

CORPORATE SOCIAL RESPONSIBILITY REPORTING: A BUSINESS STRATEGY BY AUSTRALIAN BANKS?

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Abstract

The growth of voluntary corporate social responsibility (CSR) reporting reflects society's expectations for business to set higher ethical standards and to undertake business in a way that meets the profit imperative (the bottom line). Additionally, the community expects socially and environmentally responsible behaviour practices; the so-called triple bottom line approach. The paper briefly reviews the development of corporate social responsibility reporting from the perspective of two large Australian banks and attempts to understand their motivation for voluntary disclosure. Stakeholder theory and game theory provide a means to analyse why banks undertake CSR reporting. The paper compares Westpac and National Australia Bank's CSR reporting over the period 2004-2005 utilising external rating agencies and CSR reports to determine the extent of disclosure in relation to employees, environment, community and customers. The paper concludes with a discussion of the pros and cons of CSR, the role of regulation and recommendations for future policy direction.

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Introduction

There are strong divergent views about the role of corporations in society. These views and expectations of the stakeholders of business: employees, consumers, shareholders, politicians and community groups are changing rapidly, with the expectation that business will give as well as take from a society and the environment in which it operates. The first responsibility of any business is to be profitable, the traditional bottom-line economic (financial) performance. However, as interdependence of all individuals in society is recognised, corporate social responsibility (CSR) or the triple bottom-line approach is seen to be all encompassing, where the organisation should measure and be judged on economic (financial), social and environmental parameters Elkington (1998). The results of increased pressure by green groups and environmentally aware investors is seen in varying forms of self-disclosure by companies about their social and environmental accountability (SEA).

It is the aim of this paper to examine the nature and growth of corporate social responsibility and CSR reporting with particular reference to the experience of two large Australian banks. The research question that arises from the 'information asymmetry' (Akerlof, 1970) and the 'information impactedness' literature (Williamson 1985) is 'why do organisations have an interest in voluntarily disclosing information, above what is legally mandated and does the information disclosure have a positive impact on corporate governance, the business strategy and firm performance?' This is of particular interest given that much of the information and disclosure literature finds that firms tend to increase their voluntary disclosures during performance declines or when the firm is seeking additional market-based finance (Holland, 2005). Westpac and National Australia Bank (NAB) are part of a growing group of businesses that have recognised the new CSR paradigm and have incorporated the publicizing of a socially responsible reputation into their overall business strategy. It is recognized that whilst there are costs to the firm, these can be offset against advantages such as reduced cost of capital, reduced

uncertainty and the attraction of investors to the firm (Filatotchev, Jackson, Gospel and Allcock, 2007).

The paper commences with an outline of the recent development and growth of CSR and a brief review of the theoretical literature pertaining to CSR. It assesses the internal and external (reputational) perspectives of CSR and attempts to understand the motivation for voluntary disclosure. The CSR reports of Westpac and NAB are compared over the period 2004-2005 to determine the extent of disclosure in relation to employees, environment, community and customers. The voluntary CSR reporting of these banks has implications for the wider banking and finance community, leading to a discussion of the pros and cons of CSR with recommendations for future policy directions. Further, the paper explores governance and CSR, and in particular whether there is a role for regulation in CSR and CSR reporting in Australia.

The Development of CSR Literature and Theory

Interdependence of individuals in society and evidence of the business community's concern for society can be traced back for centuries. Carroll (1999) suggests that the modern era of CSR commenced in the 1950s when Bowen wrote on the social responsibilities of businessmen. Bowen defined these social responsibilities as "...the obligations of businessmen to pursue those policies, to make those decisions, or to follow those lines of action which are desirable in terms of the objectives and values of our society" (Bowen, 1953, p. 6). CSR has since been defined by the World Bank as 'commitment of business to contribute to sustainable economic development – working with employees, their families, the local community and society at large to improve the quality of life, in ways that are both good for business and good for development' (Ward, 2004). The major features to emerge from the literature on CSR in the 1960s were the addition of ethical consequences of a firm's actions and in the 1970s the beginnings of the 'stakeholder approach' referred to by Johnson (1971) as the 'multiplicity of interests', with stakeholder groups including employees, suppliers, dealers, local communities and the nation. However it is only in the last three decades that CSR has become a widely debated topic.

While there is no consensus on what is good corporate governance, the CSR literature suggests that organizations have a responsibility to protect and enhance the community's interest while serving its own business objectives. Theory and evidence on different aspects of corporate governance come from various streams of the social sciences, including economics, finance, law, political science, sociology and management studies (Filatotchev, et al, 2007). At the heart of this debate is the fact that there is no agreed theoretical perspective to drive systematic research. CSR can be seen as an addition to traditional

accounting reporting but it fails to have the core certainties of traditional accounting (Gray, Kouhy & Lavers, 1995). The lack of these defined parameters has made compliance measurement of CSR traditionally difficult. It is further confounded by the lack of systematic reporting by firms and corporations, its highly emotive nature and political sensitivity (Cooper & Sherer, 1984 as quoted in; Gray *et al.*, 1995). Alternatively, the theoretical frameworks of agency theory, stakeholder theory and legitimacy and accountability theory provide an informing framework, while the political economy accounting theories, green and social ecology theories place CSR as having a key information role in the organisation-society dialogue (Parker, 2005). For a more complete review of the history of corporate accountability and CSR evolution see Bendell (2004) and in the UK, Gray, Kouhy & Lavers (1995).

Traditional theories of the firm have asserted the Friedman (1970) view that the primary function of the corporation is to maximize the returns to the shareholders. Opponents of CSR, Friedman and Drucker, argue strongly that market forces should direct the role of the corporation. Friedman believes that market forces should be allowed to dictate a corporation's responsibility to any person or entity and that social responsibility is best left to democratic governments and public servants. Drucker (1946), a more liberal Austrian economist, states that a corporation's responsibility is to obey the law of the land and to attend to the interests of their shareholders. Governments should take full responsibility for the public good rather than relying on corporate philanthropy. Giving money to "worthy causes" raises normative questions, which are not easily resolved because different stakeholders have different values. Drucker suggests that companies should distribute their funds to their shareholders and let them, as natural people with a variety of values, decide what charity to support.

