged to create a cost advantage or a differentiation advantage (Porter, 1998). Crucially, what is important to firms is how to prevent their competitors from cheaply replicating their assets, which in turn protects a firm from losing its competitive advantage. However all barriers to imitation can be eventually accessed though some barriers will be higher than others and therefore more difficult for rivals to overcome. The height of the barriers to imitation also determines how contestable or sustainable the firm's advantage will be (Clulow et al., 2003; Reed and DeFillippi, 1990). Falkenberg and Brunsæl (2011) further highlight the imitability of assets by proposing four CSR outcomes, Strategic Disadvantage, Strategic Necessity, Temporary Strategic Advantage, and Strategic Advantage. Similarly Collis and Montgomery (1995) provide a clear exposition of the RBV and its role in strategy and contend that resources must pass tests as to their inimitability, durability, appropriability, substitutability and competitive superiority in order to qualify for an effective role in strategy. Falkenberg and Bransael (2011) therefore argue that when resources lead to an economic advantage for a firm, then other firms may look to see if the activity can be copied in their firms. Firms may hence want to see if there are ways

in which their SER activities can be made hard to imitate or copy; and to make them more attractive than potential substitutes.

2.4 Lobbying, SER Regulation and Strategic attitudes – Empirical Analysis

2.4.1 Lobbying in Regulation

Lobbying has been defined as ‘*A process of influencing public and government policy at all levels: federal, state, and local*’¹². It involves the advocacy of an interest that is affected, actually or potentially, by the decisions of government leaders. Individuals and interest groups alike can lobby governments, and governments can even lobby each other¹³. The practice of lobbying also provides a forum for the resolution of conflicts among often diverse and competing points of view; provides information, analysis, and opinion to legislators and government leaders to allow for informed and balanced decision making; and creates a system of checks and balances that allows for competition among interest groups, keeping any one group from attaining a permanent position of power.

Lobbying thus largely represents the process by which organisations seek ‘insider’ status in the policy-making system, in order that their views might input as directly as possible into the process of policy development and decision-making. “Insider” groups are those groups which are ‘[firstly] recognised by government as legitimate spokespersons for particular interests or causes ... [proven partly through their ability to] talk the language of the government and civil servants, [secondly] allowed to engage in a dialogue on issues of concern to them ... [through] formal [and informal] consultation processes ... [and thirdly] those that agreed to abide by certain rules of the game’¹⁴. ‘Outsider groups, meanwhile, composed that “disparate and heterogeneous category” of organisations not subject to the disciplines imposed by acceptance of the informal rules of the game . . . [either because] they lacked the necessary skills or

¹² Law Encyclopædia Online (2010). Lobbying', Available from: <<http://www.encyclopedia.com/topic/lobbying.aspx>> [Accessed 10 October 2010].

¹³ Law Encyclopaedia (2012) Lobbying - Should Lobbyists Be Strictly Regulated. Available from: <<http://law.jrank.org/pages/8343/Lobbying.html>> [Accessed 10 June 2012].

¹⁴ Grant, W. (2004) Pressure Groups: The Changing World of Pressure Groups. *Parliamentary Affairs* 57(2), 2004, p. 408 – 409.

resources to gain recognition [or because they were] ideological protest groups that did not want to be drawn into the embrace of government'¹⁵.

Lobbyists can help the legislative process work more effectively by providing lawmakers with reliable data and accurate assessments of a bill's effect¹⁶. They also emphasise the important role that they play as providers of information and facilitators of debate. Parvin (2007) further argues that British parliamentary democracy entrusts elected politicians with the huge responsibility of legislating across a wide range of often very technical and complex issues and that it is important for MPs and government to have access to all the information necessary to make decisions and develop policy responsibly.

Trade associations also occupy an important place in the policy-making process (Parvin, 2007). The CBI, for example, has over 2,000 individual company members employing around four million people, plus a further six million employed by companies whose trade associations are members. The CBI also claims to be the 'Voice of Business' with networks including 'government ministers, MPs, civil servants, opinion formers and the media'. Furthermore, they state that they are so formidable that the organisation is 'second to none at achieving [lobbying] wins for business...'¹⁷

Lobbying on regulatory outcomes takes several forms. Submissions on exposure drafts are however the most observable form of lobbying, forming the main basis for previous lobbying research. As such, research has addressed the factors motivating lobbyists to respond on exposure drafts and described the resultant impact on decisions made by standard setters (see for example, Deegan et al., 1990; Francis, 1987; Lindahl, 1987; Puro, 1984; Sutton, 1984 and Watts and Zimmerman, 1986). Currie et al., (1987) however identified that, in classifying respondent positions, researchers have generally failed to analyse the content of submissions. Such an approach ignores the possibility that responding to exposure drafts provides lobbyists with means of persuasion in

¹⁵ Grant, W. (2004) Pressure Groups: The Changing World of Pressure Groups. *Parliamentary Affairs* 57(2), 2004, p. 408 – 409.

¹⁶ Law Encyclopædia Online (2010). Lobbying', Available from: <<http://www.encyclopedia.com/topic/lobbying.aspx>> [Accessed 10 October 2010].

¹⁷ The Confederation of British Industry (CBI) (2006) Membership Available from <<http://www.cbi.org.uk/ndbs/content.nsf/802737aed3e3420580256706005390ae/0E1BB828380B86A580256BA500357701?OpenDocument>> [Accessed 10 January 2013].

excess of casting votes. Other researchers also recognised that exposure draft responses may entail more than votes of position and hence conducted analysis of the content of respondents' submissions (MacArthur, 1988; O'Keefe and Soloman, 1985; Sutton, 1984).

2.4.2 The Impact of Regulation on SER

Central to this study are the legal requirements contained in the Companies Act 2006 Chapter 5, Section 417 (5b); *Contents of directors' report: business review*. For reports relating to financial years beginning on or after 1 October 2007, the content requirements for a business review in the directors' report for quoted companies were extended significantly, that; 'In the case of a quoted company the business review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include -

(b) Information about -

- (i) environmental matters (including the impact of the company's business on the environment),
- (ii) the company's employees, and
- (iii) social and community issues,
including information about any policies of the company in relation to those matters and the effectiveness of those policies;

Empirical evidence provides conflicting evidence on the impact of regulation on SER. A study by Grosser et al., (2008), for example, identified that regulation in Australia, has acted as a prompt, or catalyst, to alert companies to the business drivers for equal opportunities for women, which they found are also drivers of external reporting. Owen et al., (2005) in studying the SER of FTSE100 companies, also found that that of six reasons given as the drivers of social and environmental reporting, the highest was regulation or legislation. Furthermore, Mobus (2005) looked at environmental disclosures and environmental performance in 17 US petroleum refining companies in the period 1992-1994 and found that mandatory accounting disclosures were influential in inducing cooperation with regulatory standards. Moreover, studies carried out by government agencies show that in several environmental areas where there are regulatory protections, there has been significant improvement over the past decades. A

report by BERR in 2006, for example, suggested that regulation has led to the improvement of river quality, and cleaner bathing water, meeting EU mandatory standards. The Environment Agency also proactively communicates how the regulation it enforces, is helping deliver benefits. Its report “Spotlight on business, 10 years of improving the environment” issued in July 2008, states that serious pollution incidents have halved since 2000, due to regulation.

On the other hand, not all studies have supported the effectiveness of regulation on SER. Tauringana and Mangena (2009) for example, examine the annual reports of media firms to determine the reporting of financial and non-financial key performance indicators in compliance with the EBR. They find that in spite of an increase in reporting over a four year period, the reporting of non-financial Key Performance Indicators (KPIs) is particular low and the general compliance with the statutory EBR also remains low. In Henriques (2010) survey of the annual reports of the FTSE100 firms, he also argues that the Business review, (the regulatory requirement) did not appear to be serving the purpose for which it was intended, that is to improve the quality of reporting; as evidenced by the lack of the reporting of relevant social and environmental information in annual reports. Furthermore, an extensive survey on how well FTSE350 companies responded to the Business Review legislation, conducted by PricewaterhouseCoopers (PwC), shows that there have been some improvements in narrative reporting over the past year, that is, between 2006 and 2007; however there remains improvement in terms of the quality of information reported. Adams (2004) also states that annual reports do not demonstrate a high level of accountability to key stakeholder groups on ethical, social and environmental issues.

Of particular concern according to Adams, is the lack of ‘completeness’ of reporting, hence a call for mandatory reporting guidelines and better developed audit guides. Similarly, Spence and Gray (2007) in their study of twenty five firms, find that although some interviews mentioned regulatory pressure as a key factor for firms to engage in SER and CSR; complying with legislation was the lowest bar. Moerman and Van Der Laan (2005) best summarise the state of SER when they state,

‘the laudable purpose of producing a social report has been undermined by the less than subtle purpose of this document as a vehicle for the

process of legitimation, an exercise in smoke and mirrors at its best' (p. 385).

Having discussed the conflicting evidence on the effectiveness of regulation by previous studies, this thesis therefore seeks to add to literature by analysing the impact of the EBR on firms' disclosures.

2.4.3 The Relationship between SER and Competitive Advantage

In recent times, the idea of SER has evolved from a philanthropic, ethical, legitimate behaviour to a more strategic view. Firms have become increasingly sensitive to their 'CSR¹⁸ image' and aware of the positive relationship between their SE actions and consumers' reaction to their products, as well as the negative effects when SE efforts are deleterious or not perceived as legitimate (Creyer, 1997; Mahon and Cochran, 1991; Sen and Bhattacharya, 2001). McWilliams and Siegel (2001) further argue that SER is a mechanism of product differentiation, as demand for SER attributes is generated by consumers and other stakeholders such as investors, employees, and community groups. Strategic SER thus goes beyond good corporate citizenship and reducing harmful value chain impacts to mounting a small number of initiatives whose social and business benefits are large and distinctive, and strengthen company competitiveness (Porter and Kramer, 2006).

Empirical research further supports the notion that firms have realised that engaging in SER and the strategic use of SER programs provides them with a competitive advantage (Clulow et al., 2003; Falkenberg and Brunsæl, 2011; Vilanova et al., 2009). For example, Vilanova et al., (2009) argue that integrating SER in the strategic management process can contribute to implementing a successful strategy in the firm insofar as it can help to develop simple and consistent long-term goals, improving the understanding of the complexity of a competitive environment. Competitiveness is therefore one of the key drivers for adopting a SER approach (Bansal and Roth, 2000; Haigh and Jones, 2006; Hess et al., 2002; Porter and Van der Linde, 1995). On the issue of competitiveness, Porter and Kramer (2006) highlight the 'ratings game' where firms

¹⁸ The difference between CSR and SER is that CSR encompasses firms' social, environmental and economic impacts (The Department of Business, Innovation and Skills) whilst SER covers the social and environmental aspects of firms impacts. This study focuses on SER only, though references are sometimes made to the use of CSR in other studies.

join ‘ethically responsible’ indexes such as FTSE4Good and Dow Jones, in a bid to portray a sense of social responsibility and hence seek favour within the market.

Furthermore, as a result of increasing stakeholder demand for SER, firms have realised that engaging in SER helps to maintain a good relationship with their stakeholders which in turn could result in a competitive advantage (Clulow et al., 2003; Deloitte, 2012; Hall, 1993; Jones and Bartlett, 2009, p. 7; McWilliams and Siegel, 2001). Margaret Hodge, former Minister for Industry and the Regions, also stated, ‘Businesses do not operate in a vacuum; they operate within communities and as part of society. All responsible businesses recognise what they do and how they do it impacts on the community in which they operate and more widely in society’¹⁹. A good stakeholder relationship could thus be a result of companies realising the attractiveness in the value of engaging in SER. Longer-term relationships with primary stakeholders like customers, suppliers, and communities, as well as present and future employees, are also not easily copied (Hillman and Keim, 2001). As such, these relationships can give the firm a strategic competitive advantage. However, some industries are more vulnerable to criticism due to the nature of their operations. Firms in these industries which include Tobacco firms may therefore need to engage in higher levels of SER to appease a variety of stakeholder groups (Bhattacharya and Sen, 2004, p. 22).

Moreover, prior research suggests that firms engagement with Social and Environmental Reporting (SER) provides them with a competitive advantage (Branco and Rodrigues, 2006; Clulow et al., 2003; Falkenberg and Brunsæl, 2011; Hart, 1995; Jones and Bartlett, 2009; McWilliams and Siegel, 2001; Porter and Kramer, 2006; Sandhu et al., 2012). Hart (1995) for example, attempts to explain why firms engage in environmental responsibility by arguing that the firm’s relationship to the natural environment encompasses three interconnected strategies (pollution prevention, product stewardship, and sustainable development). Because these three environmental strategies are rooted in costly-to-copy resources and capabilities, such an external orientation could enhance competitive advantage, differentiating the firm’s position through the effects of a good reputation (p. 999).

¹⁹ *Hansard* HC Deb. vol. 450, col. 913, 18 Oct 2006.

Vilanova et al., (2009) further argue that integrating SER in the strategic management process can contribute to implementing a successful strategy in the firm, insofar as it can help to develop simple and consistent long-term goals, improving the understanding of the complexity of a competitive environment. It is claimed that social legitimacy is therefore a performance criterion and significant risks await firms that do not hold true to expressed principles (Hart, 1995). Furthermore, it is possible, based on previous research, that the quantity and quality of firms' SER output can be related to their need to maintain competitive advantage, which can be done by means of SER. But other empirical research has also suggested that the increase in firms' engagement with SER could be related to the Stakeholder theory (Owen et al., 2005). Thus if there are any significant change in firms' SER levels, could this be attributed to stakeholder demands, for example, increased Government requirements?

Further empirical studies report that reputation arising from a firm's engagement with SER enhances competitive advantage (Hall, 1992; Ljubojevic et al., 2012; Vilanova et al., 2009). Hall (1992) for example, argues that reputation, which is usually the product of years of demonstrated superior competence, is a fragile resource; it takes time to create, it cannot be bought, and it can be damaged easily. A good reputation further leads to positive performance, and strategic efforts aimed towards building and maintaining a good reputation is essential in the management of firm resources (Galbreath, 2005), consequently helping to build a positive image with stakeholders (Dowling, 1986; Fombrun, 1996). Positive firm reputation is therefore a source of sustained competitive advantage, and the relationships between a firm and its stakeholders are socially complex and therefore imperfectly imitable (Barney, 1991). Although reputation can be influenced by other factors, such as the impact of unpredicted events, reputation *can* be created and managed through the disclosure process (Toms, 2002), giving an edge over rivals who do not manage their reputation through disclosure. SER is therefore a communication instrument that firms use to create, protect or enhance their image or reputation (Hooghiemstra, 2000).

Moreover, social responsiveness helps managers, and induces constructive contributions from their stakeholders (Donaldson and Preston, 1995), which in turn augments the firm's reputation since the expectations both of managers and other stakeholders are satisfied (Brammer and Pavelin, 2004). Investing in social responsibility activities could therefore have internal benefits particularly in relation to employees and external

benefits with relation to a better corporate reputation (Branco and Rodrigues, 2006). Russo and Fouts (1997) however, warn that although proactive policies translate into internal competitive advantages; a firm's pro-environment reputation demands continued investment in consistent action, so that the firm's advantage does not erode from within. Furthermore, widespread SER may no longer bring about the reputational benefits, by differentiating companies and leading to competitive advantage (Hillman and Keim, 2001; Jones and Bartlett, 2009). Porter and Kramer (2006) further argue that 'The reputation argument seeks that strategic benefit but rarely finds it. Concerns about reputation, like license to operate, focus on satisfying external audiences. In consumer-oriented companies, it often leads to high-profile cause-related marketing campaigns.

In stigmatized industries, such as chemicals and energy, a company may instead pursue social responsibility initiatives as a form of insurance, in the hope that its reputation for social consciousness will temper public criticism in the event of a crisis. This rationale once again risks confusing public relations with social and business results' (p.4). SER is also now highly transparent, especially in competitive markets (McWilliams et al., 2006) and society has also become increasingly distrustful of what 'CSR' really means (Orlitzky et al., 2011). A good example of this scepticism is BP who received good marks from many influential CSR rating agencies but was also responsible for the Deepwater Horizon oil spill (Steverman, 2010). Notwithstanding, the effective management of reputation by firms could result in competitive advantage as reputation (both brand and corporate) appears to depreciate relatively slowly (Grant, 1991).

In summary, this chapter suggests that the relationship between SER and competitive advantage is synonymous as firms have increasingly recognised the benefits of engaging in high levels of SER. Firms gain a competitive advantage when they implement strategies that exploit their resource strengths, respond to environmental opportunities, and neutralise weaknesses. The competitive advantage is then held by the firm while it is difficult for competitors to duplicate the successful approach (Branco and Rodrigues, 2006; Reed and DeFillippi, 1990). Whilst there is evidence to suggest that firms engage in SER to maintain a competitive advantage, we explore this assertion in practice by analysing the evidence obtained from our respondents, thereby contributing to literature.

2.5 Developing the Research Agenda

The previous literature discussed in this chapter has highlighted issues surrounding lobbying, SER regulation and firm strategic attitudes towards SER. The research agenda in this thesis is therefore aimed at addressing those issues unexplored by previous literature, which will lead to a significant enhancement of the extant appreciation of the role of regulation in SER.

Adams (2002) argues that there is still little explanation in CSR theory regarding the extent of contextual variables: culture, the extent of regulation, and the influence of political pressures in social reporting. Furthermore, previous lobbying research has identified which groups are successful in exerting influence on final enacted accounting standard (see for example, Kirsch and Day, 2001; McLeay et al., 2000; Tutticci et al., 1994; Zülch and Hoffmann, 2010). In so doing, the majority of these studies have tended to base their analyses of the impact of lobbying on comment letters. However, this poses a problem as argued by Lindahl (1987) who posits that simply tallying comment letters is unlikely to capture the extent of firm participation in lobbying, especially if other channels for lobbying are present. Furthermore, academic literature pays little attention to evidence of lobbying practices in the changes that occurred in the OFR and the EBR. However a recent study conducted by Rowbottom and Schroeder (2014) analysed the impact of lobbying on the OFR, though they failed to adequately explore the role of the CBI in lobbying against the mandatory OFR.

In addition, a number of reports have been published which examine the annual reports of firms to measure their compliance with the EBR and measure its effectiveness (see for example, Accounting Standards Board, 2009; Deloitte, 2009; Henriques, 2010; Tauringana and Mangena, 2009). However, despite extensive evidence on firms' compliance with SER regulation, little is known on the impact of the EBR on the quantity and quality of firms' SER. Finally, the sparseness of empirical evidence on the relationship between SER and competitive advantage is another hindrance to objective and comprehensive SER research. In addition, far too little empirical research has been carried out on the relationship between regulation and competitive advantage. Of those studies that have attempted to explore this concept, they fail to consider the impact of SER regulation on firms' attitudes, or the effect that the regulatory system has on firms.

In summary, the general conclusion to be drawn from the existing studies is that there is an increasing awareness of the importance of regulation in SER, and the use of SER as a form of strategy by firms. However it remains unclear whether stakeholders are fully aware of the issues surrounding the development of SER regulations, in particular that regulatory outcomes are a dynamic function of lobbying and previously enacted legislation.

2.6 Summary and Conclusion

The literature review has presented and discussed previous studies on lobbying in regulatory processes, on the debate surrounding the efficacy of regulation, and firms' strategic attitudes towards SER; both theoretically and empirically. In particular, the literature discussed the evidence showing how lobbyists are fundamental to regulatory developments, though there is little evidence to support the argument that embedded legislative principles impact pressure group lobbyists' effectiveness. This has prompted an investigation, undertaken in empirical chapter 4, into how path dependency impacted on lobbying group effectiveness and the scope for regulatory modification in the removal of the OFR and the EBR. Furthermore, the literature discussed previous studies on the impact of regulation in SER, showing that some studies support the notion that regulation has an impact on SER and other studies arguing against this assertion. Hence this debate and the scant evidence on the impact of the EBR on firms SER, has fuelled an investigation into the impact of the EBR on firms SER output, an investigation which is undertaken in empirical chapter 5.

In addition, the literature discussed previous findings on the relationship between SER and competitive advantage, providing evidence on how firms are increasingly using SER as a form of strategy. However there is very little evidence provided in the literature which examines the relationship between firms' attitudes to regulation and SER, in particular one that is undertaken from an investigative direction. Thus an examination into the relationship between firms' attitudes to regulation and SER is undertaken in empirical chapter 6. In sum, the evidence from the existing studies has shown that more research needs to be undertaken in order to explore the issues left unanswered by literature.

Consequently, in showing the legitimacy of this thesis and reinforcing its foundations, the next chapter, Chapter 3, presents and discusses the data and methods employed in this research, used to investigate these unexamined issues.

CHAPTER 3

Chapter 3 . Data and Methodology

3.1 Introduction

This thesis aims to provide answers to the following major research questions:

1. How did pressure group lobbying impact on the removal of the Operating Financial Review (OFR); and the implementation of the Enhanced Business Review (EBR?)
2. What is the impact of regulation in Social and Environmental Reporting (SER) in firms' annual reports?
3. Why do firms display a strategic attitude towards SER and regulation?

This chapter presents the research methods employed in this research which enable the above questions to be explored. The research combines the use of quantitative and qualitative research methods, as they are appropriate in answering the research questions. The chapter is organised as follows. In the next section, 3.2, a discussion on the quantitative and qualitative methods is presented. Section 3.3, then presents the sampling design which discusses how the coding sample and interview sample used in the study, were derived. Following the sampling design section, section 3.4 presents the data sources and data collection methods of the research. Section 3.5, the conclusion, then presents a summary of this chapter and introduces the first empirical chapter.

3.2 Quantitative and Qualitative Research Methods

The use of quantitative methods in social sciences is drawn from natural sciences, (Morgan and Smircich, 1980). Quantitative methods employ 'the use of standardised measures so that the varying perspectives and experiences of people can be fit into a limited number of predetermined response categories to which numbers are assigned' (Patton, 2002, p.14). The use of quantitative methods is therefore helpful in evaluating the level of SER in annual reports as it allows for the facilitation, comparison and statistical aggregation of data (Patton, 2002).

Quantitative methods do not go without criticism however. One important feature of quantitative techniques is that the process of data collection becomes distinct from

analysis (Easterby-Smith et al., 2002). It requires the use of standardised measures so that the varying perspectives and experiences of people can be fit into a limited number of predetermined response categories to which numbers are assigned (Patton, 2002).

Therefore, ‘in manipulating data through sophisticated approaches, quantitative methods, tend to freeze the social world into structure immobility and presumes that the social world lends itself to an objective form of measurement, without considering that human beings may actively contribute to the creation of the social world’ (Morgan and Smircich, 1980, p. 498). Thus quantitative methods, is merely contented with the production of narrow empirical snapshots of isolate phenomena at fixed points in time, and does not do complete justice to the nature of the subject. Though they may play a role in the analysis and understanding of the process of social change, its use is much more restricted in subjectivist positions (Morgan and Smircich, 1980). As such, whilst the quantitative method is helpful in answering the ‘*what* is the impact of regulation in SER in annual reports’, it does not address the ‘*how* did lobbying impact on regulation and ‘*why* do firms display a strategic attitude towards SER and regulation’. Therefore, as this research seeks to explore the impact of lobbying as well as the strategic attitudes of firms towards SER and regulation, this research also employs the use of qualitative methods. This is discussed next.

Qualitative research methods have been increasing in use in the social sciences. Alvesson and Deetz (2000) indicate that there are inadequacies identified with quantitative hypothesis testing hence the increasing use of qualitative methods (see also Denzin and Lincoln, 1994; Morgan and Smircich, 1980). Qualitative research fits purposes of description, interpretation, and explanation. It addresses questions such as ‘what is occurring’ and ‘how is it occurring’. It produces a wealth of descriptive data from ‘people’s own written or spoken words and observable activities’ (Taylor and Bogdan, 1984, p. 125). These methods are also great for examining and articulating processes. Miles (1979), however argues that ‘the analyst faced with a bank of qualitative data has very few guidelines for protection against self-delusion, let alone the presentation of “unreliable” or “invalid” conclusions to scientific or policy-making audiences’ (p. 591). Qualitative research methods are hence not well suited for issues of prevalence, generalizability and ‘how many’ questions. Nevertheless, it is worth noting that both quantitative and qualitative research methods are not entirely opposites, even though they are based on different epistemologies and ontological assumptions (Denzin

and Lincoln, 1998; Morgan and Smircich, 1980; Patton 2002; Silverman, 1997). Indeed, they work well together to achieve an element of triangulation (Alderson, 1999; Jick, 1979; Leedy, 1997). In the next section, this element of triangulation is briefly discussed.

Triangulation

Broadly defined by Denzin (1978, p. 291) as ‘the combination of methodologies in the study of the same phenomenon’, triangulation is the main technique adopted in this research. This technique is in line with Tsang (1998) who employs both semi-structured interviews and questionnaires in his study. In particular, the examination of the role of regulation in SER involves several facets, which each have to be analysed to arrive at appropriate conclusions. Campbell and Fiske (1959) who established the idea of ‘multiple operationism’, further argue that more than one method should be used in the validation process to ensure that the variance reflected is that of the trait and not of the method. Thus if the conclusions from each of the methods are the same, then validity is established. This element of triangulation is therefore directly linked to this thesis which uses combines the use of quantitative and qualitative methods to answer the research questions posed. Green et al., (1989) also suggest that combining quantitative and qualitative methods is to use the results from one method to elaborate, enhance, or illustrate the results from the other. Combining methods therefore seems an appropriate way to identify and represent the issues being investigated.

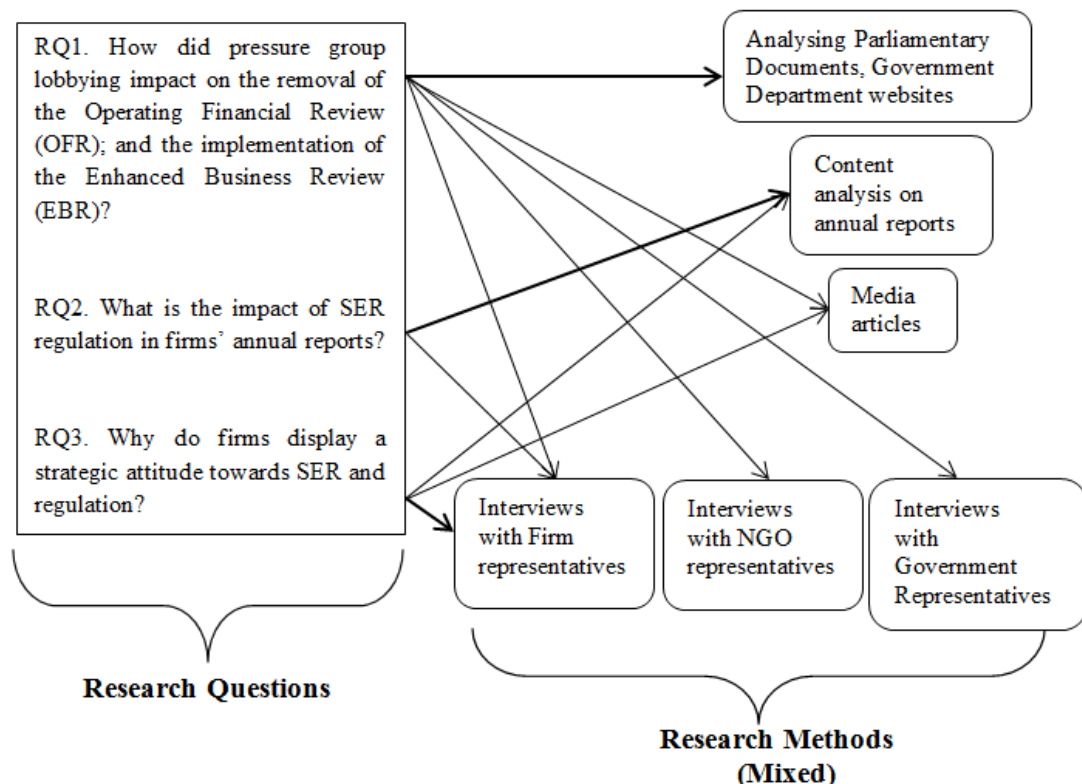
Triangulation however can be time-consuming. Collecting more data requires greater planning and organization and resources are not always available to researchers (Thurmond, 2001). Easterby-Smith et al., (2002), also warn that one should be wary of mixing methods simply for the sake of getting a slightly richer picture as it could lead to contradictions between the findings of each method. Nonetheless, Jick (1979) promulgates the use of quantitative and qualitative methods. He indicates that it should be complementary. Gray et al., (2005b) also argue that authors and researchers, who work in organisations and with managers, should attempt to mix methods to some extent, because it provides more perspectives on the phenomena being investigated. To this end, both quantitative and qualitative research strategies are employed in this research to explore the research questions posed. In addition, Adams’ (2002) call for more case study work and a much closer engagement with practice, seems to be answered with an increased shift from content analysis to case based experiments, field

based research and interviews (Parker, 2005). As such accounting studies have progressively combined ‘the use of content analysis of annual reports together with semi-structured interviews’ (Guthrie & Abeysekera, 2006, p. 118). Hence, this latter approach is adopted in this research, extending previous social and environmental reporting studies by combining the literature, content analysis and interview study research methodologies. In sum, the triangulation technique adopted allows this research to focus on:

- ‘How did pressure group lobbying impact on the removal of the OFR and the implementation of the EBR?’
- ‘What is the impact of regulation in SER in annual reports?’
- ‘Why do firms display a strategic attitude towards SER and regulation?’

In Figure 3.1, the relationship between the research questions and the research methods is illustrated.

Figure 3.1 The Relationship between the Research Questions and Research Methods



Research question one will be analysed using parliamentary documents, including consultation (White) papers, government department websites, media articles and interviews. This analysis is to explore the impact lobbying had on changes that occurred

in the OFR and the EBR. Research question two will be analysed with the use of content analysis on annual reports and interviews, to determine the impact of regulation on SER. Research question three, seeks to identify the strategic attitudes of firms towards SER and regulation and will be explored with the use of annual reports, media articles and interviews.

3.3 Sampling Design

As this research seeks to examine the impact of regulation on firms SER, the main sample chosen are firms. Publicly listed companies have been used in prior research due to the easy accessibility of company information. Again, in order to explore in detail the perceptions of SER regulation from a spectrum of stakeholders, interviews with NGOs and regulators are also analysed. Two samples are used in the research; a coding sample and an interview sample. Details of how each of these samples was determined are discussed next, however it is of note to mention that this section, 3.3, provides a broad overview of the coding sample, with the specific details of the sampling method, being provided as appropriate in each of the three empirical chapters.

3.3.1 Coding Sample

The FTSE350 firms were used as the sample for this study, in particular, to answer research question two. The use of the FTSE350 firms is also in line with previous studies (see for example, Abraham and Cox, 2007; Campbell et al., 2003; Cumming et al., 2005; Owen et al., 2005; Page, 2009; Walmsley and Bond, 2003) and reports (Department for Business Innovation and Skills, 2013; PricewaterhouseCoopers, 2009). In addition, this sample as a FTSE Index, represents the UKs largest firms, offer a wide range of industries and have the experience and resources to engage in CSR. Furthermore, as this index consists of some of the UKs largest firms, it is expected that they are more liable to complying with regulation. Further details on the selection and matching of eligible firms are seen in Chapter 5, section 5.3.

3.3.2 Interview Sample

The perceptions of managers and social stakeholders regarding CSR issues are of the utmost importance when studying corporate accountability in a given context (O'Dwyer, 2002). Prior studies have not fully utilised the perspectives of Senior CSR

directors or managers who are instrumental in ensuring that their companies engage in SER. As a result, the issue of regulation and how it is impacting on companies SER levels has been largely ignored in the literature. Using evidence derived from semi-structured in-depth interviews, this thesis adds to literature by presenting an exact awareness and critical insight into the behaviours of stakeholders toward SER regulation.

In selecting the participants to be included in the interview sample, Heads and Directors of the CSR division of firms in the FTSE350 were targeted for this research. It is expected that the heads and managers of CSR departments have a broader understanding of the whole process of SER as well as a notion of how regulation affects their organisation. This process of contacting the heads of departments is in line with O'Dwyer (2002) who also targeted specific interviewees as they had some input into the formulation of the corporate annual report, could be expected to have a broad perspective on their organisation's operations, and be viewed as being able to address questions investigating perceptions (p.411). In addition, key players who were included in the debate for the implementation of the OFR as well as members of the Committee of the OFR were targeted and invited to participate.

The respondents covered a wide range of industries: Aerospace and Defence, Gas, Water and Multiutilities, Household goods and Home Construction, Media, Real Estate Investment Trusts, Life Insurance, Software and Computer Services and Tobacco. Other groups such as advocacy NGOs, Government agencies, independent regulators as well as a Trade union were interviewed to further investigate firms' attitudes towards regulation of CSR. Of a total of 24 invitation letters sent to UK FTSE4Good firms whose details (The name of the person directly responsible for CSR, direct contact number, email address and postal address) could be obtained, a total of 9 responded with 5 agreeing to be interviewed and 4 rejecting an interview. Within the non FTSE4Good group, 18 CSR Directors details were obtained. A total of 5 agreed to be interviewed. Follow up letters and emails were also sent within a month of first contact. These reminders increased the response rates as suggested by Meho and Tibbo (2003). 20 interviews, with 22 interviewees, were eventually conducted between December 2011 and September 2012.

The interviews were a mix of face-to-face and telephone interviews and were all digitally recorded. Confidentiality was guaranteed and all respondents agreed on the issue of anonymity as some of the information divulged, involved government actions which were sensitive to firms' reputation. Furthermore, to protect the identity of the respondent, but give the reader an overall idea of firms operations, industry sectors were chosen as a reference to respondents (see Spence and Gray, 2007). Thus respondents are referred to throughout as CSR position and industry type, e.g. Head of Sustainability, Tobacco. Table 3.1 shows a summary of the interviewees.

Table 3.1 Summary of Interviewees and Basic Information

Businesses	Pressure Groups	Regulators
Insurance - Head of CSR	Academic / NGO Representative	Board Member - Accounting Standards Board
Gas, Water and Multiutilities - Head of CSR	NGO Environmental Lawyer	Board Member -Accounting Standards Board
Media - Corporate Responsibility Manager	NGO Policy Officer	OFR Advisory Committee Member
Real Estate Investment Trusts - Head of Corporate Responsibility	NGO Executive Director	Head of Government Agency
Real Estate Investment Trusts - Director of Corporate Responsibility	NGO Coordinator	Manager in Government Agency
Software and Computer Services - Leader of Sustainability Services		
Aerospace and Defence - Corporate Responsibility Manager		
Household goods and Home Construction - Company Secretary		
Tobacco - Head of Sustainability		
Tobacco - Corporate Responsibility Manager		

As seen in Table 3.1, the interviewees were representatives of ten businesses, five NGOs and five regulators and government officials. Whilst this number isn't entirely representative of each group (businesses, NGOs and regulators), it was felt that the total number of interviews represented the group enough and the saturation point was reached (Glaser and Strauss, 1967). Thus, the final interview sample consisted of twenty interviews with twenty-two participants, giving a response rate of 31 percent.

3.4 Data Sources and Data Collection

This research utilises multiple data sources which includes annual reports, interviews, parliamentary and government documents, and media articles. These sources are discussed next. Again, it is of note to mention that this section, 3.4, provides a broad overview of the data sources and data collection, with the specific details of the methods employed and why each data source has been used, being provided as appropriate in each of the three empirical chapters.

3.4.1 Annual Reports

Annual reports are a useful indicator of corporate priorities as it represents what is probably the most important document in terms of the organisation's construction of its own social imagery (Hines, 1988; Neimark, 1992). In addition, many studies have used annual reports as a form of data sources and as the basis of analysis for the reasons that it is produced regularly, that the company has a substantial editorial input into it and that it is widely read (Deegan and Rankin, 1996; Gray et al., 1995). Thus, annual reports are used as a source of data collection with reports collected from firms' websites. Also as the EBR became effective in October, 2007, for firms whose year-end falls in December, the 2006 report was used to measure the 'pre EBR' period, with the 2008 annual report used to measure the 'post EBR' period. Likewise for firms whose year-end falls in March, April or any month before October, the 2007 report was used to measure the 'pre EBR' period, with the 2009 annual report used to measure the 'post EBR' period.

As well as the directors reports which were used for the analysis except where specific reference was made within the report to the availability of CSR information in another section/ part of the Annual report, the corporate governance sections, directors remuneration report, chairman's statement, corporate social responsibility section and operating and financial review section, were all selected for inclusion in the SER performance analysis. Further information on how data was collected in annual reports, is described in section 5.3, Methods.

3.4.2 Interviews

Interviews are the best way of understanding a complicated situation and viewing it from someone else's perspective. Then, as it is very difficult to measure perceptions and attitudes from secondary sources such as the annual report, obtaining information 'direct from the source' is the best possible way of obtaining a person's view. Gray (2002) and Parker (2005) also call for more engagement based studies as a better way of gaining information. In addition, interviews have been widely used in CSR studies as it enables the researcher to obtain first-hand information. The next subsections discuss the interview process which includes the designing of the interview guide, the process of contacting the interviewees, the interviews themselves and difficulties encountered, and last but not least the process of analysing the interview data.

Interview Process

The interview process started with designing the interview topic guide²⁰. Semi – structured interviews were chosen and considered as appropriate due to the flexibility it gives to respondent's answers.

1. Designing the Interview Guide

The interview guide was grouped under five broad headings. These headings are:

1. Background about respondent and the company
2. Respondent's concept of regulation
3. Respondents concept of SER
4. Respondents view on Government responsibility
5. Respondents view on External influence

The first group of questions relate to the interviewees career background and the background of the company in general. In particular, these questions sought to find out the experience of the respondent in relation to social and environmental issues, as well as the commitment of the company to SER. The second group asks questions, which relate to respondents' views on current and past SER regulations as well as how involved the company is in complying with SER. The third group of questions pertained to respondents' views on the importance of SER and how he / she felt it contributed to

²⁰ The interview guide, together with the invitation letters for interview, participants' information sheet and the consent form are provided in Appendix A.

the development of their organisation. Group four questions centred on respondents' views on the UK government's responsibility and role in developing SER regulation. Finally, questions in group five centred on respondents' views on external influences on SER regulation, such as pressure groups lobbying for or against SER regulation.

Following the design of the interview guide, ethical consent was sought from the University's ethics committee. Patton (1990) states that the very personal, conversational nature of interview situations highlights many of the basic ethical issues of any research or evaluation method. Furthermore, ethical consent is in accordance to the UK Research Ethics Framework which is intended to sustain and encourage good ethical practice in UK social science research.²¹ Thus a consent form as well as a participant information sheet which assured respondents of the confidentiality surrounding the research and the benefits to be derived, were also utilised.

2. Contacting the interviewees

Once interviewees had been identified, and following ethical consent approval, invitation letters were sent out to participants which also included a participant information sheet. The participant information sheet was included to give the reader more information on the intended project. It is of note to mention that it was difficult to obtain the names of CSR Heads, Directors or Managers as the information was not readily available on the firm's website. Hence in a bid to obtain the names of the heads, directors and managers, companies were contacted via email and telephone to find out the names of those responsible for CSR matters. This was however, met with suspicion and secrecy. It further became apparent during these name searches that companies are becoming increasingly private on divulging names of CSR heads on their websites or annual reports. Names of the Chief Executive Officers as well as members of the Board were however readily available online in particular on company websites. Of the sixty four invitation letters sent out to the managers and directors of FTSE 350 firms, a total of twenty agreed to be interviewed. Of the rest who declined to be interviewed, some invitees sent back responses with reasons such as; the addressee has left the company; they are too busy to grant an interview; they cannot agree to an interview as they have

²¹ Economic and Social Research Council (ESRC), (2010). The Framework for Research Ethics. Available from <http://www.esrc.ac.uk/_images/Framework_for_Research_Ethics_tcm8-4586.pdf> [Accessed 10 October 2010].

had to reject numerous interview requests from researchers; hence do not want to show favouritism by agreeing to my request.

3. The interviews and difficulties encountered

The interviews were a mix of face-to-face and telephone interviews. There is a benefit of face-to-face interviews due to additional data being generated, however this was not relevant to this research due to the nature of questions asked. The interviews were mostly conducted on a one-to-one basis, except for two interviews which involved two participants, hence twenty interviews with twenty-two participants. Majority of the face-to-face interviews were held in respondents office premises with some of these interviews being held at the office canteen or company meeting rooms. Other interviews were held in cafes. Before the interview began, respondents were asked to sign the consent form. Confidentiality was again verbally guaranteed to respondents, although it had been outlined in the participant information sheet. Respondents were then advised that the interview will be audiotaped, which received no objection. The interviews ranged from twenty minutes to one hour and twenty minutes and were conducted in various months between December 2010 and September 2011.

Difficulties encountered in conducting the interviews included the expense it involved. As most of the face-to-face interviews were conducted from company headquarters, mostly based in London, the expense included travelling by train to these destinations which sometimes included overnight stays. Other difficulties included respondents cancelling interviews, with some rescheduling to other dates. In addition, some telephone interviews proved challenging. Some of the respondents whilst interviewing were interrupted, causing the interview to be suspended for a while or even having to be rescheduled. It is also of note to mention that respondents may have been less than candid in the opinions they expressed and attempted to express views which are perceived as socially desirable and representative of what they believe the interviewer wishes to hear (Saunders et al., 2000).

4. Analysing Interview Data

The interviews were digitally recorded and transcribed. Transcription is a pivotal aspect of qualitative inquiry (Oliver et al., 2005). Furthermore, there are three concurrent themes during qualitative data analysis: data reduction, data display, and conclusion drawing and verification (Miles and Huberman, 1994). With these themes in mind,

NVivo a software analytical tool was employed to help with the data reduction and identify amongst other links, relationships between the most frequently used words; and to help draw out possible meanings and assumptions.

3.4.3 Parliamentary and Discussion Documents

In examining the impact of lobbying on the changes that occurred in the OFR and the EBR, a selection of parliamentary debates and government documents were analysed. Furthermore, in conducting an examination of parliamentary proceedings relating to the OFR and EBR, Hansard²² was consulted. All debates on the Company Law Review (CLR) in the House of Commons and House of Lords between 1st November 2005 (1st reading of the CLR in the House of Lords) and 8th November 2006 (CLR completes its passage through parliament and receives Royal assent), were examined. Furthermore, archives from the Department of Trade and Industry were checked for consultation processes on the Business Review and responses (comment letters).²³ In section 5.3, details on how parliamentary and discussion documents were utilised are presented.

3.4.4 Media Articles

In analysing the impact of lobbying on SER as well as investigating the attitudes of firms towards SER regulation, media articles and records were obtained from the LexisNexis database. The media articles related to the OFR and the EBR were then scrutinised for evidence of lobbying by pressure groups as well as evidence of opinions on any aspects of the OFR and the EBR. In particular, popular phrases related to social and environmental reporting and sustainability were identified. These phrases include “social and environmental reporting and the OFR”, “enhanced business review”, “corporate social responsibility and the enhanced business review”, “the operating and financial review”, “CBI and OFR”, “FoE and OFR”, “CBI and lobby”, “CBI and Environment”, “FoE and lobby”, “FoE and Environment”, and “ Government and

²² Hansard (the Official Report) is the edited verbatim report of proceedings of both the House of Commons and the House of Lords.

²³ It is of note to mention that whilst some responses were publicly available, for example, responses to the 2005 White paper, others were not. For example responses to the December 2005 consultation ‘Invitation for comments on the Business Review’ and the February 2006 consultation ‘A consultation on narrative reporting requirements for companies’, were not available on any of the archival webpages. Upon further investigation, these responses were finally obtained under the Freedom of Information Act (2001) from the Department for Business, Innovation and Skills (Known as the Department for Trade and Industry until June 2007).

OFR”. In addition, media articles were consulted to validate as well as add information obtained from the interviews conducted with firms. This was in order to help establish firms’ attitudes towards SER and regulation that had been reported in the media.

3.5 Conclusions

This chapter has presented a discussion of the mixed methods approach used in the thesis. Further specific details of the methods employed are provided as appropriate in each of the three empirical chapters. The coding sample and interview sample were also discussed. This chapter further presented the data sources and data collection methods employed in this research. The next chapter is the first of the three empirical chapters in this thesis. It examines the impact of lobbying in the changes that occurred in the OFR and the EBR.

Appendix A

Appendix A 1 Invitation Letter to Interview (Firms)

[University Address]

«Position»
«Company»

«Date»

Reference number: «Ref_Number»

Dear «First_Name»,

Assessing the Impact of Regulation on Social and Environmental Reporting (SER)

As part of a York Management School project, I am conducting a research on the impact of regulation on Social and Environmental Reporting and would like to understand how changes in regulation affect your organisation. Your participation, by interview, in this research will provide valuable insight on the effects of regulation.

The research is being conducted across a section of FTSE4Good and FTSE 250 companies and your company has been chosen as it is one of the largest companies listed on the London Stock Exchange and as such is expected to be most affected by regulation. It is important to firms that regulation is drafted correctly and this project is intended to contribute to this matter. Furthermore, your participation will be beneficial as it will contribute to the debate on current regulatory practices in SER in the UK.

Following the interview, and with your permission, we will send you a summary of the findings of the research. However, please be assured that this research is confidential and all information that we receive will be *anonymised* with no comments or responses attributed to any specific individual or organisation. The name of your organisation will also not be publicly released.

If you would like to take part in this research, please fill in the attached reply slip and return to the above address (attn. Gloria Botchway). Alternatively you could send an e-mail to [insert email address] indicating if you would like to participate in an interview (by telephone or in person). This interview should last approximately half an hour.

Thanking you in anticipation.

Yours sincerely,
Gloria Botchway

Appendix A 2 Invitation Letter to Interview (NGO's and Regulators)

[University Address]

«Prefix»«First_Name»«Last_Name»
«Company»

«Date»

Reference number: «Ref_Number»

Dear «First_Name»,

Assessing the impact of Regulation on Social and Environmental Reporting (SER)

As part of a York Management School project, I am conducting research on the impact of regulation on Social and Environmental Reporting and would like to understand how regulation is affected by changing policies, by arranging an interview with you. Your participation in this research will provide valuable insight on the effects of regulation.

The research is being conducted across a section of top FTSE companies and key individuals and you have been chosen as we believe that you could help shed light on current regulatory policies. It is important that regulation is drafted correctly and this project is intended to contribute to this matter. Furthermore, your participation will be beneficial as it will contribute to the debate on current regulatory practices in SER in the UK.

Following the interview, and with your permission, we will send you a summary of the findings of the research. However, please be assured that this research is confidential and all information that we receive will be *anonymised* with no comments or responses attributed to any specific individual or organisation.

If you would like to take part in this research, please fill in the attached reply slip and return to the above address (attn. Gloria Botchway). Alternatively you could send an e-mail to [insert email address] indicating if you would like to participate in an interview (by telephone or in person). This interview should last approximately half an hour.

Thanking you in anticipation.

Yours sincerely,
Gloria Botchway

Appendix A 3 Interview Topic Guide

Investigator:

Gloria Botchway

Research Title:

The Role of Regulation in Social and Environmental (SER) reporting in the UK

Introduction:

Research Background and Aim:

- The regulation of SER has been a contentious issue due to the several changes in regulation that occurred over the past decade. Corporations are known to lobby to keep reporting requirements to a minimum for reasons including cost minimisation. On the other hand pressure groups are calling for increased corporate accountability through increased SER regulation. The government on the other hand tries to keep regulation of SER to a minimum whilst encouraging companies to increase their voluntary practices of SER.
- This research aims to explore the development of regulation and its impact on SER reporting.
- The purpose of the interview will be to explore respondents' expertise on key issues associated with regulation of SER. Interviews will therefore focus on how involved individual groups and persons were in the changes that occur in SER regulation. Interviews will also focus on motivations of SER reporting as well as individual perceptions on the impact of regulation on SER.

Assurance of Ethical Conduct

- All information will be treated confidentially.
- Respondents' names will not be revealed in any part of the report.

THEMES AND ISSUES FOR COMPANY INTERVIEWS

Brief background about respondent and the company

1. What is your role in the company?
2. How long have you been working for the company?
3. Which department do you work in?
4. Does your company have a separate Corporate Social Responsibility (CSR) department and what is your policy in that area?
5. Is the board of directors involved in the SER operations? What are their roles?

Respondent's concept of regulation

1. Do you think regulation of SER is important and why?
2. Has regulation had any impact on your organisations reporting practices? What is the evidence?
3. What was your reaction to the removal of the Operating and Financial Review (OFR) and how did its removal affect your organisation?
4. How involved were you in the repeal of the OFR and what the motive behind your role or lobbying, if any?
5. Which channels did you use (for lobbying) and how was it successful?
6. What was your reaction to the introduction of the Business Review (BR) and the Enhanced Business Review (EBR) ? Do you think they adequately replace the OFR?
7. What was your reaction to the likely reintroduction of the OFR, in particular what aspects were you concerned about?
8. Do you see the value in reintroducing the OFR and do you think a statutory reporting standard will help to improve the quality of reporting?

Respondent's concept of SER

1. Do you find the presentation of Social and Environmental (SE) reports useful or beneficial?
2. What are your motivations, if any, of producing SE reports?
3. Are there any constraints on your organisation producing SE reports and if so what are they?
4. Of the four themes in Social and environmental reporting (namely Environment, Employee, Consumer/ Products and Community), which of the four do you think your company reports on most and why?
5. Can you provide any information on costs associated with preparing your reports on SE issues?
6. Do you think the benefits of reporting outweigh the costs? And why do you think so?
7. If your level of reporting has increased over the years why do you think so? Alternatively if it has decreased what do you think is the cause of this? (For e.g. could it possibly be due to requests from stakeholders)

Respondents view on Government responsibility

1. Do you think the government has provided adequate guidelines on the amount and direction on how to report on your SE issues effectively?
2. Does the government provide adequate consultation when it comes to SER regulation?
3. Do you think the current reporting requirements should be reduced or simplified or rather increased?

4. Are there non-regulatory solutions to increasing the quality of reports?

Respondents view on External influence

1. What do you think of the lobbying activities by Business Lobbyists such as Confederation of British Industry for minimising regulation of SER?
2. What do you think of the lobbying activities by NGO's such as Friends of the Earth calls for increased regulation?

THEMES AND ISSUES FOR 'KEY PLAYERS' INTERVIEWS

Brief background about respondent

1. As a member of board of directors in a company are you involved in CSR?
2. How long have you been working for the company?

Respondents Concept of Regulation

1. Do you think regulation is important and why?
2. Does regulation have any impact on organisations reporting practices?
3. What was your reaction to the removal of OFR and do you think its removal affected organisations?
4. How involved were you in the repeal of the OFR and what the motive behind your role or lobbying, if any?
5. Which channels did you use and how was it successful?
6. What was your reaction to the introduction of the BR/EBR?
7. What was your reaction to the likely reintroduction of the OFR, in particular what aspects were you concerned about?
8. Do you see the value in reintroducing the OFR and do you think a statutory reporting standard will help to improve the quality of reporting?

Respondents Concept of SER

1. Do you find the presentation of SE reports useful or beneficial?
2. Of the four themes in Social and environmental reporting (namely Environment, Employee, Consumer/ Products and Community), which of the four do you think companies should report on most and why?
3. Do you think the level of reporting has increased over the years and why? Alternatively if it has decreased what do you think is the cause of this? (For e.g. could it possibly be due to requests from stakeholders)
4. Do you feel the presentation of reports in the annual reports is enough or do you think there should be other forms of medium for e.g. the website and why?

Respondents view on Government Responsibility

1. Do you think the government has provided adequate guidelines on the amount and direction on how companies should report their SEI effectively?
2. Does the government provide adequate consultation when it comes to SER regulation?
3. Do you think the current reporting requirements should be reduced or simplified or rather increased?
4. Are there non-regulatory solutions to increasing the quality of reports?

Respondents view on External Influence

1. What do you think of the lobbying activities by Business Lobbyists such as Confederation of British Industry for minimising regulation of SER?
2. What do you think of the lobbying activities by NGO's such as Friends of the Earth calls for increased regulation?

Appendix A 4 Participants Consent Form

CONSENT FORM

[University Address]

Reference number: «Ref_Number»

Assessing the Impact of Regulation on Social and Environmental Reporting

Researcher: Miss Gloria Botchway

Please tick
each box

1.	I agree to participate in this study	
2.	I understand that my participation in this study is voluntary and I am free to withdraw from the research at any time without giving any reason and without any detriment to myself and my organisation	
3.	I confirm that I have read and understand clearly the information sheet for this research and have had the opportunity to ask questions about the study. These questions have been answered satisfactorily by the researcher.	
4.	I understand that the interview will be audio-taped	
5.	I understand that only the members of the research team have access to the information collected during the study	
6.	I am aware that the information collected during the interview will be used to write up a PhD thesis, and in future research	
7.	I understand that information collected during the course of the research project will be treated as confidential. This means that my name, or any other information that could identify me, will not be included in anything written as a result of the research	
8.	I understand that when this research is completed the information obtained will be retained in locked filing cabinets in a storeroom in the Department of Management, University of York for 5 years and then will be destroyed	
9.	Would you like to be informed of the outcome of the research via a report summary, and / or be informed of any future publications?	

Name of Participant	Date	Signature
Name of Researcher	Date	Signature

Appendix A 5 Participants Information Sheet

[University Address]

Participants Information Sheet

Reference number: «Ref_Number»

Assessing the impact of Regulation on Social and Environmental Reporting (SER)

You are invited to take part in a research study which is being conducted as part of a Doctoral Research degree at [insert University name] by Miss Gloria Botchway, [insert name] and [insert name]. We appreciate your participation which we believe will greatly enhance the findings of this study.

Before you decide whether or not to take part, it is important for you to understand why the research is being undertaken and what it will involve. Please take time to read the following information carefully and do ask if there is anything that is not clear or if you would like more information.

The Purpose of the Research

Recent responses from consultations by the Coalition government indicate that there will be a requirement for companies to provide an Operating Financial Review (OFR) as part of financial statements. An OFR is a narrative explanation, provided in the annual report, of the main trends and factors underlying the development, performance and position of an entity during the financial year covered by the financial statements, and those which are likely to affect the entity's future development, performance and position. It is important to understand how regulation, specifically the OFR, is significant to companies. The aim of this study therefore is to explore the development of regulation and analyse its impact on social and environmental reporting.

Your Participation

You are being asked to participate as the study is being conducted across selected companies from the FTSE4Good and FTSE250 index. The interview will be to explore your expertise on key issues associated with regulation of SER. Interviews will also focus on motivations of SER reporting as well as individual perceptions on the impact of regulation on SER.

Also participating are selected individuals such as Members of Parliament (MPs) and persons who were directly or indirectly involved in regulations surrounding SER such as the Enhanced Business Review and the OFR. Participation is entirely voluntary and you are free to withdraw from the research at any time without giving a reason and without any detriment to yourself or your organisation.

Your Involvement

If you decide to take part in the research, you will be interviewed. The interview will take approximately half an hour, and with your permission, will be audiotaped. Before we start the interview, you will be given an opportunity to ask questions and I will ask you to sign a written consent form confirming that you are happy to take part in the study.

Benefits

Your involvement is an opportunity to voice your opinions about current regulatory requirements surrounding SER. It is hoped that the findings will help shed light on the benefits of regulation and help government better understand the role of regulation in SER.

Risks or inconvenience

There are no risks attached to this study. Your interview scripts will be kept strictly confidential; available only to the researchers.

The information you provide

Interview tapes will be transcribed. All tapes and transcriptions will be locked in a safe place. All information collected during the course of the study will only be viewed by the research panel committee, and remain strictly confidential. The confidential handling, processing, storage and disposal of data will be in accordance with Data Protection Guidelines.

At the end of the study, this information may be used to write up a PhD thesis, and may be used in publishing articles in professional and academic journals and conference presentations. The names of the people, who have taken part in the research or any other information that could identify them, will not appear in the thesis or in other written forms when the study is completed.

All who take part in the research and indicate their agreement, will be sent a summary of the final report. When the study is completed, all the information will be kept in a locked filing cabinet in a storeroom of the York Management School, University of York for 5 years and will be destroyed after that time.

Further Information:

If you have any concerns or questions about this study, please feel free to contact the main researcher Miss Gloria Botchway, on [insert telephone number] or e-mail [insert email address].

Thank you for reading this information sheet

CHAPTER 4

Chapter 4 . Lobbying and SER Regulations

4.1 Introduction

This chapter examines the impact of pressure group lobbying on the removal of the Operating and Financial Review (OFR), and the introduction of the mandatory Enhanced Business Review (EBR), highlighting the relationship between path dependency of legislation and the power of lobbyists. The chapter further argues that the government is greatly influenced by external stakeholders and relies on evidence from these stakeholders, in making amendments to regulations.²⁴

Following the removal of the mandatory OFR in 2005, and subsequent implementation of the EBR, numerous expressions of opinion were written on the removal of the OFR.²⁵ The majority of these expressed disappointment at the removal and criticised the government for having made a ‘U-Turn’ on social and environmental reporting (SER) regulations, despite promises to remain committed to improving forward-looking narrative reporting by companies. Some of these reports further identified the power dynamics and reasons behind the changes in SER regulations, with some evidence suggesting the involvement of business lobbyists as the sole reason behind the change. For example, an article by Friends of the Earth (FoE)²⁶ accused the Confederation of British Industry (CBI) of lobbying against mandatory social and environmental

²⁴ In a bid to influence legislation, the pressure groups resort to mechanisms such as policy briefings, media campaigns and partaking in consultations, with an aim to show how regulation will be beneficial / detrimental to their cause.

²⁵ See for example: Association of Certified Chartered Accountants (2005). Chancellors proposed U-turn on operating and financial review (OFR) - ACCA response. Available from <<http://www2.accaglobal.com/databases/pressandpolicyold/archive/2518997>> [Accessed 12 February 2014]; Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12 May 2011]; Association of British Insurers (2006) Business Review and Operating and Financial Review – ABI response to DTI consultation Available from <https://www.abi.org.uk/~/_/media/Files/Documents/Consultation%20papers/2006/03/Business_Review_OFR_240306165319.ashx> [Accessed 10 February 2014]; Friends of the Earth (2005). Browns’ big green failure. Available from <https://www.foe.co.uk/resource/press_releases/browns_big_green_failure_28112005> [Accessed 12 February 2014]; The Financial Times (2005) Brown criticised for abolishing operating and financial reviews. Available from: <<http://www.ft.com/cms/s/0/7a44c598-6533-11da-8cff-0000779e2340.html#axzz2yxKKMDMy>> [Accessed 9 February 2014]; The Times (2005) Chancellor’s U-turn over reviews sparks fury Available from <<http://www.thetimes.co.uk/tto/business/industries/banking/article2161196.ec>> [Accessed 10 February 2014].

²⁶ Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12 May 2011].

reporting for companies, though other opinions contested the influence of the CBI or lobbyists in these changes.²⁷ In addition, studies have been carried out on lobbying processes in accounting standards, identifying the groups which are successful in exerting influence on the final enacted accounting standard (see for example, Jupe, 2000; Kirsch and Day, 2001; McLeay et al., 2000; Tutticci et al., 1994). However, whilst there have been many studies on the lobbying processes in financial accounting standards setting, there have been a few on lobbying of social and environmental accounting standards; Weetman et al., (1996) and Rowbottom and Schroeder (2014) being the exception. Yet Weetman et al., (1996) investigated consultation responses relating to the Accounting Standards Board (ASB) 1993 Operating and Financial Review, a study carried out when the OFR was relatively new and non-mandatory. Again, Rowbottom and Schroeder's (2014) study examined the rise and fall of the OFR, charting its history and the events that led to its removal. However Rowbottom and Schroeder fail to acknowledge the extent of the CBI's involvement in the events that led to the removal of the OFR, rather suggesting that the government wanted to act quickly in removing the OFR in a bid to please businesses. Contradicting their findings, this chapter provides evidence, showing how in the years prior to the removal of the OFR, the CBI was actively attacking and threatening the government over social and environmental regulations, in particular the introduction of a statutory OFR.

Thus, in spite of extensive reports and studies examining the impact of lobbying on regulatory standards as well as investigating the influence corporations and interest groups have on regulators, far too little empirical evidence has been produced on the lobbying process and power relations exerted during the removal of the OFR.

Furthermore, previous literature is lacking the empirical foundations examining the impact of lobbying during the regulatory process resulting in the amendments to the Business Review (BR). Examining the influence of lobbying on the OFR and EBR further enhances the understanding of the impact and processes of lobbying on SER regulation, thus contributing to literature. For, as Chandler (1997) argues, 'greater insight into the political process may be gained by seeing a "product" move through the standard-setting process' (p. 412). Again, in examining the lobbying process of these

²⁷ See for example, (Rowbottom and Schroeder, 2014); House of Commons Debate. (2005-6) 447, col. 152).

two significant SER regulations, the OFR and the EBR, this chapter explores how SER regulation is influenced by political ideology and how the effect of ideological power is framed by regulatory preferences. Moreover in analysing the reasons behind lobbying activities on the OFR and the EBR, it is revealed how businesses are increasingly using SER as a form of strategy while at the same time opposing mandatory regulation in a bid to ensure continued competitiveness in the SER field.

The chapter proceeds as follows. In the next section, the theories associated with this chapter and previous literature on the relationship between regulation and lobbying, as well as the research question is presented. Next, the methods employed in collating and analysing the data, are discussed. Following the discussion of the research design and methods, a brief background detailing the introduction and removal of the OFR, as well as the process which led to the implementation of the EBR is reviewed. The findings of the impact of lobbying are then presented and discussed. The chapter ends with a summary of these findings and an introduction of the next empirical chapter.

4.2 Related Literature

This section reviews the previous studies undertaken on the lobbying aspect of regulation. The main theoretical frameworks, which have been discussed in detail in Chapter 2 and adopted in this chapter, are first, the political economy of accounting theory, which is used to interpret business approach to social disclosure as well as the use of power to sustain their interests. Second, the public interest theory of regulation is used to interpret the actions of NGOs who act in the public interest, by lobbying for mandatory SER regulations. Third, the regulatory capture theory of regulation is used to explain pressure group lobbying in SER regulation and how the government was pressured into amending regulations by the “regulated”.

4.2.1 The Relationship between Lobbying and Regulation

It is the right of any citizen to lobby his Member of Parliament, and if he considers that his case can be better advanced with professional assistance he has every right to avail himself of that assistance

First Report of Members Interests Committee, 1984-85.²⁸

The relationship between regulation and lobbying²⁹ has been well documented, with some research suggesting that lobbying has a direct impact on regulation. Although lobbying is carried out to a lot of different government or regulatory activities, such as legalising or banning certain activities, promoting industries, and relations with other governments for example, this chapter focuses on accounting lobbying as it emphasises the social and environmental activities of businesses and the lobbying activities carried out by interested parties.

Sutton (1984) one of the first to analyse the link between lobbying and regulation, used the Downsian voting model,³⁰ to discuss the characteristics of lobbyists, the timing of their lobbying and the methods lobbyists are likely to employ during accounting standard setting. Sutton's finding suggests that a rational individual will only allocate resources to lobbying if the expected benefits to him from doing so exceed the costs. Furthermore, the level of lobbying differs across regulatory environments depending on the cost of non-compliance. Finally, Sutton argues that lobbying is most productive when the rule makers' preferences are still undecided, during which time disguised lobbying could be used.

²⁸ First Report of Members Interests Committee, (HC 408, 1984-85), para 3.

²⁹ Lobbying largely represents the process by which organisations seek 'insider' status in the policy-making system, in order that their views might input as directly as possible into the process of policy development and decision-making. 'Insider' groups are those groups which are '[firstly] recognised by government as legitimate spokespersons for particular interests or causes . . . [proven partly through their ability to] talk the language of the government and civil servants, [secondly] allowed to engage in a dialogue on issues of concern to them . . . [through] formal [and informal] consultation processes . . . [and thirdly] those that agreed to abide by certain rules of the game'. (W. Grant, 'Pressure Groups: The Changing World of Pressure Groups', *Parliamentary Affairs* 57(2), 2004, p. 408 – 409).

³⁰ The Downsian Voting Model refers to Anthony Downs (1957) economic model which suggests that the rational individual will vote only if the perceived benefits from voting exceed the costs. Sutton draws on Down's single-period voting model and adapts it to his lobbying context.

Lobbying of regulatory standards takes many forms. For example, Schultz and Hollister (2003) suggest that lobbying can be conducted through formal or informal channels. Formal channels include submitting comment letters in response to invitations, having meetings with regulators and speaking at public hearings. Georgiou (2004) investigated the nature and extent of lobbying activity by a sample of U.K. listed companies and found that comment letters are likely to be a good proxy of the direct corporate lobbying activity to which the ASB is subjected. Similarly, Tutticci et al., (1994) suggest that respondents viewed the combination of both conceptually based supporting arguments and statements of strong position as a useful strategy in influencing standard setters. Informal channels are often confidential and include media commentaries, the influence of government officials or ministers affiliated to a firm, luncheon discussions and word of mouth communications. As obtaining evidence of informal lobbying and verifying its authenticity is difficult, previous studies have tended to base their analysis on submissions made by respondents to exposure drafts and compared their impact to the final enacted legislation and regulatory framework (see for example, Kirsch and Day, 2001; McLeay et al., 2000; Tutticci et al., 1994; Zülch and Hoffmann, 2010).

Lindahl (1987) however argues that simply tallying comment letters is not likely to capture the extent of firm participation in lobbying, especially if other channels for lobbying are present. Thus, with the increased use of mixed methodological approaches to analyse firm participation in lobbying, such as the use of both content analysis and interviews, the problem of identifying the extent of firm participation is reduced, as with such dual analysis, more evidence is gathered which gives further insight into the extent or level of involvement by participants (see for example, Deaconu et al., 2009; Georgiou, 2004; Kirsch and Day, 2001; Parvin, 2007; Weetman et al., 1996).

The extent of the influence wielded by lobbyists is further discussed in the literature. McLeay et al., (2000) for example, with the use of published commentaries, examined the impact of constituent lobbying activities on accounting regulators. They find that there are three main lobby groups, the industry, auditors and academics, and that the industry group exerted the greatest level of relative power over the legislature, with the proposals from the academics displaying the least likelihood of success. However, when it came to the interaction terms of agreement and disagreement between the lobbyists, decisions of the legislative body are influenced only when these lobby groups act in unison. Similarly, Kirsch and Day (2001) with the use of interviews and comment

letters, find that lobbying is multidirectional. They suggest that the international standard setter had been lobbied by external parties in support of their points of view, and had also lobbied some of those same parties to gain support for its points of view, hence the mutual agency concept. In effect, lobbying influenced the language of the final Standards enacted.

Kirsch and Day's findings are supported by Zülch and Hoffmann (2010) who employed a detailed content analysis to identify possible connections between decision makers and lobby groups. Findings suggest that there are considerable similarities in statements of parliamentarians and interest groups, from which some kind of linkage may be concluded. Indeed during parliamentary debates several ministers declare an interest in working with and for pressure groups or lobby groups. Lord Bishop of Winchester, for example speaking in the House of Lords in November 2006, stated that he is glad to have been briefed by a range of NGOs, among them Traidcraft. MP Lembit Öpik also speaking in the House of Commons declared an interest in working with the Chartered Institute of Marketing,³¹ with MP for Suffolk Coastal, Mr Gummer, also declaring himself as a sponsor of the Aldersgate Group,³² an alliance of sustainable economy leaders.

Furthermore, Dal Bó (2006) argues that as many regulators come from industry or end up working in industry, they could be biased in regulatory decisions. In fact, coming from industry could encourage regulators to make pro industry decisions as they have been "socialised" in an industry environment. Moreover Robson (1988) suggests that the role of government in its interactions with standard setters involves political interferences. Cohen (1986) also finds that commissioners with previous industry experience are more supportive of industry interest all along their careers as regulators. However these kinds of linkages and interferences as well as the appointment of business leaders as ministers for example,³³ could be seen as raising conflicts of interest.

Aguilera et al., (2007) also discuss the power concept of lobbying in their study. They argue that power is a necessary motive for the purpose of advancing lobbying causes.

³¹ *Hansard* HC Deb. vol. 450, col. 891, 18 Oct 2006.

³² *Hansard* HC Deb. vol.447, col. 163, 6 Jun 2006.

³³ An example of such a linkage is the appointment of (the CBI) Digby Jones as a Minister of State in the Department for Business, Enterprise and Regulatory Reform), which raises conflict of interest questions.

They go on to cite the example of NGOs who desire power not for their own interests but for altruistic reasons; as against the lobbying nature of business which is directed towards shareholder benefit (Henriques, 2007, p.156). Thus polling data indicates that NGOs are more trusted than either the government or business in promoting the public interest, with SER related issues likely to be lobbied for by pressure groups. This lack of trust in companies is supported by a 2005 report produced by AccountAbility, the UK research and advisory institute, and the Global Compact, the UN citizenship initiative, which identified a gap between the public corporate responsibility statements and sustainability commitments of many companies and their lobbying activities that push for narrow commercial interests. Anne Snelgrove MP, speaking in parliament further stated that MORI³⁴ and other polls have proved that NGOs are much more trusted by the public than are Governments, politicians or even business.³⁵ Nevertheless, ‘Companies that move beyond responsible lobbying to lobbying for social issues that are relevant to them may be practicing one of the most powerful forms of corporate social responsibility’ (Peterson and Pfitzer, 2009).

The final issue to be covered in this section of the literature review, is the debate on the importance of regulation in SER, which drives some groups to lobby to reduce/increase regulation. Prior studies argue that stakeholder experience of voluntary environmental reporting is disappointing and less than reassuring, with reporting geared more towards a public relations exercise, hence a more interventionist regulative approach is warranted (Gallhofer and Haslam, 1997; Gray et al., 1995). History further suggests that regulation and other social and political forces have been much more effective than SER at making businesses more socially responsible (Reich, 2008). In fact, ‘social reformers have long exposed [negative] corporate practices as means of mobilizing political support for new legislation or regulation aimed at curbing them’(Reich, 2008, p. 18-19). However, critics such as the Confederation of British Industry (CBI) argue that regulation interferes with the efficiency of the market and that increasing, or making SER regulations mandatory, will expose businesses to undue competition (Stern, 2005).

Academic studies further suggest that there is an increase in the levels of SER as evidenced in firms annual reports, (Brown and Deegan, 1998; Deloitte and Touche,

³⁴ IPSOS MORI is a leading market research company in the UK and Ireland.

³⁵ *Hansard* HC Deb. vol. 447, col. 180, 6 Jun 2006.

2005; Gray et al., 1995; Hooghiemstra, 2000; KPMG, 2011), with this increase being attributed to issues such as stakeholder pressure, the need to conform to the norm whilst maintaining a competitive edge (Gray et al., 1995; Owen, 2003; Williamson and Lynch-Wood, 2008), and regulation (Henriques and Sadosky, 1996; Owen et al., 2005; Spence and Gray, 2007). Based on the evidence showing the increase in SER levels, the chapter questions why businesses are arguing against the introduction of mandatory regulation (Stern, 2005), yet at the same time wholly complying with voluntary regulatory requirements. Indeed, evidence suggests that at the time of the removal of the OFR and implementation of the EBR, companies' adherence to SER was on the increase. For example, Deloitte and Touche (2005), reported that four out of five companies listed on the London Stock Exchange were producing OFRs or complying with OFR guidelines at the time it was abandoned. Furthermore, companies adopt voluntary regulations for reasons including the business case. A rationale for the business case is that SER will, either directly or indirectly, result in a corporation's improved financial performance, thus inciting them to voluntarily behave ethically, eventually leading to positive social and environmental change (Hart, 2010). Firms could also try to deflect any further regulation from being imposed on their operations (Deegan and Blomquist, 2006; Moon and Vogel, 2008) as a means of strategy in maintaining a competitive advantage. As regulation offers a level playing field, companies may thus want to maintain a competitive advantage, by remaining leaders in the SER field. Furthermore, preventing competitors from catching up and assuming that leadership position, is suggested as another motivational factor in companies' reservations against mandatory regulation.

In summary, the literature has discussed evidence showing that group lobbying, for a variety of reasons, has a significant impact on changes that occur in legislation. In this study, the impact of lobbying is applied to the removal of the OFR and implementation of the EBR, hence the research question:

Figure 4.1 Research Question and Analysis

How did pressure group lobbying impact on the removal of the Operating Financial Review (OFR) and the implementation of the Enhanced Business Review (EBR)?

Based on contrasts in:


- a) Evidence by corporates
 - b) Evidence by lobby groups
 - and
 - c) The final enacted legislation
- 
- Relationships and Influence**
-

Figure 4.1 presents the research question examined in this chapter, based on how evidence presented by corporates and by lobby groups is used in influencing the final enacted legislation. In examining the research question, the next section thus discusses the data collected and methods employed in answering this research question.

4.3 Research Design and Methodology

As previously stated in section 4.1, the aim of this chapter is to examine the impact of lobbying in setting SER regulations, in particular the removal of the Operating and Financial Review (OFR) and the implementation of the Enhanced Business Review (EBR). Previous research on the impact of lobbying in regulation has been undertaken from different methodological perspectives. For example, empirical qualitative approaches have included interviews (Georgiou, 2004; Kirsch and Day, 2001; Parvin, 2007; Weetman et al., 1996), and content analysis (Hansen, 2011; Schultz and Hollister, 2003; Tutticci et al., 1994; Zülch and Hoffmann, 2010). Empirical quantitative methods approaches have included regression analysis (Georgiou, 2004) and descriptive statistics (Tandy and Wilburn, 1992). Lastly, mixed methods approaches have included content analysis and regression analyses (McLeay et al., 2000) as well as content analysis and descriptive statistics (Deegan et al., 1990).

This chapter adopts a critical investigative approach (a thorough analysis of information) and uses content analysis³⁶ as well as interview evidence to examine the

³⁶ Content analysis is defined as: ‘a research technique for making replicable and valid inference from data to their context’ (Krippendorff, 1980, p. 21).

influence of lobbying on the removal and implementation of the OFR and EBR respectively. In applying content analysis on relevant documents such as comment letters and media articles, this chapter compares the contents of these documents to the final enacted legislation, in order to make an inference on the impact of these documents. The use of interviews in this chapter is in order to analyse the transcripts and to identify the level of involvement and motivations of specific key persons who were involved in the lobbying of SER regulations. This method of using both content analysis and interviews is in line with Kirsch and Day (2001).

4.3.1 Data Sources

The data sources are:

1. Hansard - Parliamentary proceedings on the OFR and the EBR between 1st November 2005 and 8th November 2006
2. Department of Trade and Industry (DTI) Company Law reform -White paper (March 2005)
3. DTI - Invitation for comments on the Business Review – Consultation processes (December 2005 and February 2006).
4. Websites of respondents to the December 2005 and February 2006 consultations. For example, Friends of the Earth (FoE), Corporate Responsibility Organisation (CORE) and Confederation of British Industry (CBI) websites.
5. Media articles and records obtained from the LexisNexis®³⁷ database (January 1993 to December 2008).
6. Interviews with selected key persons

As discussed in section 3.4.3, Hansard was consulted in analysing parliamentary proceedings relating to the OFR and EBR. All debates on the Company Law Review (CLR) in the House of Commons and House of Lords were also examined, in addition to DTI archives checked for consultation processes on the Business Review and responses (comment letters).³⁸ Moreover, information was obtained from the websites

³⁷ Lexis Nexis is a searchable database of news articles and gives access to many different databases through a single search interface. It contains thousands of publications which provide extensive sources of information. Files are updated continuously. LexisNexis (2014) About Us. Available from: <<http://www.lexisnexis.com/en-us/about-us/about-us.page>>. [Accessed 5 May 2014].

³⁸ It is of note to mention that whilst some responses were publicly available, for example, responses to the 2005 White paper, others were not. For example responses to the December 2005 consultation ‘Invitation for comments on the Business Review’ and the February 2006 consultation ‘A consultation on

of those who responded to the consultations, for example Friends of the Earth's (FoE), Corporate Responsibility Organisation's (CORE), and Confederation of British Industry (CBI) website. In addition, media articles relating to the OFR and the EBR, were obtained from LexisNexis and scrutinised for evidence of lobbying by pressure groups as well as evidence of opinions on any aspects of the OFR and the EBR.

Lastly, evidence from interviews conducted was used to identify the roles of selected key persons to determine their level of involvement as well as their reasons for engaging in the SER regulatory process. Selected persons were chosen based on their perceived expertise on key issues associated with regulation of SER, or who were directly or indirectly involved in the OFR and EBR regulatory processes. Furthermore, interviews have been widely used in lobbying studies (see for example, Georgiou, 2004; Parvin, 2007; Weetman et al., 1996) as it enables the researcher to obtain first-hand information. Thus regulators, MPs, company representatives, government representatives, members of the OFR committee and NGOs were identified and contacted for interviews. Follow up letters and emails were also sent within a month of first contact. These reminders increased the response rates as suggested by Meho and Tibbo (2003). 20 interviews, with 22 interviewees, were eventually conducted between December 2011 and September 2012.

The interviews were semi-structured consisting of a mix of face-to-face and telephone interviews. All were digitally recorded and respondents were guaranteed confidentiality. Therefore, to protect the identity of the respondent, organisational sectors were chosen as a reference to respondents (as in Spence and Gray, 2007). Respondents are thus referred to throughout this chapter by position and sector type, e.g. Coordinator, NGO. The interviews were then transcribed for later examination.

4.3.2 Data Analysis

The first step in conducting the data analysis was to examine the evidence obtained from the data sources. It is important to note here that the debates and responses are all examined in the framework of the following consultations:

narrative reporting requirements for companies', were not available on any of the archival webpages. Upon further investigation, these responses were finally obtained under the Freedom of Information Act (2001) from the Department for Business, Innovation and Skills (Known as the Department for Trade and Industry until June 2007).

Table 4.1 Proposals on Narrative Reporting Consultations

Consultation	Invitation for views / comments on:
The White Paper - Company Law Reform Bill – March 2005.	<ul style="list-style-type: none"> • Embed in statute - directors must take due account of both the long-term and short-term, and wider factors such as employees, effects on the environment, suppliers and customers • Proposal to remove requirements for disclosures in respect of the employment of disabled persons, and employee involvement, and amend, but not remove entirely, the requirement to disclose political and charitable donations. • All quoted companies to produce an Operating and Financial Review (OFR).
Invitation for comments on the Business Review - To ensure effective forward looking narrative reporting – December 2005 and February 2006.	<ul style="list-style-type: none"> • Whether any particular requirements of the Business Review need to be clarified to achieve more effectively the Government’s objectives regarding the Business Review • Any considerations which Ministers should take into account in deciding whether, and if so how, to frame amendments to these or other provisions of the Company Law Reform Bill to ensure effective forward looking narrative reporting by quoted companies, including, where appropriate, on social, community, employee and environmental matters.

Source: Table constructed from archived documents by the Department of Trade and Industry, on the Company Law Review.³⁹

The responses received by the DTI, as a result of the above consultations and analysed in this chapter, are seen next.

Table 4.2 Responses to Consultation on Narrative Reporting

Consultation on Narrative Business Reporting	Businesses	Pressure Groups	Individuals	Trade associations/Chartered Bodies/Regulators
Company Law Reform White Paper	37	7	16	36
Invitation for comments on the Business Review - To ensure effective forward looking narrative reporting	4	3	5	2

Source: Table constructed from responses submitted to the Department of Trade and Industry⁴⁰

This chapter has classified the responses received by the DTI, on the comments relating to the CLR and the BR, as shown in Table 4.2.⁴¹ Although ninety four responses were

³⁹ The National Archives (TNA) Archived Documents: Company Law Review. Available from: <<http://webarchive.nationalarchives.gov.uk/20121029131934/http://www.bis.gov.uk/policies/business-law/company-and-partnership-law/company-law/publications-archive>> [Accessed 10 February 2014]

⁴⁰ The National Archives (TNA) Archived Documents: Company Law Review. Available from: <<http://webarchive.nationalarchives.gov.uk/20121029131934/http://www.bis.gov.uk/policies/business-law/company-and-partnership-law/company-law/publications-archive>> [Accessed 10 February 2014]

received on the CLR consultation, only thirteen out of those commented on the OFR, with an even lower number of eleven, commenting on specific SER issues. Fourteen responses were however received on the Business Review consultation. Hence in making an inference on the impact of these comment letters, the thirteen responses on the CLR consultation and the fourteen responses from the BR consultation are examined. The analysis of respondents into groups, and the finding that majority of responses relating to the CLR and BR were from businesses, is consistent with other studies which find that preparers of accounts, in this case, businesses, formed the largest respondent group (see for example, Jupe, 2000; Tutticci et al., 1994; Weetman et al., 1996).