Contrary to the pure market view, proponents of CSR believe that it is market failures (information asymmetries, externalities and injustices) that are the principal concerns of CSR and a desire to change current practice (Gray, Kouhy, and Lavers 1995). This view recognises that corporations are made of individuals and that there is an individual and collective responsibility of the corporation to all stakeholders and the society in which it operates. While CSR does not seem to have an explicit theory to explain the nature of relationships between organisations and society, stakeholder and legitimacy theory fill a role and see the enterprise in terms of the broader relations between all stakeholders with an interest in the firm and a broader set of goals to be maximised or satisfied (Freeman 1984; Donaldson 1989, Donaldson and Preston 1995). The literature often sees these theories as competing theories rather than two overlapping perspectives. According to Gray *et al* (1995) stakeholder and legitimacy theory are both concerned with but see the issues of 'mediation,

modification and transformation' from different points of view. Stakeholder theory sees the world from the perspective of the management of the organisation. The chief managerial concern is with the ongoing success of the company and gaining the necessary support and approval required from stakeholders, with the activities of the corporations changing as required to gain that approval. The more powerful the stakeholders the more the company must adapt (Roberts, 1992). The asbestos and corporate moral responsibility case of James Hardie Industries provides a recent example of a corporation changing its behaviour due to immense and successful pressure of stakeholders (Cooper, Leung and Dellaportas 2007).

Legitimacy theory requires that we first distinguish between legitimacy – which is a status or condition – and legitimation – which is the process underlying that state (Lindblom, 1994). She defines legitimacy as:

...a condition or status which exists when an entity's value system is congruent with the value system of the larger social system of which the entity is a part. When a disparity, actual or potential, exists between the two value systems, there is a threat to the entity's legitimacy (p. 2).

Legitimation of the corporation's activities can occur via any of the four strategies outlined by Lindblom. First, in response to a recognition that the "legitimacy gap" arose from an actual failure of performance of the organization the corporate may seek to educate and inform its 'relevant publics' about changes in its performance and activities. Second, when the organization sees that the legitimacy gap has arisen through misperceptions on the part of the 'relevant publics' the organization may seek to change the perceptions of the 'relevant publics' – but not change its actual behaviour. Third, the organization may seek to manipulate perception by deflecting attention from the issue of concern to other related issues through an appeal to, for example, emotive symbols. Fourth, when the organization considers that the 'relevant publics' have unrealistic or 'incorrect' expectations of its responsibilities the company may seek to change external expectations of its performance or may attempt to repair legitimacy (Gray, et al 1995). Both Westpac and NAB illustrate such legitimacy gaps in relation to the first, third and fourth legitimacy strategies. Westpac's closure of rural banks in 1998 and NAB's foreign currency losses and subsequent board dysfunction in 2004 were issues that affected both banks' performance. Both banks wanted to inform their public or stakeholders about changes in their activities and share "good news" stories concerning their involvement in reducing environmental emissions, gifts to charities, and the launching of their Corporate Social Responsibility reports.

Gaming theory provides another perspective to the regulatory trade-off that occurs between

enforcement of legal regulation and the flexibility of 'soft' regulation built around the principle of 'comply or explain' (for example, the Australian Stock Exchanges' 'Principles of Good Corporate Governance and Best Practice Recommendations, 2003). The regulatory trade-off may cause different sets of unintended consequences related to game theory. If socially responsible behaviour is costly, then any firm in a competitive industry that engages in such behaviour is likely to incur a competitive disadvantage where the participation is voluntary. This may create a case for "harder legal" regulation to achieve 'good' corporate governance principles and requirements for CSR reporting, which has been the route followed by Europe and the U.K., whereas the 'softer' approach has been followed in Australia where participants can engage in 'ticking-the-box' exercises without facing sanction from the market.

Game theory assumes that the players in the game try to maximise their pay-offs – the amount they win in the game or minimise costs. The aim of classic game theory to CSR reporting and banking corporations is to analyze the choices facing each player (banking firms) and to determine which is the dominant strategy for both firms to adopt (Taylor and Frost 2002). The payoff matrix that we apply to CSR strategies assumes that there are only two banking firms who will act to maximise their profits or in this case minimise their costs. Game theory thus provides an example where individual incentives lead to a non-optimal (non-co-operative) outcome, whereas if players (banking firms) can credibly commit to co-operate then they achieve the best (co-operative or collusive) outcome. The three options for the banks are: engage in CSR behaviour (both banks comply with CSR); not engage in CSR behaviour (both banks don't comply); or one bank undertakes CSR and the other doesn't.

If engaging in socially responsible behaviour (CSR reporting) is costly, then both firms are better off by co-operating and not engaging in the activity. If, however, socially responsible behaviour has beneficial outcomes, as suggested by legitimacy theory, then corporations are likely to engage in CSR reporting voluntarily and without 'hard' regulation. Westpac and NAB are the first two of the major five banks in Australia to publish corporate social responsibility reports in the absence of 'hard' legal requirements and both institutions state upfront that there was a need to change the perception and image of their corporate profiles, from employees within each organisation to their wider customer base and other stakeholders. A payoff could be measured by the firm's utility, where the firm, board, management and even employees derive satisfaction from being involved in CSR activities, that is gain a positive outcome. For example, Westpac's and NAB's employees are involved in one day of 'volunteering' activities each year resulting in employee satisfaction measures improving.

Figure 1. Prisoner's Dilemma Payoff Matrix where CSR Benefits

		Bank 1 Strategy	
		Don't Comply with CSR	Do Comply with CSR
Bank 2 Strategy	Do Comply with CSR	0, 0	-1, +1
	Don't Comply with CSR	+1, -1	-0.5, -0.5

Figure 1 illustrates the optimal strategy for two banking firms where CSR benefits accrue. In the upper left quadrant both financial institutions collude and agree to not undertake CSR reporting with zero costs. If the potential exists for one bank to achieve real or perceived benefits from compliance with CSR compared to the bank that doesn't comply, we derive the outcomes seen in the upper right-hand and lower left-hand quadrants. Here the bank that does comply receives benefits worth \$1 million, and the bank that fails to comply loses benefits equal to minus \$1 million. But if competitive pressure exist then the dominant strategy in this scenario is where both banks comply with CSR reporting, without regulation, with a -\$0.5 million cost to each (demonstrated in the lower right-hand quadrant). Clearly this is not an optimal strategy unless there are social or external benefits derived from socially responsible behaviour that exceed the costs. For example, the building of image comes at an expense, but can the one banking firm afford to not build image if the other one does? If

the gain to society is sufficient to offset the loss of complying with CSR then corporations will undertake costly CSR voluntarily. The bank's payoff may be measured by cost reduction (used in the above example).