Content Analysis

Content analysis was employed in examining the CLR parliamentary debates and media articles. These debates and articles were scrutinised for references to the OFR, the EBR and social and environmental reporting; words and phrases searched for were, business review, Confederation of British Industry, community, customer, employee, environment, Friends of the Earth, lobby, operating and financial review, pressure group, regulation and social. The relevant sections were then recorded. This procedure of scrutiny was chosen to help uncover and chart the progress of the amendments made to the OFR and the EBR; and to analyse the effectiveness of commentators or lobbyists influence on the language of the final Standards.

Furthermore, as one of the objectives of this chapter is to analyse any comments which are specific to narrative reporting, comment letters were analysed in detail to determine the nature of the response. In line with Jupe (2000), this chapter uses the voting system of support or oppose as a measure to indicate the direction of the respondent's comments. Thus, comment letters were scrutinised for evidence relating to the respondent's opinions on social and environmental issues, and views on narrative reporting. NVivo was further used to help identify relevant words and statements in the responses; business review, customers, community, employee, environmental, narrative,

⁴¹ For reference, the group 'Businesses' includes all responses from companies. 'Pressure groups' include responses from all pressure groups including NGOs, Non Profitable organisations and Charities, whilst the third group includes responses from Trade Associations Chartered Bodies and Regulators such as the FRC's Auditing Practices Board. Furthermore, as with Pong and Whittington (1996) our categories includes the group 'individuals', which refers to respondents whose submission did not state any affiliation to any group or business, or who had had their names redacted (due to the Data Protection Act).

operating and financial review, regulation, reporting, and social. Lastly, as with Kirsch and Day (2001) and Georgiou (2004), content analysis was applied to the transcripts⁴² to uncover any group involvement in the lobbying process or influence on the final enacted legislation.

Thus, having discussed the research design and methodology, the next section, Background of the OFR and the EBR, charts the progress of the OFR and the EBR through parliament, forming the basis of the Discussion in Section 4.5, which further examines the influence of lobbying in these regulations.

4.4 Background of the OFR and the EBR

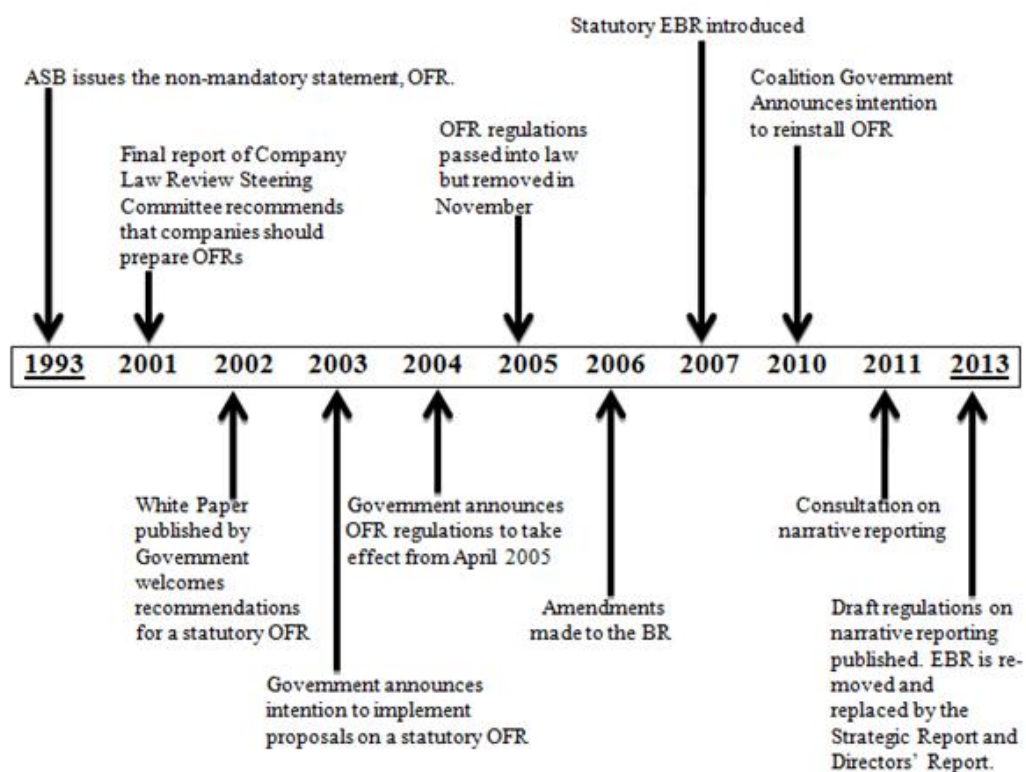
Prior to discussing the OFR and the EBR, it is important to present a timeline of regulation between 1993 and 2013, in order to enhance our understanding of the development of SER regulations in the UK.

Timeline development of SER regulations

The timeline as seen in Figure 2.1, shows the development of SER regulations in the UK, including periods when it was voluntary and when it was mandatory. Most particular to this research are the Operating and Financial Review (OFR) and the Enhanced Business Review (EBR).

⁴² Three concurrent themes were used during qualitative data analysis: data reduction, data display, and conclusion drawing and verification (Miles and Huberman, 1994). With these themes in mind, NVivo a software analytical tool was employed to help with the data reduction and identify amongst other links, relationships between the most frequently used words; and to help draw out possible meanings and assumptions.

Figure 4.2 Timeline of SER Regulations



The timeline as seen in Figure 2.1 shows how regulations have evolved over the years from 1993, when the ASB issued the non-mandatory OFR, until 2013 when the EBR was replaced by a Strategic Report and Director’s Report. In Appendix A, further details of this timeline are presented with reference to the parties involved in its implementation.

4.4.1 The Operating and Financial Review (OFR)

The ‘Operating and Financial Review’ was originally issued as a statement by the Accounting Standards Board (ASB) in July 1993. Then in 2001, a recommendation by the Company Law Review (CLR) Steering Group, resulted in a White Paper ‘Modernising Company Law’ (2002),⁴³ after which the Government decided to require quoted companies to prepare and publish OFRs. In January 2003, a revised version of the OFR Statement was issued to reflect improvements in narrative reporting. In May 2004, the Government issued proposals on the detailed implementation of the new OFR requirement in a consultation document ‘Draft Regulations on the Operating and

⁴³ The Company Law White Paper published in July 2002 indicates that public companies with a turnover exceeding £50m, and private companies with a turnover exceeding £500m, will be required to publish an OFR.

Financial Review and Directors' Report'. The DTI then published the White Paper 'Company Law Reform' in March 2005, inviting comments by June of the same year. The final OFR Regulations were passed into law in March 2005, taking effect for financial years beginning on or after 1 April 2005.

In 2005, 7 years after being commissioned by an independent group of experts, practitioners and business people, the OFR, as part of the Company law reform (CLR) bill, was introduced in parliament. The CLR bill⁴⁴ was introduced into the House of Lords on 1st November 2005. It had 885 clauses and 15 schedules on first printing. Modelled on the Companies Act 1985, the Company law reform bill, required companies to report amongst Directors Duties, their social and environmental activities.

Several businesses and organisations welcomed the OFR, including The Work Foundation Group which reported that the OFR was a significant contribution to the development of corporate reporting in the UK. The Institute of Chartered Accountants in England and Wales (ICAEW), Investment Management Association (IMA), and the Institute of Directors (IoD) all confirmed that the OFR by helping companies to write more on their social and environmental issues will be drawn upon by investors when analyzing the future performance of a company. The introduction of the OFR however was opposed by some. For example Henry Bellingham MP, argued in parliament that the number of responses received from the OFR consultation rounds were only 140 and did not cover a large enough array of organisational representation to push forward a mandatory OFR. He further stated that it was costly and burdensome as well as over and above the EU directives.⁴⁵ The CBI also expressed reservations on the introduction of a statutory OFR, citing reasons including excessive liability burdens on firms and costs (Tucker and Eaglesham, 2004). Regulations were nevertheless passed in March 2005, requiring quoted companies to produce an OFR.

In January 2006, however, the OFR was abolished under the Companies Act 1985 (Operating and Financial Review) (Repeal) Regulations 2005 (SI 2005/3442). The backlash following the removal of the OFR was widespread. According to a survey by accountants (Deloitte and Touche, 2005), four out of five companies listed on the

⁴⁴ Company Law Reform Bill [HL] Bill 34 2005-06.

⁴⁵ Second Standing Committee on Delegated Legislation, Draft Companies Act 1985 (Operating and Financial Review and Directors' Report Etc.) Regulations 2005 (HC 2004-05), paras 6-7.

London Stock Exchange were producing OFRs or complying with OFR guidelines at the time it was abandoned, hence its removal did not go down well with some businesses. In parliament for example, the repeal was disapproved by some MPs. For example, Baroness Tonge indicated that the government had taken a backward step by abolishing the OFR which would have gone a long way to ensure transparency and accountability among UK companies. The FoE further challenged Gordon Brown to justify his decision to repeal the OFR,⁴⁶ consequently filing a judicial review⁴⁷ in the administrative court on the 11th January 2006, at which a thirty two page document challenging the removal of the OFR, was produced. The document included statements that the Chancellor's decision to abolish the OFR had been unlawful because he did not follow proper procedures or the Government's own consultation policy. Thereafter, following the filing of the judicial review, to avoid FoE taking the government to a higher court, a ministerial statement was issued on the 15th January 2006, setting out a fresh consultation on the future of company environmental reporting, and a review of the OFR, including measures contained in the scrapped OFR.⁴⁸ The Treasury also agreed to pay FoEs legal costs. On 1st February 2006, Alun Michaels, then the Minister for Industry and Regions announced that the January 2006 consultation was extended from February to March 2006 to allow for more responses.

4.4.2 The Enhanced Business Review (EBR)

Following the abolition of the OFR in November 2005, listed companies were reminded to continue to produce a Business Review (BR), though on a non-statutory basis. The Government stated that the contents of the BR will be similar to an OFR but more flexible. Its introduction was to align reporting requirements with those in the EU Directive, a sensible adjustment of policy, representing a cautious approach to the

⁴⁶ The FoE described the chancellor as a 'sop to the CBI' as he was interested in protecting his reputation as a 'pro-business' Chancellor rather than act in the interest of society as a whole. They further stated that the decision to abolish the Operating Financial Review was also 'unlawful' because it was 'procedurally unfair, irrational/perverse, a breach of legitimate expectation, and based upon material errors of fact' Source: Friends of the Earth (2005) Brown faces legal challenge after scrapping OFR [Online] Available from <https://www.foe.co.uk/resource/press_releases/brown_faces_legal_challenge_07122005> [Accessed 18 May, 2012].

⁴⁷ Friends of the Earth (2005) Grounds for Judicial Review [Online] Available from <http://www.foe.co.uk/sites/default/files/downloads/ofr_grounds.pdf> [Accessed 18 May, 2013]

⁴⁸ Friends of the Earth (FoE), (2006) claimed the decision was made as a tokenistic gesture to big business, stating, 'This was a flagrant case of the Chancellor breaching the Government's own consultation policies and of carrying out an entirely one-sided, informal and unfair consultation. Issues around environmental and social reporting affect more than the business community - and the Chancellor has now recognised the valid rights of other stakeholders'.

imposition of additional regulation.⁴⁹ For financial periods beginning on, or after, 1 April 2005 all companies (except small companies) were thus required to prepare a business review in accordance with section 234ZZB of the Companies Act 1985. It was in effect, a much less detailed, less prescriptive version of the statutory OFR. Furthermore, the government stated that the cost of the BR was substantially lower than that of providing an OFR and provided for broadly similar reporting of the principal areas of narrative reporting. Consequently, the Company Law Reform Bill, under which the Business Review was incorporated, received its second reading in the House of Lords on 11th January 2006. The Government issued a statement saying that it believed that disclosures, both mandatory and voluntary, were only part of the picture.

*‘On their own, disclosures are insufficient to generate responses by businesses to the legitimate concerns of civil society. Dialogue with and pressure from stakeholders, including the public, NGOs, shareholders and Government, is vital for achieving this outcome’.*⁵⁰

Thus, introducing the Bill, Lord Sainsbury, Parliamentary Under-Secretary of State at DTI stated that the Bill has four key objectives:

- Enhancing shareholder engagement and a long-term investment culture
- Ensuring better regulation and a “think small first” approach
- Making it easier to set up and run a company
- Providing flexibility for the future.

In March 2006, following the narrative reporting consultation launched in February 2006, medium sized companies were included in the requirement to report on social and environmental issues, whereas they had previously been exempt. Thereafter, on 10th May that same year, at the 3rd reading, and following several amendments, Lord Sainsbury announced in parliament, that following the February 2006 consultation, quoted companies were now specifically required to provide a business review which

⁴⁹ ‘The business review was introduced to fulfil the EU directive requirements. On Report, we discussed at length our commitment to encouraging companies to develop their corporate responsibility and we accept that the business review, with its requirements for listed companies to report on environmental and community issues, should play a role in that process’.(*Hansard* HC Deb. vol. 451, col. 669, 6 Nov 2006).

⁵⁰ Association of Corporate Treasurers. (2005). Statement on the Operating and Financial Review. Available from: www.treasurers.org/system/files/chancellorsstatement_28nov05.pdf. [Accessed 10 May 2011]

includes information relating to the environmental, social and community matters as set out in Clause 395(5). The Bill completed the Commons Committee stage on 20th July 2006. During the committee stage in the House of Commons, the title of the Bill was changed from ‘Company Law Reform Bill’ to ‘Companies Bill’. The final amendment to the Business Review, now publicly referred to as the Enhanced Business Review, thus introduced a mandatory reporting standard for all large and medium sized listed businesses, and applied to all company accounts, with reporting periods beginning on or after 1st October 2007.⁵¹

In the next section, the chapter examines the evidence obtained from the analysis of parliamentary debates, respondent’s comments and interview comments. These are compared to the final enacted legislation, to enable an effective analysis of the influence of lobbying.

4.5 Discussion

4.5.1 The Impact of Lobbying

In line with Sutton (1984), this chapter argues that an accounting standard setting process is a political lobbying process and as such offers potential participants several opportunities and means by which they can influence its outcomes. The changes that occurred in the removal of the OFR and implementation of the EBR can largely be attributed to the influence specific lobbying groups exerted, as this chapter will demonstrate. In order to appropriately discuss the influence of lobbying, this chapter identifies three groups, (CBI, the government, and FoE) who were instrumental in the removal of the OFR and implementation of the EBR. The ideologies and mechanics employed by these groups, in their lobbying activities, are briefly discussed next.

The first group are identified as the CBI. On its website, the CBI claims to be the UK’s foremost business lobbying organisation, with a mission to enhance the competitiveness and prosperity of businesses. Widely regarded as the main voice of the UK business

⁵¹ Companies House. The Business Review and Directors Report: Available from <<http://www.companieshouse.gov.uk/companiesAct/implementations/businessReviewDirectorsReport.shtml>> [Accessed 12 May 2014]

world, the CBI is reportedly viewed as an economically right-wing lobbying group and openly advocates the free-market ideology.⁵²

The second group who contributed to the removal of the OFR and the implementation of the EBR are the government, mainly represented by HM Treasury and the Department of Trade and Industry (DTI). In terms of SER regulation, the ideology of the government is to work on deregulation in order to reduce the burdens of reporting on businesses. Evidence supporting this stance suggests that in October 2004, the Better Regulation Task Force advised the government that in order to improve regulations, deregulation might be necessary in some areas.⁵³ This deregulation agenda was supported by the Hampton Report (2005)⁵⁴ which also advocated deregulation to help reduce administrative burdens on businesses. Here, it is argued that the deregulation agenda of the government is closely aligned with the free market ideology of the CBI, which led both groups to be accused of ‘being in a cosy relationship’ with each other.⁵⁵ It is also reasonable to state that the political economy of the era reflects how the government in seeking to gain political support from businesses, seeks to preserve their own self-interests, and therefore attempts to operate within the system through various relationships with businesses (Dahl, 1982, 1986).

The third group is FoE aided by some NGOs such as CORE. Having an Environmentalist ideology, FoE campaigns on issues of corporate social responsibility, as well as the environmental and social practices of companies. It also campaigns on sustainability issues, especially for companies to be accountable to the society and to the environment, and for government to set rules forcing all businesses to engage in reporting, as past voluntary initiatives have not worked.

⁵² Harvie, P. (2014) Referendum or no referendum, it's perfectly obvious the CBI is an economically right-wing lobbying group. Available from <<http://www.eveningtimes.co.uk/opinion/columnists/referendum-or-no-referendum-its-perfectly-obvious-the-cbi-is-an-161549n.24084161>> [Accessed 10 May 2014]

⁵³ Better Regulation Task Force (BRTF). (2005). Less is More. Available from <<http://www.bis.gov.uk/files/file22967.pdf>> [Accessed 10 May 2014]

⁵⁴ The Hampton Review (2005) Available from: <<http://www.bis.gov.uk/files/file22988.pdf>> [Accessed 10 May 2014]

⁵⁵ ‘I think it becomes frustrating when you have a government that sort of ‘fetishises’ the views of business if you like, and I think there is a real obsession at the moment in government, with the idea that if you were going to get growth we have to be proponents and being proponents means doing everything that the business lobby asks for’ (Policy Officer, NGO)

Hence, having presented the main groups involved in lobbying on the OFR and the EBR, the next sections examine the influence each of these groups had, detailing their roles and the mechanisms used in the removal of the OFR and implementation of the EBR.

4.5.2 Lobbying and the Removal of the OFR

'The CBI is business' most powerful lobbying force in the UK...Such is the strength of the CBI's reputation that Government frequently approaches the CBI for advice and opinion. No other business organisation has such an extensive network of contacts with Government ministers, MPs, civil servants, opinion formers and the media'.⁵⁶

This section follows the events that led to the removal of the OFR. In analysing the events, the chapter questions the arguments as put forward by Rowbottom and Schroeder (2014) on, the absence of concerted lobbying in the removal of the OFR. In particular, Rowbottom and Schroeder (2014) downplay the extent of the involvement of the CBI, by stating 'Rather than reacting to pressure from "big business", Treasury officials instigated the deregulation of the OFR and then sought bodies such as the CBI to support it (p. 670). Moreover, Rowbottom and Schroeder (2014) argue that '...the Treasury only approached the CBI after it identified the OFR as a deregulatory opportunity' (p.674). Furthermore, they state that the briefing papers reveal that the UK government was under no significant pressure from interest groups and the intervention was derived by political opportunism. However the authors previously acknowledged, in the same article, that political support for the government by businesses had waned by 2005 (p.665), implying that the government was indeed, especially with elections coming up, under pressure to reduce the criticism being levelled against them by business. This is therefore a marked contrast, which needs further clarification by the authors. Hence, in questioning these arguments, this section presents, through a chronology of events, evidence of the role played by the CBI in lobbying to reduce SER regulations, protesting against a statutory OFR, and pressuring the government.

Furthermore, although it is difficult or near impossible to know exactly what went on

⁵⁶ The Confederation of British Industry (CBI) (2006) Membership Available from <<http://www.cbi.org.uk/ndbs/content.nsf/802737aed3e3420580256706005390ae/0E1BB828380B86A580256BA500357701?OpenDocument>> [Accessed 10 January, 2013].

behind closed doors, unless one has privy or exclusive access, it is argued that in order to come to a sound conclusion, and make valid claims, one has to investigate and exhaust all avenues of information and sources. Hence, in contrast to Rowbottom and Schroeder, the chapter analyses not only Treasury documents, but bases its argument on a larger set of evidence, which are Treasury Documents, Parliamentary debates, Media articles spanning several years, and interviews. In the next section, the evidence showing how the CBI were involved in opposing regulations and pressuring the government, is presented.

The CBI's Opposition to the Mandatory OFR and Environmental Regulations

The involvement of the CBI in opposing rules requiring companies to disclose environmental, social and ethical policies is seen when in August 2000, they stated,

'It [The CBI] is against making the operating and financial review narrative in company reports, which would take in disclosure of environmental, social and ethical polices, a statutory requirement. We would prefer, on the basis of flexibility, that the operating and financial review be maintained as a voluntary disclosure'.⁵⁷

Further, in July 2001, the CBI is quoted stating, *'While we feel that the Operating and Financial Review has been a success on its current voluntary basis, this should not be a statutory requirement'.⁵⁸* The CBI was also able to reduce hugely, the number of companies that would be covered by the voluntary OFR; achieved through lobbying the Government to reduce the coverage of the OFR to only the largest UK public companies.⁵⁹ However, at the same time, a pilot OFR was adopted by a number of companies, including British Airways, BT, Clydesdale Bank and Great Universal Stores. They reported that they found no problems with the OFR as it incurred little extra cost to business.⁶⁰ In addition, the Economist Intelligence Unit published a document on the assessment of the UK economy, indicating that Britain remained the

⁵⁷ Mcconnell, I. (2000). CBI opposes laws requiring firms to reveal public interest details; Challenges to key planks of Government shake-up of company law. *The Herald* (Glasgow), 7 August, p. 18.

⁵⁸ Buckley, C. (2001). Reforms could start quiet revolution. *The Times* (London), 27 July, [Online] Available from Lexis Nexis. [Accessed 11 June, 2014].

⁵⁹ Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12 May 2011].

⁶⁰ Buckley, C. (2001). Reforms could start quiet revolution. *The Times* (London), 27 July, [Online] Available from Lexis Nexis. [Accessed 11 June, 2014].

world's second best business environment for inward investors, due to a combination of low taxation and light regulation. This report thereby counteracted the position of the CBI, who had claimed that the Labour government was strangling business with ever more taxes and a jungle of red tape.⁶¹

Nevertheless, the CBI continued its attack on the government and on regulation. In July 2002, Phil Charles, head of enterprise at the CBI, stated '*The burden of red tape has got worse over the past few years. New regulations are added while the old ones are not removed. The layers just keep growing.*'⁶² Further attacks were levelled at the government by the CBI in December 2002, with the CBI arguing that a new business regulation is launched every 26 minutes of the day and that the Government will have imposed billions in additional taxes on UK businesses within 7 years.⁶³

In August 2003, the CBI protested against environmental regulation in the form of the new EU chemicals law, writing to the then Secretary of State for the Environment, Margaret Beckett, urging her to ensure that the extent and cost of the extra work imposed by the new regulation is significantly reduced. The "employment card" was also "played" as the CBI stated that extra burdens brought on by regulation will drive jobs away from Britain to countries such as China.⁶⁴

Then, in January 2004, the CBI accused the government of putting jobs at risk '*on the altar of green credentials*' and of '*platinum plating*' its emission targets,⁶⁵ citing the issue of competitiveness and further campaigning for business leaders to tackle the environmental challenge and lobby for less stringent regulations. The CBI in this case used the "competitiveness card", implying that too many regulations will put UK firms

⁶¹ Outlook: Inward Investment. *The Independent (London)*, 3rd June 2000 [Online] Available from Lexis Nexis. [Accessed 11 June 2014].

⁶² Armistead, L. (2002). Flood of red tape drowns UK's enterprise culture. *Sunday Times (London)*, 7 July, p.15.

⁶³ E-commerce Remains Strong despite Government help. *New Media Age*, 12 December 2002 [Online] Available from Lexis Nexis. [Accessed 8 June 2014].

⁶⁴ CBI Protests at New EU Chemicals Law. *The Independent (London)*, 11 August 2003 [Online] Available from Lexis Nexis. [Accessed 11 June 2014].

⁶⁵ Harrison, M. (2004). Industry Warns Over Suicidal Increase in Emissions Target. *The Independent (London)*, January, p.17.

at a disadvantage compared to their counterparts in Germany or France.⁶⁶ Digby Jones, director-general of the CBI further stated, *'UK businesses need the government to fight as hard as it can to make sure companies here are not handicapped with onerous targets when other states are not making the same commitment'*⁶⁷, further implying that the UK should not go over and above what other states are doing on emissions.

In July 2004, the CBI further launched scathing attacks on the government, when John Cridland, the CBI deputy director-general, accused the government of failing to implement environmental regulations in a *'business-friendly way'*, labelling the regulations as *'sloppy'* *'implemented poorly'* and *'enforced in an ill-considered fashion'*. They then slammed the *'heavy-handed'* and *'inconsistent'* environmental regulations which they claimed were costing firms billions of pounds a year to comply with, further stating in a report that the laws had little sensitivity to the extremely competitive field that UK business worked in.⁶⁸

However, in a counter attack to this report, Barbara Young, the head of the Environment Agency at the time, refuted the CBI's claims and stated,

*'It [the CBI report] is completely at odds with the findings of numerous institutions, including the Organisation for Economic Cooperation and Development and the World Bank, which rate UK regulation amongst the least burdensome and offering least barriers to competition of any regime. It [the CBI report] is based on perception with little sound underpinning data or relevant international comparisons.'*⁶⁹

Then in the early part of August 2004, John Cridland, stated in response to the proposed OFR,

⁶⁶ 'Face Environmental Challenge'. *The Bristol Post*, 7 May 2004 [Online] Available from Lexis Nexis. [Accessed 8 June 2014].

⁶⁷ Reynolds, R. (2005). Blair Angers The Green Lobby By Defying Brussels on Emissions. *The Scotsman*, 15 February, p.15.

⁶⁸ Stanton, J. (2004). CBI Attacks GBP 4bn for Environment Rules. *Evening News (Edinburgh)*, 5 July, p.3.

⁶⁹ Stanton, J. (2004). CBI Attacks GBP 4bn for Environment Rules. *Evening News (Edinburgh)*, 5 July, p.3.

'The existing voluntary arrangements have given shareholders valuable information they wouldn't have otherwise had. This has happened without putting an excessive burden on companies. The proposed statutory OFR must be no less workable for companies and equally useful to shareholders. The danger is that value will be undermined as companies are pushed into sterile, formulaic reporting. The CBI is seriously concerned that the new proposals for statutory reporting requirements will expose companies to substantial extra reporting and damaging litigation. The standards of compliance must not be over the top, and at the moment it looks as if the DTI has inadvertently gone too far'.⁷⁰

Following these comments by the CBI, the DTI delayed implementation of the scheme from January to April 2005.⁷¹ Here, it can be stated that the DTI, facing opposition from the CBI, acted in favour of the special interests of the CBI, hence suggestive of regulatory capture (MacMahon, 2002) being at play here. Nevertheless, the scaling back of the OFR requirements were criticised by some. For example, FoE's corporates campaigner Sarah-Jayne Clifton stated,

'It is about time the Government stopped bowing down to CBI scaremongering and recognised that regulation is essential to tackle market failure and protect people and the environment from the negative impacts of corporate activity. Skimping on measures now to improve business impacts will mean much greater costs in the long-term'.⁷²

The campaign against regulation by the CBI nevertheless continued, when in November 2004, the CBI warned that the OFR will *'expose companies to unnecessary and excessive reporting burdens, not to mention damaging litigation.'*⁷³ In the same month, the Government again conceded to the CBI by agreeing to replace the requirement for company directors to make "due and careful inquiry" when considering what is relevant for the OFR with the less legally onerous "consistency with the company's accounts".

⁷⁰ (Grant, 2004) Business groups say OFR goes too far. Available from: <http://www.accountancyage.com/aa/news/1774434/business-ofr-goes> [Accessed 13 March 2012]

⁷¹ Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12 May 2011].

⁷² Friends of the Earth (2005). Browns' big green failure. Available from <https://www.foe.co.uk/resource/press_releases/browns_big_green_failure_28112005> [Accessed 12 February 2014]

⁷³ Thomas, S. (2004). Insider; Life in the Goldfish Bowl. *Accountancy Age*, 4 November, p.19.

The enactment of the OFR was therefore delayed until May 2006, with enforcement scheduled for May 2007.⁷⁴ The CBI then accepted that of the approximately 250 environmental standards directives issued by the European Union, it had to some degree opposed every one of them.⁷⁵ In the next section, further evidence of the CBI's stance against regulation is discussed.

The CBI and the Issue of Climate Change

In January 2005, an inquiry was held by the Environmental Audit Committee on the international challenge of climate change. The Committee invited the Director General of the CBI, Sir Digby Jones, to speak as a witness on the issue of climate change. At the inquiry, Digby Jones stated,

*'Britain should lead the world on the environmental issues but not to the extent that some other EU members and other competitor countries profit from our good intention...I worry that we go into the ring of global competitiveness with one hand tied behind our back because we are one of the few nations that lead from the front and others do not and that renders us uncompetitive.'*⁷⁶

This stance was however rebuffed by the Mr. Peter Ainsworth, the Chairman,

*'Whilst we welcome the fact that you recognize the potential profound seriousness of the problem [of climate change], the qualification you have subsequently places on the issue means that the CBI has been actively engaged in trying to water down various governmental measures to seek to mitigate the problem...'*⁷⁷

The Chairman then accused the CBI of spreading false information as there was no threat to jobs and competitiveness to firms if the UK tackled climate change. One of the members of the Environment Audit Committee, Mr. Challen further asked Digby Jones (who had earlier argued that *'the rules by forcing Britain to be green, will force British*

⁷⁴ Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12th May 2011].

⁷⁵ Vidal, J. (2005). Business as usual: The leaders of British Industry always oppose legislation that benefits the environment – but they are coming under fire. *The Guardian (London)*, 17 August, p.10.

⁷⁶ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q459

⁷⁷ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q460

companies abroad and consequently impact on British jobs’), ‘which British companies have relocated abroad purely as a consequence of environmental pressures’; to which Digby Jones replied, ‘nil’.⁷⁸ Furthermore, a member of the Environment Audit Committee inquiry, Mr. Flynn, questioned the CBI’s stance on the loss of competitiveness,

‘Those countries that have been leaders in investing in environmental protection and gearing up their industries do not seem to have lost any competitive advantage and there may well be a benefit in this and those countries...’⁷⁹

In response to Mr. Flynn, Digby Jones stated, *‘one of the contributing factors might be it is because other competing countries were not making it as difficult to do business from an environmental point of view.’⁸⁰*

Nevertheless, in summing up the meeting, the Chairman of the inquiry rejected the CBI’s stance on the issue of environmental regulations causing competitiveness stating,

‘There is absolutely no evidence – you yourself said there was no evidence – of companies leaving Britain to go elsewhere. There is absolutely no evidence from the European Commission competitiveness report or the substantive documentation produced by WWF that the threat that you always come up with that if we do the right thing by the environment we are going to lose British jobs is true and there is plenty of evidence that it is extremely exaggerated.’⁸¹

Here it is seen that the mechanisms used by the CBI in attacking regulation, was to justify their stance through arguing on the issue of cost, potential loss of jobs, and competitiveness; should Britain go green.

Further evidence of the CBI’s opposition to regulation is seen in February 2005, when

⁷⁸ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q470

⁷⁹ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q507

⁸⁰ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q508.

⁸¹ Environmental Audit Committee, The international challenge of climate change: UK leadership in the G8 and EU (HC 105, 2004-05) paras Q520.

more OFR measures were watered down by the DTI. This was after intense lobbying from the business community claiming that the OFR draft proposals were too demanding.⁸² Commenting on this change, John Cridland, the CBI deputy director-general, stated,

*'It is excellent news that the government has listened to our representations. The changes enable firms to explain activities to all stakeholders in plain language without checking every comma for exposure to legal challenge.'*⁸³

The above statement further highlights the powerful lobbying nature of the CBI as it is claimed that the government had '*listened*' to their '*representations*'. In addition, documents provided by the Treasury⁸⁴ showed that the Treasury liaised with the CBI prior to the removal of the OFR. In these documents, the Treasury admitted that '*There was informal contact with the CBI about this [the repeal of the OFR] on one occasion some time before the decision was made*'.⁸⁵ The Treasury also admitted that further meetings were held with business leaders, who all voiced some reservation at the statutory OFR.⁸⁶ Then, on the 28th of November 2005, Chancellor Gordon Brown announced the repeal of the OFR at a CBI dinner, stating,

'Best practice is of course for companies to report on social and environmental strategies relevant to their business. But I understand the concerns about the extra administrative cost of the gold-plated regulatory requirement that from April next year all quoted companies must publish an operating and financial review. So we will abolish this requirement and reduce the burdens placed on you. I hope this

⁸² Macalister, T (2004). New rules for audits watered down by lobbyists. *The Guardian*, 26 November, p.21.

⁸³ Pandya, N. (2005). Showing how they manage: New rules are forcing top companies into revealing how they handle their staff. *The Guardian (London)*, 26 November, p.23.

⁸⁴ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

⁸⁵ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

⁸⁶ The Treasury provided evidence of businesses suggesting to abolish the need for an OFR from listed companies, quoting Hermes note (08/06), ABI email/filenote (12/08), Filenote of meeting with London Stock Exchange (19/08), Note of meeting with informal advisory group (08/11) (Representatives1 from: APCIMS, LIBA, IMA, London Stock Exchange, BBA). HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

will be the first in a series of regulatory requirements that we can remove by examining these concerns together'.⁸⁷

Announcing the repeal at a CBI dinner further fuelled the impression that the government wanted to please business. Hence, even though the DTI were practically in charge of corporate reporting policy, the Treasury went behind the back of the DTI, by excluding them in the decision making. Perhaps, the lure of businesses was too powerful, such that the government was keen to please businesses, yet incur the wrath of its own ministers, such as Alan Johnson (DTI) and Margaret Beckett (DEFRA)? Furthermore, is it possible that the Treasury were more concerned about securing support from the CBI, as indicated by this statement '*it is important that there is good support from business and investors*'⁸⁸, and in the process ignore any concerns from the DTI?

In addition, a week before the announcement at the CBI conference, the Chancellor had addressed the Institute of Directors (IoD) at which he pledged to wage war on regulation. However, although at this time the Chancellor was preparing to abolish the OFR, none of this was made known at the IoD conference, with the Chancellor rather choosing to announce it at the CBI conference. Here it is reasonable to state that the choice of the Chancellor in aligning with the CBI could be related to the influence wielded by the CBI or the importance accorded the CBI, as opposed to the IoD.

Further documents provided by the Treasury⁸⁹ give insight into the lobbying process that resulted in the abolition of the OFR. According to these Treasury documents, a fund manager from Hermes, in June 2005, suggested to a senior official at the Treasury's enterprise unit, that if the government wanted a quick win, they could get rid of the OFR, as this move would be a good deregulatory measure which will go down well in the city. This was after Treasury officials had been told to identify de-regulatory

⁸⁷ Elliott, L. and Seager, A. (2005). Financial: Brown pledges to cut red tape in drive to woo industry: Chancellor hopes to win back business community: Social and environmental audit to be scrapped. *The Guardian (London)*, 28 November, p. 22.

⁸⁸ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

⁸⁹ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

opportunities. Consequently, the official worked on the suggestion by Hermes, sending a memo to the Chancellor who authorised it without neither speaking to the DTI nor following government consultation protocol. Moreover, there is no further evidence to suggest that once the CBI knew that the OFR was going to be abolished, they objected to it. The opposition to the introduction of a statutory OFR was also acknowledged in parliament by Lord Sainsbury, Parliamentary Under-Secretary of State at DTI stating, ‘...some business organisations argued strongly against reintroducing the OFR reporting burdens’.⁹⁰

Consequently, Digby Jones, in response to the abolition announcement stated that relations with the Government were deteriorating rapidly, calling on Tony Blair's most likely successor to adopt a more pro-business stance. In this way, the decision of the government to change regulation was based on the likelihood that the votes gained from the lobbying group will be greater than the votes lost from the group harmed by the regulation (Richardson and Kilfoyle, 2008). Therefore it is apparent that the CBI had been active in criticising the government over the issue of ‘less regulation’. Digby Jones then cautiously welcomed the Chancellors announcement, saying, ‘Business has said it wanted to see Government action rather than fine words, and this is a very tangible deregulation move’.⁹¹ Further commenting on the removal of the OFR, the CBI deputy director general, John Cridland, also stated, ‘It is perfectly understandable why we should be very happy and other people less so. You can't please everyone all the time’.⁹²

Finally, in June 2006, during parliamentary debates, Mr Gummer MP, accused the government of having a close relationship with the CBI, stating,

“Why are the Government so afraid? What is the deal that has been done in the Digbyisation⁹³ of the Government? There is a closeness—a kind of relationship—with a particular bit of the CBI that I find difficult to understand. ...All the people

⁹⁰ Hansard HL Deb. vol. 681, col. 933, 10 May 2006.

⁹¹ Condie, B. (2005). Brown surprise move to ease 'gold plate' burden. *The Evening Standard (London)*, 28 November, p. 24.

⁹² Treanor, J. and Milner, M. (2005). Brown surprise move to ease 'gold plate' Brown plan to cut red tape for business provokes chorus of disapproval: Dismay at Brown plan to cut red tape. *The Guardian (London)*, 29 November, p. 1.

⁹³ Digby Jones was the head of the CBI at the time.

whom we rely upon to set the standards in British industry are saying the opposite to what the Government are saying in the Bill... We need the OFR'.⁹⁴

This statement was made although Mr Stephen O'Brien MP, had earlier stated,

'No pressure was exerted by business or the CBI to get rid of OFRs—it was one of those strange instances when business was rather compliant and accepted the proposal—but it is clear that the Chancellor wanted something to announce at the CBI conference'.⁹⁵

However, in view of Mr O'Brien's statement indicating that the CBI did not exert any pressure, as well as the evidence provided by FoE, statements by interviewees and the media articles, it is argued that that the removal was in a bid to please business. This situation further highlights the political economy argument describing the behaviour of government pleasing those who it felt are most likely to threaten its stability, and hence allowing themselves to be captured by power-wielding businesses.

Therefore, having presented a chronology of events detailing the lobbying by the CBI in minimising regulations, opposing a statutory OFR, including evidence from third parties such as the Treasury and parliamentary debates, it is argued that the involvement of the CBI in contributing to the removal of the OFR cannot be downplayed due to the amount of pressure they levelled at the government and their long and constant opposition to the mandatory OFR. Thus, this chapter counteracts the arguments of Rowbottom and Schroeder (2014), and provides evidence showing the extent to which lobbying contributed to the removal of the OFR. Further evidence on the influence of the CBI as recounted by interviewees is presented next.

Respondents' Views on Corporate Lobbying

Some respondents' statements support the argument that the CBI contributed to the removal of the OFR, which was deemed a 'significant contribution to the development of corporate reporting in the UK'⁹⁶. For example,

⁹⁴ *Hansard* HC Deb. vol. 447, col. 162, 6 Jun 2006.

⁹⁵ *Hansard* HC Deb. vol. 447, col. 152, 6 Jun 2006.

⁹⁶ Memorandum submitted by The Work Foundation to the Select Committee on Trade and Industry, Appendices to the Minutes of Evidence. Available from:

'Well, they got the [Government] to go back on their promise, so I see that as a huge impact [on the part of the CBI]...It [Lobbying] is such a shadowy process, that nobody really knows what goes on. Which I think is dirty. That is not how democracy works'

Environmental Lawyer, NGO

'I am not sure how much they were lobbying against it [the OFR], but... I know it was rejected at this CBI dinner. I think a lot of the members were, I know for a fact they were CBI members'

Executive Director, NGO

A CSR manager interviewed, however frowned at the actions of the CBI in attacking regulation stating,

'Right now the CBI should realise that the future of business really depends on taking sustainability seriously...So we, we would say to the CBI, listen to your members and also listen to the voices inside your members, that you might not yourself agree with, and think how can we make a contribution to sustainability to move it forward rather than obstructing it'

CSR Manager, Media

Moreover, some regulators voiced their concern at the CBI's behaviour,

'...we [The CBI] would like to be paid a great deal, we would like to be given the credit for what goes right. We would not like to be penalised for what goes wrong. We would like everybody to love us, and appreciate all the good things we do. But we don't want people to hear about, or understand, or penalise us for the mistakes we make. So their [The CBI] move towards, please reduce regulation, I think has to be treated very carefully'

Board Member, Accounting Standards Board

Nevertheless the role of the CBI was acknowledged by some respondents. For example,

'They're not like a separate organisation with its own agenda, they are the voice of business. And they operate and consult in that way. And I also get, from the experience I've had with the CBI, they are an organisation which does a lot of

<<http://www.publications.parliament.uk/pa/cm200203/cmselect/cmtrdind/439/439ap13.htm>>. [Accessed 2 June 2013].

engagement and dialogue, both with government and business. So I think it provides a very helpful role'

Corporate Responsibility Manager, Tobacco B

Based on these statements, it can be argued that the free market ideology, as propagated by the CBI, is increasingly being rejected by many, including notably some businesses. Indeed, previous studies suggest that the free-market ideology is unlikely to deliver sustainability (see for example, Gladwin et al., 1997) with Shrivastava (1996) suggesting that free markets are responsible for environmental problems. Moreover, this view could be related to the fact that stakeholders are increasingly being made aware of the importance of regulation in SER. In addition, central to the issue of CBI lobbying to reduce regulation for all businesses in its capacity as the 'Voice of Business', is the question, does the CBI represent the views of all business? This is discussed next.