A second scenario is demonstrated in Figure 2, where there are no benefits from complying with CSR and only costs. The dominant and optimal strategy is for both banks to comply with CSR with zero costs as demonstrated in the upper left-hand quadrant. If one bank undertakes CSR reporting and one bank doesn't comply, then there is a cost of \$1 million to firm 2 who complies and zero costs to firm 1 (lower, left-hand quadrant) and the reverse scenario in the upper, right-hand quadrant, where bank 1 has costs of \$1 million and bank 2 has zero costs. If both firms agree to comply (lower right-hand quadrant) they would both face equal costs of \$1 million. The results of this game indicate a case for mandatory CSR and reporting, as corporations won't undertake socially responsible behaviour without regulation.

Figure 2. Dominant Strategy Equilibrium Where CSR Costs

		Bank 1 Strategy	
		Don't Comply with CSR	Do Comply with CSR
Bank 2 Strategy	Do Comply with CSR	0, 0	0, -1
	Don't Comply with CSR	-1, 0	-1, -1

One must question whether CSR activities and reporting was undertaken by these banks purely for PR reasons or for self-interest reasons due to private benefits accrued to the individual bank. Often it is difficult to know where the dividing line between PR and CSR is. Alternatively, has there been an increase in corporate philanthropy and other forms of social spending due to its pro-cyclical nature and the current high corporate profits resulting from the strong phase of the business cycle.

Growth of CSR Reporting

Over the last two decades various arms of the United Nations, in particular under the ambit of the United Nations Environmental Programme (UNEP) the Finance Initiative and the Global Reporting Initiative (GRI), have played a significant role in the introduction of new sustainable accounting and reporting standards. The objective of the GRI Guidelines is to permit companies and other organisations to produce comparable Triple Bottom Line-reports about the economic, environmental and social performance (UNEP, 2006; Institute of Chartered Accountants of England and Wales, 2006). Kolk (2003) examined the trends in sustainability reporting by the Global Fortune 250 companies. He found that apart from the U.S. (where sustainability reporting is slightly decreasing), that the reporting of non-financial issues has increased significantly, with Japan and European countries being the most active. Kolk noted that, in both Europe and Japan, reporting legislation, related requirements and government encouragement of disclosure have also increased in the past few years. A further worldwide study (ACCA, 2004) indicates that the incidence of CSR reporting has increased substantially, from less than 50 organisations with stand-alone CSR reports in 1990 to over 1200 by 2003. These findings are supported by the KPMG Global Sustainable Services survey (2005), which found 52% of Global (see *endnote 1*) 250 (GS 250) and 33% of National (see *endnote 2*) 100 (N100) companies issued separate CSR reports, compared with 45% and 23% respectively in 2002.

In the UK, new environmental reporting guidelines were made available in 2005, by the Department for Environment, Food and Rural Affairs (Trucost, 2005) with clear key performance indicators (KPI) for business sectors. The KPIs have been defined on the basis of transparency, accountability, credibility, potential for quantitative analysis, relevance and comparability. Details of these 22 KPIs for emissions to land, water and air, in addition to the supply chain and product management, are now clearly defined.

Since sustainability reporting commenced in Australia in 1995, the KPMG report (2005) found that there has been a sequential increase in the number of companies providing sustainability reports, from 1% in 1995 to 24% in 2005. A longitudinal study, examining 41 companies over the years 1938-2003,

by Gibson and O'Donovan (2005) found that 46% of those Australian companies reported environmental information in annual report in 1983, rising to 100% in 1999-2003. Despite this increase, Australia's average number of companies providing CSR reports fares badly by comparison with the other OECD nations, Japan (81%) and the UK (71%). The higher reporting and higher compliance in those countries may be a reflection of the compulsory legislative requirements that are in place (Parliamentary Joint Committee on Corporations and Financial Services, 2006).

The Australian Government Department of Environment commissioned PricewaterhouseCooper (PwC) to prepare a report on the role of sustainability in financial institutions in Australia (2001). The PwC report found that at that time only two Australian financial institutions were signatories to the UNEP financial incentive. There was low demand for socially responsible products, low general implementation of environmental risk assessment plans, minimal energy efficiency and recycling programs by stakeholders, as well as low uptake of triple bottom line reporting. The report finds that the lack of legislative requirements, small market size and poor development of voluntary disclosure (see *endnote 3*) all contributed to this position. As yet there is no coherent legislation to enforce CSR guidelines, the nature and scope of reporting varies according to the popularity of the concept at any given time. Although this is the case, the importance of non-economic and non-financial factors in organisational reporting and accountability continues to increase (Arrington, 1990; Gray *et al.*, 1995).

Further growth in the area of CSR is seen with the creation of the corporate responsibility index by *Business in the Community* (BITC). It is a joint venture with The St James Ethics Centre and Ernst & Young providing an independent assessment of the overall impact of business activities on the community in Australia. The Business Council of Australia has invited the top 250 companies to participate in this index, run by the Australian Centre for CSR, with the aim to promote the five main tenets of CSR: stakeholder engagement, ethical business behaviour, social accountability, value attuned communications and dialogue. Reputex, an Australian independent private company formed in 2001, produces an annual reputation ratings index based on four key dimensions – corporate governance, workplace practices, social impact and environmental impact. It provides a broad appraisal of a company's commitment to meet expectations of community-based stakeholders. Adams (2002) found the main motivation for corporate ethical reporting was to enhance corporate image and credibility with stakeholders. This appears to be in accordance with both the Westpac and NAB experience, with the publication of independent annual CSR reports, initiated in 2001 for Westpac and 2004 for NAB and the reporting of their various CSR scores.

CSR Implications for Regulation and Policy

Society's expectations for CSR differ from that of organisations and the industry perspective leading to implication for policy makers. The Millennium Poll on Corporate Responsibility (Enviro-nics International Limited, 1999) comprised interviews on CSR with over 25,000 citizens across 23 countries on 6 continents. It included three essential components that when combined, add up to socially responsible behaviour and performance: doing business responsibly; taking a leadership position in community investment and social issues relevant to the business; and transparency and public reporting of the social, environmental and financial impacts and performance of the business (Department of Immigration and Citizenship, 2005). Their findings indicate that 50% of citizens want companies to contribute to broader societal goals and expected companies to go beyond their historical role of making a profit, paying taxes, employing people and obeying all laws (See Figure 3). Western developed nations generally want companies to be socially responsible but Australia had the highest proportion of any respondents in the world with 88% of respondents from Australia wanting companies to contribute to broader societal goals with only 8% indicating that the traditional accounting bottom-line items were the most important for a corporation. Interestingly, these results provide an inherent contradiction as without a healthy bottom line corporations cannot function and cannot support CSR initiatives, which come at a definite financial cost.

Insert Figure 3 here

The most important CSR actions identified across an average of 20 countries were protecting the environment, creating jobs, supporting the economy, giving back to the community, the health and safety of employees, equitable treatment of employees, avoiding bribery and corruption, and refraining from using child labour – social responsibilities ranking above profit and paying a fair share of taxes (See Figure 4) (Burmeister, 2000).

Insert Figure 4 here

A reflection of society's expectations and values is found in the strong demand for socially responsible investment (SRI) options in Australia. A survey of 1000 investors conducted by Resnik and KPMG (2000) found that 76% would like to know where their superannuation is currently invested, and 69% would consider an SRI option if it was made available to them. A separate study conducted by Monash University in 2000 found that 87% would consider an SRI option (Monash Sustainability Enterprises and KPMG, 2001). Additionally, a survey conducted by the Australian Institute of Superannuation Trustees in early 2001 found that 73% of trustees believe that SRI

is a legitimate investment class. Importantly, the Monash study found that 92% of investors felt that financial performance should not be the only criterion for selecting investments. Both surveys found that most investors would be willing to accept slightly reduced returns for SRI investments. However, support for SRI tapers off if investment returns are significantly lower (Monash Sustainability Enterprises and KPMG, 2001).

In regards to regulation and the most effective approaches to making MNCs more socially responsible, the Environmental Monitor (2002) found that in nearly all countries surveyed on governance and environmental performance that majorities of consumers indicate that domestic environmental laws and regulations do not go far enough. The implication is that there is widespread appeal among the general public for strengthening environment legislation as opposed to voluntary or market-based approaches. Consumers in developing nations had the highest dissatisfaction with domestic regulatory regimes, perhaps foreshadowing an increase in environmental regulation in these countries with G7 countries having the highest support for international laws to promote CSR. Nearly 50% of consumers surveyed across the world indicated that either international or domestic laws are the most effective way to improve CSR, with people in wealthy countries more supportive of international laws (see Figure 5). This suggests that if governments were serious about CSR, perhaps the best way forward would be to have international legislative compliance.

Insert Figure 5 here

Despite these findings the Australian Parliamentary Joint Committee on Corporations and Financial Services (JCCFS, 2006) takes the view that legislation is likely to drive compliance into the hands of compliance managers who are likely to take an approach of 'tick the box'. JCCFS believes that this is against the spirit of the CSR movement and the environmental protagonists and states that the United States CSR legislation has done little to advance the cause of non-shareholders. It also argues that legislating CSR would make the job of the Australian Securities and Investments Commission more difficult in monitoring the role of directors. The JCCFS felt that the nature of institutional investment in Australia placed the institutions in a position of being able to vote with their dollars for good corporate governance in a company: in other words the federal government is happy to let institutional investors use market forces to coerce firms to comply with CSR/ GRI guidelines. The JCCFS report recommends that institutional investors formalise this role by becoming signatories to the United Nations Principles for Responsible Investment. While the Committee does not recommend mandatory reporting standards or legislation, it does recommend seed funding from the Federal government to start the Australian Corporate

Responsibility Network along the lines of Business in the Community initiative in the UK.

There is clearly a role for both government and industry to further economic and sustainable development reporting. Both need to take an equal responsibility for the development of combined covenants, development of voluntary industry initiatives, national standards and legislation/regulation. There is some disagreement between corporate and government experts as to the degree of prominence the role of regulation should have in the negotiating of industry/government covenants. These differing views may stand in the way of achieving legislative compulsion for CSR compliance. For example, development experts believe that legislation and regulation will play a less prominent role, in stark contrast to government experts who believe that regulation will play a major role in negotiating "action covenants" (The Environment Monitor, 2002).

While it would make intuitive sense for Australia to follow the UK and Europe in legislating CSR compliance requirements, there is still doubt whether CSR is a distinct entity that can be measured and complied with. Further, even in the UK, company directors are not bound by legislation to CSR compliance for taking any decision. The Australian Conservation Foundation believe that it is possible for industry to play a significant role in private sector reform, but suggests that governments can play an essential role in overcoming the problems of collective action. For example, taking strong and decisive decisions on pricing environmental externalities (carbon tax and emission trading) and ensuring transparency of ownership and environmental and social performance in the corporate sector (Australian Conservation Foundation 2006). One view is that board of directors should be made responsible for CSR compliance by law. Until this occurs it is unlikely to have a significant impact on real CSR issues unless stakeholders gain significant power to change corporate views or the corporation itself recognises a 'legitimacy gap' where it seeks to change perceptions of the organisation. There seems to be a mood for change within society and within corporations with HSBC becoming the first financial institution to achieve full carbon neutrality in 2005 and the announcement by Rupert Murdoch in 2007 that his News Corporation planned to incorporate carbon neutrality into their business plan. On the other hand, sustainability reporting could be seen as merely window dressing driven by government and public pressure.

Advantages of CSR and CSR Reporting to the Organisation

Empirical research has demonstrated a positive relationship between a company's reputation index, a measure of its social performance and return on equity (Karake, 1998). Brennan (2002) found that 70% of Irish consumers' purchases were influenced to

some degree by environmental concerns. Orlitzky et al's (2003) meta-analysis of 52 studies, with data over 30 years, found that corporate social performance (CSP) is likely to enhance corporate financial performance (CFP) by providing internal or external benefits or both. Across studies it finds that (1) CSP is positively correlated with CFP, (2) the relationship tends to be bi-directional and simultaneous, and (3) reputation appears to be an important mediator in the relationship. They conclude that 'corporate virtue in the form of social responsibility and to a lesser extent environmental responsibility is likely to pay off', although a constant problem in the assessment of CSR has been its objective measurement (Orlitzky, Schmidt & Rynes, 2003). These authors have further categorised the measurement of corporate social performance into four main subdivisions: 1. disclosures: including content analysis, letters to shareholders, public disclosure, 2. use of reputational indices, the so called badges of honour, 3. social audits as assessed by third parties, objective CSP processes and values and 4. assessment of values and principles inherent in a company's culture.