The CBI – The Voice of Business?

It has been suggested that Treasury officials and government ministers recognise the value of the CBI, in that as a broad-church lobby, it acts as a first filter for Budget suggestions that would otherwise go direct to the Treasury.⁹⁷ In other words the CBI can pull together a more balanced view about what industry as a whole might want. Some businesses therefore engage the services of the CBI in order to propagate their interests,

*'...for decades, corporations have known that, if they lobby for their own interests, public opinion won't take them seriously. Whatever their sugar-coated words, we'll be aware that they are speaking not out of public-spiritedness but to protect the share-options of their boards. Hence some companies use the CBI who bark whenever they hear mention of environmental regulation.'*⁹⁸

However, interviews with stakeholders, point to the fact that in spite of claiming to be the voice of UK business, the CBI does not represent the views of all businesses, especially with relation to SER issues. For example,

⁹⁷ Bassett, P. (1993). Why the Treasury is listening again when the CBI speaks. *The Times (London)*, 20 January, [Online] Available from Lexis Nexis. Accessed 10 June 2014.

⁹⁸ Blackhurst, R. (2005). Your Planet: Clouding The Atmosphere; Part One: Facing The Facts: One Reason Why Western Governments Have. *The Independent (London)*, 19 September [Online] Available from Lexis Nexis. [Accessed 11 June 2014].

'We are not members of the CBI and I don't think they speak for us or they speak for all companies.'

CSR Manager, Media

'Yes, we do subscribe to it [CBI]. I think we pay a subscription and whatever. But we don't ask them to lobby on our behalf. And certainly not on that [minimising regulation of SER] topic. We might ask them to intervene on some other topics. But we've never asked them to intervene on this particular topic.'

Head of Sustainability, Tobacco A

'So we've obviously got a very strong link with the CBI but at the time...I certainly don't recall anything we were doing at the time to support the CBI, and what they were doing [lobbying on SER regulations]...I think it was probably other businesses lobbying because they felt, you know, the actual implications were too great for them, but I don't think that was the case for us.'

Head of Corporate Responsibility, Gas, Water and Multiutilities

Furthermore this stance by some businesses can be related to the fact that complying with SER regulation is increasingly being seen as vital by stakeholders. Again the abolition of the OFR legislation did not appear to win government much political support as it was largely rejected by some businesses, whereas it was intended to appease them. Some of the reasons it is surmised, could be that businesses had already begun to incorporate OFR's in their operations and some had already gone through the process of preparing for the statutory OFR, hence its removal not going down well with some. It could also be that as SER was becoming widespread and society was increasingly being made aware of the importance of SER regulation, some businesses were prepared to continue producing OFRs in a bid to please their stakeholders and the society in general; and in the process, improve their competitive strategy. Therefore, having presented evidence on the impact of CBI lobbying, the next section discusses the impact of FoE's lobbying on the EBR.

4.5.3 Lobbying and the Final Enacted EBR

Following the backlash at the removal of the OFR,⁹⁹ in January 2006, environmental campaign group Friends of the Earth (FOE) launched legal action against the Chancellor

⁹⁹ Please refer to the section 'Background of the OFR' for further information on the backlash.

and Trade Secretary Alan Johnson. Prior to the legal action, FoE on the 2nd December, 2005, sent a letter to the Treasury demanding that the OFR decision be reversed. Addressed to Chancellor Gordon Brown and DTI secretary Alan Johnson, the letter claimed that the move to abandon the OFR, which would require disclosures on environmental and social policies, was unlawful. FoE then gave the Chancellor a deadline of December 21 to justify his decision or face an application for judicial review. The Treasury's response however, implied that it would resist any challenge, stating, '*The government believes it has a strong case for removing the requirement for the OFR and is opposing the application for a judicial review...*'¹⁰⁰ Furthermore, in its conclusion, the response letter stated, '*In the light of all of the above, the decision to abolish the OFR will not be withdrawn and the steps taken consequent upon it will continue*'.¹⁰¹

Thereafter, following the refusal of the government to reverse its decision, the FoE, on the 11th January 2006, filed a Judicial Review¹⁰² in the administrative court. The FoE claimed that the Chancellor's decision to abolish the OFR had been unlawful, in particular it argued that there was: inadequate one-sided consultation on the decision to abolish the OFR, differences between the OFR and the BR,¹⁰³ absence of a mandatory reporting standard, alteration to environmental reporting and removal of the requirement to report on social and community issues. The FoE further stated in the judicial review document, that it is a responsible non-governmental organisation, and their claim and its resolution was in the public interest. A coalition of NGOs were also referred to in the document as providing witness evidence,¹⁰⁴ suggestive of FoE's mechanics of soliciting support in order to advance their environmentalist ideology. Subsequently the application for judicial review was withdrawn as the government agreed to review the

¹⁰⁰ Milner, M. (2006). Friends of the Earth seek U-turn on end of business review. *The Guardian (London)*, 12 January, p. 26.

¹⁰¹ HM Treasury (U.K), (2005), Meeting Notes Released to FoE as part of Pre-Action Response [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012].

¹⁰² Friends of the Earth (2005) Grounds for Judicial Review. [Online] Available from: http://www.foe.co.uk/sites/default/files/downloads/ofr_grounds.pdf [Accessed 18 May 2013]

¹⁰³ The Treasury had earlier stated that the principal requirements of the Business Review are in key respects identical or very similar to those of the OFR, and that the Business Review was an appropriate requirement for narrative reporting.

¹⁰⁴ Friends of the Earth (2005) [Online] Available from: http://www.foe.co.uk/resource/press_releases/friends_of_the_earth_force_02022006 [Accessed 12 May 2013]

abolition of the OFR, and the Treasury agreed to pay FoEs legal costs. Furthermore, it is of note that throughout the judicial review, and although notified, the CBI did not make any statements¹⁰⁵ in support of the government position, despite them being instrumental in the removal of the OFR.¹⁰⁶

FoE later stated,

'This reversal by the Chancellor is a major victory for the environment, democracy and those companies who genuinely want to reduce their impacts on people and the planet. It is a defeat for lobby groups like the CBI which have become far too used to dictating government policy regardless of the wider impacts on society. Gordon Brown's decision to abolish the OFR was also unlawful, and that is why the Government has backed down'.¹⁰⁷

The government then detailed a package of measures to be included in its overhaul of company law, with Alun Michaels announcing on the 1st February, 2006 that the Bill might be amended and government was now inviting comments to, '*... ensure effective forward looking narrative reporting by quoted companies, including, where appropriate, on social, community, employee and environmental matters*'.¹⁰⁸

Thus in agreeing to review its policies on narrative reporting, the government was bound by the judicial review, as the evidence FoE presented proved that due process was not followed before the announcement to abolish the OFR was made. Interestingly, in widening the consultation on narrative reporting, the government made no reference

¹⁰⁵ It is of note to mention that the CBI continued its propaganda for the free market ideology, using an attack mechanism to threaten the government, when in October 2006, a month before the CLR was given royal assent, the CBI leaders threatened to go over Margaret Hodge's head to Downing Street if they don't get what they want in an upcoming meeting with her, with regards to the new requirement for businesses to publish their dealings with suppliers. The government however refused to heed to the demands from businesses with MPs such as Colin Burgon, MP urging Tony Blair not to cave in to pressure from big business over planned new laws which will force large companies to reveal their social and environmental record (*Hansard* HC Deb. vol.450, col. 1516), 25 Oct 2006.). In this regard it is argued that on this occasion, the CBI seemed to have lost its influence on government with matters relating to SER.

¹⁰⁶ In January 2006, however, as part of the DEFRA release of environmental reporting guidelines code, Digby Jones, Director General of the CBI, expressed his support for the guidelines. Department for Environment, Food and Rural Affairs. (2006). *Environmental Key Performance Indicators Reporting Guidelines for UK Business*, archive.defra.gov.uk/environment/business/reporting/pdf/envkpi-guidelines.pdf [Accessed 5 May 2014]

¹⁰⁷ Friends of the Earth (2006) Friends of the Earth forces Chancellor to cave in on environmental reporting. [Online] Available from: <http://www.foe.co.uk/resource/press_releases/friends_of_the_earth_force_02022006> [Accessed 18 May 2011]

¹⁰⁸ *Hansard* HC Deb. vol. 442, col. 549W, 1 Feb 2006.

to the FoE judicial review, instead stating that the government ‘decided’ to widen the consultation. However, it is known that this widening of the consultation was facilitated by FoE’s judicial review, as the government agreed to the review. Therefore in omitting any reference to FoEs legal challenge, the government tries to avoid to be seen as reacting to pressure in dealing with narrative reporting issues. Furthermore, as noted by Sutton (1984), lobbying does not begin with the issuance of the exposure draft. Sutton cites an example by Horngren (1975) who notes that discussions between the Accounting Principles Board (APB) and the insurance industry took place for three years before the APB was ready to issue an exposure draft. This situation is therefore likened to the review of the OFR and narrative reporting, which began not with the exposure draft, but with the court proceedings started by the FoE.

Major EBR amendments

Further examples of evidence of lobbying, which resulted in major amendments to the Business Review are discussed next. Of interest to this chapter, are three amendments which changed the course of SER regulations. These are:

1. The inclusion of social and community issues in reporting requirements.
2. The inclusion of medium sized companies in reporting requirements.
3. The change of the BR from a voluntary to a statutory requirement.

The Inclusion of Social and Community Issues in the BR

In the CLR Bill as presented in the House of Lords on the 1st November 2005, Clause 390 of Part 15, Chapter 5, specified that the Business Review must include information on matters relating to the environment and the employees. However by the 3rd reading in the House of Lords, on the 10th May, 2006, the Bill¹⁰⁹ now specified in what was now Clause 396, Part 15, Chapter 5, that the Business Review must include information on matters not only relating to the environment and employees, but also on social and community issues. Hence what evidence can be found to explain the changes between the 1st and 3rd reading of the Bill?

¹⁰⁹ The Bill completed the Commons Committee stage on 20th July. The title of the Bill was changed from ‘Company Law Reform Bill’ to ‘Companies Bill’ during the committee stage in the House of Commons. The Companies House (2006) Available from: <http://www.companieshouse.gov.uk/infoAndGuide/compLawReform.shtml>> [Accessed 19 June 2013]

The first document that can be directly linked to this change is the argument that was produced in court by FoE in January 2006. Section 50 of the document states,

'Removal of requirement to report on social and community issues: There is no requirement in the Business Review to report on "social and community issues". The social and community effects of a major listed company may well be very significant. The explicit requirement to report on social and community issues would cover important issues such as human rights and labour rights issues. Its removal is significant... [and is] an important requirement that is not contained in the Business Review'.¹¹⁰

Furthermore, CORE issued a press statement stating,

'CORE and the Trade Justice Movement demanded improvements to company law so that Companies are legally required to report on their social and environmental impacts. Thanks to your campaigning, the directors of UK companies now have a duty...to consider the impacts of their business operations on the community and the environment. This is the first time that the words 'community' and 'environment' have been mentioned in UK company law in this way...'¹¹¹

Moreover, evidence on the influence of key persons on issues leading to the amendments in the business review is seen from debates made in the House of Lords and the House of Commons. For example,

'We recognise that the CORE coalition, the TUC and some other interest groups called for all or some of the OFR provisions to be reinstated or inserted into the business review. We have therefore elaborated on specific information relating to environmental, employee, social and community issues to be included for a better understanding of the company's business'.¹¹²

¹¹⁰ Friends of the Earth (2005) Grounds for Judicial Review [Online] Available from: http://www.foe.co.uk/sites/default/files/downloads/ofr_grounds.pdf [Accessed 18 May 2013]

¹¹¹ Corporate Responsibility Coalition (2006) Right Corporate Wrongs. Available from: http://corporate-responsibility.org/wp-content/uploads/2013/11/Companies_Bill_Supporter_Verdict_Long_Nov061.pdf. [Accessed 10 October 2012].

¹¹² *Hansard* HL Deb. vol. 681, col. 933, 10 May 2006.

Continuing, Lord Sainsbury stated that the government took careful account of the issues respondents to the recent consultation on narrative reporting pressed on. As a result of lobbying therefore, Clause 390 was removed and replaced with Clause 396 incorporating social and community issues.

The Inclusion of Medium sized Companies in Reporting Requirements.

As of 11th January 2006, medium sized companies were exempt from the strict requirements for narrative reporting. However by 10th May 2006, at the 3rd Reading of the CLR, Lord Sainsbury as the Parliamentary Under-Secretary of State at DTI, announced that,

'Amendment No. 194C would remove the exemption for medium-sized companies from having to disclose non-financial KPIs...We recognise that the CORE coalition, the TUC and some other interest groups called for all or some of the OFR provisions to be reinstated or inserted into the business review'.¹¹³

There is however very little evidence in the comments received during the consultation, calling for the requirement for medium sized companies to be included in the requirement to report on the BR. This suggests that respondents were less interested in this issue. Nevertheless evidence from CORE and TJM explicitly requested, *'Large and medium sized companies should have to report annually on their environmental and social impacts'*.¹¹⁴

Furthermore, Lord Sainsbury, in his statement at the 3rd reading, mentions CORE and the TUC, lending credence to the fact that these organisations were influential in their lobbying efforts. Another reason for extending the requirement to include medium-sized companies is that these businesses also have an impact on society and the environment and thus should be required to report as well. For example, Jim Cousins, MP¹¹⁵ stated that some companies whose environmental impact was high were exempt because they were either subsidiaries or medium-sized. Specifically, he cited the example of Asda, a subsidiary of Wal-Mart, which would be exempt from reporting social and

¹¹³ *Hansard* HL Deb. vol. 681, col. 933, 10 May 2006.

¹¹⁴ Corporate Responsibility Coalition (2006) About CORE Available from <<http://corporate-responsibility.org/about-core/history/>> [Accessed 3rd June 2013]

¹¹⁵ *Hansard* HC Deb. vol. 450, col. 885, 18 Oct 2006.

environmental matters if the requirement to report were not extended. Therefore it was of essence that both medium-sized and large businesses should be required to report on their non-financial matters. Consequently on the 18th October 2006, New Clause 1, which contained the extension of the category of companies to produce a business review from large quoted companies to include medium companies, was tabled by Jon Trickett, MP and signed by 51 other members of parliament, thus, extending the legal reporting requirement to include medium-sized businesses.

The Change of the BR from a Voluntary to a Statutory Requirement

The final amendment of particular interest to this chapter is the change of the BR from being voluntary to statutory. Again, majority of comments submitted on the BR consultations made no reference to this issue, with only a few demanding this change. For example,

'We recommend...that...UK Company Law should include a statutory duty on company directors to consider, report on and mitigate external impacts on the company's stakeholders...and... must take account of fostering relationships with suppliers, customers and others and; considering, measuring and mitigating the impact of its operations on the community and the environment'.¹¹⁶

Further evidence, however suggests that CORE was influential in its lobbying to make this change.¹¹⁷ They further issued a pamphlet at a parliamentary briefing for MPs, which expressed their support for a legal framework for narrative reporting and responsible corporate behaviour.¹¹⁸ Again in the House of Lords, debates indicated that proposals submitted requested the legal nature of the BR. For example, The Secretary of State for Trade and Industry (Mr. Alistair Darling) stated,

¹¹⁶ Action Aid response to the CLR White Paper March 2005.

¹¹⁷ Corporate Responsibility Coalition (2006) Right Corporate Wrongs [Online] Available from: <http://corporate-responsibility.org/wp-content/uploads/2013/11/Companies_Bill_Supporter_Verdict__Long_Nov061.pdf> [Accessed 3 June 2013]

¹¹⁸ Friends of the Earth (2006) Make UK business work for people and planet. [Online] Available from: <http://www.foe.co.uk/sites/default/files/downloads/make_uk_business_work_for.pdf> [Accessed 18 May 2013]

'Like every other hon. Member, I have had many letters and cards from constituents. I have also seen the letter written on behalf of all those groups that was sent to the Prime Minister today. They make three demands. The first is that companies be legally required to report on their social and environmental impacts'.¹¹⁹

Lord Judd also stated,

'As Friends of the Earth, ActionAid, Oxfam, Christian Aid, Amnesty International and others, with all their front-line expertise, have argued, there are altogether too many indications that the voluntary approach is not working. ...this has been acknowledged both by the World Bank and OECD'.¹²⁰

There was however opposition to the legal requirement of the BR. Lord Patten¹²¹ for example, dismissed the issue of regulation by stating that he does not believe that trying to characterise the activities of modern British business through regulation would work. Moreover, the CBI and Law Society¹²² protested against mandatory regulation suggesting that legislation will introduce a novel concept into English Company Law: interference by the judiciary in the exercise of business judgements by directors.¹²³ Comments submitted by the Institute of Directors further protested mandatory regulation,

'The IoD does not consider that legislation need go further than it now does in relation to social, community, employee and environmental matters. This is an area where engagement between directors and shareholders, and the growing awareness among directors of relevant issues in their decision-making and reporting, has already produced significant and improving results and should be allowed to develop'.¹²⁴

¹¹⁹ *Hansard* HC Deb. vol. 447, col. 126, 6 Jun 2006.

¹²⁰ *Hansard* HL Deb. vol. 677, col. 212, 11 Jan 2006.

¹²¹ *Hansard* HL Deb. vol. 677, col. 214, 11 Jan 2006.

¹²² The Law Society takes the view that creating greater clarity for the law reader would be better achieved by the publication of a non-statutory guide to directors' duties (James Brokenshire MP)

¹²³ *Hansard* HL Deb. vol. 677, col. 237, 11 Jan 2006.

¹²⁴ Institute of Directors (IoD) response to the CLR White Paper March 2005.

Nevertheless the majority of cases were made for the importance of mandatory reporting of SER. For example, Sarah McCarthy-Fry MP stated that SER is too important to be left to a voluntary code and regulation is needed, with transparency and accountability being quoted as the main reasons for requesting a mandatory nature for the EBR. Consequently Section 417 (contents of directors' report: business review); came into force on the 1st October 2007, legally requiring all quoted large and medium sized businesses to include the Enhanced Business Review in their Directors Report. In short, regulation was supplied in response to the demand from the public for the correction of inefficient or inequitable market practices (Pigou, 1932).

In summary, having reviewed the evidence highlighting the impact of lobbying on narrative reporting requirements, it is reasonable to state that lobbying played an important part in the removal of the OFR, and to amendments to the EBR. There is therefore a relationship between the evidence submitted to regulators and the final enacted legislation. The influence of groups such as CORE, TUC and TJM were acknowledged in parliament due to their 'persistence, commitment and assistance on these extremely important issues'.¹²⁵ Furthermore, the impact of path dependence is seen as the FoE group was able to use some sections of the old OFR, to justify their argument, finally leading to implemented changes in the EBR. Moreover, current practice at the time (for example, several instances of companies abusing the environment and maltreating employees) is what led the coalition of environmental groups, charities, and unions to support the campaign to seek to improve the Bill in an appropriate manner. This suggests that government is influenced by the most powerful groups and those who it feels are able to threaten their popularity.

The changes that occurred in SER regulations also show that to a large extent the CBI was influential in the removal of the OFR, whilst the FoE was instrumental in the implementation of the EBR. Hence, the political pressures which occurred during the changes in the OFR and the EBR, can be related to the interplay of power, the goals of power wielders and the productive exchange system (Zald, 1970, p. 223). In light of this argument that pressure group lobbying played a huge role in the changes made to SER regulation, the next section discusses the consultation responses, which this chapter argues, played a part as well.

¹²⁵ *Hansard* HL Deb. vol. 681, col. 934, 10 May 2006.

4.5.4 Consultation Responses

The Business Review, as with the CLR, also underwent two consultations in December 2005 and February 2006 respectively, as well as several amendments, before the final legislation came into force on the 1st November 2006. The comments received as result of the December and February consultations are summarised in Table 4.3.

Table 4.3 Comments Submitted on the Business Review

Government Proposal	Businesses	NGO's	Individuals	Trade associations /Chartered Bodies
Clarification of the Business Review - To ensure effective forward looking narrative reporting by quoted companies, including, where appropriate, on social, community, employee and environmental matters	1 - Support 3 - Oppose	3- Support	5 - Support	2 - Oppose

Source: Table constructed from responses submitted to the Department of Trade and Industry¹²⁶

Table 4.3 shows that the proposal on the issue of considerations which Ministers should take into account in deciding how, to frame amendments to ensure effective forward looking narrative reporting by quoted companies, including, where appropriate, on social, community, employee and environmental matters, fourteen comments were submitted, including one duplicate. Although the researcher expected the Business Review consultation to have received more than fourteen comments, the responsible department for holding these records (BIS), confirmed that there were no further available comments. Nevertheless, as stated by Lord Sainsbury, then Parliamentary Under-Secretary of State at DTI, the responses to the consultation were noted by government and may have contributed to the changes made in the CLR,

'We have developed what we believe to be a balanced and consistent package of proposals on narrative reporting, which reflects the outcome of our recent consultation and our discussions with interested parties'.¹²⁷

¹²⁶ Responses obtained under the Freedom of Information Act (2001) from the Department for Business, Innovation and Skills.

¹²⁷ *Hansard* HL Deb. vol.681, col. 934, 10 May 2006.

In short, although few, these responses submitted by interested parties, reflected the opinions of lobbyists. Having discussed the comments submitted on the EBR consultation, the next section discusses lobbying and strategic SER, a concept which this chapter suggests, is a significant reason for corporate lobbying and the attack on regulation by the CBI.

4.5.5 Lobbying and Strategic SER

Comments made by the CBI¹²⁸ and evidence from the FoE,¹²⁹ suggest that the CBI was instrumental in opposing SER regulation. Reasons for their opposition include the view that, as organisations pay taxes to government to ensure that society and the environment are not adversely affected by business activities, there is no need for regulation to be implemented or enforced; furthermore, SER legislation would constrain business activity. These reasons are supported by the London Stock Exchange (LSE) suggestions that the increased transparency requirements of the OFR opens main market companies to unfair competition by forcing them to expose their business strategies in ways that competitors off the main market are not required to.¹³⁰ Porter and Van der Linde (1995) also report that there is a lingering belief that regulations erode competitiveness.

Further evidence suggests that compliance with SER is on the rise (Deloitte and Touche, 2005; Hooghiemstra, 2000; KPMG, 2011). Therefore, if there is evidence to suggest that SER levels are increasing, yet at the same time businesses are lobbying to reduce or prevent regulation, what can be concluded to be driving this apparent contradiction? In trying to answer this question, the attitude of businesses is linked to

¹²⁸ Sources: Grant, P. (2004). Business groups say OFR goes too far. *AccountancyAge*, 13 May, [Online] Available from: <<http://www.accountancyage.com/aa/news/1774434/business-ofr-goes>> [Accessed 12 May 2014]; Elliott, L. and Seager, A. (2005). Financial: Brown pledges to cut red tape in drive to woo industry: Chancellor hopes to win back business community: Social and environmental audit to be scrapped. *The Guardian (London)*, 28 November, p. 22.

¹²⁹ Friends of the Earth (2005). Browns' big green failure. Available from <https://www.foe.co.uk/resource/press_releases/browns_big_green_failure_28112005> [Accessed 12 February 2014]; Friends of the Earth (2005) Hidden Voices. Available from http://www.foe.co.uk/sites/default/files/downloads/hidden_voices.pdf [Accessed 12 May 2011].

¹³⁰ HM Treasury (U.K), Meeting Notes Released to FoE as part of Pre-Action Response [Online], Available from: [Online] <http://www.hm-treasury.gov.uk/media/BB6/BA/eascstakeholdermeetingnotes020306.pdf> [Accessed 12 October 2012]

the increasing use of SER as a form of strategy¹³¹ by companies. As suggested by previous studies (see for example, Clulow et al., 2003; Falkenberg and Brunsæl, 2011; Vilanova et al., 2009), companies are increasingly using SER as a form of strategy. Elkington (1994) also, for example, describes how corporate lobbyists are fighting tooth-and-nail to sink proposals for carbon energy taxes and to push through deregulation, yet wonders why at the same time growing numbers of corporate presidents and CEOs declare themselves as “corporate environmentalists”. In addition, Hancher and Moran (1989) posit, ‘Time and time again, the corporate strategy of individual firms is a major determinant of the direction of the regulatory process’ (p.275). Therefore in opposing SER regulation which offers a level playing field¹³² companies do not want to be exposed, nor do they want regulation to level the ground, in order to prevent competitors from catching up and assuming their competitive advantageous position. As evidenced by a respondent,

‘...but companies...say, well if we do that [advocate for regulation] our competitors won’t do it and then we’ll be at a disadvantage. It’s a really serious issue. But companies would never say publicly, we want more regulation. They’ll never, ever say that’

Coordinator, NGO

Thus, new regulations may enable competitor businesses to catch up on the company’s current levels of reporting and lessen the perceived quality of their own reports. More so, it is also possible that companies negative attitude towards regulation is part of a strategy of trying to deflect any further regulation from being imposed on their operations (Deegan and Blomquist, 2006; Moon and Vogel, 2008). Regulation will make these businesses more susceptible to competition and cause them to lose their competitive advantage. Yet, the attitude of companies towards regulation reinforces the notion that businesses are not adequately punished for non-compliance with regulation,

¹³¹ Strategic SER has been described by (Porter and Kramer, 2006) as going beyond good corporate citizenship and reducing harmful value chain impacts to mounting a small number of initiatives whose social and business benefits are large and distinctive, and strengthen company competitiveness.

¹³² ‘Sometimes we need regulation in order to move forward and in particular to provide a level playing field so that those who want to do the right thing do not find themselves unable to compete with those who are prepared to sacrifice planet and people in the scramble for profits’ *Hansard* HC Deb. vol. 447, col. 188, 6 Jun 2006; ‘The whole point of this exercise [The drawing up of Company Law Review Bill] is to achieve a level playing field, with all companies operating on the same level and considering seriously their community and environmental responsibilities. That has to be done.’ *Hansard* HC Deb. vol. 450, col. 786, 17 Oct 2006.

and as such display an attitude indicating that SER regulation is not important. Their focus is rather on how to improve their competitive advantage through the use of SER, as non-compliance with SER could elicit retribution from the market. Indeed, Chapter 6 will establish that firms which display a negative attitude to regulation show a high strategic attitude to SER.

It is therefore suggested that some businesses, including those represented by the CBI, will lobby to reduce regulations in a bid to focus on enhancing their competitiveness in the SER arena. In discussing relationships further, it is determined that the lobbying process revolves around the issue of power as well as the associations between the lobbyists and the lobbied. In effect, the relationship between these groups contributed in informing their lobbying activities.

4.5.6 The Relationship between the Key Players

To examine the institutional context of lobbying on SER regulation, it is necessary to understand the relationship between the government and the pressure groups involved. As previously discussed at the beginning of the discussion section, the chapter identifies three groups, namely CBI, FoE, and government. Based on interview evidence, it can be concluded that there is a tension between these groups, which impacts on the power and influence exerted in the lobbying process. This tension is found primarily between NGOs and companies, with NGO respondents claiming that the CBI and businesses have a cosy relationship with the government, resulting in the NGO's views and comments being side-lined. For example,

'I think it becomes frustrating when you have a government that sort of "fetishises" the views of business if you like, and I think there is a real obsession at the moment in government, with the idea that if you were going to get growth we have to be proponents and being proponents means doing everything that the business lobby asks for'

Policy Officer, NGO

Furthermore, a press release issued by CORE during the CLR period states,

'Some big business interest groups lobbied against our call for widening the application of the reporting requirements to a much larger number of companies'

and for legal standards on how they should report on these issues. The Government sided with these groups on these matters...We hope that... the Chancellor understand[s] that big business is not the only stakeholder he has to represent. He cannot continue to sideline the environment just because the CBI has told him to'.¹³³

Thus this 'cosy relationship' the CBI is reported to have with the government is likened to Puxty's (1986) ideology that the social structure is a mere reflection of the power of large institutions, such that business regulations are moulded to business requests. Furthermore, the lobbying process has been claimed to be shadowy and transparency in lobbying is weak in many places (Henriques, 2007). Again, although lobbying is an essential process and is widespread in the U.K., it hasn't been formalised. The UK also does not have a list of registered lobbyists adding to the shroud of secrecy surrounding lobbying. Further evidence points to the tension between NGOs and the CBI. For example, during a BBC radio programme¹³⁴ on the 6th June 2006, the Aldersgate group, an NGO, was attacked by the CBI, who were not prepared to go along with a proper estimate of the issue about climate change and emissions. Furthermore, interview evidence highlights the frustration companies feel when having to deal with NGOs, indicating that more needs to be done to bridge the gap and tension between businesses and NGOs,

'I think sometimes the NGOs... are expecting too much...I think the NGOs have got to understand that if more businesses are going to pick this up without being regulated they've got to make it easier in terms of you know, getting them to understand that actually this stuff is vitally important to the future success of businesses. So I wouldn't always agree with NGOs just pushing, pushing, pushing for more regulation. You are more likely then to turn businesses off... businesses are more likely to say... 'well alright if that's regulation, I'll toe the line, but I'm not going to go any further', nobody wins that way'

Head of CSR, Gas, Water and Multiutilities

¹³³ Corporate Responsibility Coalition (2006) Right Corporate Wrongs. Available from: <http://corporate-responsibility.org/wp-content/uploads/2013/11/Companies_Bill_Supporter_Verdict_Long_Nov061.pdf>. [Accessed 10 October 2012].

¹³⁴ Today Programme (2006) BBC Radio 4, 6th June. Available from <http://www.bbc.co.uk/radio4/today/listenagain/listenagain_20060606.shtml> [Accessed 10 April 2014]

In light of the unfriendly nature of the relationship between NGOs and businesses, together with evidence suggesting that businesses in particular fail to adequately work with the actors of society in order to promote a healthy relationship (AccountAbility, 2005), it is therefore unsurprising that interested parties will seek to promote their private interest (Posner, 1974; Stenka and Taylor, 2010). It is also in this light that the political economy theory of regulation is played out.

In particular it is determined that the success of lobbying is sometimes positively related to the ability of the lobbyist to provide information to the government; results consistent with Hansen (2011). Moreover, the issue of conflict arising from the unfriendly relationship reveals that the more power a lobbyist wields, the more they are likely to influence the language of the final standards. Thus, any group that achieves some degree of influence over a policy has gained power¹³⁵ (Nagel, 1975, p.165). Furthermore, the influence exerted by FoE, TJM and CORE in supplying a substantial amount of evidence resulted in the successful review of narrative reporting and consequent implementation of the mandatory BR. As revealed by a respondent,

'Because when you're reviewing a consultation, putting my ASB hat on, as a recipient of all these consultation letters, what you're looking for are the new ideas, rather than the weight of opinion. And if nobody comes back saying that what you're proposing is unworkable or won't achieve these objectives, then you'll carry on and do what you said you were going to do'

Board Member, Accounting Standards Board

Although power and influence are conditional on the nature of the reporting issue (McLeay, 2000) and the distribution of power among factions, varies as a function of the particular accounting issue under consideration (Sutton, 1984), the findings further suggest that in the particular case of the implementation of the EBR, path dependence impacted on the effectiveness of FoE's lobbying, increasing FoE's influence over the government and helping to justify their arguments and advancing their cause.

¹³⁵ Power is the distinction between the possession of resources and the actual exercise of power and insistence on rigor (Nagel, 1975, p. 177).

4.6 Conclusions

This research contributes to Social and Environmental Reporting (SER) literature by examining the influence pressure groups exerted in the removal of the Operating and Financial Review (OFR) and framing of the Enhanced Business Review (EBR). In examining this impact of lobbying, the chapter refers to the political economy of accounting (Cooper and Sherer, 1984) and argues that the removal of the OFR and the implementation of the EBR resulted from conflicting political, social and economic motivations within society (Gray, Owen and Adams, 1996). Thus, the influence of lobbying activity to the changes and amendments of the OFR and the EBR is conclusive.

Through the use of a diverse range of sources, including media articles, parliamentary debates and interview evidence, it is argued that the process of regulatory changes resulted from the ideologies and mechanisms displayed by the groups. Hence evidence was presented which showed that the CBI was instrumental in attacking regulation and involved in the events leading up to the removal of the OFR. Furthermore, it is argued that the government's deregulation agenda in 2005 aligned with business interests, leading the Chancellor to announce the removal of the OFR without following proper procedures. In effect the ideologies and mechanisms of the government and the CBI, enabled the former to act in a manner intended to please the latter, as the CBI was looking to protect its free market ideology and the government looking to deregulate. However, NGOs, operating in the public interest, were able to force the government to review its SER regulatory policies, as the government was bound by the terms of the judicial review. This eventually resulted in medium and large sized companies to legally report on their SE activities.

This 'victory' was a result of a campaign led by NGOs over a number of years to get the government to get businesses to be more accountable to society. In addition, further evidence suggests that although labelled as the voice of business, the CBI is not representative of all firms, and hence cannot be solely viewed as responsible for business actions, nor can businesses be directly linked to the decisions taken by the CBI. However, this chapter is unable to completely rule out the possibility that the nature of the evidence submitted, or the lobbying processes, are the sole reason for the numerous amendments that took place in framing the EBR. Yet, several mentions in

parliament of evidence submitted by CORE and TJM are sufficient to infer that these specific groups made a significant contribution to the BR amendments. Indeed, the Financial Times reported that ‘business had been comprehensively outmanoeuvred by environmental and corporate responsibility campaigners, in a stunning lobbying victory’.¹³⁶ With such pressure arising from NGOs therefore, it is surmised that the government felt compelled to listen to the lobbyists concerns and address these concerns, highlighting the issue of power balance.

Furthermore, the concept of strategy and competitiveness was discussed, supported by evidence showing that the increase in lobbying against SER by the CBI, was accompanied by an increase in the levels of SER. The results further lend support to the political economy argument that organisations or groups protect their self-interest and will seek to deflect further regulatory burdens. Likewise, it is demonstrated that the regulatory capture theory is at play here, given the instances where using their influence and knowledge, the regulated capture the regulators.

An important issue, which emerged from our examination of the influence of lobbying, is the nature of the relationship between the CBI, NGOs and the government. Having determined that the influence or knowledge a group possesses, contributes to their ability to lobby, this chapter documents that the “cosy relationship” of the CBI with the government, contributed to the government’s removal of the OFR. Likewise, the information presented by the NGOs to the government, supported by compelling evidence detailing the futility of the voluntary nature of social and environmental reporting, as well as the judicial review, contributed to the successful review of the OFR and the final enacted statutory EBR.

In summary, the evidence presented shows path dependency at work. It is seen that the CBI lobbies to influence future legislation, but is ultimately unsuccessful as the FoE was able to invoke existing legislation to prevent any dilution of regulation. Thus the chapter contributes to literature by arguing that the biggest influence on future regulation is past regulation, making the task of the CBI difficult in terms of reversal, but at the same time creating a slow incrementalism of regulation, further falling short

¹³⁶ Eaglesham, J. (2006). Alarm bells ring too late for companies bill. [Online] Available from: <<http://www.ft.com/cms/s/0/12b53f7a-63c5-11db-bc82-0000779e2340.html>> [Accessed 17 April 2014]

of the expectations of the NGOs. Accordingly, the next empirical chapter, examines whether the consequences of the legislation that was apparently feared by the CBI, is founded; by examining the SER disclosures in firms annual reports.

Appendix B

Appendix B 1 Timeline of SER Regulations

In summarising the development of SER regulation, a timeline is shown next, including timelines of the OFR and EBR regulations.

Timeline development of the OFR

- **July 1993:** The ASB issues the non-mandatory statement, Operating and Financial Review, to build on the foundations of best practice whereby directors can discuss the main factors underlying the company's financial performance and position.
- **May 2001:** Company Law Review Steering Committee emphasises the need for companies to provide high quality information that will enable shareholders to hold directors to account.
- **July 2002:** Modernising Company Law; White paper. The Government welcomes many of the Company Law Review's recommendations.
- **January 2003:** OFR Statement Accounting Standards Board, the non-disclosure of commercially sensitive information, permitted in the 1993 statement, is no longer made apparent
- **June 2003:** Consultation document, OFR working group on materiality. Agrees with Company Law Review that directors may not be required to disclose certain material information if such disclosure would of itself result in material prejudice to the company's interests.
- **May 2004:** Department for Trade and Industry (DTI) and OFR Working Group publications. Draft regulations on the operating and financial review and directors' report: a consultative document (DTI) and Practical guidance for directors (OFR working group).
- **November 2004:** Reporting Exposure Draft issued. Accounting Standards Board, explicit that the OFR shall focus on matters that are relevant to the interests of investors.
- **January 2005.** Draft Statutory Instrument removal of the process review element from the auditor's role. Auditors are now required to check OFR contents for consistency with the accounts. Commencing date for the OFR is postponed to financial years beginning on or after 1 April 2005, from original date of 1 January 2005.
- **March 2005:** Final OFR Regulations passed into law.
- **May 2005:** Introduction of the Reporting Standard 1 by the ASB.
- **August 2005:** Consultation period between government and the ASB closes.
- **November 2005:** Government proposal to scrap OFR.
- **December 2005:** Regulations to repeal the requirement for the OFR laid.
- **January 2006:** Regulations to repeal OFR come into force.

Timeline Development of Enhanced Business Review

- **March 2005:** Legislation in force to require quoted companies to prepare an OFR and all other companies (except eligible small companies) to expand their Directors' Reports to include a Business Review.
- **May 2005:** the Accounting Standard Board (ASB) issued an accompanying Reporting Standard (RS1). Those companies complying with RS1 were presumed to have complied with the OFR Regulations.
- **November 2005:** The Chancellor announced Government's intention to scrap the requirement for quoted companies to prepare an OFR.
- **December 2005:** The DTI updates their guidance on the changes to the Directors' Report requirements in the Companies Act 1985.
- **January 2006:** The Companies Act 1985 (Operating and Financial Review) (Repeal Regulations) 2005 becomes effective thereby removing the requirement for quoted companies to produce an OFR.
- **January 2006:** The ASB converts RS1 into a Reporting Statement. This is a voluntary guidance for those companies producing an OFR.
- **February 2006:** Government invites comments on any considerations which ministers should take into account in deciding whether, and if so how, further to amend narrative reporting requirements.
- **March 2006:** Consultation between government and the ASB closes.
- **May 2006:** Government announces proposed amendments to the Business Review legislation.
- **November 2006:** The Companies Act 2006 is given royal assent. The changes to the Business Review requirements for quoted companies are finalised.
- **October 2007:** Enhanced Business Review introduced - Quoted companies are required to include in their Business Review 'the main trends and factors likely to affect the future development, performance and position of the company's business' and information on their employees and environmental, social and community issues.

Appendix B 2 Excerpts of Evidence of Corporate Lobbying

Report by Friends of the Earth: Hidden Voices (June 2005)

CBI concerns

The CBI was involved from the beginning in the consultation over the need to broaden company reporting. The Chair of the CBI's Small to Medium Enterprise (SME) Council was a member of the initial steering group for the project. The Company Secretary of the chemical company ICI also represented the CBI on the consultative committee. At the beginning of August 2004, as the consultation period for the OFR was drawing to a close, the CBI went public with its final rearguard lobbying action against the new element of company law. The CBI made clear that it was in favour of better company reporting but stated that it found fault with the detail. It wanted the measure delayed, and then phased in, and wanted protection for directors who made statements in the OFR that turned out to be inaccurate.

The comments of CBI Deputy Director-General John Cridland suggest that the OFR had come out of nowhere, leaving companies with no time to set up their reporting processes. He talked about companies "*not having enough time to make the changes work properly*" and the danger of losing the opportunity "*to achieve genuine and meaningful reporting.*" Yet the CBI has been involved in developing the OFR for no less than six years. If its members do not have enough time to achieve decent reporting, they should blame the CBI for failing to ensure that they are prepared. In October 2000 Prime Minister Tony Blair had issued a challenge to the top 350 UK companies (the FTSE 350) at the Green Alliance conference to voluntarily issue their own environment reports by the end of 2001. According to the Government's own figures, by December 2001 only 79 companies (23 per cent) were able to do so.

The Evidence Does Not Stand Up

The gap between the CBI rhetoric and hard evidence was illustrated in an extract taken from the UK House of Commons Environmental Audit Committee hearings on the 'International challenge of climate change: UK leadership in the G8 and EU' on 18th January 2005. The quotes are from Mr Collin Challen who is a member of the Environment Audit Committee and Sir Digby Jones representing the CBI.

Mr Challen (MP): *Which British companies have relocated abroad purely as a consequence of environmental pressures?*

Sir Digby Jones (CBI): *In terms of they have left somewhere where there is a strict environmental regime and cleared off to a place where they can pollute, I would say nil.*

The key question is: do the CBI's claims that environmental regulations are costing UK business some £4 billion annually actually stand up?

Appendix B 3 Process that led to the Repeal of the OFR

The Process that led to the repeal according to the HM Treasury is as follows:

- 1) In July 2005 officials at HM Treasury were asked to identify deregulatory opportunities.
- 2) In September 2005 a discussion note concerning OFRs was produced at HM Treasury for use at official level
- 3) On 11 October 2005 a submission on OFRs was made to the Chancellor of the Exchequer
- 4) On 11 November 2005 a further submission was made to the Chancellor
- 5) On 23 November 2005 a final submission was made to the Chancellor

The Chancellor thereafter spoke to ministerial colleagues as set out in this submission, using the draft letter annexed to the submission (the letter was not in fact sent) as a speaking note. “For the sake of completeness, I can advise you that the issue of OFRs was discussed with HM Treasury officials by third parties on the following occasions before the decision was made:

- (i) On 8 June 2005, at a meeting with Hermes
- (ii) On 12 August 2005, at a meeting with the ABI
- (iii) On 19 August 2005, at a meeting with the London Stock Exchange
- (iv) At the end of October/beginning of November 2005, in a telephone conversation with the CBI.

There is no contemporary written record of this conversation. We are instructed that it was a call at official level in which the CBI representative was informed that although no decision had been taken, an option being considered in the context of deregulatory possibilities was paring back the OFR. The CBI official was asked, hypothetically, how he thought the CBI might react to this. He indicated that the CBI would be strongly supportive.

- (v) On 8 November 2005, at a meeting with an informal advisory group

After the decision was made, there was contact with the CBI about the OFRs on the weekend of 26/27 November. The purpose was to give the CBI notice of what the Chancellor would be saying in his speech on 28 November (HM Treasury, 2006).

Appendix B 4 Correspondence between Mr. Brown and HM Treasury Prior to the Removal of the OFR

Directors' Reporting – Removing The Statutory Requirement To Produce An Operating And Financial Review

Note to Chancellor

23 November 2005

Issue:

Securing agreement from Ministers of deregulatory opportunity: removal of gold-plating from directors' reporting for quoted companies

Recommendation:

Note the attached letter to Alan Johnson, DTI, Margaret Beckett, DEFRA and John Hutton, DWP.

Timing: Urgent. Action required this week.

Background

1. Attached to this submission is a letter proposing to DTI, DEFRA and DWP Ministers that you announce in the pre-budget report the removal of the goldplating from directors' reporting requirements for quoted companies.
2. It is anticipated that a number of Ministers will have concerns about this proposal, given their departments' specific interests in the initiative. It is therefore suggested that you discuss this with them (a letter is attached as an aide memoire, and you may choose to send this later).
3. While Alan Johnson was not the Secretary of State for Trade and Industry when the OFR was introduced, he may raise concerns. The DTI has spent some years bringing the OFR to fruition and have put it at the heart of their corporate governance strategy. It is important that this proposal is positioned so that DTI, who are the lead agency, see this as a positive deregulatory opportunity, rather than as an implicit criticism of their policies. Margaret Beckett is likely to oppose the proposal, as DEFRA was very keen on more extensive disclosures and explicit reporting requirements for social and environmental issues, even though the Business Review requires the consideration of these issues and inclusion of them, where material. John Hutton (DWP) may be concerned about reducing mandatory reporting on social matters and employee

matters because of possible reactions from unions, however, his previous role focused on reducing regulatory burdens, thus he may support the initiative. Patricia Hewitt, Secretary of State for Health, may also show an interest in this proposal, as she championed this initiative while she was Secretary of State for Trade and Industry.

4. The following are the key points for discussion with your Ministerial colleagues:

- The Government supports improvements in forward-looking narrative reporting by companies to better inform shareholders. However, the statutory OFR is not the best way of achieving this
- Removing the requirement for quoted companies to produce OFRs signals the Government's commitment to removing unnecessary goldplating and to the Better Regulation Agenda
- Quoted companies will still be accountable to shareholders, and would need to produce a Business Review (i.e., the EU Directive minima).
- The Business Review has broadly similar content requirements (except social and environmental reporting) to the OFR but is less detailed and prescriptive and has a lower assurance standard.
- Important to signal to mainstream investors that the Government is committed to further improving narrative reporting and good corporate governance. The Government will keep a close eye on reporting practices to make sure companies are improving disclosures.
- The accounting standard for producing OFRs (reworked and substantially improved) will be retained as a voluntary standard.

DEFENSIVE LINES

For Secretary of State for Trade and Industry, Alan Johnson (current 'owner' of OFR policy) and possibly Secretary of State for Health, Patricia Hewitt (former champion of OFR reporting)

1. This will be seen as a U-turn on our commitment to improving corporate governance / reporting. A great deal has changed since the OFR was mandated. We are more focused on reducing the regulatory burden facing business, and there is a stronger presumption against 'gold-plating' EU Directives. We have heard the growing concern from business and are responding to this. There have also been significant advances in improving corporate reporting and governance:

- Listed companies will need to produce a Business Review (i.e., the EU Directive minima) and must apply the principles in the Combined Code.
- The ASB (Accounting Standards Board) has produced a rigorous new standard which reflects best practice for producing OFRs.

- The Company Law Reform Bill contains provisions for the FSA to make corporate governance rules.

- Companies and shareholders are increasingly aware of the importance of good corporate governance.

2. We will lose the strategic, forward-looking narrative which shareholders demand. The Business Review, which companies will have to produce, is in large part identical or similar to the OFR. While it is not principally focused on providing strategic narrative, companies will be required to describe the principal risks and uncertainties facing the business. This will need to include some consideration of the strategy of the company in identifying how it will manage these. (In addition, the Combined Code reinforces the importance of managing risk by recommending reviews of the effectiveness of risk management systems to safeguard shareholders' assets and the company's investments). Disclosures will also be partly driven by shareholder demand, and shareholders are increasingly vocal about their desire for this type of narrative.

3. Companies will only produce the bare minimum they are legally required to produce. The OFR will be retained as a voluntary standard, and we expect many companies will decide to comply with it. (The previous OFR was a voluntary standard and more than 60% of listed companies were producing an OFR or an OFR-type report). Many companies with strong interests in the environment and social development are also likely to produce these in response to shareholders and interest groups. Numbers of the larger quoted companies also have their securities traded on US exchanges. The overlap between US disclosures and OFR content will provide an incentive to produce an OFR.

For Secretary of State for Environment, Food and Rural Affairs, Margaret Beckett, (who has a strong commitment to enhancing social and environmental reporting) and Department for Work and Pensions Secretary, John Hutton.

4 Reducing mandatory reporting on social, environmental and employee issues will mean less of this information is disclosed. Probably, but the primary purpose of directors' reporting is to inform shareholders and the company about the company's position, performance and development. Complying with the EU Directive minimum (i.e., the Business Review) will still require analysis of information relating to environmental and employee matters, to the extent necessary to understand the company position, performance and development. Responsible companies will still disclose material information on social and environmental matters.

We would also expect many companies with strong interests in the environment and social development to choose to produce OFRs in response to demands from shareholders and interest groups.

Dear

Deregulating Directors' Reporting Requirements

As you know, I have been working with my officials to find ways of reducing regulatory burdens on business. The Company Law Reform Bill seeks to build on the significant improvements the Government has made to corporate governance and to improve the efficiency of the investment chain, through measured and proportionate responses. Following representations from interested parties, I have concluded that there is an opportunity to take this a step further by announcing in the PBR that the Government is, on reflection, removing the mandatory requirement for quoted companies to produce an Operating and Financial Review (OFR). This would represent a bold step and some would no doubt seek to portray it as a reversal. However, for these very reasons, it would send out the strongest signal that we are serious about the Better Regulation Agenda.

A great deal has changed since the OFR was mandated. In Government, we are focusing more resources on reducing the regulatory burden on business. In the business community the growing appreciation of forward-looking narrative reporting is tempered by growing concern about the burden of the OFR. We are also adopting a much stronger presumption against 'goldplating' EU Directives, as we did when we introduced the OFR.

This has prompted me to think further about directors' reporting requirements, and I am not convinced that a strong positive case exists for mandating the incremental requirements of the OFR over the newly introduced Business Review (which is in line with the requirements for director reporting in the EU Accounts Modernisation Directive). Whilst I believe we should continue to emphasise that reporting in this way remains best practice, removing the requirement for quoted companies to produce an OFR could reduce business costs by up to £33 million p.a. according to the DTI's Regulatory Impact Assessment (RIA). There would nonetheless be an appreciable improvement in narrative reporting, when compared to the pre-statutory OFR situation, because of the higher reporting requirements imposed through the EU Accounts Modernisation Directive (the Business Review). A substantial part of the benefits identified by the DTI as resulting from the OFR (including enhanced credibility and improved investor relations, lower average cost of capital and more liquid capital markets) would still be realised.

In terms of handling, I propose that we move quickly to remove the reporting requirement before companies are required to report against it from April 2006.

As I understand it, this will require changes to the Company Law Reform Bill, currently before Parliament, and Statutory Instrument 2005 No. 1011. I am also keen that we build on the good work of the Accounting Standards Board in developing the OFR standard RS1 and look at how best to retain it as a voluntary standard for use where shareholders and companies believe an OFR would add value.

I believe we should announce this initiative in the speech I am giving to the CBI on 28 November, and it would be helpful to have your views before then.

I am copying this letter to [...]

Appendix B 5 Differences between the OFR and the BR

The OFR	The Business Review
All companies (except those exempted under the small companies regime) required to include an OFR in their Directors' report.	Basic content requirements broadly similar to the original legislation as detailed on the left.
To cover: <ul style="list-style-type: none">(a) information about environmental matters (including the impact of the business of the company on the environment),(b) information about the company's employees, and(c) information about social and community issues.	To cover: <p>To the extent necessary for an understanding of the development, performance or position of the business of the company</p> <ul style="list-style-type: none">(a) analysis using financial key performance indicators, and(b) (b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.
The review must, in particular, include: <ul style="list-style-type: none">(a) information about the policies of the company and(b) information about the extent to which those policies have been successfully implemented.	The review must, where appropriate, include: <p>References to, and additional explanations of, amounts included in the annual accounts of the company.</p>
The review must also include: <ul style="list-style-type: none">(a) information about persons with whom the company has contractual or other arrangements which are essential to the business of the company; and(b) information about receipts from, and returns to, members of the company in respect of shares held by them.	
It must also contain: <p>Analysis using financial and, where appropriate, other key performance indicators, including information relating to environmental matters and employee matters.</p>	

Source: The Companies Act 1985.

In the case of the differences between both regulations, the main issues identified are the questions of Why, For Whom, And How. The differences are as outlined in Appendix B 5. There are however clear similarities between the Enhanced Business Review legislation and the Operating and Financial Review (OFR). Both require companies to report on their key performance indicators and principal risks, on the trends and factors likely to influence future performance, as well as on social, ethical and environmental issues. Unlike the OFR best practice guidance, the Enhanced Business Review legislation nevertheless omits two important elements - the requirement to explain the market context and the strategy of the company.

CHAPTER 5

Chapter 5 . The Impact of Regulation on SER

5.1 Introduction

This chapter explores the impact of the Enhanced Business Review (EBR) on Social and Environmental Reporting (SER) in three ways. First, it examines the annual reports of firms to analyse the effect the EBR had on the quantity and quality of SER. Second, it carries out a comparison between the SER of two different indices, firms listed on the FTSE4Good and those not listed on the FTSE4Good. Third, in line with previous research, the firm characteristics of size, profitability, industry sector, and presence of a CSR¹³⁷ committee will be statistically tested to analyse and determine the effects, if any, the characteristics had on the SER output.

The Enhanced Business Review (EBR) was implemented in 2007, following the removal of the 2005 Operating and Financial Review (OFR). However, as a result of the failure of the OFR, doubts were raised about the effectiveness of the implemented EBR, which was similar to the OFR. Accordingly, a number of reports were published which examined the annual reports of firms to measure their compliance with the EBR and measure its effectiveness (see for example, Accounting Standards Board, 2009; Deloitte, 2009; Henriques, 2010; Taurigana and Mangena, 2009).

Other studies also reviewed firms' SER in order to determine their motivations and drive for reporting (see for example, Aguilera et al., 2007; Grosser et al., 2008). However, in spite of the extensive evidence on firms' compliance with SER regulation and motivations for SER, far too little empirical research has examined the impact of the EBR on firms' SER through analysing its quantity and quality, prior to and after the implementation of the EBR. As it is important that the SER performance of firms is monitored, in order to evaluate their compliance with regulation, this chapter examines the annual reports of firms', pre and post EBR to determine the effectiveness of the EBR on firms SER. Examining the SER performance of firms is also carried out to explore the argument as articulated by the CBI, that should British firms be forced to go green, this would impact on firms' competitiveness as well as increase firms' costs. Thus, in

¹³⁷ The difference between CSR and SER is that CSR encompasses firms' social, environmental and economic impacts (The Department of Business, Innovation and Skills) whilst SER covers the social and environmental aspects of firms impacts. This study focuses on SER only, though references are sometimes made to the use of CSR in other studies.

examining the pre and post EBR periods, this chapter distinguishes between the voluntary and mandatory aspects of the EBR, a method in line with Gray et al., (1995a). Furthermore, in line with Raar (2002), this chapter examines the quantity and quality of both the voluntary and mandatory aspects of the EBR.

In order to explore the impact of regulation further, a comparison between two different indices, FTSE4Good¹³⁸ and the Non-FTSE4Good is carried out. Although, previous studies have examined for example, average performance, share value, and cumulative abnormal returns, of the FTSE4Good firms and compared it to firms on other indices (see Clacher and Hagendorff, 2012; Walmsley and Bond, 2003) or examined the ethical values of FTSE4Good, and compared it to other ethical indices such as the Dow Jones (see for example, Collison et al., 2008), no empirical study has systematically conducted a comparison of the SER levels (quantity and quality) between the FTSE4Good and the Non-FTSE4Good.

Previous literature is therefore lacking the empirical foundations examining a systematic comparison of the SER levels (quantity and quality) between the FTSE4Good and the Non-FTSE4Good. Therefore in plugging this gap and contributing to literature, this chapter is at the same time, able to test the impact of regulation through examining the annual reports of these separate indices. Comparing the SER of these two indices will again enable us to identify the differences and the extent to which these indices report. Thus, if the test results show a statistical difference between the two groups, particularly the FTSE4Good performing better than the Non-FTSE4Good, it will endorse the well-known concept that the FTSE4Good *differ* from all the other indices mainly due to their ‘commitment’ to social and environmental matters. On the other hand, if the results show that there is no significant statistical difference in reporting levels between the two groups, it will raise questions as to what the purpose of an investment firm is, for example, in choosing the ‘ethical’ FTSE4Good over the ‘non-ethical’ others, or indeed of government introducing the EBR (mandatory regulation) that did not impact reporting levels?

¹³⁸The FTSE4Good Index Series encompasses four tradable and five benchmark indices, representing Global, European, US, Japan (benchmark only) and UK markets. The FTSE4Good benchmark indices include all companies in the broad market index, or starting universe that meet the FTSE4Good criteria. Tradable indices cover the largest 50 or 100 companies in the benchmark index, as measured by their market capitalisation.

Lastly, in order to analyse the effects of firms' characteristics on their engagement with SER, a number of statistical tests are employed. This follows previous research (for example, Aupperle et al., 1985; Cobb et al., 2005; Cowen et al., 1987; Hackston and Milne, 1996; Roberts, 1992; Trotman and Bradley, 1981) which employ firm characteristics such as size, profitability, industry, and presence of a CSR committee to determine if these characteristics have an influence on the total output of SER. The quantitative analysis is further supported by a small number of interviews conducted with firms, NGOs and regulators. This is to analyse the perceptions of Government's relationship with firms in terms of SER consultation and to gauge firms' attitudes towards regulation. The chapter therefore contributes to literature by presenting findings which suggest that the EBR did have an impact on the quantity and quality of SER by firms, and that there is no significant difference in the SER performance between the FTSE4Good and the Non-FTSE4Good. Furthermore, the findings suggest that there is a positive relationship between the firm characteristics of size and presence of a CSR committee, and SER output. Overall, evidence is provided, which shows the effectiveness of SER regulation on firms' social and environmental disclosures, an area previously under researched.

The remainder of the chapter is structured as follows. In the next section, a review of the literature, together with the hypotheses generated, is presented. Next the data sources and research methods used in this study are discussed. Following the discussion of the research methods, the results together with a discussion of the results are presented. In the final section of the chapter, conclusions are drawn from the findings together with an introduction of the next empirical chapter.

5.2 Related Literature and Hypotheses

This section first examines the literature on the quantity and quality of SER. The literature on the impact of regulation is then discussed. Following this, the FTSE firms used in this chapter are presented. Finally, previous research on firms' characteristics and their impact on SER is discussed. This section also uses the existing evidence and research in each of these areas to build and state the hypotheses used in this chapter. In this chapter the stakeholder theory of the firm, as discussed in Chapter 2, section 2.3., is used as a framework as it encapsulates the issue of firms' reporting for stakeholders.

5.2.1 The Quantity and Quality of SER

Previous studies suggest that the quantity of SER has increased. Disasters such as oil spillages, climate changes and mostly concerns from the society regarding safety in the environment (Brown and Deegan, 1998; Gray et al., 1995a), has resulted in firms increasing their reports on their social and environmental actions. The increase in SER has also made necessary as a result of pressure from stakeholders as well as the need to conform to the norm whilst maintaining a competitive edge (Gray et al., 1995a; Owen, 2003; Williamson and Lynch-Wood, 2008). Additionally, (Hooghiemstra, 2000) suggests that increases in corporate social disclosure represent a strategic business response to alter the public's perception about the legitimacy of the organisation. Moreover, a KPMG (2011) report suggests that companies are increasingly realising that corporate responsibility reporting is about more than just being a good corporate citizen; it drives innovation and promotes learning, which helps companies grow their business and increase their organization's value. The results of this report further shows that ninety five percent of the 250 largest companies in the world (G250 companies) now report on their corporate responsibility (CR) activities, representing a jump of more than fourteen percent over their 2008 survey.

However, although empirical evidence suggests that the level of SER by firms is on the rise, its quality is not. Moerman and Van Der Laan (2005) for example, highlighted the issues that reflect the discretionary nature of the social reports of British American Tobacco (BAT). They suggest that reports are selective because only thirteen of the 180 countries that BAT operate in participated in the reporting process; and argue that 'the negative effects of the tobacco industry extend disproportionately to the unrepresented – "undeveloped nations".' The report therefore 'cannot be seen as complete and consequently a "true" representation of BAT's social interactions with the communities in which it operates' (p. 384). Gallhofer et al., (2000) further call for organisations to remind themselves of their broader purpose, and move beyond narrow economic objectives, as reporting tends to go little beyond a summarised account of the activities of a reporting entity in financial terms. Henriques (2010) survey of the annual reports of the FTSE100 firms, also suggests that detailed quantitative information was provided by only forty eight percent of firms and that there was almost no analysis of the sensitivity of the firm to climate change or the consequences of adaptation. Furthermore, the Environmental Agency's (2007) Review of Environmental Disclosures found that an increasing number of companies provided their environmental disclosure in the audited

sections of the annual report but that the levels of quantitative disclosure on environmental risks or opportunities were relatively low (Environment Agency, 2007, p. 4). In summary, as there is evidence to suggest that the quantity of SER is on the rise, but the quality is low, hence the impact of SER regulation not being strengthened, this assertion is explored by analysing the annual reports of firms for the pre and post Enhanced Business Review (EBR) period, that is, before and after the introduction of the EBR. Furthermore, research to date has focused more on analysing firms' SER behaviours; such as motivations for reporting (Porter and Kramer, 2006; Unerman & O'Dwyer, 2007), and the content of reports (Gray et al., 1995; Hackston and Milne, 1996; Campbell and Slack, 2008) but there are not enough studies on how regulation impacts SER. This chapter is therefore dealing with an area where more should be done.

5.2.2 The Impact of Regulation on SER

As previously discussed in Chapter 2, section, 2.4, previous studies indicate that there is an increase in SER as a result of regulation (see for example, Grosser et al., 2008; Owen et al., 2005; Mobus, 2005). On the other hand studies (see for example, Tauringana and Mangena, 2009; Henriques, 2010; Adams, 2004; Spence and Gray, 2007) dispute the notion that regulation has an impact on SER. Therefore, in light of the above argument on the effectiveness of regulation on SER, and given the limited research analysing the impact of the EBR on SER, this chapter examines whether the introduction of the EBR influenced the quantity and quality of firms SER as presented in annual reports. Hence the first hypotheses,

H1a. There is a significant increase in the quantity of firms SER following the year after the EBR was introduced.

H1b. There is a significant increase in the quality of firms SER following the year after the EBR was introduced.

In developing further hypotheses, the FTSE firms, used as the sample, are discussed next.

5.2.3 The FTSE Firms

This chapter further carries out a comparison between the FTSE4Good and Non-FTSE4Good to analyse to what extent firms belonging to the FTSE4Good and Non-

FTSE4Good firms report on their social and environmental issues. A brief outline of the FTSE4Good is discussed next, culminating in the hypotheses generated.

FTSE4Good Index

The FTSE4Good differ from all the other indices mainly due to their ‘commitment’ to social and environmental matters. FTSE4Good also meet the needs of socially responsible investors by appealing to a broad range of institutional and retail socially responsible investors who are looking to;

- Only invest in companies that demonstrate good standards in corporate responsibility
- Minimise the social, ethical and environmental risks within their portfolios
- Capitalise on the benefits of good corporate responsibility (e.g. eco-efficiencies, improved brand image etc.)
- Avoid investing in traditionally excluded Sustainable and Responsible Investment (SRI) sectors such as tobacco, defence and nuclear power and
- Actively encourage companies to be more responsible.

For UK companies to be selected for inclusion in the FTSE4GOOD Index Series, they must be in the FTSE All-Share Index or FTSE Developed Index and must meet certain criteria requirements in the following five areas;

1. Working towards environmental sustainability
2. Developing positive relationships with Stakeholders
3. Up-holding and supporting universal human rights
4. Ensuring good supply chain labour standards
5. Countering bribery

Therefore, in conforming to these values, member companies ensure that they follow set FTSE4Good rules and regulations contrary to which they risk being expelled from the Index. This attitude is unlike their counterparts who do not belong to a sustainability index, hence are under less pressure, but could nonetheless be deemed responsible. There is also evidence to suggest that there is an increase in investor awareness of firm social and environmental adherence (Hockerts and Moir, 2004; Kahlenborn, 2002;

O'Rourke, 2003). Consequently choosing the FTSE4GOOD Index Series as a sample could help determine the effectiveness of regulation, that is, if any group has to adhere to regulation, it would be the FTSE4Good, who are propagated as upholding corporate responsibility standards.

Previous empirical studies have also focused more on analysing the performance of firms listed on the FTSE100 and FTSE 350 as opposed to analysing the performance of firms listed on the FTSE4Good, whilst even less studies have carried out a comparison of the SER performance between firms listed on the FTSE4Good and the Non-FTSE4Good. Furthermore, the vast majority of studies which have carried out a comparison of ethical indices to non-ethical indices, have done so by either analysing the performance of investment funds or comparing the financial performances/profitability of these ethical indices. Curran and Moran (2007) for example, examined whether corporate financial performance is affected by public endorsement of environmental and social performance, with results showing that companies were not rewarded for being included in the index and they were not penalised for being deleted from it. Their results are supported by Clacher and Hagendorff (2012) who find no strong evidence that the announcement of inclusion in the FTSE4Good index creates value for firms. Again, Collison et al. (2008) examined the financial performance of the FTSE4Good indices with results suggesting that investors who invest in a portfolio of companies that satisfy FTSE4Good's corporate social responsibility criteria, do no worse than their counterparts who do not follow a socially responsible strategy when purchasing equities.

Following the above studies which investigate the financial performance of ethical indices and comparing it to non-ethical indices, this chapter explores an area where more needs to be done, that is, to compare the social and environmental performance of an ethical index to a non-ethical index. Therefore in following previous studies reporting that there is no statistically significant difference in the performance levels of the ethical index versus the non-ethical index, as well as the concept that the FTSE4Good *differ* from all the other indices mainly due to their 'commitment' to social and environmental matters, this chapter seeks to add to literature. Hence the next hypotheses:

H2a. The quantity of SER reporting is the same for the FTSE4Good, compared to the Non-FTSE4Good, both before and after the introduction of the EBR.

H2b. The quality of SER reporting is the same for the FTSE4Good, compared to the Non-FTSE4Good, both before and after the introduction of the EBR.

5.2.4 Firm Characteristics and SER

Size of firm

The size of the firm can be measured in different ways, including number of employees, market capitalisation and turnover (Cooke, 1989; Gray et al., 2001). The association of turnover as a measure of firm size and social and environmental disclosures is found to be consistent with previous studies of accounting disclosure (Gray et al., 2001; Hackston and Milne, 1996; Toms, 2002). The generalised concept is that the bigger a firm is in terms of its market capitalisation, the more it is prone to scrutiny. Lang and Lundholm (1996) argue that due to response to pressures exerted by their stakeholder or community, listed companies, especially the large ones, usually attract high analysts following. KPMG's (2011) international survey of CSR also reinforces the widely-held belief that bigger companies are better at CR reporting. Their findings suggest that companies with revenues of more than US\$50 billion were twice as likely as those with revenues under US\$1 billion to report on their CR activities.

The impact of firm size on SER involvement is also related to the issue of access to resource (Brammer and Millington, 2006). Larger firms are associated with greater resource-slack, and this was found to significantly affect their SER commitment (Johnson and Greening, 1999). Larger organizations may also have more evolved administrative processes (Donaldson, 2001) and perceive and deal with the external environment differently, given their business exposure (Miles, 1987). Ljubojevic et al. (2012) further report that large companies are more efficient in SER activities and generate more positive responses in relation to small companies. In this way a higher level of competitiveness is achieved. This is the result of both the size and the quality of the Board of Directors where big companies again have a great advantage. Further evidence from previous studies support the positive relationship between firm size and level of disclosure (see for example, Alnajjar, 2000; Hackston and Milne, 1996; Trotman and Bradley, 1981).

Not all studies investigating the link between size and SER however support this positive relationship. Cowen et al. (1987), for example find that corporate size is

negatively correlated with total disclosure. Furthermore, Bowen (1999) notes that organizational size is an unsatisfactory measure of organizational visibility because it captures much more than an organization's visibility. Nevertheless, the number of employees is for example, consistent with the Enhanced Business Review (EBR) requirement, with firms being asked specifically to report on their employees. Gray et al. (2001) therefore argue that there is a plausible hypothesis that the number of employees will be linked to the importance of those employees both *in* and as a *subject* of employment-related disclosure, as more recent research has suggested that employees are the corporation's principal target in environmental and community disclosure.

Using sampling and analytical methods similar to other studies, this chapter therefore re-examines the impact of firm size on SER practices during the EBR period, using two different proxies. First size is defined as market capitalisation. Market capitalisation is a figure determined externally and is a reflection of market perception. It is related to shareholders future performance expectations. Second size is defined as number of employees. Based on prior evidence, a positive relationship is expected between firm size and social and environmental disclosure. Therefore;

H3a. The size of a firm in terms of market capitalisation has a positive correlation with the quantity and quality of SER.

H3b. The size of a firm in terms of number of employees has a positive correlation with the quantity and quality of SER.

Profitability - Return on Equity (ROE)

The concept that companies with higher levels of Return on Equity (ROE) have higher levels of compliance has also been widely researched in the literature. For example, Herremans et al., (1993) study, finds that more profitable firms are likely to be more socially responsible, and consequently are likely to exhibit steadier performance. These results are along the lines of Roberts (1992) whose studies indicate that corporations exhibiting relatively strong economic performance in prior periods, as measured by growth in return on equity, are more likely to have high current levels of social disclosure. Furthermore, McGuire et al., (1988) argue that firms with higher cash flows can better respond to a wider set of stakeholder pressures, through discretionary activities such as CSR initiatives, stating that 'Firms with high performance and low risk

may be better able to afford to act in a socially responsible manner' (p. 869). McGuire et al., (1988) and Roberts (1992) studies are consistent with Ullmann's (1985) notion that acceptable levels of economic performance are necessary before firm resources will be devoted to meeting social demands.

On the other hand, Alnajjar (2000) finds that ROE is negatively associated with SER. His findings fail to support the hypothesis that corporate SER is a function of firms' profits. Alnajjar however reports that one explanation for his observed negative relation might result from the possibility that firms that are less profitable may include more SER in an attempt to improve their public image. Other studies discover similar results to Alnajjar's (see for example, Patten, 1992; Richardson and Welker, 2001). Moreover, Cowen et al., (1987), find that corporate profitability is an insignificant factor influencing social disclosure. Alnajjar (2000) however, suggests that Cowen et al.'s (1987) studies are inconsistent as they did not investigate the effects of the explanatory variables on each type of disclosure within each of their seven major areas of disclosure. More recently, El Mosaid and Boutti's (2012) study again suggests no relation statistically significant between performance indices (Return on Assets, Return on Equity) and Corporate Social Responsibility Disclosure index. In this regard, given the mixed results on the relationship between ROE and SER as reported in previous research, and given that profitability may be a potentially significant variable in explaining SER, it is important to test the correlation between ROE and SER in this study. Therefore the next hypotheses are:

H4a. The profitability of a firm is positively related to the quantity of social and environmental reports in the annual reports.

H4b. The profitability of a firm is positively related to the quality of social and environmental reports in the annual reports.

Industry Category

The relationship between the industry a firm belongs to and its compliance with SER has been widely researched. For example, Roberts (1992) reports that, corporations in high profile industries¹³⁹ are expected to have higher levels of social responsibility

¹³⁹ This chapter categorises firms into high and low profile firms. High profile firms include firms such as Chemicals, Energy, Mining, Oil and Gas, Pharmaceuticals and Tobacco. They are reported as operating in

disclosures. His results indicate that industry category has the expected positive relationship to social disclosure. Of the seven industries included in the sample used in his study, the automobile, airline, and oil industries have the highest levels of consumer visibility, a high level of political risk, and concentrated, intense competition. Patten (1992) also documents that social disclosure is greater in highly visible and politically sensitive industries. Furthermore, Deegan and Gordon (1996) find an interaction effect between firm size and industry, such that the size effect is particularly pronounced in sensitive industries. Kolk (2003) also stated that industries differ in their tendency to engage in CSR initiatives. Moreover, KPMG (2011) report that those industry sectors that have the greatest influence over society and the environment (such as certain sectors of the energy and natural resources industry) show a higher commitment to reporting than other sectors that may be seen as wielding less influence.

Alnajjar (2000) results however do not support the positive relationship between industry group and SER. He suggests that the industry a firm belongs to, has no significant influence on total disclosure. Similarly, Cowen et al., (1987) argues that disclosure types are not a function of whether an industry is consumer oriented or is a “high-profile” environmental impact industry. Moreover, Herremans et al., (1993) found evidence suggesting misleading and or mixed results about the impact of industry category on SER. Therefore, following previous literature on the relationship between industry category and SER, the following hypothesis is drawn:

H5: There is no distinction between the SER performance of high profile industries and low profile industries in terms of the quantity and quality of SER.

CSR Committee or Department

Firms have increasingly begun to set up special CSR committees and or CSR Departments in a bid to show their level of commitment to SER. Social and Environmental reporting issues are now discussed at board meetings. This chapter argues that the presence of a CSR committee portrays to a certain extent, the lengths to

risky and controversial environments, and are under much scrutiny, hence expected to produce a high level of disclosure. They have high political risk and /or high competition (Roberts, 1992). Firms belonging to industries such as Real Estate and Retail on the other hand, are deemed ‘safe’ and are generally not expected to disclose to a high standard.

which a firm is prepared to invest in SER. Furthermore, when a firm invests in SER activities, it uses its resources and capabilities, which can be interpreted as a strategic move to achieve competitive advantage; thereby inevitably showing how important SER is to firms operations.

Few studies have analysed the impact of corporate social responsibility committees on SER, though it is an important aspect in measuring firm's attitudes to SER. Cowen et al., (1987) were one of the first to use this characteristic. In examining whether the presence of a social responsibility committee (ascertained through the annual reports of the corporations studied) impacts on corporate responsibility disclosure, Cowen et al., find that the disclosure of human resources information appears to be related to the presence of a corporate social responsibility committee, and suggest that such disclosures, which include employee safety, health and training, may be a major concern of social responsibility committees. Roberts (1992) also find that corporations confronted with a high level of political exposure are more likely to disclose social responsibility activities, suggesting that social responsibility disclosures and political action committee contributions may be aspects of an overall corporate strategy for managing government stakeholders.

Aupperle et al., (1985), however question the impact of a corporate social responsibility committee on CSR. They conclude that firms with a corporate social responsibility committee on their boards did not differ in profitability from other firms. Thus following the above evidence found in the literature the next hypothesis examines the relationship between the presence of a CSR committee and firms' engagement with SER.

- 6) There is a positive correlation between firms with a CSR committee and the quantity and quality of SER.

Having discussed previous studies on firms' characteristics on SER, the next section, Methods, discusses amongst others, the data sources utilised in this chapter together with how the quantity and quality of firms SER is measured.

5.3 Methodology

5.3.1 Sample and Data Collection

The FTSE350 firms were used as the sample for this study, in line with previous studies (see for example, Abraham and Cox, 2007; Campbell et al., 2003; Cumming et al., 2005; Owen et al., 2005; Page, 2009; Walmsley and Bond, 2003) and reports (Department for Business Innovation and Skills, 2013; PricewaterhouseCoopers, 2009). The FTSE350 was also selected as a sample, as the index represents the UKs largest firms, offer a wide range of industries and have the experience and resources to engage in SER. Furthermore, as this index consists of some of the UKs largest firms, they are more liable to complying with regulation.

Consistent with the majority of previous studies investigating firms' behaviour towards social and environmental reporting (SER), (see for example, Deegan and Rankin, 1996; Gray et al., 1995b; Hines, 1988; Neimark, 1992), this study uses annual reports. Although the sole use of the annual report has been criticised for its potential to show an incomplete picture of reporting (Unerman, 2000), this study nevertheless focuses on the information provided in firms' annual reports. The use of annual reports in this study is appropriate, as the Enhanced Business Review states that firms' social and environmental issues should be included within the Directors Report¹⁴⁰ as contained in a firm's annual report. Annual reports are also a useful indicator of corporate priorities as it provides voluntary as well as mandatory information (Gray et al., 2001). Thus, annual reports are used as a source of data collection with reports collected from firms' websites. As the EBR became effective in October, 2007, for firms whose year end is in December, the 2006 report was used to measure the 'pre EBR' period, with the 2008 annual report used to measure the 'post EBR' period. Likewise for firms whose year-end is in March, April or any month before October, the 2007 report was used to measure the 'pre EBR' period, with the 2009 annual report used to measure the 'post EBR' period.

¹⁴⁰ In line with (Bubna-Litic, 2008; Day and Woodward, 2004), only the directors reports were used for the analysis except where specific reference was made within the report to the availability of SER information in another section/ part of the Annual report. In this chapter, all firms 'directors report' as well as the corporate governance sections, directors remuneration report, chairman's statement, corporate social responsibility section, operating and financial review were all selected for inclusion in the SER performance analysis.

Further, data for firms' characteristics are collected as follows. (1) Size was collected based on number of employees and market capitalisation, obtained from *Datastream*¹⁴¹. (2) Return on Equity (ROE) was collected from *Datastream* with INDUSTRY SECTOR collected from the London Stock Exchange Group. (3) The presence of a CSR committee was retrieved from firms' annual reports, in line with Cowen et al., (2007), for the pre and post EBR periods. Thus in examining annual reports for evidence of CSR committee or department, words and phrases such as Corporate responsibility committee, CSR committee, Environmental and Corporate Social Responsibility Committee, Environment, Safety and Sustainable Development Committee, Safety and Environment Committee, Social committee, Sustainability committee, and Sustainability Governance Committee, were searched for.

5.3.2 Firm Selection

The first step in selecting eligible firms was to eliminate all FTSE350 firms that were not in operation in either 2007 and 2008, i.e. 2007 being the year in which the EBR became mandatory (October 2007) and 2008 being the year after the EBR became mandatory. In so doing this chapter is able to distinguish between voluntary reporting (pre EBR) and mandatory (post EBR) reporting. As noted by Gray et al., (2001), most studies have failed to distinguish between mandatory (meaning that required by law or code of practice) and voluntary disclosures. The patterns of mandatory and voluntary disclosure however differ (Gray et al., 1995b; Guthrie, 1990). Consequently, having eliminated some firms, the sample was reduced from 350 to 299 firms. Furthermore, all firms belonging to the financial and utilities industry were removed. The Financial industry is known to be heavily regulated and is not a good match for comparison. Equally the Utilities industry is also heavily regulated and thus not included. This resulted in 231 firms remaining. These firms were then split into FTSE4Good and Non-FTSE4Good firms to enable the comparison of the SER performance of these two groups. Finally, all FTSE4Good firms which were not listed on the FTSE4Good Index, in both 2007 and 2008 were removed bringing the selected sample down to 106 FTSE4Good firms and 98 Non-FTSE4Good firms.

¹⁴¹ Where the data was not available from *Datastream*, this was collected from the firm's annual report.

5.3.3 Matching

The procedure to match FTSE4Good firms to Non-FTSE4Good firms is based on the traditional method of firm selection, i.e. industry and market capitalisation (Deegan and Rankin, 1996; Ritter, 1991). Firms were grouped according to the Industry Classification Benchmark code (ICB code)¹⁴². The use of the ICB codes to allocate firms into industries is in line with other studies, (see for example, Knox et al., 2005; Yekini and Jallow, 2012). Therefore, all firms listed as FTSE4Good were grouped with Non-FTSE4Good firms belonging to the same industry sector. As expected some industries are represented more than others in the FTSE350.

The matching was conducted as follows. FTSE4Good firms were selected in reverse order of market capitalisation¹⁴³ (starting with the lowest market capitalisation), and matched to a comparable Non-FTSE4Good firm within its industry sector. Johnson and Greening (1999) and Ljubojevic et al., (2012) suggest that larger firms produce on average more SER than smaller firms. Therefore, using this method ensures that smaller firms are part of the sample and will provide evidence of the SER practices of smaller FTSE350 firms. Furthermore, comparability in terms of market capitalisation is defined as a 3 year average market capitalisation of between 70% and 130% of the FTSE4Good firm (Barber and Lyon, 1997). If a match could not be established, the FTSE4Good firm was dropped from the sample and the next suitable firm selected.

5.3.4 Measurement of Variables

In discussing how the quantity and quality of data for SER was measured, this chapter first explains the categories of SER, seen next.

Categories of SER

The requirements of the Enhanced Business Review (EBR) of the Companies Act 2006 Section 417(5), states that all quoted large and medium sized companies should include information on the environment, employees, social and community in their annual reports. Furthermore, Campbell and Slack (2008) suggest that the usual contents of SER

¹⁴² Industry Classification Benchmark Available from: <<http://www.icbenchmark.com/>>. [Accessed 10 March 2013]. Further explanation of ICB industry codes is seen in the Section ‘Measuring firms characteristics’.

¹⁴³ The market capitalisation of a firm, which is used as a measure of firm size, is defined as the market price per share times the number of shares outstanding.

should include information on human resources, communities, environmental resource consumption and environmental impact (p. 3). Additionally, Gray et al., (1995a) summarised social disclosures into four broad categories; employment, environment, community and customers. Therefore, in line with the Enhanced Business Review (EBR) requirements, the Accounting Standard Board (ASB) Reporting Standard (RS1) and following Gray et al. (1995a) and Campbell and Slack (2008), the four broad categories are extended to include relevant social and environmental issues disclosed by firms. This is presented in Table 5.1.

Table 5.1 Social and Environmental Disclosure Data

Environment	Community	Consumer	Workplace/Employee
<ul style="list-style-type: none"> • Environmental Policy • Environmental Audit • Emissions, spills and waste • Environmental Financially-related data 	<ul style="list-style-type: none"> • Community • Charity 	<ul style="list-style-type: none"> • Customer • Products • Suppliers 	<ul style="list-style-type: none"> • Disabled Employment • Health and Safety • Employee Data • Equal Opportunities

Source: Gray et al., (1995a).