The *Internal-Resource perspective* suggests that investments in CSP may help firms develop new competencies, resources and capabilities, which are noticeable in a firm's culture, technology and human resources (Wernfelt 1984 as quoted in Kock & Santalo, 2005). As these managerial competencies are acquired internally through the CSP process, they lead to more efficient utilization of resources. In addition CSP may have external effects on organisational reputation.

Proponents of CSR believe that CSR disclosures provide informational signals for investors and bankers to base assessment of corporate reputation under conditions of incomplete information. The improved banker and investor relationship may facilitate the financial institution's access to capital, attract "better employees", improve employee satisfaction and customer satisfaction. Westpac has seen sustained reductions in their employee turnover rate since 2000, and both Westpac and NAB have experienced significant increases in customer satisfaction over the two-year period to 72% and 71% respectively in 2005 (see outcomes in tables 1 and 2).

Adams (2002) found a number of real and/or perceived benefits of ethical reporting that accrues to the organisation. Ethical reporting improves understanding of corporate activities; reduces criticism; influences or delays legislation; minimises risk (for eg. reduces consumer boycott, which has been a significant issue for Nike); attracts and retains the most talented people (both Westpac and NAB indicated that they had been able to attract highly qualified people as a consequence of their change in culture); promotes inclusion in ethical investment funds (see Westpac's Eco Index, Figure 6); improves internal systems and control leading to better decision making and cost savings; and communicates the

group's values and targets to all groups and companies.

According to the *External or Reputational Perspective* the external communications with other parties may help build a positive image with customers, investors, bankers and suppliers as the financial institution receives 'the badges of honour'. Westpac's image has been enhanced, being the only organisation to have achieved number one on the DOW Jones Sustainability Index for the past four years. Westpac's CSR report suggests that this has increased their ability to attract and retain staff (Westpac, 2004a, 2005a). Both Westpac and NAB acknowledge in their reports that their emphasis on CSR has been to address an identified legitimacy gap of failure of performance, which was reflected in poor reputations. Westpac's reputation suffered when it was the subject of intense media coverage following the its numerous rural bank closures during the 1990s. NAB saw its market valuation fall by 33% (Thomson & Jain, 2006) in 2001 with their HomeSide US home loan losses of \$4.1 billion and again in 2004 with the \$360 million losses associated with the fraudulent foreign exchange traders. The foreign currency debacle triggered a chain of events within the Board that saw fifty percent of NAB's board members and top executives either step down or resign. The behaviour of both banks following these events is consistent with legitimacy theory's first strategy that the organisation may attempt to inform its stakeholders of failures in performance or the third strategy where they may seek to deflect public attention away from the issue. For example, the re-badging of NAB released simultaneously with their large commitment to sponsoring the Melbourne Commonwealth Games (*see endnote 4*).

Disadvantages of CSR to the Organisation

CSR gained sufficient notoriety that the *Economist* chose to denounce its ability to improve capitalism and increase profitability of an organisation (The Economist, 2005). Maintenance of CSR would intuitively come at a significant dollar cost with consequent negative impact on net profit or the bottom line in the short run (Centre for Australian Ethical Research, 2006). The *Economist* was not alone in denouncing CSR. Mainstream financial literature and the Australian Parliament have taken the view that CSR is a judgment best left to the board of directors of companies. Australian Corporation Law does not recognise stakeholder theory or CSR instead there are various statutory duties and liabilities imposed on company directors within the common law and by statute under the Corporations Act 2001, where directors owe strict fiduciary duties to the company.

Claims about CSR profitability arise in the areas of ethical consumerism, ethical investment and CSR ratings. Auger *et al* (2003) found that whilst a market for the ethical consumer exists, its importance tends to be over-estimated and that consumers were not

prepared to sacrifice cost for ethical considerations. Similarly, a study by Ali and Gold (2002) found that costs were higher for socially responsible investment (SRI) funds than for other funds not advertising in this category. They concluded that 'ethical products and their marketers were simply using an attractive label to lure the boutique investor.

Johns' (2005) review of CSR involves a critical analysis and deconstruction of CSR. He points out that the agencies driving CSR are predominantly NGOs. These are becoming the new transnational governments, extending their spheres of influence to large corporations. This viewpoint argues that stakeholders do not have a right to impose their views on any firm or corporation in a democracy. Further (Weiss, 1995) argues that the stakeholder theory does not clearly separate the issue of ownership of economic value produced by a corporation.

Whether CSR is profitable remains debatable. It seems that a company is defined by proponents of CSR as socially responsible, if it maximises its economic and social performance, at the same time reducing its environmental impact (Johns, 2005). Laffer *et al* (2004) suggests a second bias as only profitable companies engage in CSR, and for an unprofitable company to engage in CSR would indicate a socially irresponsible company as energies and resources should be focused on survival. They found no real corporate benefit accruing from CSR.

The measurement of compliance with CSR guidelines and laws is tenuous at best. Indices to measure CSR such as Reputex, have been devised, which measure parameters such as signing the UN declaration, participating in a CSR program and making voluntary declarations about energy use. It seems that 'success' in the rankings comes from participation rather than any measurable performance and is seen as a game that corporations play to win favour from the regulator (Johns, 2005). The administration of the Corporate Responsibility Index by agencies such as St. James in Australia and New Zealand results in financial gain for these institutions, resulting in a conflict of interest in their quest for the promotion of social responsibility.

Westpac and NAB: A Comparison of the Evolution of CSR Reporting

Westpac

Westpac Banking Corporation has a long history as Australia's first and oldest bank. To end the confusion that existed in the new colony due to a lack of a stable monetary system, Governor Macquarie signed a charter of incorporation establishing the 'Bank of New South Wales' in February 1817. The Bank became the first company to incorporate in 1850 and changed its name to Westpac Banking Corporation following the merger with the Victorian-based Commercial Bank of Australia Ltd in 1982 (*see endnote 5*). As at 30 September 2006 the Westpac Group, is ranked in the top 10 listed companies by market capitalisation on

the Australian Stock Exchange Limited (ASX), had global assets of \$300 billion and market capitalisation of \$42 billion. Stakeholders include: 330,000 shareholders, 7 million customers and approximately 27,000 employees (full time equivalents) in Australia, New Zealand and around the world (Westpac, 2006, 2006a).