Table 5.1¹⁴⁴ highlights the categories of SER and some of the various requirements reported under each of these categories. It is further noted that firms, in reporting social and environmental issues, do not have to individually list all the information and rather list only the issues relating to what is relevant or pertains to their operations. For example, a firm operating in the Finance sector, such as a banking institution need not highlight or report their commitment to environmental pollution or emissions, spills and waste as these issues are not a direct impact as a result of their operations. Instead, they will be expected to report more on issues such as community involvement and employee relations. Furthermore, the ASB Reporting Statement 1 states that it is for directors to consider how best to use the framework to structure the OFR (comparable to the EBR) and the precise content, including the level of detail to be disclosed, relating to the key elements, given the particular circumstances of the entity. These circumstances may include:

- 1) The industry or industries in which it operates;
- 2) The range of products, services or processes it offers;
- 3) The number of markets it serves.

¹⁴⁴ A more detailed list which includes the 40 index items measured in this chapter is presented in Appendix B, 1.

Quantity of SER data

Content analysis is used to collect social and environmental information from annual reports. Content analysis is defined as: ‘a research technique for making replicable and valid inference from data to their context’ (Krippendorff, 1980, p. 21). Furthermore, the management of measuring the quantity of SER was assisted by entering all annual reports into NVivo, a software analytical tool. Once uploaded, all social and environmental information were retrieved from these annual reports according to the specified themes (Table 5.1). These SER sections were then downloaded, and re-read. Krippendorff (2013) states that in order to read and interpret texts, coders’ need a level of familiarity with what they are looking for and this usually cannot be made explicit by any instruction¹⁴⁵. The reading of sections was then followed by counting each retrieved sentence or paragraph and then aggregating the score for each firm for the pre and post EBR periods. Thereafter, coding each firm’s SER details to the dimensions of the quality 3 scale-Likert (Appendix C, 2), was done. This is discussed next.

Quality of SER data

To further determine the effectiveness of the EBR, and in line with previous research (Gray et al., 2001; Toms, 2002; Wiseman, 1982), the quality of the disclosures over the pre and post EBR period was examined. Freedman and Stagliano (1992, p.115; 1995, p.168) suggest that assessment of quality, is relevant because content analysis focuses on what is included in the theme, rather than how much is said. Therefore, in the prior step, once the total number of sentences for each firm on their social and environmental issues was obtained, each of these sentences was then coded for quality using the coding scheme developed (Appendix C, 2 – rating scale); in other words, the use of quantitative scales being derived to permit further analysis.

Furthermore, it was necessary to sometimes refer to paragraphs, a method in line with Ingram and Frazier (1980). This was in order to get a more meaningful observation or understanding of the issue at stake and to further test the quality of the reporting issue. The paragraph method is more appropriate than word count for drawing inferences from narrative statements, as meaning is commonly established with paragraphs rather than

¹⁴⁵ After each section was re-read, and it was found that NVivo was unable to pick up a complete sentence or paragraph, the respective annual report was referred to, in order to ascertain the overall meaning of the sentence or paragraph.

through the reporting of a word or sentence (Guthrie and Abeysekera, 2006). Krippendorff (2013) also states that the best context analyses define their context units as large as is meaningful (adding to their validity) and as small as is feasible (adding to their reliability). Sometimes an analyst might need to examine larger context units, such as a paragraph (p. 102). Thus, looking for a characterisation of a concept within a context no larger than a paragraph, is, therefore considered to be more reliable and efficient.

Following (Wiseman, 1982), as well as the Accounting Standards Board's (ASB) framework for *best practice* (effectiveness, impact and quantifiable information), a 3 point Likert scale was therefore used to assess the quality score of each sentence or paragraph.¹⁴⁶ Robertson & Nicholson (1996) and Cormier et al., (2005) also suggested a 3-point scale system, with Cormier et al., (2005) using ratings based on a score of one to three: *three* for items described in quantitative terms, *two* when an item is described in specific terms and *one* for an item discussed in general terms. Also, quantified disclosures are more likely to represent actual activities, and represent the important and distinguishing differences between competitors (Toms, 2002, p. 270). Thereafter, the quality score for every sentence or paragraph in each firms report was aggregated to compute a final score for each firm.

Voluntary and Mandatory requirements

Further to measuring the quantity and quality of SER, this chapter also distinguishes between the regulatory requirements during the pre and post EBR period. Hence, as shown in Table 5.2, for the pre EBR period, regulations pertain to the Companies Act 1985 (CA 1985), whilst the post EBR period pertains to the Companies Act 2006 (CA 2006).

¹⁴⁶ Appendix C, 2 shows the rating scale applied in this chapter, together with examples of statements scored.

Table 5.2 Voluntary and Mandatory SER Requirements

	Voluntary	Mandatory
Pre EBR – 2006/2007	Customers/ Products Community	Environmental matters Employees
Post EBR – 2008/2009		Environmental matters Employees Customers / Products Community

Source: Compiled from Companies Act 1985 and 2006

Table 5.2 shows the classification as guided by the requirements listed in the Companies Act 1985 and 2006 (Enhanced Business Review Section). The requirements are coded into 2 separate categories. The first category is ‘Voluntary’ (Pre EBR) which means that quoted firms which included community and customer/products issues in their annual reports were not required to do so by law. The second category ‘Mandatory’ – Pre EBR (CA 1985) means that quoted firms were required by law to report on their employees and environmental matters. The Post EBR (CA 2006) however meant that as well as issues relating to Environmental matters and employees, firms were required to report on issues relating to customers and products and the community.

Reliability

It should be noted that this method of scoring is an assessment of reporting and not of the firms’ actual social and environmental performance; hence to determine if the sentence or paragraph had been correctly coded and to increase the reliability, the scoring process was independently assessed by the main researcher and one other coder. Any disagreements were then examined and resolved by carefully re-examining the disclosure in question (Wiseman, 1982). Consequently, after three rounds of coding, Krippendorff’s alpha was calculated for the main themes (Pre EBR) of Environment, Employee, Consumer /Products and Community as = .723, .612, .686 and .897 respectively and for the main themes (Post EBR) of Environment, Employee, Consumer /Products and Community as = .788, .642, .684 and .885 respectively. However, in spite of our efforts to ensure coding reliability, there remains an amount of subjectivity in the determination and undertaking of coding practices in content analysis research, as noted by Deegan and Rankin (1996), Guthrie and Abeysekera (2006) and Raar (2002).

Firm characteristics

As discussed earlier in section 5.2.4, the firm characteristics of size, profitability, industry, and presence of a CSR committee are measured for statistical analysis. These firm characteristics are collected from different sources. The SIZE is measured using market capitalisation and number of employees, whilst ROE is calculated as the firms' 3 year average. The presence of a CSR committee is coded on if a firm had a separate CSR committee or CSR department on the board, pre and post EBR. Firms which report on the CSR committee are given a score of 1, whilst firms which do not report on the committee are given a score of 0. Finally INDUSTRY is based on the FTSE's Industry Classification Benchmark¹⁴⁷ (ICB). In order to refine the data, industry sectors were selected, based on ICBs 3 digit code. The final industry and sectors used in this chapter are seen in Table 5.3 together with the ICB sector classification.

¹⁴⁷ FTSE Industry Classification Benchmark (2012). Available from: <<http://www.ftse.co.uk/Indices/Industry%20Classification%20Benchmark/index.jsp>> [Accessed 12 January 2010].

Table 5.3 Classification of Industry Sectors and Sector Distribution

Category Number	Industry	Sector	Frequency	%
0001	Oil & Gas	Oil and Gas Producers.	2	2.4
1000	Basic Materials	Chemicals	2	2.4
		Mining	6	7.3
2000	Industrials	Construction and Materials,	2	2.4
		General Industrials	2	2.4
		Electronic & Electrical Equipment	2	2.4
		Industrial Engineering	4	4.9
		Support Services	22	26.8
3000	Consumer Goods	Household Goods and Home Construction	4	4.9
		Personal Goods	2	2.4
5000	Consumer Services	Food and Drug Retailers,	2	2.4,
		General Retailers,	6	7.3,
		Media,	4	4.9
		Travel and Leisure.	16	19.5
9000	Technology	Software and Computer Services,	4	4.9
		Technology Hardware & Equipment.	2	2.4%).
Total			82	100

Source: Industry Classification Benchmark code

Table 5.3 shows that the total number of firms sampled are eighty two. As previously discussed in the ‘Matching’ section, a number of industries were omitted due to a lack of appropriate matches, including the removal of firms belonging to the Financials and Utilities Industries. Table 5.3 further shows that the final industry sectors sampled were sixteen. The sector with the highest percentage of firms is the Support Services (26.8%), followed by Travel and Leisure (19.5%).

5.3.5 Data Analysis

The data was first explored by running normality tests of Total Quantity Score (TQnS) and Total Quality Score (TQIS), on the two groups FTSE4Good and Non-FTSE4Good, over the pre and post EBR period. The analysis of skewness and kurtosis, as well as the inspection of histograms, showed that the data was not normally distributed. In particular, out of the 4 variables tested (TQnS pre EBR, TQnS post EBR, TQIS pre EBR and TQIS post EBR) for each group, only the TQnS post EBR and TQIS post EBR for the Non-FTSE4Good was normally distributed. Furthermore, in order to ascertain whether the data could be utilised in parametric tests, the variables were transformed

using SPSS v21. However, further tests showed that even after transformation, the Total Quantity Score post EBR for the FTSE4Good group was still highly skewed. Further inspection of the data revealed that this was due to a number of larger firms in high impact industries reporting abundantly, in comparison to the remainder of the sample. It was thus not possible to normalise all variables without removing a significant portion of the sample. Therefore this study uses only non-parametric tests to explore the data.

In order to test hypothesis 5, which is to determine if there is a distinction between the SER performance of high profile industries and low profile industries in terms of the quantity and quality of SER, this chapter in line with previous studies (see for example, Patten, 1991; Roberts, 1992; Newson & Deegan, 2002; Rettab et al., 2009) controls for sector profile. Table 5.4 below shows the categorisation of the sample companies into high or low profile.

Table 5.4 Categorisation of Industry Sector

Industry Code	High Profile Sectors	Low Profile Sectors
0001	Oil and Gas Producers.	
1000	Chemicals, Mining.	
2000	Construction and Materials, General Industrials, Electronic & Electrical Equipment, Industrial Engineering, Support Services.	
3000		Household Goods and Home Construction, Personal Goods.
5000		Food and Drug Retailers, General Retailers, Media, Travel and Leisure.
9000		Software and Computer Services, Technology Hardware & Equipment.

Source: Roberts (1992).

Table 5.4 shows that eight out of sixteen sectors are classified as belonging to the high profile sector with the remaining eight being classified as belonging to the low profile sector. The next section, Results, presents the statistical tests, including descriptive statistics, hypotheses testing and correlations between the variables.

5.4 Results

5.4.1 Descriptive Statistics

Before testing the hypotheses, descriptive statistics are provided for further insight into the reporting nature of the sample. The descriptives are provided for the untransformed

variables for each group, FTSE4Good and Non-FTSE4Good, as well as for the pre and post EBR periods. Information about the actual social and environmental reporting incidence of the FTSE4Good and the Non-FTSE4Good, for the pre and post EBR periods is thus shown in Table 5.5.

Table 5.5 Descriptive Statistics - All Firms

		Pre EBR (n=41)				
		Mean	Median	Std. dev.	Min	Max
Total Quantity Score	FTSE4Good	43.98	40.00	19.05	17	110
	Non-FTSE4Good	42.05	41.00	13.87	14	82
Total Quality Score	FTSE4Good	62.54	54.00	31.93	28	201
	Non-FTSE4Good	56.15	52.00	20.13	19	108
Market Capitalisation	FTSE4Good	3082.59	1267.05	6705.05	384	34893
	Non-FTSE4Good	3199.46	1210.25	6756.41	384	37471
Number of Employees	FTSE4Good	15778	11034	17475	309	95500
	Non-FTSE4Good	20359	9643	30974	121	162000
Return on Equity	FTSE4Good (n=30)	33.82	22.87	37.12	-1.18	180.75
	Non-FTSE4Good (n=29)	5.14	19.62	92.22	-454.30	87.69
		Post EBR (n=41)				
		Mean	Median	Std. dev.	Min	Max
Total Quantity Score	FTSE4Good	55.44	50.00	24.460	23	129
	Non-FTSE4Good	50.49	49.00	15.115	20	85
Total Quality Score	FTSE4Good	82.73	69.00	43.450	28	241
	Non-FTSE4Good	70.22	70.00	23.751	27	131
Market Capitalisation	FTSE4Good	2046.01	683.06	4923.92	151	28559
	Non-FTSE4Good	1635.56	637.52	3432.11	154	20499
Number of Employees	FTSE4Good	18428	12778	20801	378	98600
	Non-FTSE4Good	20686	8697	27983	156	112262
Return on Equity	FTSE4Good (n=28)	15.93	14.53	15.11	-12.19	55.91
	Non-FTSE4Good (n=26)	16.53	13.08	24.86	-16.90	120.67

Table 5.5 shows that the mean TQnS increased for both groups over the pre and post EBR period, with the mean for the FTSE4Good increasing from 43.98 to 55.44, and the mean for the Non-FTSE4Good increasing from 42.05 to 50.49. Furthermore, the descriptives show an increase in TQIS for both groups, with the mean for the

FTSE4Good increasing from 62.54 to 82.73, and the mean for the Non-FTSE4Good increasing from 56.15 to 70.22.

The mean market capitalisation of each group has dropped during the period. The FTSE4Good mean market capitalisation has dropped by 34%, whilst for the Non-FTSE4Good; mean market capitalisation has dropped by 49%. Interestingly, however, the number of employees has risen for both groups with the mean number of employees for the FTSE4Good increasing by 17%, and the mean number of employees for the Non-FTSE4Good increasing by 2%.

With relation to the ROE, some data was missing for both periods, hence a reduction in the total amount of firms ROE analysed. However the mean ROE for the FTSE4Good, showed a decrease from 33.82, pre EBR, (29 firms), to 15.93 (28 firms). The mean ROE for the Non-FTSE4Good, however showed an increase from 5.14, pre EBR, (29 firms), to 16.53 (26 firms). In addition, this chapter sought to determine if firms with a CSR committee perform better in SER than their counterparts. Table 5.6 below presents the CSR committee descriptives.

Table 5.6 Firms with CSR Committee

	Pre EBR	Post EBR
FTSE4GOOD	39.02%	60.98%
NonFTSE4GOOD	41.46%	58.54%

Table 5.6 shows that pre EBR, there were more Non-FTSE4Good firms with CSR committees than the FTSE4Good. However following the introduction of the EBR, it is shown that the FTSE4Good firms had developed or created a CSR committee and had surpassed the Non-FTSE4Good firms in this regard. It is of note to mention that whilst collecting the data from firms' annual reports, some firms had explicitly stated that they had since developed or created a new CSR committee to oversee the SER or sustainability issues of their operations. It is further surmised that having been exposed to the requirements of the EBR, some firms decided that it was important to allocate more resources to SER issues, hence the development of these committees. In addition, it is possible that the increase in the setting up of CSR committees underlines the strategic nature of firms' engagement with SER. Of note however, is the minor

difference in percentage between these two groups, FTSE4Good - 60.98% and Non-FTSE4Good - 58.54%. This minor difference could be related to the fact that the chapter utilises only a subsample of the whole population of the FTSE firms, hence may not be representative of the entire population.

5.4.2 Hypotheses Testing

Difference in Reporting Levels; Pre and Post EBR

To test hypothesis 1 which is, ‘There is a significant increase in the quantity and quality of firms SER following the year after the EBR was introduced’, Wilcoxon matched pairs signed ranks tests were run. The results are shown in Table 5.7.

Table 5.7 Wilcoxon Signed Ranks Tests examining the changes in the Quantity and Quality of SER, pre to post EBR.

	FTSE4Good	Non-FTSE4Good
Panel A: Tests between Groups		
Difference in <i>Quantity</i> of Reporting pre to post EBR	-3.409***	-3.509***
Difference in <i>Quality</i> of Reporting pre to post EBR	-3.761***	-4.005***
Panel B: Change from Voluntary to Mandatory reporting		
Difference in <i>Quantity</i> of:		
Consumer /Products Disclosure	-3.511***	-1.369
Community Disclosure	-2.763***	-1.599
Difference in <i>Quality</i> of:		
Consumer /Products Disclosure	-3.744***	-1.603
Community Disclosure	-3.415***	-1.852
Panel C: Change in Mandatory reporting		
Difference in <i>Quantity</i> of:		
Environment Disclosure	-2.404**	-2.990***
Employee Disclosure	-2.838***	-3.686***
Difference in <i>Quality</i> of:		
Environment Disclosure	-2.603***	-2.914***
Employee Disclosure	-2.941***	-4.033***

Significant at $p \leq 0.05$, * Significant at $p \leq 0.01$

Table 5.7, shows the Wilcoxon signed ranks tests carried out, between groups, and tests on changes in voluntary and mandatory reporting. The results provided in Panel A,

which are absolute values, further show sufficient evidence to support the notion that there is a significant difference in the quantity and quality of social and environmental reporting, before and after the introduction of the EBR. This significant difference is the same across both groups. Furthermore, within hypothesis 1b, this chapter sought to examine whether the EBR had an effect on the voluntary reporting aspects of SER, which are the Community/Products and Community categories. The result of this examination is shown in Panel B: Change from Voluntary to Mandatory Reporting. Panel B shows that for the FTSE4Good there is a statistically significant change from the pre EBR (voluntary) reporting to the post EBR (mandatory) reporting across all variables, whilst the opposite can be said for the Non-FTSE4Good. Thus, the Non-FTSE4Good show no statistically significant change in any reporting category. Moreover, further tests on the mandatory aspects of SER reporting, showed a statistical significant change for both groups between pre and post EBR, as reported in Panel C: Change in Mandatory Reporting.

Difference between Groups

To test hypothesis 2 which is, ‘The quantity or quality of SER reporting is the same for the FTSE4Good, compared to the Non-FTSE4Good, both before and after the introduction of the EBR’, and to determine whether a significant difference between the scores of the FTSE4Good and the Non-FTSE4Good exists, a Non-parametric Levenes test was performed. The results of these tests are presented in Table 5.8.

Table 5.8 Non-parametric Levenes Test of Equality of Variance between FTSE4Good and Non-FTSE4Good

	F	Sig.
Panel A: Test between FTSE4Good and Non-FTSE4Good		
Total <i>Quantity</i> Score:		
Pre EBR	223	.638
Post EBR	4.306	.041**
Total <i>Quality</i> Score		
Pre EBR	.003	.955
Post EBR	1.635	.205
Panel B: Test between Total Quantity Score Post EBR of the FTSE4Good and Non-FTSE4Good		
<i>Quantity</i> Score:		
Environment	2.608	.002
Employee	1.319	.192
Consumer/Products	1.378	.158
Community	1.236	.253
Panel C: Test between FTSE4Good and Non-FTSE4Good for voluntary compliance (Pre EBR)		
<i>Quantity</i> Score:		
Consumer /Products	.059	.809
Community	.866	.355
<i>Quality</i> Score:		
Consumer/Products	.027	.870
Community	.435	.511
Panel D: Test between high profile sector firms and low profile sector firms		
Total <i>Quantity</i> Score:		
Pre EBR	.589	.445
Post EBR	.759	.386
Total <i>Quality</i> Score:		
Pre EBR	.402	.528
Post EBR	.000	.999

**Significant at $p \leq 0.05$.

Table 5.8 shows the results of non-parametric tests run, to test the equality of variance between the FTSE4Good and Non-FTSE4Good. The results provided in Panel A: Test between FTSE4Good and Non-FTSE4Good, shows the robustness tests run on the

equality of variances. The results further show that of the 4 main variables tested only TQnSPost ($p=.041$), has a statistically significant difference at the 5% level. Equality of variance is therefore assumed for three out of four variables tested, and reject equality of variance for one, TQnSPost EBR. Hence, hypothesis 2a and 2b, which states that the quantity or quality of SER reporting is the same for the FTSE4Good, compared to the Non-FTSE4Good, is rejected, as there is not enough evidence to support the notion that the SER performance after the introduction of the EBR differed significantly between the two groups. Furthermore, it was important to examine which mandatory aspects were responsible for the difference in equality for the TQnS post EBR ($.041^{**}$ - Panel A). The results are shown in Panel B: Test between Total Quantity Score Post EBR of the FTSE4Good and Non-FTSE4Good.

Panel B, shows that the variable which accounts for the difference in equality of variance is the Quantity Score for the environment ($.002$). This further shows that the FTSE4Good firms allocated more importance to the quantity of reporting, post EBR, than the Non-FTSE4Good did. Furthermore, to test if there is a variance in the voluntary reporting of both groups, i.e. pre EBR, further non-parametric tests were run. From these results as presented in Panel C: Test between FTSE4Good and Non-FTSE4Good for voluntary compliance (Pre EBR), equality of variance is assumed for both groups, due to the significance levels recorded.

Difference between High and Low Profile Sectors

In testing hypothesis 5 which is, ‘There is no distinction between the SER performance of high profile industries and low profile industries in terms of the quantity and quality of SER, and to determine whether a significant difference between the scores of firms belonging to the high profile and the low profile exists, a Non-parametric Levenes test was performed. The results of these tests are presented in Table 5.8, Panel D: Test between high profile sector firms and low profile sector firms.

The results as presented in Panel D, show that there is no statistical difference between the scores of firms belonging to the high profile groups and those of firms belonging to the low profile group. Hypothesis 5 therefore, cannot be rejected and equality of variance is assumed. It is of note to mention that prior to testing, it became apparent that the number of firms belonging to the high profile sector, outweighed the number of firms belonging to the low profile group by two, therefore two firms belonging to the

Support services (as they are the largest group) were removed to bring down the total number of firms to an equal number, that is forty high profile firms versus forty low profile firms.

5.4.3 Correlations

The correlations presented and discussed in the following tables are to test hypotheses 3a and 3b, 4a and 4b, and 6. Spearman's rho correlations are computed as the variables are not normally distributed. Table 5.9 provides insights into the association between the Total quantity score (TQnS) and Total quality score (TQIS) and the market capitalisation, number of employees, return on equity, industry profile, and CSR committee, for both pre and post EBR.

Table 5.9 Correlations – All Firms - Spearman's Rho

Variables	Total Quantity	Total Quality	Market Capitalisation	Number of Employees	ROE	Industry	CSR Committee
Total Quantity Score	1.000	.924**	.268*	.254*	-.057	.032	.356**
		.000	.015	.021	.671	.772	.001
Total Quality Score		1.000	.232*	.294**	-.088	.100	.360**
			.036	.007	.508	.372	.001
Post EBR							
Variables	Total Quantity	Total Quality	Market Capitalisation	Number of Employees	ROE	Industry	CSR Committee
Total Quantity Score	1.000	.913**	.270*	.335**	.053	.038	.251*
		.000	.014	.002	.704	.732	.023
Total Quality Score		1.000	.254*	.335**	.090	.115	.222*
			.021	.002	.517	.303	.045

* Significant at $\alpha = .01$ (two-tailed) ** Significant at $\alpha = .05$ (two-tailed)

Table 5.9 shows that there is a positive correlation between TQnS and TQIS and the variables, market capitalisation, number of employees, industry profile, and CSR committee, for both pre and post EBR periods, except for return on equity, which shows a negative correlation pre EBR, but a positive correlation post EBR. Of the eleven correlations for both pre and post EBR, seven are statistically significant with three statistically significant at $\alpha = .01$ (pre EBR) and four statistically significant at $\alpha = .01$ (post EBR). For both the pre and post EBR periods, TQnS and TQIS are statistically significantly correlated with market capitalisation, number of employees and CSR committee. Further investigation of the relationship between the number of employees

and the quantity and quality of employee disclosure, before and after the introduction of the EBR, is seen next.

Table 5.10 Correlation – Number of Employees and Quantity/ Quality of Employees disclosures

	Quantity of Employee disclosure	Quality of Employee disclosure
Number of Employees Pre EBR	.232 .036**	.255 .021**
Number of Employees Post EBR	.267 .015***	.336 .002***

****Significant at $p \leq 0.05$, ***Significant at $p \leq 0.01$**

As presented in Table 5.10, a significant and positive correlation between the two variables, number of employees and the quantity and quality of employee disclosure is observed, with further increases showing for the post EBR period.

Further correlation tests were carried out on the relationship between industry profile and the TQnS and TQIS, for both pre and post EBR. The results showed that there was a statistically significant positive correlation between sector category and the quality of environmental disclosure, pre and post EBR. However, although a positive relationship existed between sector category and quantity of environmental disclosure, pre EBR, there was no significant correlation between sector category and quantity of environmental disclosure, post EBR. Nevertheless, the quality of the SER output is viewed as complying with ‘completeness, accuracy and reliability’ (Singhvi & Desai, 1971, p. 131), and can have a significant influence on the quality of the decisions made by stakeholders (Singhvi & Desai, 1971). Hence this chapter assumes a significantly positive correlation between sector category and environmental disclosure.

5.5 Discussion

5.5.1 The Impact of Regulation - Quantity and Quality of SER

The results showed that each group improved both the quantity and quality of SER, between the pre and post EBR period. Hypothesis 1a and 1b¹⁴⁸ stating that there is a significant change in the quantity/ quality of SER, over time with each group, cannot be

¹⁴⁸ 1a. There is a significant increase in the quantity of firms SER following the year after the EBR was introduced; 1b. There is a significant increase in the quality of firms SER following the year after the EBR was introduced.

rejected. Indeed, previous empirical research indicates that regulation has an impact on firms' level of SER. For example, Aaronson & Reeves (2002) suggests that the governments of France, Germany, and the United Kingdom have each passed laws requiring pension fund managers to disclose the extent to which they consider the social and environmental records of the companies in which they invest. These laws, they report, have encouraged pension funds and their investment managers to pay more attention to companies' social and environmental performance, creating additional pressures for companies to consider those issues in their investment decisions as well (Williams & Conley, 2005). Again, the laws governments pass to encourage CSR are uniquely powerful because they can achieve broader coverage than voluntary initiatives, such as the UN Global Compact (substantive human rights standards) or the Global Reporting Initiative (social, economic, and environmental disclosure format) (Aguilera et al., 2007).

Another example is the Climate Change Act of 2008, which following extensive consultation was implemented and is now being adhered to by the UK's largest companies. Moreover, the laws and policies that governments enact send a strong signal about the importance of a subject, a signal that, with regard to SER, is amplified by the business culture, consumers' interests, institutional investors' actions, the corporate governance regime, to name a few (Aguilera et al., 2007). For example, some UK are companies going one step ahead to implement award schemes for employees' engagement with community matters.

Again, it is of note to mention that whilst examining the annual reports of firms, it became apparent that over the two periods, pre EBR and post EBR, the very nature of reports had changed. This was observed in the improvements and changes in the structure and wording in the Business review section of annual reports; leading to the assumption that these changes could be a result of the increased guidelines the introduction of the EBR provided. Thus as much as there is evidence to suggest that regulation is having little impact, (see for example, Benston, 1982; Ely and Waymire, 1999), this chapter provides evidence to the contrary and suggest that regulation is having some impact on firms SER.

In addition, with relation to the quality of SER, a significant change is observed, which is supported by other studies. For example, Raar's (2002) results, suggest a trend to

triple-bottom line reporting, and a significant change in the quantity and quality of environmental information. Furthermore, a report by Deloitte (2009), analysing the annual reports of 130 listed firms shows an overall improvement in compliance with SER regulation over the years. However, again, it is also possible that this increase in quality may have arisen from the extra guidelines firms received with the introduction of the EBR. Furthermore, interview evidence provided showed that respondents acknowledged the importance of regulation as well as regulation being a factor in their increase of SER. For example,

'I would say that an increase in sustainability reporting requirements has definitely influenced the way we report. 4 years ago we did not have a corporate responsibility report as part of the annual report...now we do. 4 years ago we did not disclose our carbon footprint, now we do. 4 years ago we didn't show our community investment now we do'.

CSR Manager, Media sector.

Nevertheless, it is recognised that this increase in quantity and quality may not be attributable solely to regulation, as there may be other factors such as improved SER practices, experience with pressure groups, and media profile (Gray et al., 2001).

5.5.2 SER Performance between the FTSE4Good and Non-FTSE4Good

Following previous studies reporting that there is no statistically significant difference in the financial performance of the ethical fund versus the non-ethical fund (see for example, Kreander et al., 2005) as well as the theory that the FTSE4Good differ from all the other indices mainly due to their 'commitment' to social and environmental matters, the second hypothesis set out to test whether any statistically significant difference between the SER performance of the FTSE4Good and that of the Non-FTSE4Good exists. The results showed that there was no significant difference in the SER performance between both groups. Thus on average, it is reasonable to state that both groups performed equally in terms of the quantity and quality of SER. These results are consistent with previous studies which showed that ethical funds do not underperform benchmark indices and indeed match their non-ethical fund counterparts (Kreander et al., 2002) or that ethical funds do not perform any differently compared to their non-ethical counterparts (Schröder, 2004). Although these studies relate to financial performance, they nonetheless examine how an ethical fund or index performs in

relation to other non-ethical indices. Likewise, in examining the SER performance of the ethical FTSE4Good and comparing it to the non-ethical Non-FTSE4Good, the results of our tests provide further evidence that there is no statistically significant difference between the performance of both groups in the SER field. We should however not discount the results showing that the FTSE4Good performed better in changing from voluntary to mandatory regulations whilst the Non-FTSE4Good did not. From the perspective of this research, this could mean that the FTSE4Good are more willing to conform to SER change as evidenced by the significant increase of voluntary reporting levels.

5.5.3 Firms Characteristics and SER Performance

This chapter further sought to analyse the relationship between the firm characteristics of size, profitability, industry, and presence of a CSR committee on the total output of SER. First, tests showed a positive relationship between SER disclosure and the size of the firm in terms of market capitalisation and number of employees. Additionally, tests showed that there was a positive relationship between number of employees and employee disclosure by firms. Larger companies it is argued are more efficient in CSR activities as in this way a higher level of competitiveness is achieved (Ljubojevic et al., 2012). These results are further consistent with previous studies indicating that the larger a firm is, the more SER it will provide (see for example, Donaldson and Preston, 1995; Johnson and Greening, 1999; Ljubojevic et al., 2012). A high correlation between number of employees and quantity and quality of employee disclosure was also observed. As discussed earlier on in the literature review on firms' characteristics (Section 5.2.5.1), this positive relationship and increase in employee disclosures, could be attributed to the importance firms place on employee matters.

Second, correlation tests run on the relationship between quantity and quality of SER, and ROE, pre and post EBR, showed that there was no significant correlation between these two variables. In other words, the results indicate that the profitability of a firm has no direct relevance to its SER output. These results are consistent with several other studies (see for example, Alnajjar, 2000; El Mosaid and Boutti, 2012; Patten, 1992; Richardson and Welker, 2001). Furthermore, in trying to explain the reasons behind these results, the reason behind Alnajjar's (2002) study is considered (he states that his observed negative relation might result from the possibility that firms that are less

profitable may include more SER in an attempt to improve their public image). Therefore all firms were tested under the median and correlations tests were run, yet a negative relationship was still observed. In addition, the small sample size used, mainly fifty nine firms tested for pre EBR and fifty four firms for post EBR, is considered. The small sample size could therefore be a factor for the observed relationship, and hence may not be a reflection of the entire population of FTSE firms. This chapter therefore concludes that ROE isn't a driver for either the quality or quantity of SER by firms.

Moreover tests were carried out to determine the relationship between the quantity and quality of SER and industry sector profile. The results showed no statistical difference between the scores of firms belonging to the high profile groups and those of firms belonging to the low profile group. These results are in line with previous studies such as Alnajjar (2000); Cowen et al., (1987); Herremans et al., (1993). As with the ROE results, this chapter suggests that the equality of variance observed between the high and low profile firms could be attributed to the subsample used in this study, hence not representative of the entire population.

Last but not least, a positive correlation test between total scores and CSR committee, pre and post EBR is observed. This positive relationship could be attributed to the evidence suggesting that as stakeholders are increasingly being made aware of the importance of SER, firms are thus being proactive in the SER arena in order to show their commitment to SER. Furthermore, it is possible that firms that developed a CSR committee over the pre and post EBR period, determined that the formation of a dedicated CSR committee will be beneficial to their operations and offer them a competitive advantage. Again the increase in the number of firms developing a CSR committee over the period could be attributed to the introduction of the EBR which offered more guidelines on SER. Nevertheless, it should be noted that the lack of reporting on a CSR committee in the annual report, does not imply that a firm has no CSR committee, as this characteristic is not a statutory requirement. As such, these particular results are speculated and only based on the data collected.

5.6 Conclusions

This chapter contributes to literature by examining the impact of the Enhanced Business Review (EBR) on firms' SER performance. The results showed that there was

significant change in the reporting levels for both groups (FTSE4Good and Non-FTSE4Good), over the pre and post EBR period. Although other factors, such as experience with pressure groups and media profile (Gray et al., 2001), could account for this increase, the likelihood of this change being due to the introduction of the EBR is highly suggested. This interpretation is supported by evidence from our tests showing a significant change in reporting levels, after the transition from voluntary to mandatory requirements. Moreover, evidence from the interviews conducted as well as previous studies; suggest that for some firms, regulation is indeed making an impact on firms' attitudes towards SER.

Furthermore, this chapter tested the nature of the social and environmental reporting (SER) of firms belonging to two indices, the FTSE4Good and the Non-FTSE4Good, over a period that the Enhanced Business Review was implemented. Results obtained by running statistical tests on the data, suggests that there was no significant difference in the SER performance between these two groups, replicating the findings of previous empirical studies. However in spite of the lack of a significant difference, it is seen that there is a change for the FTSE4Good, during the move from voluntary to mandatory requirements, results which were not applicable to the Non-FTSE4Good. This leads us to believe that the FTSE4Good are more willing to embrace change, an opinion resonating from the interviews.

In addition, correlation tests were run to determine the relationship between the total SER quantity and quality and the market capitalisation, employee number, ROE, industry category and CSR committee, of firms. The tests showed a significantly positive correlation between the total SER quantity and quality and market capitalisation, employee number and CSR committee, indicating the strength of this relationship. Additionally, this chapter determined that the number of employees of a firm is positively related to the firm's employee disclosure. This development, regardless of the EBR requirement, lends credence to the fact that employees are one of the most valuable resources to the firm. As such, the trend and attitude of firms towards employee disclosure is one which is expected to last.

Moreover, the CBI's fears about mandatory reporting has been brought into question in this chapter, in that firms increased their levels of reporting, some voluntary and most due to the EBR. The results show an increase in quantity and quality of SER, post EBR

and thus suggest that firms are willing to increase their reporting levels, in spite of the claimed 'cost' and loss of 'competition'. However, it is important to note that some firms (as interviewed) were supportive of the arguments put forward by the CBI. These firms oppose regulation and, as the chapter argues, are using SER as a form of strategy. This concept is discussed in detail in Chapter 6. Accordingly Chapter 6 examines whether firms are using SER as a form of strategy and what their attitudes to regulation are.

Appendix C

Appendix C 1 Categories of SER

Environmental Data

1. environmental pollution including ozone depleting substances, carbon reduction
2. environmental audit
3. climate change including emissions, spills and waste, recycling
4. sustainability and sustainable development
5. energy use
6. water use

Employment / Workplace Data

1. Employee details/ profiles
2. Details of Directors' Emoluments and Remuneration including (employee) pensions and share options
3. Employee training
4. Employment of minorities or women
5. Arrangements for consultation with employees
6. Details on the employment policy for disabled persons
7. Statement of Value Added
8. Details of Health and Safety at Work
9. Employee share Ownership Schemes
10. Statements of Equal Opportunities
11. Corporate Governance
12. Recruitment and retention
13. Training and development
14. Employee morale/ motivation
15. Workforce performance and profile
16. Diversity in the employee base

Consumer/Products

1. Information relating to consumers/customer/client/marketplace
2. Product development
3. Product safety
4. Product quality
5. Customer Churn
6. Satisfaction with relationship – feedback results, levels of complaints, fines etc.
7. Diversity in the customer base

Community Data

1. Charitable and political donations
2. Involvement with the community
3. Sponsoring public health projects
4. Summer or part-time employment of students
5. Public health issues such as Obesity
6. Noise
7. Transport Congestion
8. Smoking
9. Perceived safety issues related to high use of mobile phones
10. Social risks existing in the supply chain, for example the use of child labour and payments of “fair wages”
11. Indigenous and human right issues relating to communities local to overseas operations

Appendix C 2 Rating Scale

Score	Policy
0	No mention of social or environmental policy in place.
1	General mention of policy – general rhetoric.
2	Firm mentions and indicates the impact or effectiveness of policy.
3	Firm calculates and measures or quantifies and compares its performance with SER issues.

Examples of Rating Scale

Theme	Statement	Score ()
Environment	<p>1. Extended the monitoring of supplier and subcontractor performance to include environmental factors. In 2007, the Group will continue to monitor and improve its environmental impact by recording and then taking appropriate action upon the following data: • total tonnage of waste diverted from landfill • total CO2 (Morgan Sindall Annual report, 2006)</p>	(1)
	<p>2. In the environmental field, meanwhile, we are supporting PRUPIM in its commitment to reduce carbon emissions through efficiencies in transport, energy and waste management. At The Mall, Cribbs Causeway, alone, we have achieved a reduction in CO2 emissions in the region of 300 tonnes per year, generating annual savings of £30,000 on energy bills. We have also implemented recycling programmes and are recycling 320 tonnes of waste annually (Interserve, Annual report, 2006)</p>	(2)
	<p>3. Rio Tinto believes that emissions of greenhouse gases (GHGs) from human activities are contributing to climate change. Controlling GHG emissions is one of our biggest challenges, and the Group is working to reduce emissions from its processes and in the use of its products. We have five year targets to reduce our GHG emissions by four per cent per tonne of product and improve our energy efficiency by five per cent per tonne of product by 2008, compared with a 2003 baseline. In 2006, energy efficiency improved by 2.6 per cent compared with 2003, while GHG efficiency improved by 0.3 per cent. Both areas slipped from 2005 and remain below the trajectory needed to achieve the 2008 targets. Our emissions efficiency result is affected by both production interruptions and changes in the emissions intensity of purchased electricity. The scheduled maintenance shutdown of the Kennecott Utah copper smelter significantly impacted our performance per unit. Without the smelter shutdown our performance would have been one per cent better (Rio Tinto, Annual report, 2006).</p>	(3)

Examples of Rating Scale (continued)

Theme	Statement	Score ()
Employee	<p>1. In Victrex, diversity encompasses differences in ethnicity, gender, language, age, sexual orientation, religion, socio-economic status, physical and mental ability, thinking style, experience and education. We believe that the wide array of perspectives that result from such diversity promotes innovation and business success. As part of this policy, Victrex gives due consideration to employment applications from disabled people consistent with their capabilities and provides every opportunity to employees who become disabled to continue employment with appropriate training and career development (Victrex, Annual report, 2007).</p> <p>2. In addition, the Company regularly publishes Optima (available on the Company’s website) and AngloWorld, which contain items of news, current affairs and information relevant to Group employees. During the year, the Company continued to enhance the new enterprise information portal – the source – aimed at promoting knowledge-sharing across the Group and keeping employees up to date with developments in those business sectors in which the Group is active. The availability of the source continues to grow and it is now available to over 13,000 computer-connected employees across the Group. Following a Groupwide communication and culture survey in 2005 measures have been implemented to address weaknesses identified and a number of business units also undertook climate surveys amongst their workforces in 2006 (Anglo American Plc Annual report, 2006)</p> <p>3. Employees At 31 December 2008, we had 39,937 employees (31 December 2007: 38,740). The net addition of just under 1,200 employees reflected the net effect of recruiting over 8,500 new employees, offset against employee churn through annualised voluntary attrition and actions taken to reduce (Logica Plc Annual report, 2008)</p>	<p>(1)</p> <p>(2)</p> <p>(3)</p>

Examples of Rating Scale (continued)

Theme	Statement	Score ()
Customer / Product	<p>1. Our customers are a combination of polymer processors and end users located worldwide. We have long-term supply assurance agreements in place with all of the implantable medical device manufacturers that comprise Invivio's PEEK-OPTIMA polymer customers. These agreements guarantee the specification of and production methods for the biomaterial over the term of the agreements. We also have supply agreements in place with some major processing customers and supply to other customers on an order by order basis in accordance with the Group's applicable terms and conditions of sale. The loss of a major processing customer or a worsening of commercial terms could have a material impact on the Group's results, accordingly we devote significant resources to supporting our customer global ethics policies, including maintaining regular contact with major customers and undertaking surveys of customer satisfaction (Vitrex, Annual report, 2009).</p>	(1)
	<p>2. Delivering best customer service - For the last 20 years, we have conducted regular customer surveys to understand customer behaviour. Throughout that time, location has been the primary reason for a customer choosing a particular shop. In 2009, however, customer service became the primary driver, reflecting changing customer requirements. Four years ago, we launched CBS, our Competition Beating Service strategy, throughout the estate, The factors influencing a customer's choice of shop which focuses on friendly service a customer's choice of shop which focuses on friendly service and expertise, and we are focused on providing the best customer experience in high street betting. Our Retail business attracts a broad range of customers, with a different demographic from Online. Typically, customers are older in Retail, although 40% of customers are under the age of 45. Younger customers are being attracted by products such as machines and football, with the proportion Retail and Online customers by (William Hill, Annual report, 2009)</p>	(2)
	<p>3. Customer Service "Providing high standards of customer service" Our customer satisfaction level for our core new home range has increased to 78% (76%: 2006) and our recommendation level is 82% (82: 2006). For Debut, our innovative, first time buyer home range, satisfaction is 94% and our recommendation level is 88%. We are currently undertaking a comprehensive review of our customer service to ensure continuing improvement in our customers' experience, through all stages of the purchasing process. Communication Redrow recognises that CSR (Redrow, Annual report, 2007)</p>	(3)

Examples of Rating Scale (continued)

Theme	Statement	Score ()
Community	1. Charitable initiatives – at a corporate level our charitable strategy is to support initiatives that address social and educational exclusion whether due to disability, economic or social circumstances. Our current charitable partnerships are with the NSPCC and the Prince’s Trust and a 3rd charity voted for annually by employees –which was Cancer Research UK in 2006. Fundraising events are arranged centrally and locally and a volunteering scheme is in place to support the Prince’s Trust young people programmes (Capita Plc, Annual report, 2006).	(1)
	2. Charitable and Political Donations During the year the Group made charitable donations amounting to £1,270 (2005: £2,231). A Social Investment Policy has recently been developed based around our employees’ links in the local communities. No political donations were made (Venture Production Plc, Annual report, 2006)	(3)

CHAPTER 6

Chapter 6 . SER and Regulation – The Strategic Attitude of Firms

6.1 Introduction

This chapter argues that competitive dynamics explain firms' Social and Environmental Reporting (SER) behaviour. In line with previous research suggesting that companies use SER to develop their image and hence increase their competitiveness (for example, Porter and Kramer, 2006), the chapter argues that firms use SER to build their competitive position in two specific ways.

First, following the resource based view (Barney, 2001) firms aim to achieve competitive advantage through the creation of difficult to replicate assets. Where the firm's strategy involves engagement in SER, resulting in valuable assets such as ethical reputation, success depends on preventing competitors from cheaply replicating the strategy (Hasseldine et al., 2005; Toms, 2002). To create the required barriers to entry in such circumstances, the strategy must involve investment in causally ambiguous competencies that are difficult to access by other firms (Reed and DeFillippi, 1990).

Second, because SER also arises from the activities of regulators, the firm's attitude to regulation forms an important part of its SER strategy. One of the main benefits of regulation is that it is a tool which creates a level playing field. In parliament this benefit of regulation has been acknowledged by several Ministers, indicating that regulation is needed in order to provide a level playing field, so that those firms 'who want to do the right thing do not find themselves unable to compete with those who are prepared to sacrifice planet and people in the scramble for profits'¹⁴⁹. Therefore, firms either adopt a positive attitude to regulation by focusing their efforts into trying to ensure a level playing field for all and be on a par with competitors, or adopt a negative attitude towards regulation, by channelling their efforts into preventing effective regulation to ensure that competitors are not given the opportunity to improve on their SER activities, eroding their competitive advantage.

Previous studies further suggest that regulation can be used as a form of competitive advantage (Barrett, 1991; Hart, 1995) though the literature has paid far too little

¹⁴⁹ *Hansard* HC Deb. vol.447, col. 188, 6 Jun 2006.

attention to SER regulation and if and how it is used as a form of competitive advantage. Consequently, these studies do not consider the impact of SER regulation on firms' attitudes towards SER, or the effect that the regulatory system has on firms. Based on this gap in the literature, it is argued that, firms use SER as a means of differentiating themselves yet at the same time, pursue level playing field oriented objectives as far as regulation is concerned. Also, following previous studies on firms' use of SER as a form of strategy, this chapter presents further insight into the relationship between firms' strategic use of SER and their attitude towards regulation. Furthermore, due to its history of frequent changes in mandatory regulation of social and environmental issues, the country of focus in this study is the UK. The interest of this chapter further lies in the regulatory part of SER in the Companies Act 2006 (Section 417), by which this chapter refers only to the social and environmental aspect (Section 5 (b)) of the requirements.

This chapter proceeds as follows. In section 6.2, an examination of the prior literature on SER and competitive advantage, and the relationship between SER and Regulation is presented. Following the review of the literature, the research method used in gathering and analysing the data is discussed in section 6.3. This is followed by the results and a discussion of the results in section 6.4, and 6.5 respectively. In the final section of the chapter, section 6.6, conclusions are drawn from the findings together with an introduction of the final conclusion chapter.

6.2 Related Literature and Hypothesis

This section first discusses the literature on the relationship between SER and regulation before discussing the relationship between regulation and competitive advantage. These discussions then proceed to the building and stating of the hypothesis.

6.2.1 The Relationship between SER and Regulation

The subject of regulation of SER has been one of the most contentious, with critics such as the Confederation of British Industry (CBI)¹⁵⁰ arguing that regulations interfere with

¹⁵⁰ The CBI (the UK's leading business organisation) believes that if SER is to develop successfully, it should remain voluntary and market-driven. Brian Cress, the CBI's senior CSR policy adviser states, 'Companies must be allowed to define CSR according to their own activities and context. We are therefore extremely concerned that some individuals and interest groups favour the idea of legislating on companies' CSR activities. Public authorities should adopt a carrot-led rather than a stick-driven

the efficiency of the market, and advocates for regulation, arguing that well designed regulations not only make markets more efficient but also help ensure that market outcomes are more equitable (Stiglitz, 2009). In the UK, SER regulation has a strong voluntary aspect with mandatory SER requirements having only been introduced in the last decade. Voluntary initiatives have a longer history with some of these initiatives being the publishing, by firms, of social and environmental information in separate Corporate Social Responsibility (CSR), Corporate Responsibility, Sustainability, or stand-alone Environmental reports. Currently, based on government directives given by BIS, all large and medium sized businesses now have to produce a Strategic Report and Directors' Report (as part of the annual report), which includes an added requirement for quoted companies to include information on human rights issues. For a more comprehensive understanding of the history of SER regulations in the UK, a timeline summary has been developed, showing the three different mandatory regulations which have been implemented in eight years; Operating and Financial Review (OFR), Enhanced Business Review (EBR) and the latest Strategic Report and Directors' Report (seen in Appendix B). As stated in the introduction, the focus of this chapter is on the social and environmental aspect of the mandatory EBR.

The debate about the efficacy of regulation of SER is ongoing. KPMG (2011)¹⁵¹ reports that unlike financial reporting, the disclosure of sustainability metrics to the market is largely unregulated. Consequently, incidents such as the Enron Case in 2001, oil spills in countries such as Australia, and climate changes for example, prompt governments to bring about sanctions and regulations in order to discourage further occurrences and foster a responsible attitude amongst businesses. History also suggests that regulation and other social and political forces have been much more effective than SER at shaping firm behaviour. In fact, 'social reformers have long exposed [negative] corporate practices as means of mobilizing political support for new legislation or regulation aimed at curbing them' (Reich, 2008). Consequently, it matters little that a few companies implement SER activities ahead of the law. Regulation and legislation,

approach to CSR. Legislation in this area would simply constrain business activity and reduce CSR to a lowest common denominator" CBI (2008), Corporate Social Responsibility, the Confederation of British Industry's website. Available from
<<http://www.cbi.org.uk/ndbs/content.nsf/802737AED3E3420580256706005390AE/9D502144AC9F644380256F58005BD16C>> Accessed 4 May 2013.

¹⁵¹ KPMG are one of the world's largest professional services firms and has three lines of service; audit, tax and advisory.

Karnani (2011) argues, are required to ensure that all companies implement socially desirable activities that reduce firm profits. Karnani's (2011) stance is in direct rebuttal to Rivoli and Waddock's (2011) argument that 'laws and regulations are often the *end* point of the issue life cycle', thus clearly favouring voluntary SER. Karnani (2011) argues that Rivoli and Waddock (2011) offer no empirical evidence and have misrepresented history with their examples showing that 'public policies often respond to emerging corporate behaviour rather than the reverse.' Karnani further gives the example of racial discrimination which is still very much alive, and though there has been change, it is not enough, therefore public policies are needed.

On the other hand, the CBI's opposition to the implementation of mandatory regulations for SER stems from reasons including the view that as organisations pay taxes to government to ensure that society and the environment are not adversely affected by business activities, there is no need for regulations to be implemented or enforced. The HM Treasury also stated that 'Deregulating in this area [SER] will also help to shore up support for other measures by showing that Government is committed to ensuring only demonstrably effective measures are implemented' (HM Treasury, 2006, p. 7). Studies by Benston (1973) and Ely and Waymire (1999) also suggests that regulation has not improved the information environment for investors, with Benston (1973) stating that regulation requires an economically unsound use of resources to disclose information that is not needed. One concept that is also being propagated in favour of less regulatory requirement is the business case for SER, which is increasingly being promoted by the government and corporations as justification for self-regulation (Hart, 2010). This 'justification' was used by Gordon Brown in his speech repealing the OFR in 2005. A more recent example of promoting the business case and consequently advocating for this form of deregulation by the UK government is the introduction on 1st September 2010 of a 'one in - one out' rule effective for all regulations which begun after 1st January 2011. The 'one in - one out' rule therefore ensures that the current amount of regulatory requirements is not increased, with an aim to further decrease the requirements.

Empirical research further suggests that "regulating self-regulation" is most successful in companies "... that have a 'natural interest' in safety matters, due to the high risk in the production process or the social 'visibility' of the company" (Aalders and Wilthagen, 1997, p. 420). Consistent with this view, Cragg (2005) holds that reliance on

the business case is doubtful. If the business case cannot then be relied upon to tackle systemic discrimination, then one complementary route to change is by implementing regulation (Dickens, 1999, p. 12). In terms of government policy and management practice therefore, the business case (Hart, 2010) argues, will need to be supplemented by strong proactive legislation and worker involvement. Furthermore, the Companies Act 2006 (Section 417(5)) states that firms should report to an extent necessary regarding impacts of social and environmental issues. Though reporting relevant issues could be true in the case of companies who do not have to report on factors that do not relate to them, it could however give rise to exploitation by some firms; as evident in the several studies carried out showing the low quality of reporting (Hine, 2010) and the lawsuits brought against companies for failing to include relevant impacts (Case brought against Rio Tinto by Client Earth in 2010¹⁵²). Critically, it is claimed there is a lack of thoroughness in the way that social and environmental information are dealt with honestly and competently by the business and accounting communities (Gray, 2006) resulting in ‘cherry-picking’ – firms choosing to include information which is most likely favourable to them.

Evidence from empirical studies (Grosser et al., 2008; Henriques, 2010) further suggests that the impact of regulation in SER is low, with firms reporting mainly to maintain a competitive edge and not due to mandatory EBR requirements. For example, Henriques (2010) survey of the annual reports of the FTSE100 firms, finds that detailed quantitative information was provided by only forty eight percent of companies and that there was almost no analysis of the sensitivity of the company to climate change or the consequences of adaptation. Henriques reports that in essence, the Business review, (the regulatory requirement) which requests companies annual reports to contain information pertinent to stakeholders did not appear to be serving the purpose for which it was intended, as evidenced by the lack of the reporting by companies of relevant social and environmental information in their annual reports.

On the other hand, other studies have found that regulation does make an impact in the level of SER reporting, or as testified by managers. Mobus (2005) for example, looked at environmental disclosures and environmental performance in 17 US petroleum

¹⁵² Client Earth (2008) Referral to the Financial Reporting Review Panel. Available from: <<http://www.clientearth.org/reports/clientearth-submission-to-frfp-re-rio-tinto-annual-report-2008.pdf>> [Accessed 10 March 2013].

refining companies in the period 1992-1994 and found that mandatory accounting disclosures were influential in inducing cooperation with regulatory standards. Similar findings were found by Owen et al., (2005) and Henriques and Sadosky (1996). However, Spence and Gray (2007), in their study of twenty five firms, find that although some respondents mentioned regulatory pressure as a key factor for firms to engage in SER and CSR¹⁵³; complying with legislation was the lowest bar. Clarke (1994) also reports that some number of firms realise the regulatory system has become inefficient and ineffective and as a result of this, have adopted the view that engaging in SER is costly and unnecessarily high. As a result these firms may adopt a negative attitude towards regulation, but in order to maintain competitiveness, continue to engage in SER.

6.2.2 The Relationship between Regulation and Competitive Advantage

Given the debate about the efficacy of regulation of SER, Porter and Van der Linde (1995) report that there is a lingering belief that regulations erode competitiveness. This has resulted in a stalemate with one side pushing for tougher standards, and the other side trying to roll standards back. In other words, the advocates for regulations claim it will increase competitiveness and competitive advantage, whereas the opposition claims that it will expose firms to undue competition and therefore try to reduce existing regulations or prevent new regulations from being implemented. Furthermore, Bichta (2003) suggests that one of the objectives of the implementation of the Companies Act was to level the competitive playing field, by exploring alternative ‘means’ to boost confidence in industry and therefore guarantee it an increased ‘competitive’ edge. There is however very little evidence to suggest that SER regulations have been used by firms to achieve competitive advantage. One would assume that firms who argue for more regulation would have a high strategic attitude to SER, as this may result in regulatory barriers to imitation (McWilliams et al., 2006). However this does not seem to be the case. As seen in the timeline of regulation (Figure 2.1 in Chapter 2), SER regulations have changed on average every two years during the last eight years. This has undoubtedly led to an uncertain regulatory environment as well as a lack of clarity of

¹⁵³ The difference between CSR and SER is that CSR encompasses firms’ social, environmental and economic impacts (The Department of Business, Innovation and Skills) whilst SER covers the social and environmental aspects of firms impacts. This study focuses on SER only, though references are sometimes made to the use of CSR in other studies.

these mandatory regulatory rules (Henriques, 2010), resulting in the unclear nature of SER regulations in the UK.

Empirical studies also suggest that regulation is not beneficial. Sandhu et al., (2012) for example, report that none of the organisations interviewed in their study, credited their environmental responsiveness to environmental regulatory requirements. Importantly, had these firms realised that competitive advantage is a benefit of complying with regulation; regulation would be more pronounced in their credits. This view is however not supported by all firms. Indeed there is evidence to suggest that the CBI supported the Climate change Act of 2008 stating that ‘Climate change is no longer a threat to be feared, but a business opportunity’ (CBI, 2013¹⁵⁴). The CBI were however accused by Friends of the Earth of contradicting their agenda as it was at odds with its lobbying efforts to prevent other environmental regulations from being implemented¹⁵⁵.

Based on the above arguments this chapter concludes that adhering to SER regulation in the UK does not, give firms a competitive advantage, hence the prevalence of mimetic isomorphism amongst firms, which DiMaggio and Powell (1983) suggest happens, when firms, uncertain of their environment, copy the behaviours of other firms. This chapter therefore attributes mimicking of the SER reports of others and benchmarking, to the unhelpful regulatory system and the lack of clarity of the regulations, and argue that regulation is only useful when it can be enforced. Furthermore, following the argument from the CBI on firms’ attitude to regulation and the business case for SER, which is increasingly being promoted by the government and corporations as justification for self-regulation (Hart, 2010), it is assumed that firms generally oppose SER regulation due to the restrictions it imposes and the lingering belief that regulations erode competitiveness. Also as evidenced by the low impact of regulation in SER (Henriques, 2010), and the increasing use of SER as a form of strategy (Clulow et al., 2003; Falkenberg and Brunsæl, 2011; Vilanova et al., 2009) this chapter argues that firms engage in strategic SER rather than comply with regulations as that is where they will less likely be punished for non-compliance. Based on the above arguments, and using evidence obtained from the interviews, it is hypothesised that:

¹⁵⁴ The Confederation of British Industry (CBI) (2006). Energy and climate change Available from <<http://www.cbi.org.uk/business-issues/energy-and-climate-change/>> [Accessed 12 January 2013].

¹⁵⁵ Adam, D. (2007). CBI report urges business to tackle climate change. Available from: <<http://www.theguardian.com/environment/2007/nov/26/climatechange.carbonemissions>> [Accessed 12 March 2013].

H1) Firms which portray a high strategic attitude to SER exhibit a negative attitude towards regulation.

6.3 Methods

6.3.1 Data Sources

The aim of this chapter is to explore firms' strategic behaviours to social and environmental reporting and examine firms' attitudes to SER regulation. In order to achieve this aim, interviews were decided on as the main mode of investigation, as they are the best way of understanding situations and viewing it from someone else's perspective. Interviews have also been widely used in SER studies (see for example, Amran and Devi, 2007; Belal and Owen, 2007; Blomgren, 2011; Cobb et al., 2005; O'Donovan, 2002; O'Dwyer, 2002; Spence and Gray, 2007) as it removes bias and enables the researcher to obtain first-hand information. In selecting the companies to be analysed for this study, companies belonging to the FTSE4Good were first targeted as this index are advertised as environmentally and socially responsible companies¹⁵⁶. This chapter seeks to determine if these firms engaged in SER not as a form of strategy, but due to their core ethical principles of engaging in SER 'for good'. Further companies were selected from the FTSE350. Heads and Directors of the CSR/Sustainability division of companies were targeted for this research. Similar to O'Dwyer (2002), heads of the CSR / Sustainability Department were targeted, as it was expected that they would have a broader understanding of the whole process of social and environmental reporting as well as a notion of how SER regulation affects their organisation. Data obtained from the interviews were supplemented by other sources, such as the firm's annual reports and media articles, to validate as well as add information obtained from the interviews.

¹⁵⁶ FTSE4Good Index Series (2012). Available from <<http://www.ftse.co.uk/Indices/Industry%20Classification%20Benchmark/index.jsp>> [Accessed 12 January 2010].

Table 6.1 Summary of Firm Interviewees and Basic Information

Respondent Industry Category (FTSE4Good / Non-FTSE4Good)	Position	Years of Experience in SER	Average Spend on SER per annum	Board of directors Involved in SER	Separate SER department
Insurance (FTSE4Good)	Head of CSR	0.2	£25,000+	Yes	No
Gas, Water and Multiutilities (FTSE4Good)	Head of CSR	20	£50,000	Yes	Yes
Media (FTSE4Good)	Corporate Responsibility Manager	4	£125,000	Yes	Yes
Real Estate Investment Trusts A (FTSE4Good)	Head of Corporate Responsibility	15	Unable to quantify	Yes	Yes
Real Estate Investment Trusts B (FTSE4Good)	Director of Corporate Responsibility	4	Unable to quantify	Yes	Yes
Software and Computer Services (FTSE4Good)	Leader of Sustainability Services	1.6	Unable to quantify	Yes	Yes
Aerospace and Defence (Non-FTSE4Good)	Corporate Responsibility Manager	10	Unable to quantify	Yes	Yes
Household goods and Home Construction (Non-FTSE4Good)	Company Secretary	10+	Unable to quantify	Yes	Yes
Tobacco A (Non-FTSE4Good)	Head of Sustainability	20	Unable to quantify	Yes	Yes
Tobacco B (Non-FTSE4Good)	Corporate Responsibility Manager	14	£40-50,000	Yes	No

6.3.2 Data Analysis

The first step of data analysis was to establish the importance of SER to the strategy of the firm. Respondent's statements were each examined for evidence including social and environmental issues being used by firms to for example, enhance or protect the reputation of the firm, or used as a form of competitive advantage. NVivo was also used to help identify words and statements which related to the strategy of the firm; words including competitive advantage, strategy, awards, leader, trust, reputation, and brand. Following this identification, firm's statements were then allocated a score of 1, 2, 3 or 4 based on the level of the statement's strategic input, difficulty of replication, rarity and how valuable that action is to the firm. This technique of allocating scores is as based on the conceptual framework on resources and capabilities as seen in Table 2.1 (Chapter 2). It is also noted that the correct coding of interviews requires that the coder has sufficient knowledge in the subject matter of the interviews (Campbell et al., 2013), thus this study involved the use of three coders, who following extensive discussions to

establish precise coding rules, agreed on identifying the best example on the code for each statement. Finally, after computing the average for each firm's scores, firms were placed in one of four categories as seen in Table 6.2.

Table 6.2 Group Categories for SER Strategy

Group	Description
1	Statements imply that firms actions are devoid of strategic input
2	Statements reveal that firms actions have some strategic input and are valuable to the firm, but are fairly easy to replicate and require minimal action
3	Statements reveal that firms actions have strategic input, are valuable, moderately difficult to replicate, and includes the barrier of financial cost / resources / capabilities / several years (takes time) to implement.
4	Statements reveal that firm's actions have strategic input, are valuable, but very difficult to replicate by competitors, and is expensive, specialised and/or rare.

The second step of the data analysis was to find evidence of firms' attitude to regulation. The main source of data for identifying firms attitudes to regulation were the interviews which were supplemented by other sources such as online news reports and articles. Given the limited research carried out on firms' attitude to regulation, an effort was made to adequately group the respondents appropriately, in order to generate possible explanations for their attitudes. A 5 point Likert Scale was therefore created, which rated firms' statements from highly negative to highly positive attitudes, including a scale for 'indifferent' attitudes; to account for statements in which respondents expressed no preference/dislike for regulation. The rating method is seen next in Table 6.3.

Table 6.3 Rating Method for Firms' Attitude to Regulation

Rating Scale	Description
1	Highly negative statement showing outright opposition to regulation / regulatory guidelines.
2	Negative statement showing a dislike and/ or opposition to current and/ or future regulation / regulatory guidelines.
3	Indifferent statement; respondent expresses no preference/ dislike about regulation.
4	Statements of a positive nature; respondent outlines the benefits of regulation and/ or states support for regulation / regulatory guidelines.
5	Highly positive statements; respondent agrees with and outlines the benefits of regulation and / or states support for regulation / regulatory guidelines; calls for increased regulation.

Following the rating, the average score for each firm was computed. In order to give an equal weighting to each firms ranking, as some interviews tend to be more saturated than others, statistical tests, such as the standard deviation and logarithmic scales were run for both sets of evidence to ensure that there were no significant dispersion in the statements given by each firm.¹⁵⁷ These tests showed no significant dispersion. The results obtained from the analysis of firms' strategic attitudes to SER and regulation, are described in the next section, Results.

6.4 Results

The results as presented in the following figures show details of the strategic attitudes of firms towards Social and Environmental Reporting (SER) and firms' attitudes towards regulation. For firms' strategic attitudes towards SER, firms are ranked according to being more or less strategic towards SER. For firms' attitude towards regulation, firms are ranked according to whether they display a negative, positive, or indifferent attitude towards regulation.

¹⁵⁷ Furthermore, in order to ensure that the evidence obtained from the interviews were viable and to enable us to come to justified conclusions on firms strategic attitudes to SER and regulation, annual reports and / or CSR reports online as well as online news reports and articles were scrutinised for statements relating to the firms use of SER as a form of Strategy and firms attitudes towards regulation. Thus the interviews rankings were corroborated by evidence found in firms' annual reports and other media articles.

Figure 6.1 Firms Strategic Attitudes to SER

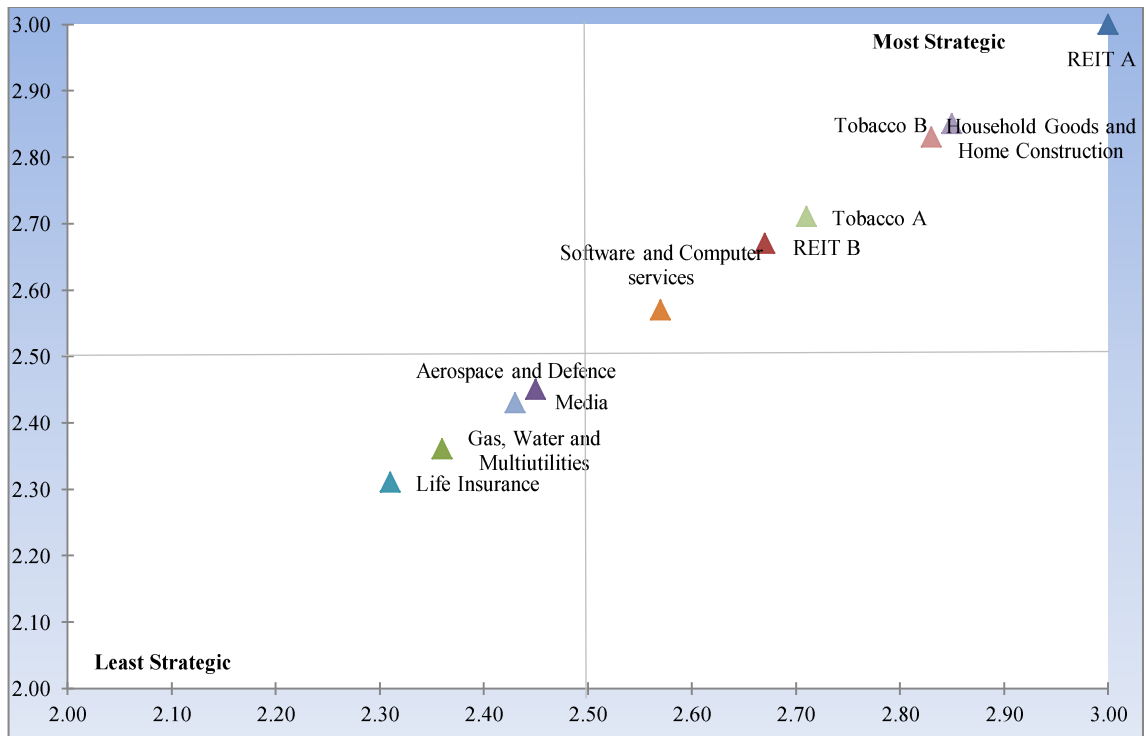
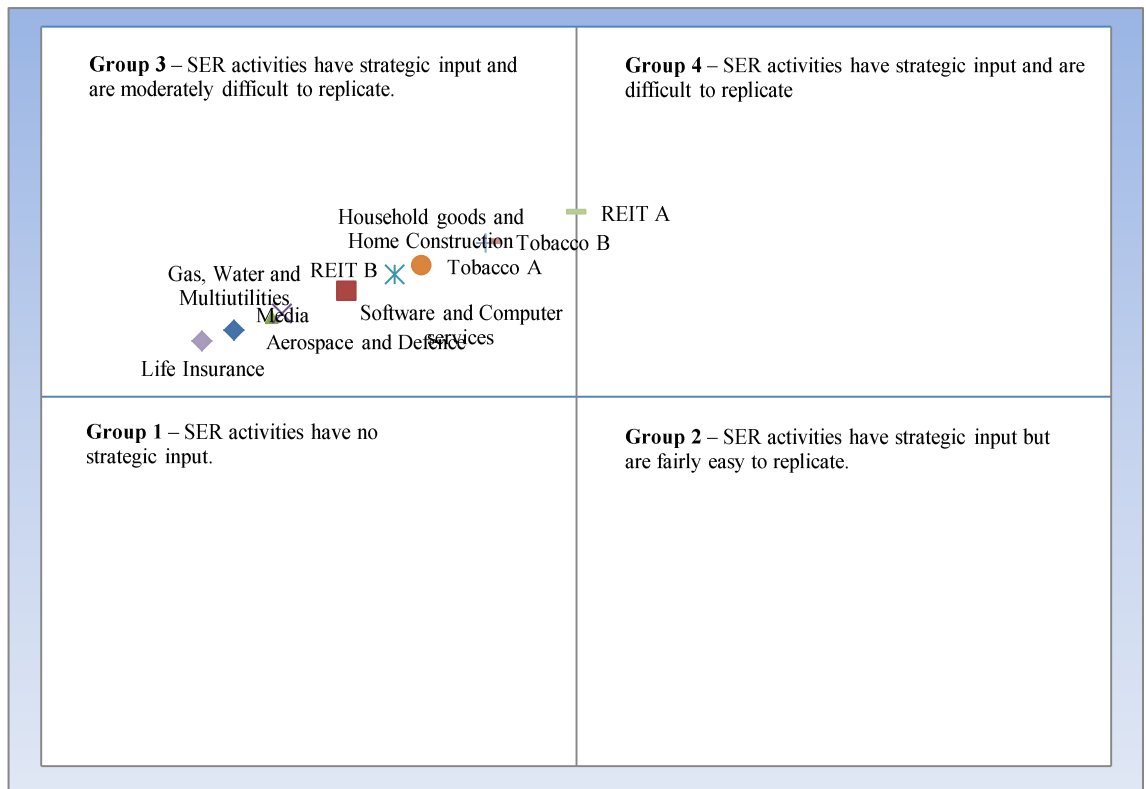


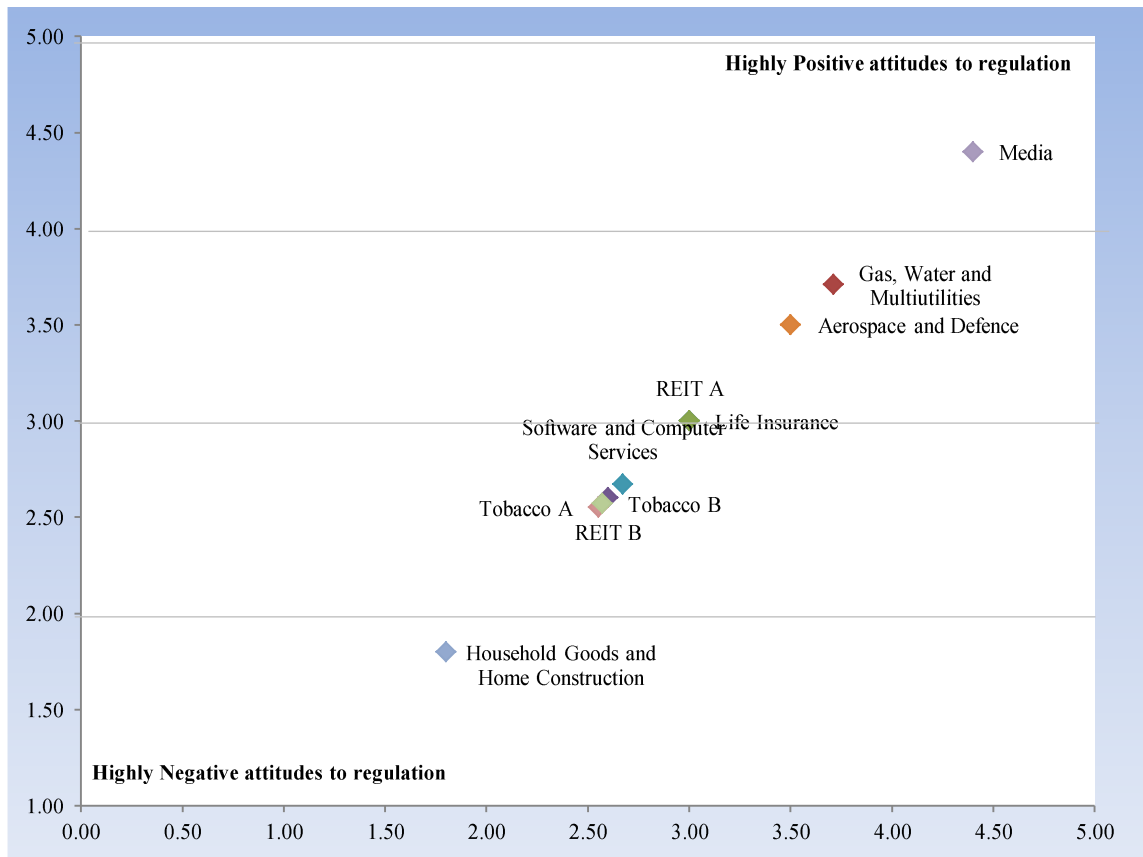
Figure 6.2 Firms Strategic Attitudes - Group Categories



6.4.1 The Use of SER as a Form of Strategy

Looking, firstly, at the strategic attitudes of firms towards SER as presented in Figure 6.1, the results indicate that over sixty percent of respondents display a more strategic attitude, with the other forty percent displaying a less strategic attitude to SER. High on the ranking scale of firms' strategic attitude to SER, is the Real Estate Industrial (REIT) A firm, with Software and Computer services on the lower end of firms displaying a more strategic attitude to SER. The two tobacco firms and the Household goods firm are also identified as being more strategic towards SER. On the other hand, firms that are identified as having a low strategic attitude to SER are Gas, Water and Multiutilities, Aerospace and Defence, Media, and the Life Insurance firm scoring the lowest on firms' strategic attitudes to SER. The difference in the scores allocated to the firms is significant with the most strategic firm, REIT A, receiving an average score of 3, and the lowest strategic firm, Life Insurance receiving a score of 2.31, a notable difference of twenty three percent. Furthermore, the results as reported in Figure 6.2 and based on Table 6.2, show that ninety percent of firms were placed in category 3; suggesting that overall, firms' attitudes towards SER have strategic input and are moderately difficult to replicate. In other words, firms' actions though valuable to the firm, offer a temporary strategic advantage, and are not perfectly inimitable, though competitors may spend several years and / or have to invest in resources and capabilities in them; which in turn could be costly.

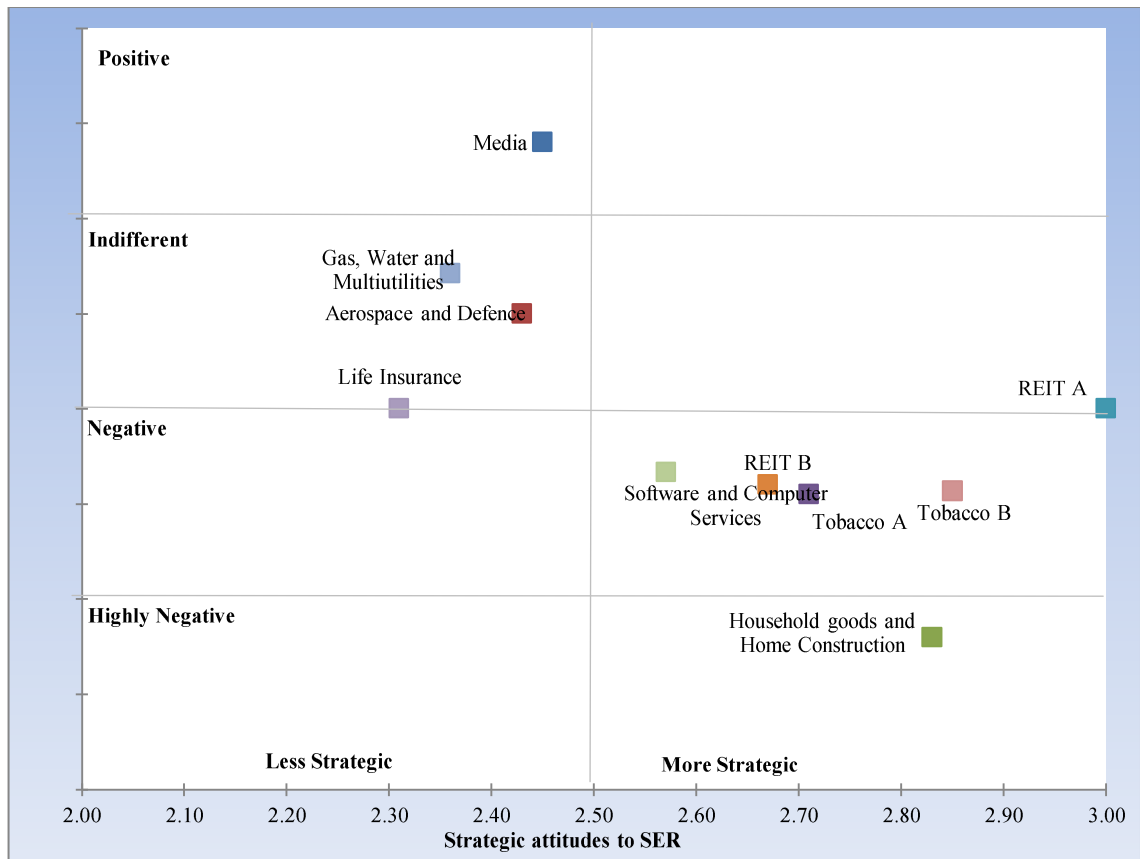
Figure 6.3 Ranking of Firms' Attitudes to SER Regulation



6.4.2 Firm Attitude to Regulation

Figure 6.3 reports firms attitudes towards regulation based on the evidence obtained from the data collected. On the top end of the scale of Figure 6.3, are highly positive attitudes and on the lower end, highly negative attitudes to regulation. From the analysis, the Media industry scored the highest on positive attitudes to regulation. On the lower end of the graph, the Household Goods scored the highest in the highly negative attitudes. In between the positive and negative attitudes to regulation are indifferent attitudes to regulation. Firms that display an indifferent attitude to regulation include Gas, Water and Multiutilities, Aerospace and Defence, Life Insurance and REIT A firms. Firms that display negative attitudes include both Tobacco firms, Software and computer services and REIT B. The difference in the attitudes towards regulation between positive and highly negative attitudes is fifty nine percent, showing how widely firms differ in their attitudes towards regulation.

Figure 6.4 Firms Use of SER as a Form of Strategy and their Attitudes to Regulation



In order to further examine firms' attitudes to regulation and strategic attitudes to SER, these two characteristics were plotted against each other, as seen in Figure 6.4. As none of the respondents showed a highly positive attitude towards regulation, this did not appear on the graph. Figure 6.4 therefore reports that the Life Insurance firm is the least strategic but has indifferent attitudes towards regulation. The Media firm also displays a less strategic attitude to SER but shows a positive attitude to regulation. Furthermore, Gas, Water and Multiutilities display less strategic attitudes to SER, but an indifferent attitude towards regulation.

On the other side of the graph, we have the Household goods and Home Construction firm showing a highly negative attitude to regulation and a more strategic attitude to SER. Tobacco firms as well as REIT B and Software and computer services show a negative attitude to regulation and display a high strategic attitude to SER. It is further noted that all firms which displayed a highly negative or negative attitude to regulation display a high strategic attitude to SER, whilst the firm which displayed a positive attitude to regulation showed a less strategic attitude to SER.

Importantly the main sample of firms chosen belongs to the FTSE4Good index. Based on the findings, the Tobacco, and Household Goods and Home Construction who are all non FTSE4Good all show negative attitudes to regulation with the exception of the Aerospace and Defence who show indifferent attitudes towards regulation. In terms of strategic attitudes to SER, again, the Tobacco and Household Goods and Home Construction (all non FTSE4Good) display more strategic attitudes towards SER with the exception of the Aerospace and Defence firm, which shows a less strategic attitude to SER. On the other hand, firms belonging to the FTSE4Good index had varied strategic attitudes to SER as well as varied attitudes to regulation.

6.5 Discussion

6.5.1 SER as a Strategy of the Firm

As one of the objectives of this study was to find out to what extent SER is a strategic endeavour, this section discusses the evidence as provided by the results. Firstly, based on the four categories in which the firms were placed (Category 1 = SER activities have no strategic input, Category 2 = SER activities have strategic input but are fairly easy to replicate, Category 3 = SER activities have strategic input and are moderately difficult to replicate, Category 4 = SER activities have strategic input and are difficult to replicate), all firms displayed actions that are strategic, and are placed in categories 3 or 4. These results suggest that firms are indeed highly strategic when it comes to SER and are using SER as a way of achieving and or maintaining their competitive advantage in SER. In addition, the cluster of firms concentrated in Group 3 (Figure 6.2), further suggests isomorphism.