Westpac's involvement with CSR commenced in 1998 when it looked at raising its corporate responsibility profile as a way to repair the community's lack of trust of the major banks in the 1990s. This era saw Westpac and other major Australian banks closing large numbers of rural and suburban bank branches, imposing fees for most forms of banking, including students and pensioner accounts, encouraging business customers to borrow on foreign exchange markets and making billion dollar profits. This era of intensified competition followed the Hawke Labour government's deregulation of the finance sector in the 1980s. Prior to deregulation large interest margins between borrowing and lending rates provided the means to cross subsidize other products such as check accounts. As interest rate spreads fell, banks began to specifically charge for other services. The introduction of fee-for-services caused widespread resentment among consumers.

Noel Purcell, (Westpac's Group General Manager, Stakeholder Communications) is of the strong opinion that engaging in measurement and reporting of the bank's non-financial performance has driven improvements in the way it does business. He further argues that the process has been good for the company's bottom line and for shareholders (Kendall, 2005).

National Australia Bank

National Australia Bank Limited traces its history back to the establishment of the National Bank of Australasia in 1858, becoming a public limited company after incorporating on June 23rd, 1893. NAB is the largest financial institution (by market capitalisation and total assets) listed on the Australian Stock Exchange. As at 30 September 2006, NAB is within the 30 most profitable financial service organizations in the world, with total assets of \$485 billion and market capitalisation of \$52 billion. Stakeholders include: 370, 502 shareholders – of which 98.7% are Australian, with the 20 largest shareholders holding 50.88% of the total shares on issue. There are 8 million banking customers and 2.3 million wealth management customers and NAB has approximately 39,128 employees (full time equivalents) in Australia, New Zealand and around the world (National Australia Bank, 2006, 2006a).

NAB has come to the CSR arena much later than Westpac, but similarly for historic reasons. NAB finally recognised that there were shortcomings in their management systems and their culture after the challenging period of the \$4.1 billion in U.S.

HomeSide mortgage loan losses in 2001, the \$360 million foreign currency trading losses and subsequent board dispute that followed in 2004. NAB has concentrated on addressing these issues and publicly acknowledges that a more balanced approach is necessary for the bank to rebuild customer and shareholder trust and confidence.

The following section allows direct comparison of a company's socially responsible performance. This has been made possible by standardised assessment criteria using CSR indices such as RepuTex, CORP RATE and the Dow Jones Sustainability index. These independent standards are reported based on an identical data set obtained for each participating firm to calculate the relevant index.

Comparison of CSR External Rankings

External agencies and rating companies are used to benchmark and monitor Westpac's and NAB's performance in CSR reporting and performance over 2004-2005. Westpac's first Social Impact Report was published in 2002, and they have now published their sixth CSR report, whereas NAB issued its first CSR report using the Global Reporting Initiative's Sustainability 2002 Guidelines for non-financial performance indicators in 2004.

Westpac is the world leader in the banking sector for CSR having achieved number one in almost every category, both nationally and internationally. It has retained the top position on the Dow Jones Sustainability Index (DJSI) for the past four years and received number one ranking in the Australian corporate responsibility index (CRI) and also on the UK index. Westpac was named CSR Bank of the Year in The Banker Awards 2005, and was the only bank to get a top ranking by the corporate governance consultants, Governance Metrics International, and top-scored by similar indices, RepuTex and St James Ethics Centre (see Table 1 for a comparison of Westpac and NAB over the years 2004 to 2005).

Whilst it is clear from both tables 1 and 2 that NAB lags significantly behind Westpac in CSR, nevertheless it has made strong inroads into improving its CSR ranking on the basis of international standards. In 2005, NAB was assessed as being one of the top ten most socially responsible companies in Australia (RepuTex), and has improved its DJSI rating from 63 to 74 in only one year. As reporting becomes more standardised and financial institutions comply with international standards direct comparisons will become easier. The relevance of these measures to the overall conventional and triple bottom line is questionable. For businesses such as banks these measures would appear to divert attention from other practices such as low-doc home loans, where 100 percent of the value of a house is made available to low-income borrowers who often are unable to afford loan repayments resulting in increased repossessions and high debt loads to society (Cooke, Schneiders & Smith, 2006). The established CSR parameters appear to look only at consumption

of businesses and not their actions. A more important measure specifically for banks would relate to the activities that they fund and how socially responsible their funding activities are. For example, ANZ has become a target for green groups due to its role as the lead lender to the Gunn pulp mill that is wishing to locate a wood chip mill in an environmentally sensitive location in Tasmania. Bank funding actions may be considered more socially irresponsible than those firms undertaking the actual activity.

Insert table 1 here

Comparison of Internal CSR Measures

Direct comparison of the CSR reports from NAB and Westpac required a detailed content analysis of their CSR reports. The data provided in the annual and the CSR reports are highly individual and often not comparable between the two banks. The reason for this is that there are no legislatively prescribed standards for CSR reporting which leads to a lack of comparable figures in each report. Despite this, there are significant components of CSR reporting common to both financial institutions, particularly as both institutions have begun to report using the external GRI reporting framework that enables organisations to communicate: 1) actions taken to improve economic, environmental, and social performance; 2) the outcomes of such sections; and 3) future strategies for improvement (BSD Brasil, (2007)). See Appendix 1 for a detailed table of the various aspects that GRI suggests should be measured.

Common internal CSR reported measures for both banks included economic, environmental and social aspects. Table 2 groups the reported findings from the respective annual reports for NAB and Westpac. Economic measures included employee commitment, employee turnover, women in senior management positions and customer satisfaction. Employee commitment was similar for each institution, with Westpac recording 68-69% over both years, slightly lower than NAB's 71%. Employee turnover rates show a different picture, with Westpac significantly reducing their employee turnover from 20% in 2000 to 16% by 2005. By contrast, NAB saw employee turnover increase significantly from 15% in 2004 to 18% in 2005. Part of this increase in staff turnover followed the foreign currency losses and board dysfunction in 2004, as NAB put in place 2,250 redundancy packages for staff in the Australian operations as they sought to improve their cost to income ratio. Westpac showed a much greater commitment to achieving more women in management positions with significantly higher numbers of women in senior management positions, 26% in 2004 and rising to 29%, compared to NAB's 19% and 21% respectively. Customer satisfaction for Westpac showed small increases over the two-year period, rising from 69% in 2004 to 72% in 2005, although had come from a low of 64% in 2002. NAB

showed a dramatic increase from 63% to 71% over the two-year period. This tends to indicate that NAB's strategy to rebrand, support the Commonwealth Games and undertake a heavy advertising campaign were successful in turning consumers around in a short period of time.

Both institutions recorded environmental measures, with a focus on equivalent tonnes of CO₂ emissions and emissions per fleet vehicle and paper consumption. Westpac recorded figures that were approximately 50% lower than NAB's in both years. For example, in 2005 Westpac recorded 124,500 tonnes of CO₂ emissions compared to NAB's 243,969 tonnes, with similar results for fleet car emissions, Westpac recording a low 4.9 per fleet car versus NAB at 9.88 per fleet car. Paper consumption is a readily measured as the number of sheets of paper per person used. Westpac ranged from approximately 20% below NAB's use of paper in 2004, but was only able to achieve a 10% improvement on NAB in 2005. The falling use of paper per person was the result of a specific implementation of paper saving initiatives and installation of printers with double-sided printing facilities across NAB's Australian operations (*see endnote 6*).

Social measures include the financial contributions to the community in the form of sponsoring, charitable gifts and voluntary service of staff (*see table 1 for details*). Westpac's total contribution of \$44 million to the community is more than twice NAB's \$17.7 million, but we see a significant increase in charitable gifts at NAB, as it more than doubled from \$1.2 million in 2004 to \$2.7 million over the two-year period.

Westpac has significantly better environmental and social outcomes than NAB. These differences could be explained by Westpac's two-year lead on NAB in implementing CSR or by the fact that these initiatives may have already become part of the culture of the institution.

Insert table 2 here

The cynic or pragmatist might question how relevant are some of the CSR compliance parameters such as reduction of paper consumption, reduction of CO₂ emissions and CO₂ emissions per fleet vehicle as a component of the overall environmental footprint for a bank and its conventional bottom line. But it may well be a part of good business practice that takes into account the law of the land and sustainability. Using double-sided printing, reducing the expenditure on energy, recycling, reducing toxic waste emissions are part and parcel of good business practice to contain costs, maximise profits and reduce risk and liability in coming years. CSR can perhaps be viewed as a subset of measures that are at the very core of good corporate governance and business practice and may make economic sense for any firm's double or triple bottom line. However the percentage of these costs would be low in any given companies balance sheet (except

perhaps James Hardie with asbestos and the tobacco industry).

Conclusion

The paper has provided a theoretical analysis of stakeholder, legitimacy and game theories in an attempt to explain why institutions undertake CSR and CSR reporting. It compares the degree to which CSR compliance has occurred at both Westpac and NAB over the two-year period 2004-5. The motives of both Westpac and NAB have been to rebuild reputations and to be seen as good corporate citizens. For the more cynical it could be seen as a good marketing tool, but both banks have chosen to voluntarily 'comply' with the CSR international guidelines, with both institutions reporting substantial benefits in retaining employees and improving customer satisfaction.

Westpac and NAB have committed to CSR voluntarily and both see it as a positive step in changing organisational culture and establishing branding of their institution. Contrary to their voluntary experience, recent opinion polls suggest that International Laws are the most important way of inducing large transnational companies to comply with CSR requirements. This is contrary to the views taken by Monash Sustainability Enterprises and KPMG, (2001) and by the Australian joint parliamentary inquiry on CSR (2006). Regardless of whether CSR is voluntary or involuntary, society now expects business to set higher ethical standards, to help build a better society for all. CSR now cuts across all facets of business. It means doing business in a way that not only meets profit imperatives but also fulfils community expectations for socially and environmentally responsible behaviour.

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Tables

Table 1. Benchmarking and Monitoring Performance of NAB and Westpac 2004-5

Indicator	Westpac		NAB	
	2004	2005	2004	2005
Dow Jones Sustainability Index (DJSI)	100 (Ranked No. 1)	100 (Ranked No. 1)	63	74
Repu Tex	AAA (Ranked No. 1)	AAA (Ranked No. 1)	AA	AA
Corporate Responsibility Index (CRI)	No. 1	No. 1, and achieved No 1 on the UK CRI	Did not participate	Did not participate
GMI (Global Metrics International)	10.0	10.0 (Top score)	Not ranked	Not ranked
FTSE4Good	Included	Included	Included	Included
UNEP FI	Signatory	Signatory	Signatory	Signatory
Storebrand SRI (SRI)	N/A	No 1	Did not participate	Did not participate
Reporting complied to GRI guidelines	Yes	Yes	GRI guide lines used as a basis	Yes
CORP RATE (2003)	77*		59*	

* CORP RATE has only been performed for the one year at this stage, with no suggestion that it will become an annual measure.

Table 2. Westpac and NAB's Internal CSR Measures 2004-2005

CSR Measure	Westpac		NAB	
	2004	2005	2004	2005
Economic Measures				
Employee Commitment	68%	69%	N/Aa	71%
Employee Turnover Rate	17% (down from 20% in 2000)	16%	15%	18%b
Women in senior management positions	26%	29%	19%	21%
Customer Satisfaction	69% (up from 64% in 2002)	72%	63%	71%
Social Measures				
Charitable Gifts	\$2.1 million	\$2.1 million	\$1.2 million	\$2.7 million
Total Community Contributions	\$42 million	\$44 million	\$12.7 million	\$17.7 million
Environmental Measures				
CO ₂ Emissions (Equivalent tonnes of CO ₂ emissions)	136, 400	124, 500	248, 073	243,969
CO ₂ Emissions per fleet vehicle	5.1	4.9	10.24	9.88
Paper consumption (sheets per person)	9,500	10,100c	11, 734	11,265
Other Measure				
Size of CSR reports – page numbers	82 pages	78	38	74 pages

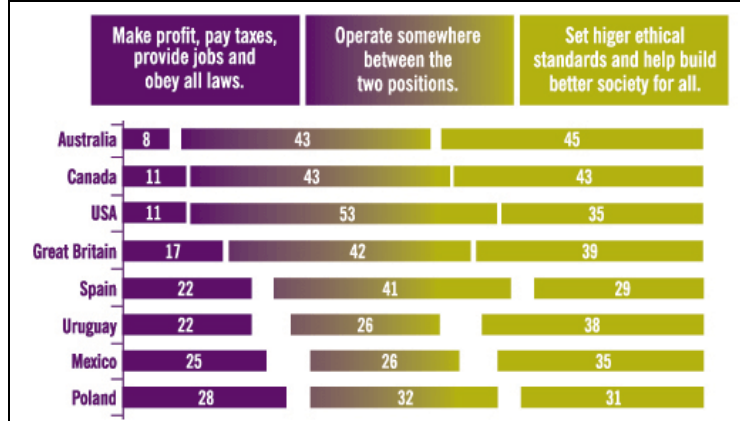
Source: CSR reports from Westpac and NAB, 2004, 2005

Notes:

- NAB measures employee commitment and satisfaction bi-annually. It was reported as 71% in 2003, with no change in 2005. This fails to measure the impact of the events of 2004 on staff.
- The significant rise in employee turnover reported for NAB may be impacted on by the 4,200 staff redundancies that are to occur over 24 months across the worldwide organisation. The figure is 2250 staff redundancies for Australia.
- Whilst paper consumption has risen from 2004 by 600 sheets per person for Westpac, it is still substantially lower than 12,000 reported in 2002.