Other studies report similar findings that firms are being strategic with relation to SER activities. For example, (Hillman and Keim, 2001) report that there is a useful distinction between the effectiveness of SER activities that are altruistic (such as social issue participation) and strategic (such as stakeholder management), with strategic SER having a positive correlation with financial performance, but a negative correlation with altruistic SER. Furthermore, a report by TobaccoTactics, an online academic resource, states that some tobacco firms engage in setting up campaigns to encourage individuals, companies and local groups to clean up after themselves, in an effort to stage themselves as firms involved in good governance. This TobaccoTactics conclude, is a stark example of firms using SER as a form of strategy. Evidence also provided by

Deloitte Touche Tohmatsu Limited (DTTL) study of Chief Financial Officers (CFO) view on sustainability, suggests that CFOs in a bid to keep up with competition find it important to keep on investing in sustainability, which they believe will eventually help them to gain a competitive advantage (Deloitte, 2012). Moreover, from the results presented, five main themes are determined which display attributes of the VRIN (Barney, 1991) concept, and further explain how firms enact their strategic use of SER. These main themes; Mature systems, Reputation, Stakeholder relationships, Accreditation and Assurance are discussed next.

Mature Systems

In order to maintain competitive strategy, firms must possess the resources as well as the capabilities to invest in SER. Firms that have practised SER for longer tend to have more mature or advanced systems, and are more innovative (Fahy, 2002; MacGregor and Fontrodona, 2008). Some respondents of the sample indicated that they had mature systems which enabled them to manage their SER operations internally rather than outsource this to an outside firm:

'We have been doing this for quite a long time compared to other businesses. So we've got fairly mature systems for covering the information internally. We used external assurance. But other than that we tend to do most of it internally'

Head of Sustainability, Tobacco A

'We report across the whole of the agenda. I think probably the environment has the most robust and mature indicators'

Corporate Responsibility Manager, Tobacco B

Having an in-house SER system and mature reporting systems creates entry barriers. It further enables these firms to stay one step ahead of competitors who will possibly lag behind in the reporting arena, as exemplified by an argument made by a firm located in the left bottom quadrant (see Figure 6.1):

'the main one I suppose would be that traditionally every business is set to report very well on its profits but not so well on its environmental and social costs...And our system might not be set up well enough for it'

CSR Manager, Media

Therefore, it seems that the more strategic firms such as Tobacco A and B are using their resource of mature SER systems to stay ahead of competitors, such as the Media firm, who are lagging behind in this resource.

Reputation

A common argument put forward by firms, for engaging in SER is that SER helps them build and or maintain a reputation with their stakeholders. Engaging in SER is used by firms to enhance their reputation and reputation is used to ward off competition, through vying to be leaders in the SER arenas, obtaining awards, and making themselves known to their competitors as leaders in the field (Dierickx and Cool, 1989; Fombrun, 1996; Galbreath, 2005; Hall, 1992). For example;

'Our vision is to become our customers' most trusted partner. Part of building that trust requires us to play a meaningful role as a corporate citizen, which takes not only commitment, but also dynamic business performance. This is not just good for our reputation - which is built on what we do as part of the communities in which we live and work - but it is also the right thing to do'

Online Responsibility Report, Life Insurance

'Our corporate responsibility strategy creates competitive advantage. It is central to delivering value and to building the best REIT [Real Estate Investment Trust] in Europe'

Online CSR Report, Real Estate Investment Trust A

'Our CR strategy and ambition directly supports Group strategic vision - to be the leading integrated energy company in our chosen markets - by seeking to gain sustainable business success through building trust with stakeholders... A strong reputation for CR can help us win business advantage and contribute to shareholder value. Conversely perceived weakness in CR may damage our reputation and cause financial risks.'

Online CSR Report, Gas, Water and Multiutilities

'We pride ourselves on a good reputation. I personally report to the chief executive on SER issues so this is how important it is to us'

Head of Corporate Responsibility, REIT A

Some companies also use the media to enhance their reputation by circulating information about their achievements in SER, for example, obtaining SER awards. The finding that several of the respondents pride themselves on maintaining a good reputation with stakeholders is supported by empirical evidence from studies carried out by Ljubojevic et al., (2012) and Vilanova et al., (2009). Furthermore, from the evidence provided above, it is clear that firms across all industries are concerned about their reputation and that although some firms are seen as being more strategic than others; reputation is one attribute which all firms are keen to maintain. This chapter however, raises the question that if all firms use SER to maintain a good reputation, how does this allow them to stand apart from their competitors. Should this be seen as a pre-emptive move, that is, if a firm doesn't engage in this form of stakeholder management, there will be negative consequences? The strategic considerations firms make in this context will be picked up again when the level playing field concept is discussed in Section 6.5.3.

Relationships with Stakeholders and Trust

Building relationships and maintaining trust with key stakeholders is also another strategy several of the firms use to ensure their competitive advantage, and ensuring their stakeholders continued interest in their operations. Stakeholder relationships have been identified as a main pillar of a trustworthy SER engagement. Calton and Payne (2003) also state that improving stakeholder relationships means engaging in talk with stakeholders. In addition, Sarah McCarthy-Fry, MP for Portsmouth argued that it makes good business sense for organisations not just to accept SER but to make it central to their strategic decision making, further highlighting the view that more and more, businesses are recognising that SER can bring them a competitive advantage.¹⁵⁸ Collaboration with stakeholders therefore not only leads to greater credibility of SER activities, it furthermore promises positive effects on reputation (Palazzo and Richter, 2005). Thus respondents stated, for example that,

'Our Values, Our Responsibility - Responsibility is central to our sustainable growth strategy – how we behave today impacts our business tomorrow'

Corporate Responsibility Manager, Tobacco B

¹⁵⁸ *Hansard* HC Deb. vol. 447, col. 192, 6 Jun 2006.

‘Corporate Responsibility is helping deliver our business strategy through engaging clients, client focused people, driving client value and delivering value for money’

Leader of Sustainability, Software and Computer Services

Moreover, obtaining stakeholder trust is key to firms as they achieve a common understanding with stakeholders based on transparency, honesty and a deep culture of doing the right thing, and stakeholders are more likely to listen to and engage more openly with a firm they trust. Thus, engaging in SER is one of the key ways firms use to portray their ‘culture of doing the right thing’ to stakeholders. According to one of the respondents, building trust requires a company to explore the challenges and tensions surrounding complex social and environmental issues, and verification of stakeholder engagement is a priority for building trust. The respondent goes on to state that *‘Stakeholders do not necessarily expect companies to have all the answers, but they do expect an open and honest treatment of the subject [SER]’*. This firm also won an award from the Investor Relations Society for ‘Best Annual Report: Most Effective Communication Award for a FTSE 100 company’, showing that engaging stakeholder trust is essential to the going concern of the business.

Additionally, the receipt of awards by firms for engaging in SER spurs them on to improve on their SER activities. These awards sometimes given to organisations that have excelled in the clarity and transparency of their reporting, in essence for ‘telling how it is’, further enables firms to increasingly engage with stakeholders. Thus,

[The benefits of SER are that] ... ‘it drives internal change. It enables you to engage with your stakeholders. It builds trust with those stakeholders’

Head of Sustainability, Tobacco A

This same firm is also a member of the Dow Jones Sustainability World Index (DJSI World) and the Dow Jones Sustainability Europe Index (DJSI Europe) which track the economic, environmental and social performance of companies that have demonstrated that they integrate sustainability into their business. Furthermore, this firm was awarded the first place in a ‘Building Public Trust Awards’, for outstanding corporate reporting and for excelling in the clarity and transparency of their reporting, which certainly enables this firm to achieve and or maintain a positive relationship with their

stakeholders. As evidenced in Figure 6.2, all firms are in category 3 or 4, indicating that they all adopt some form of strategy to SER; though some firms score higher than others. Furthermore, the three quotes above are from firms identified as having a high strategy to SER (Tobacco and Software and Computer Services) and a low strategy to SER (Aerospace and Defence), indicating the importance that *all* firms place on engaging with stakeholders. The relationship between a firm and its stakeholders are therefore the ultimate source of a firm's wealth and its ability to establish and maintain relationships (Post et al., 2002). As firms are aware of this, they are hence keen to achieve and / or maintain good stakeholder relationships, consequently developing the trust of these stakeholders.

Accreditation

Another strategy firms use to maintain competitive advantage is becoming a member of a recognised group or achieving certification from an international organisation, such as the International Organisation on Standardisation (ISO) or the Global Reporting Initiative (GRI). These accreditations are normally displayed on company websites. For example;

'Achieved an A+ rating in Global Reporting Initiative's (GRI) Sustainability Report...GRI's A+ rating is an extremely proud moment for us'

Online Press Release, Media

'This is our third year of reporting and we have reported at the B+ applicable level, which has been assured by PricewaterhouseCoopers. To demonstrate our application of GRI guidelines we have cross-referenced our sustainability reporting to the guidelines'

Head of Corporate Responsibility, REIT A

'Fulfilling consumers' demanding tastes while meeting rigorous standards. This has led to the factory's ISO 9001 certification...Our companies' laboratories work to high standards and many have scientific methods accredited against ISO standards'

Head of Sustainability, Tobacco A

Again, the quotes provided above are from firms across all industries, implying that firms believe in the value of accreditation. This form of strategy is therefore not

displayed solely by the more strategic firms but also by the less strategic firms. The evidence that firms regard assurance as valuable is further supported by the findings of Falkenberg and Brunsæl (2011) who suggest that firms which did not have a CSR/Sustainability certification would be at a disadvantage. According to their report, one of the Directors interviewed, acknowledged that survival of a firm producing coffee (because of issues related to the production of coffee) is dependent on the firm engaging in ethical trade, and in particular certification from a third party. Firms also took pride in mentioning awards they have received for engaging in SER and thereby “standing out from the crowd” which this chapter argues, is a strategy utilised by firms to stay ahead of competitors as awards can only be given to a chosen few. For example;

‘Also, awards are given to us. For e.g. Sainsburys, Barclays, Zurich have been receiving awards and so have we. The awards are substantial. Indeed there are lots of awards. In 2010, we applied for and were awarded the prestigious BitC CommunityMark award’

Director of Corporate Responsibility, REIT B

Jones and Bartlett (2009) findings further highlight the importance that firms place on receiving awards, with Deegan and Carroll (1993) suggesting that winning an award provides firms with a favourable effect in the market.

Assurance

The assurance and auditing of SER reports as well as announcing it on websites and in annual reports is another strategy that firms are using as a form of competitive advantage. Morimoto et al., (2005) argue that developing an applied SER auditing procedure will be a challenging task. As firms are thus not legally required to audit their social and environmental reports (under the Enhanced Business Review requirements), auditing and assurance can be touted as being proactive and portrays the firm in a positive way. Several firms in the sample did indeed mention their firms’ engagement in auditing or getting external verification for their SER reports. For example;

‘We feel that it’s more important to focus on getting accurate complete and consistent data. And we focus very hard on getting our data verified and assured’

CSR Manager, Media

'I suppose the other thing that is quite big at the moment is also how much investment you're giving to things like assurance, and how important that is on stakeholders. So yes there is financial commitment of one, of your resource, but also things like assurance.'

Managing Director, Corporate Responsibility, Aerospace and Defence

'Our highest cost is around assurance. We used external assurance'

Head of Sustainability, Tobacco

Again, the quotes provided above are from firms across all industries, implying that firms believe in the benefits and value of assurance. The report by KPMG (2011) also suggests that a growing number of firms are now engaging third party assurance professionals to assess and verify their Corporate Responsibility (CR) reporting controls, a result of companies making quality improvements, based on external validation and review. Around a third of G250 firms¹⁵⁹ surveyed cited the ability of assurance to reinforce the credibility of CR reporting within stakeholders and investor groups.

In summary, all five attributes as discussed above, namely, Mature Systems, Reputation, Relationships with Stakeholders and Trust, Accreditation and Assurance provide evidence that SER is being used as form of strategy by firms. Again, competition is rife in the Corporate Social Responsibility institution and firms have to keep finding clever ways of staying ahead or in the game.

6.5.2 Firms Attitudes to Regulation

One interesting aspect of this study is the analysis of attitudes to regulation. The results provided evidence that contrary to the perception, and previous studies, that firms have a negative attitude towards regulation, in reality there are also positive as well as indifferent attitudes to regulation. This study therefore determined three main different attitudes to regulation.

Firstly, the Household and Goods firm displayed a highly negative attitude to regulation stating;

¹⁵⁹ The largest 250 global companies based on the Fortune Global 500 ranking.

'[Regulation] requires an ever increasing amount of work to produce a document which can be reviewed by outside advisers and shareholders each year...it does mean an additional cost to business...I think the problem with people that actually are involved in the drafting of legislation, the politicians, that they are sitting in an ivory tower and really do not understand sometimes the law of unintended consequences...and the unnecessary cost and burden that regulation can place on companies'

Group General Counsel, Household goods and Home Construction

From this statement, the respondent is mainly concerned about the cost that regulation imposes on them. He is so concerned with cost when others aren't; and seems to perceive fewer benefits from complying with regulation, with the cost/benefit ratio of regulation being negative for him. With the lack of progress in the Household Goods industry in the last 18 months, the increase in raw materials costs continuing to be an issue, and increasing house prices, it follows therefore that the firm might be more interested in allocating resources to more pertinent issues than complying with regulatory requirements. This state of affairs could also be linked to the REIT B firm who also displayed a negative attitude to regulation.

Both Tobacco firms also displayed a negative attitude to regulation and did not welcome it, stating for example;

'Government has provided adequate guidelines - No, and they don't need to. No, because there are other organisations, better placed organisations doing that. I think we're happy where things are. So maintain the status quo...we've been led by a voluntary approach and followed good practice guidelines. So we kind of feel we've followed voluntary good practice and regulation is almost catching up behind that'

Corporate Responsibility Manager, Tobacco B

'So it's a very subjective area. I don't think it lends itself to, necessarily to hard metrics. So what would the government mandate? It will just end up being a one size fits all, and it's unlikely to be useful. It will be lowest common denominator. So I'm not sure government intervention in that area is very helpful, other than maybe provide some guidance that companies ought to report on their key

issues, rather than trying to hide them, or obfuscate them. They should be talking about the major sustainability issues that face their business'

Head of Sustainability, Tobacco A

Tobacco A and B indicate that regulation isn't required as they are going over and above the requirements, hence their obvious dislike of regulation. However, it is questioned why these firms are worried about regulation if they are already doing more than required? It may be that new regulation may require them to report on issues they are currently not reporting on, or that new regulations will enable other firms to catch up on their current levels of reporting and lessen the perceived quality of their own reports; hence their concerns. Furthermore, Tobacco firms are under the media spotlight with several documentaries on them for blatantly putting the lives of their workers including children at risk. These documentaries bring their operations under the spotlight which may result in more stringent regulation being imposed on them. On the other hand the firm which displayed a positive attitude towards regulation is the Media firm. Whilst media firms are generally not under the spotlight as are Tobacco firms, other reasons such as lack of clarity in SER regulations and the need for more guidelines, could account for this positive attitude.

From the evidence on firm's use of SER as a strategy and firms attitudes to regulation, the hypothesis set out to test if firms which displayed a negative attitude towards regulation display a high strategic attitude to SER. The findings provide evidence that this is indeed the case. The findings indicate that the both Tobacco firms portray a negative attitude to regulation. These firms compete in a market for products that have been identified as harmful to public health and therefore see strategic value in SER reports in order to improve their public image, a notion that will be returned to when considering the level playing field concept. Tobacco firms also compete in a highly regulated market, and therefore may use SER as a device to distinguish itself from their competitors, as well as an argument to deflect further regulation from being imposed on them. REIT B also displayed a negative attitude to regulation, which may be due their frustration at the current regulatory system;

'Regulation has been made complex for all companies. It is a giant issue for us...The Government has [also] not provided adequate guidelines on the amount and direction on how to report on our SEI [Social and Environmental issues]

effectively. I spent 16 years as a politician and there is a lot of ignorance from MP's. This is because maybe they have not spent time in business. As individuals they aren't so developed in their understanding. These are because the issues aren't important to them

Director of Corporate Responsibility, REIT B

Furthermore, the attitude shown by the REIT A is interesting as it is a firm whom this chapter determines, is the most strategic of all the firms; but has an indifferent attitude to regulation. It is noted however that this attitude although indifferent, is closer to negative. This attitude displayed by REIT A may in part be explained by the unhelpful regulation and lack of clarity of regulation as evidenced:

Obviously it [regulation] does have some effect on our reporting, but I would think probably other benchmarks and guides have more effect

Head of Corporate Responsibility, REIT A

Furthermore, an indifferent attitude to regulation was displayed by the Gas, Water and Multiutilities, which is again attributed to the lack of clarity in regulations;

'To be honest we don't even look at it...you know...we obviously are aware. But we don't really look at the government guidelines [or regulation] because we just instinctively report as much as we feel is absolutely necessary for our audiences'

Head of Corporate Responsibility, Gas, Water and Multiutilities

Based on the above analysis, it is argued that regulation does not seem to be used by firms directly to gain a competitive advantage. This is due to the diverse attitudes displayed by the respondents. Also Media who displayed a positive attitude towards regulation indicates that regulation lacks clarity and therefore more guidelines are needed. Therefore, the use of regulation as a form of competitive advantage, may only work in situations where regulations are more streamlined and properly clarified, in effect allowing all firms to take advantage of the level playing field regulation offers. Leading business thinkers also suggest that mandatory environmental regulation is necessary for companies to be pushed into action for several reasons including to level the playing field in order to ensure that a company cannot gain a competitive advantage by avoiding environmental improvements (Frynas, 2012). Furthermore, the lack of

support of regulation by firms (considering only ten percent of the sample displayed a positive attitude to regulation) could be directly linked to the Confederation of British Industry's (CBI) (who represent over 250,000 businesses) argument that regulation imposes restrictions on firms and exposes them to unfair competition in the market, lending credence to their strong lobbying activities and the argument that they have contributed to convincing Government to adopt a deregulation stance. There is thus a weak relationship between SER and regulation, as some firms are of the view that the regulatory system is inefficient, and hence resort to concentrating on increasing their strategic use of SER.

6.5.3 The Level Playing Field Concept

In testing the hypothesis, this chapter sought to find out if firms which express a negative attitude to regulation display a high strategic attitude to SER. Regulation offers firms a level playing field. As stated by the then Minister for Industry and the Regions, Margaret Hodge, *'Good businesses recognise the importance of good regulation and they want a clear, well-defined level playing field so that they are not at a commercial disadvantage if they do the right thing'*¹⁶⁰. Furthermore, Mr Hall, MP for Bedford stated, *'What we are trying to create through the Bill, perhaps as amended, is a level playing field to ensure that they are not disadvantaged for giving emphasis to these important matters'*.¹⁶¹ Hence to test the hypothesis, this chapter further adopted the level playing field concept and applied it to the evidence on firms' attitudes to regulation and strategic use of SER. Consequently, it was determined that there are two separate considerations for firms' attitudes to regulation which is displayed in their strategic attitudes towards SER.

The first consideration is displayed by a group of firms who are **against** the level playing field regulation offers. These are firms who are very confident in their operating SER systems, and therefore do not wish competitors to be able to create these reputational assets easily. Introduction of binding regulation and guidance would inevitably speed up the adoption of good SER practice and narrow the gap to the leaders in the SER field, thereby jeopardising their competitive advantage. Thus, a firm that already has a good reputation has an incentive to argue against the level playing field

¹⁶⁰ *Hansard* HC Deb. vol. 447, col. 216, 6 Jun 2006.

¹⁶¹ *Hansard* HC Deb. vol.450, col. 763, 17 Oct 2006.

that regulation provides, in order to maintain their competitive advantage that they gained through experience and establishing mature SER systems. For example;

'The right thing to do to help drive transparency, to help build reputation. But also to drive internal change. So I think any well run business, if you've got to a certain size, it's probably a good thing to do. You don't need a regulator to tell you to do it; you should be doing it because it's good for business, good for your business'

Head of Sustainability, Tobacco A

These firms want to maintain a competitive advantage, and remain leaders in the SER field, hence to prevent competitors from catching up and assuming that leadership position. They thereby portray confidence in being ahead of reporting requirements. Another reason for this level of confidence displayed by such firms could be attributed to their strategy of trying to deflect any further regulation from being imposed on their operations (Deegan and Blomquist, 2006; Moon and Vogel, 2008).

Firms that fall in this category were both Tobacco firms who scored highly on the use of SER as a strategy to the firm, and had negative attitudes to regulation. REIT B also fell into the category of more strategic and a negative attitude. Regulation will make these firms more susceptible and cause them to lose their competitive advantage. Thus the hypothesis is supported by the results which indicate that firms which display a negative attitude towards regulation show a high strategic attitude to SER. Furthermore, the attitude displayed by the Tobacco firms reinforces the notion that firms tend not to be adequately punished for non-compliance with regulation, and as such display an attitude indicating that SER regulation is not important. Their focus is rather on how to improve their competitive advantage through the use of SER, as non-compliance with SER could elicit retribution from the market. Furthermore, these findings strengthen the notion that firms engage in SER mainly for strategic purposes and not out of pure ethical endeavours; with all FTSE4Good firms sampled classified as Group 3 or 4 (Figure 6.2).

The second consideration is displayed by the second group of firms who are **for** the level playing field. These firms voiced their opinions by calling for more guidance and a better regulatory system. These firms displayed both a positive attitude to regulation and a less strategic attitude to SER, supporting the notion that if a firm has a positive

attitude to regulation, it displays a less strategic attitude towards SER. Additionally, other firms in this group also displayed an indifferent attitude to regulation as well as a less strategic attitude to SER (excluding REIT A). Some firms spoke about their desire to be able to equalise and compare reports with competitors for example;

'With regulation...I can compare how our business is doing with our competitors because we are all using the same metrics....we are all reporting our profit according to the same rules....we all disclose how we make profit and we can make a comparison in a benchmark...Regulation is needed to....at least that the way we report and disclose is consistent and comparable'

CSR Manager, Media

Vilanova et al., (2009) also argue that although SER is considered critical for companies due to the 'license to operate' mentality, it was rarely measured or evaluated due to the lack of a common framework for SER and competitiveness. According to their study, participants stated that SER apparently lacks organisational leadership to guide the process, as NGOs do not have the resources, public organizations do not want the responsibility and businesses do not have the legitimacy. Henriques (2010) also suggests that there is a significant lack of clarity in what companies are legally required to report, hence some respondents indicating the lack of clarity in regulatory guidelines.

Other firms in this 2nd group, had a negative view of companies who were greenwashing and or engaging in selective reporting. For example;

'So many companies think that they can pick and choose what goes into a report and then this is ...this unwritten principle that it needs to be balanced. I think more companies do need to be balanced and bear in mind that they can't just report all the good things particularly if they want investors to have a really good view of what they are doing and how they are addressing the gaps'

Head of Corporate Responsibility, Life Insurance

'I think engaging in SER is useful, but you can see companies that do it very, very well. And you can clearly see, demonstrated through the content and through the data that they use, that it's related to business strategy. And you can see why they are priorities for the company. I think where it goes into a bit more murkiness is where people are using it more as a corporate brochure. And it's

not integrated into their system, or how they do things. So I think reporting of the social and environmental issues is good, but as long as it is related to the business, and not just seen as a brochure/selling opportunity'

Managing Director, Corporate Responsibility, Aerospace and Defence

'We think that it is very important that they increase their amount of regulation in this area.....Because at the moment we are seeing insufficient action from companies themselves as well as from investors to make any significant progress on this'

CSR Manager, Media

These firms indicate that they would like a level playing field in order to be able to catch up with their competitors and leaders, thereby asking for more guidance. Falkenberg and Bransael (2011) further argue that firms will always be looking at competitors in order to keep up with trends, monitoring and analysing their competitors' activities in order to compete.

In addition, strategic isomorphism is displayed here as firms tend to copy each other and look to each other for guidance, rather than the Government;

'But to be honest I wouldn't necessarily look to the government for, once it's not mandatory... for guidance. I would look to my network of CR professionals and accounting professionals. I would look to the big four, for their guidance or other accounting firms and I would look to peer organisations and what they are doing'

Head of Corporate Responsibility, Life Insurance

Moreover, these second group of firms seem to seek a set of binding reporting requirements in order to prevent competitors from greenwashing their reports and thus gaining an unfair reputational advantage versus firms that more genuinely engage in SER. Our findings are supported by Spence and Gray (2007) who also give an example of a respondent who indicated that 'it would be nice to see a more level playing field where others who are not reporting at the moment are required to...to not just free-ride on our efforts' (p. 60). In addition, The Times reported that firms were getting frustrated as following good practices and pursuing good environmental, social and community issues, but that their competitors were not doing so, due to the lack of a level playing

field on ethical practice. Regulation on the business review will therefore resolve these issues.

Therefore in analysing the level playing field concept, it is determined that only few firms in the sample supported the implementation of better regulatory guidelines in order for them to improve their SER, highlighting the CBI's argument that SER legislation would constrain business activity and reduce SER to a lowest common denominator. Also the firms seeking more regulation are located in the bottom left quadrant (Figure 6.1), whereas firms arguing against regulation are located in the top right quadrant (Figure 6.1), giving a clear indication of the strategic considerations at stake here, as well as the strategic isomorphism at play here by these two groups. While the implementation of good SER routines by firms has been hampered by the ever changing SER regulatory system, those that have, in their own eyes, achieved a mature and advanced SER system for example, are loath to give up their advantage.

6.6 Conclusions

This chapter advances literature by shedding light on the strategic attitudes of firms to SER but most importantly giving further insight into firms' attitudes towards regulation, an area previously under researched in literature. Using robust analysis on the interview data obtained, the results provide strong evidence that firms differ in their attitudes towards regulation and strategic attitudes towards SER, with firms displaying different characteristics based on their competitive / strategic position and their chosen industry.

Furthermore, based on prior studies, it is determined that the relationship between SER and competitive advantage is synonymous as firms have increasingly recognised the benefits of engaging in high levels of SER. Again, using robust analysis on the evidence obtained, strong evidence is provided showing that firms are using SER as a form of strategy. Firms are however diverse in their attitudes to regulation though only ten percent of the sample expressed a positive attitude to regulation. These results indicate that firms do not perceive regulation to be of importance as it is seen as inefficient.

Hence firms rather resort to concentrating on increasing their strategic use of SER. Also, the regulatory system has resulted in strategic isomorphism with firms resorting to benchmarking and consulting with their peers on their SER reports. The hypothesis that

firms which show a negative attitude to regulation display a high strategic attitude to SER is also strongly supported by the results. For those firms that showed a positive or indifferent attitude to regulation, this was attributed to the lack of clarity and confusion which leads them to call for more regulation, as well as the lack of matured SER systems to enable them improve on their social and environmental reporting.

The attitude of firms that displayed a negative attitude to regulation was attributed to these firms taking advantage of the lack of adequate regulatory systems and opposing more or improved regulations as it is possible that regulation and regulatory guidelines would help other firms catch up on effective SER reporting effectively; resulting in the loss of their competitive advantage. These firms, such as Tobacco firms, were far advanced in their SER reporting and had a high strategic attitude to SER. In sum, although the EBR contributed to an increase in the quantity and quality of firms' SER, this chapter has demonstrated that firms are also using SER as a form of strategy. Chapter 7, the concluding chapter, now presents and discusses the summary of the main findings of the thesis, policy implications as well as the limitations and future avenues for research.

CHAPTER 7

Chapter 7 . Conclusion

7.1 Introduction

The changes in the development of SER regulation, in particular the removal of the Operating and Financial Review (OFR) and the implementation of the Enhanced Business Review (EBR), highlighted the role of lobbying channels in regulatory processes. Prior studies found that lobbying had an impact on the changes that occur in regulatory processes (Kirsch and Day, 2001; McLeay et al., 2000; Tutticci et al., 1994; Zülch and Hoffmann, 2010). To date however, whilst prior studies have examined the impact of lobbying on regulation, no empirical research has been carried out investigating the impact lobbying had on the changes leading to the implementation of the EBR. In addition, literature has failed to examine the nature of the groups involved in lobbying, in particular examining their ideologies and the mechanisms by which these groups lobby.

The purpose of this thesis was therefore to unravel the events which led to the removal of the OFR and the implementation of the EBR; and in the process identify the groups which were most involved in and influential in these changes. Furthermore, this thesis identified the impact the EBR had by comparing the levels of reporting of two indices: firms listed on the FTSE4Good and those not listed on the FTSE4Good. Thus, given that there is a now, yet another, SER regulation, the Strategic Report and Directors' Report (2013), it is important that the impact of lobbying in regulatory processes is investigated, as well as the impact of how regulation impacts on firms' attitudes towards SER. To examine the role of regulation in SER, and provide first evidence of the impact of lobbying in SER regulation, this thesis developed three research questions. The research questions are:

1. How did pressure group lobbying impact on the removal of the OFR and the implementation of the EBR?
2. What is the impact of the EBR on firms SER in annual reports?
3. Why do firms display a strategic attitude towards SER and regulation?

This chapter proceeds as follows. In the next section, 7.2, a summary of the main findings of this thesis are presented. Section 7.3 discusses the policy implications.

Section 7.4 then discusses the research limitations as well as gives direction for future, potentially fruitful, research avenues.

7.2 Summary of Results

This thesis presented a detailed analysis of the role of regulation in SER, with a particular focus on lobbying and on the strategic attitudes of firms to SER regulation. Chapter 2 provided a review of the extant literature, showing how there is a growing awareness of the development of SER regulation, as well as how regulation is impacting on firms attitudes and behaviours towards SER. Chapter 3 presented the data sources and methodology adopted in this thesis. The thesis then examined the three research questions in empirical chapters 4, 5 and 6. In the next section, the main findings of these three empirical chapters are presented.

7.2.1 Lobbying and SER regulation

Chapter 4 examined the influence that pressure groups exerted in the removal of the OFR and implementation of the EBR. The chapter further explored the relationship between regulation and strategic SER. The findings provide strong evidence that pressure group lobbying had a significant impact on the removal of the OFR and the implementation of the EBR. In particular, contrary to findings by Rowbottom and Schroeder (2014), the chapter discovers that the CBI was instrumental in pressuring the government to delay the implementation of the mandatory OFR. Furthermore, the chapter presents evidence showing that the FoE and other NGOs such as CORE were instrumental in the changes which occurred leading to the implementation of the mandatory EBR. Consequently, in answering the overarching research question, the findings reveal, in line with Jupe (2000) and McLeay (2000), that lobbying has a significant impact on the changes which occurred in regulation. The findings further reveal that the legal process instigated by the FoE was instrumental in the changes which eventually led to SER regulations being reformed; thus supporting the concept that SER regulation is influenced by political ideology and the effect of ideological influence is framed by regulatory preferences.

It was also suggested in Chapter 4, that the power of business in lobbying is nuanced and therefore in order to duly examine the extent of lobbying by businesses, it is important to analyse as much information and as many sources as possible.

Furthermore, the argument that strategy and competitiveness is an aspect of firms' behaviour towards SER regulation is discussed. Finally evidence of the political economy theory of regulation is presented in this chapter, showing how organisations protect their self-interests, and will seek to deflect further regulatory burdens from being imposed on their operations.

7.2.2 The Impact of Regulation on SER

Chapter 5 analysed the impact of the EBR on firms SER. The chapter carried out a statistical comparison between firms listed on the FTSE4Good and firms not listed on the FTSE4Good (non-FTSE4Good). It also distinguished between voluntary and mandatory regulations, in analysing results, a technique which tends to be ignored by previous literature. Further the chapter examined whether firms characteristics had any impact on SER disclosure. The findings of this chapter provide strong evidence showing that the implementation of the EBR resulted in an increase in the quantity and quality of SER in firms' annual reports. These findings are in line with a report published by Deloitte (2009), which states that the EBR resulted in an increase in the quantity of SER disclosures.

Furthermore, Chapter 5 reveals that there is no statistically significant difference in the reporting levels between the FTSE4Good and the non-FTSE4Good; results consistent with other studies (for example, Clacher and Hagendorff, 2012; Collison et al., 2008). However, it is also revealed that when it came to voluntary reporting, the FTSE4Good did indeed *differ* and their voluntarism had an impact on reporting on social and environmental matters, showing it to be significantly greater than the non-FTSE4Good. Hence this finding may help ethical investment decisions by providing evidence on the reporting performance of FTSE4Good firms relative to others. Moreover, the chapter argued that firms are using SER as a form of strategy, a concept which was explored in detail in the next empirical chapter, Chapter 6.

7.2.3 Regulation and SER – The Strategic Attitudes of Firms

It is important that the relationship between firms' strategic use of SER and attitudes towards regulation is examined, as well as the effect that the regulatory system has on firms. Chapter 6, the final empirical chapter, therefore explored the concept that firms which portray a strategic attitude towards SER exhibit a negative attitude towards

regulation. Exploring this concept with the use of interviews, the findings reveal that firms are increasingly using SER as a form of strategy, results consistent with Clulow et al., (2003), Falkenberg and Brunsæl (2011) and Vilanova et al., (2009). More so, the findings reveal that firms which have adopted a high strategic attitude to SER display a negative attitude to regulation. This finding can thus be linked to the argument as put forward by the CBI, implying that the opposition to regulation by some firms could be founded in their desire to deflect further regulation and hence act more strategically in their SER endeavours. On the other hand, there were also some firms which display a positive attitude to regulation. These firms recognised that regulation provides a level playing field and hence with its implementation, they will be better placed to compete effectively in the SER field.

Overall the results provide empirical evidence of how lobbying channels were used in the implementation of mandatory regulations. Furthermore, evidence is provided showing how regulatory processes can impact on the attitudes of firm's towards SER and regulation.

7.3 Policy Implications

The results of this thesis provide strong evidence of the impact of lobbying in regulatory processes. As seen from the FoE's successful use of legal channels, legal processes can therefore be pertinent to regulatory processes. Indeed Dal Bó (2006) argues that the determination of regulatory outcomes is not solely controlled by regulators ... and that in fact, the courts may affect outcomes because firms, regulators and legislators interact under the shadow of an eventual court intervention (p. 219). Hence the FoE is successful in getting the government to review SER requirements, by invoking existing legislation to prevent any dilution of regulation; further showing that the biggest influence on future regulation is past regulation. In addition, both regulatory and voluntary approaches to SER, lead to greater disclosure for some firms, doing so in an incremental fashion. This incremental fashion therefore implies that the regulation that some firms tried to prevent was nevertheless mostly complied with effectively.

The results also draws attention to the need for SER managers to be bolder in embracing regulatory processes, and in the meantime press for the development of clearer standards and / or guidelines for social and environmental disclosures that can have an

influence on the firms' reputation and its relationships with its stakeholders. Furthermore, it is suggested that in a bid to ensure better relations between firms and NGOs, to reduce misconceptions, more dialogue is needed between these groups. As stated by Anne Snelgrove, MP, NGOs should work with companies rather than stand outside and throw brickbats at them, as when they work with companies, they may find that the views of companies have changed and things are going differently.¹⁶² Although Baron (2001) notes that NGOs are increasingly abandoning the legislative process in favour of direct engagement with corporations, it is suggested that more needs to be done in a bid to improve relations. Thus, businesses need to improve on their interaction with NGOs as the interview evidence reveals that firms are not proactive in dealing with NGOs. Regulators also need to help firms improve their reporting levels by offering more guidance; as businesses have called for increased clarity in the regulatory guidelines provided.

In addition, based on the evidence, it is advised that Government needs to improve on the level playing field that regulation offers and involve firms more in regulatory processes. Some firms are taking advantage of the lack of a "clear, well-defined" level playing field to achieve a competitive advantage, whilst other firms are "left out of the loop", unsure on how to progress with their reporting.

Government consultations on narrative reporting do not seem to be working effectively as firms and NGOs equally complain that their concerns are not listened to. As Baron (1997) emphasises, effective government relations efforts enable firms to control their competitive advantages, and, in effect, build market share, sales growth, and profitability. Gallhofer and Haslam (2007) further advocate for green accounting to be open, accountable and properly subject to a democratic process. Therefore, it is important that changes are made in this area. Again, as much as an applied SER auditing procedure is a challenging task, it should be legally required, as it is possible that SER auditing can be implemented (Morimoto et al., 2005). Managers are also advised to push for further guidance on improving their SER and not just use SER as a strategic move as it is possible that regulation could become more streamlined and erode their competitive advantage, if they are not prepared for it.

¹⁶² *Hansard* HC Deb. vol. 447, col. 179, 6 Jun 2006.

7.4 Research Limitations and Directions for Further Research

In identifying the contributions this research makes, it is important, as with any research, to acknowledge key limitations. First, the generalisability of the findings as presented in Chapter 4 is limited due to the partial evidence obtained from the data sources. In particular, the responses submitted with regards to the Business Review are few, which limits the inference to its significance in impacting the amendments. This may also lead to bias in the submitted documents as only those firms with a certain agenda would respond. In this regard, it is likely that the more public spirited organisations were more likely to submit responses to the Business Review consultation. Nonetheless, the comments submitted have provided an insight into specific commentators' views on the Business Review. Publicly available documents also do not always tell the 'behind the scenes' stories, thus reducing the verifiability of the integrity of the data. Nevertheless, the combination of interviews and examination of archival documents, coupled with the evidence collated from the parliamentary debates, discussions in parliament and media articles, has provided insight into the lobbying process and its influence on SER regulations.

In addition, there is a non-response bias as some potential interviewees are more likely than others to participate. In this regard, a complete picture of opinions may not have been given, leading to the lower impact of the generalisability of the information received from the interviews. Furthermore, it is possible that the interview participants who responded had an interest in publicising their opinions and sought to enhance the reputation of their organisation. Thus, interviewees may have been less than candid in the opinions they expressed and attempted to express views which are perceived as socially desirable and representative of what they believe the interviewer wishes to hear (Saunders et al., 2000). The results therefore have to be interpreted with caution, bearing in mind that the interviewee may not fully represent the objective truth. Nevertheless, with the use of triangulation, that is using a diverse range of sources, including media articles, parliamentary debates and consultation processes, the reassurance is given that the research questions have been adequately answered.

Second, in Chapter 5, the categories chosen for the study, namely Environment, Employee, Consumer/Products and Community, are limited to the categories contained in the Enhanced Business review requirements, as well as limited to the pre and post

EBR period. While a more comprehensive consideration of social and environmental reporting items may be needed, there is difficulty in identifying all sources of firm disclosure. Furthermore, whilst annual reports are known to be an influential and valuable communication medium for reporting information, it is possible that the information provided in them may contain subjective information in an attempt to convey a message or influence others point of view. Moreover, the chapter utilises only a subsample of the whole population of the FTSE firms, highlighting the issue of selection bias, and hence these results may not be representative of the entire population.

Third, in Chapter 6, the generalisability of the findings is limited by the small sample size. In this regard, the firms interviewed may not be representative of the population, as other sectors or industries did not respond to the request to take part in this study. The results however include eight industries and provide further insight into the strategic use of SER in these industries, as well as their attitude towards regulation.

Further Research

The limitations provide avenues for future research. First, Chapter 4, which examines the role of lobbying, provides a contribution through the choice of subject. The issue of narrative reporting has not only been a source of past controversy, but still remains controversial. As recently as October 2013, a new regulation for SER was implemented, The Strategic Report and Directors' Report. This mandatory regulation was a result of the Coalitions promise in 2010 to re-introduce the OFR. Although the OFR was not eventually reintroduced, it is pertinent to draw attention to the fact that in only eight years, four different SER regulations have been introduced. Hence the subject of lobbying and power relations, as well as the influence exerted by pressure groups, remains relevant to current regulatory activities on narrative reporting. In short, the focus of Chapter 4 is relevant to present-day activities on narrative reporting and regulation, and as such this research perspective is of interest, not only for future accounting research, but also for political or social sciences. Further research could therefore focus on the comments submitted on the Strategic Report and Directors' Report consultation, in order to determine the impact that lobbying had, as well as the influence exerted by key persons, in the amendments and the language of the final enacted Standard.

Second, it is of importance that the trends in the quantity and the quality of reporting are monitored, to help evaluate the effectiveness of regulation. Further research could therefore analyse firms' SER disclosures before and after the introduction of the Strategic Report and Directors' Report, preferably on a larger sample. As evidence suggests that there was hardly any opposition to the introduction of this new SER regulation (based on consultation documents submitted (BIS, 2012)), it will be interesting and of benefit to literature and practitioners to examine the extent of firms adaptation and compliance to this new narrative reporting requirement.

Finally, it would be of interest for further research to focus on obtaining views on firms' attitudes towards the new Strategic Report and Directors' Report and determine whether firms' attitude towards regulation has changed; as it is clear from evidence presented in the empirical chapters, that firms' strategic use of SER is here to stay.

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