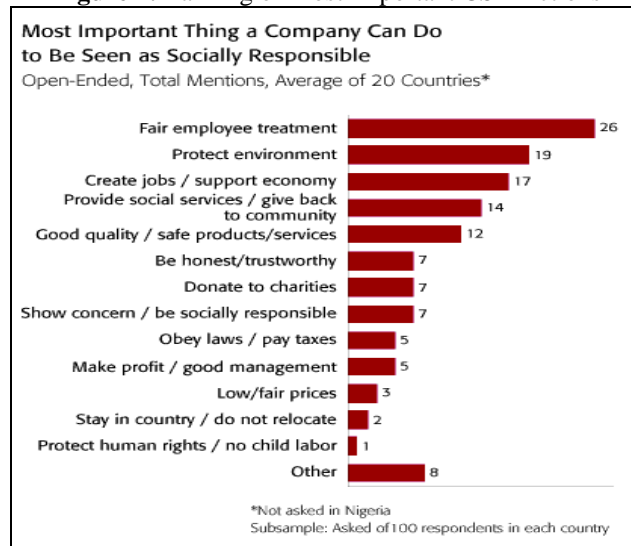
Figures

Figure 3. Role of Large Companies in Society - The Millennium Poll



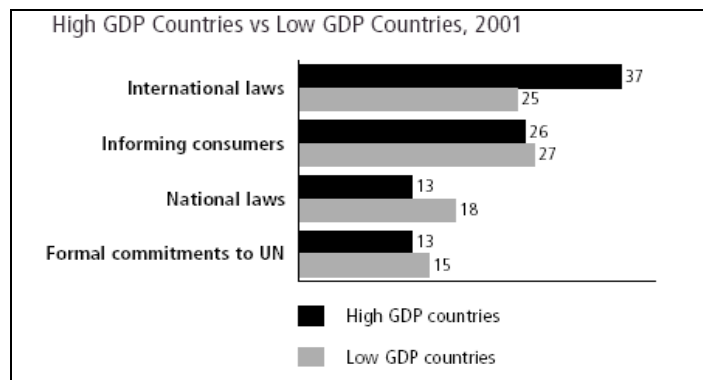
Source: The Millennium Poll, (1999) Environics International, http://www.globescan.com/news_archives/MPExecBrief.pdf#search=%22Millennium%20Poll%20on%20corporate%20responsibility%201999%22 *white spaces in the chart represents “depends”, “other” “none” and “DK/NA” (Don’t know/ not applicable)

Figure 4. Ranking of Most Important CSR Actions



Source: Expectations of Companies, Key Trends and Findings, Shareholder Opinion and Stakeholder Research, http://www.socialinvestment.ca/SIO_pres_GlobeScan.pdf

Figure 5. Most Effective Approaches in Making Global Companies More Socially Responsible



Source: International Environmental Monitor, (2002) Environics International (see endnote 7)

Appendix 1

GRI: Guidelines to standardise Sustainability Reports

Performance Indicators

Measurement of the impact and the effort of the organisation grouped through integrated, economic, environmental, and social performance indicators. Within the GRI context indicators can be both quantitative and qualitative.

Category	Aspect	
Integrated	Systemic or cross-cutting	non-standardised
Economic	Direct and indirect economic impacts	Customers Suppliers Employees Investors Public sector
Environmental	Environmental	Materials Energy Water Bio-diversity Emissions, effluents, and waste Suppliers Products and services Compliance Transport Overall
Social	Labour Practices and Decent Work	Employment Labour/Management Relations Health and Safety Training and Education Diversity and Opportunity
	Human Rights	Strategy and Management Non-Discrimination Freedom of association and collective bargaining Child labour Forced labour Disciplinary practices Security practices
	Society	Indigenous rights Community Bribery and corruption Political contributions
	Product Responsibility	Competition and pricing Customer health and safety Products and services Advertising Respect for privacy

Source: BSD Brasil, (2007) GRI: Guidelines to standardise Sustainability Reports, http://www.bsd-net.com/docs/handbookgri_e.pdf

ENDNOTES

¹ Global 250 is the top 250 companies selected from Global Fortune 500.

² National 100 is the top 100 companies in 16 identified countries selected by revenue ranking based on a recognized national source.

³ Voluntary disclosure of information into the public domain about the environmental footprint of the company and other CSR activities is better developed in North America and Europe. Firms are forced by community expectations and pressure to provide this information in the absence of legislative requirements.

⁴ It is questionable whether this was anything other than a good advertising opportunity with no social responsibility component. NAB has allocated \$1.8 billion to institution turnaround costs, but would not specify precisely the amount spent on the costs of sponsoring the Commonwealth Games (media reports suggested that \$30 million was spent on advertising, sponsoring and supporting invited guests at the Commonwealth Games) or the new branding program, a process that costs millions and takes years to complete. Nielsen Media Research indicated that NAB spent \$19.2 million on media advertising during 2005, up from \$16.2 million in 2004 (Shoebridge, 2006).

⁵ A change of name for the Bank of New South Wales had been under consideration for some time, but it was no simple matter. In 1850 the Bank had been incorporated as a corporation under its own 'Bank of New South Wales Act' of the New South Wales Parliament. This meant that the Bank operated under legislation separate from company's legislation. A proposal for amendment was presented to the New South Wales Legislative Council, and although an earlier request had been denied, permission was eventually granted in the form of the Bank of New South Wales (Change of Name) Act 1982.

⁶ In NAB's Wealth Management team alone (200 staff) their paper usage was more than halved in just one year falling from 8,000 pages per day to 3,600 pages per day and across the institution paper usage fell by 4%. By contrast, in their New Zealand operations, where they have not implemented paper saving initiatives, over the same period of time paper usage increased by 12%.

⁷ Question csr02_4 "Which one of the following approaches will be most effective in causing global companies to be more socially responsible? Would it be through.....?"