

3 March 2006

Mr John Kluver  
Executive Director  
Corporations and Markets Advisory Committee  
GPO Box 3967  
Sydney NSW 2001

**Re: Corporate Social Responsibility - Discussion Paper**

Dear Mr Kluver,

RepuTex Ratings and Research Services is pleased to provide a response to the Corporations and Markets Advisory Committee Discussion Paper on Corporate Social Responsibility.

RepuTex is an independent private company engaged in the provision of quality research and ratings services in the area of Corporate Social Responsibility (CSR) and reputation. The company has an extensive knowledge of the CSR market in Australia and Asia. In the Asia Pacific region RepuTex is the pre-eminent leader in the provision of Social Responsibility Ratings and other reputation related research services.

RepuTex has chosen to address a number of issues raised in the Discussion Paper and also directs the Committee to our submission to the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Corporate Responsibility.

Please do not hesitate to contact me if you would like to discuss further the issues and recommendations raised in this submission.

Yours sincerely



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## Response to CAMAC Discussion Paper on Corporate Social Responsibility

Prepared by Michael Moran & Kirsten Saunders

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In responding to the CAMAC Corporate Social Responsibility Discussion Paper (November 2005), RepuTex refers the Committee to our submission to the Parliamentary Joint Commission (PJC) on Corporations and Financial Markets which should be read in conjunction with this paper.

In concluding the submission to the PJC, RepuTex advised that the following measures may enhance consideration of stakeholder interests by incorporated entities and/or directors:

- 1) Greater co-ordination between government departments and agencies in order to expand the government's current approach to CSR which has traditionally been limited to community partnerships and philanthropy;
- 2) Development of a CSR specific ministerial portfolio to oversee effective implementation and encourage greater uptake of existing voluntary mechanisms;
- 3) Government to take a leadership role:
  - 3.1 By ensuring that its departments, authorities, and agencies all meet acceptable CSR standards;
  - 3.2 By supplementing existing guidelines and requirements for tenders and supply agreements to include satisfactory CSR standards;
  - 3.3 By promoting multi-stakeholder initiatives, e.g. the Global Compact, and encouraging incorporate entities to formally supporting established norms and instruments; and
- 4) Strengthening of regulatory frameworks to adopt mandatory triple bottom line reporting.

RepuTex contends that reform of the *Corporations Act* merely to provide safe harbour for company officers who engage in CSR is unwarranted. While strict interpretation of the law suggests that Australian directors must give exclusive consideration to advancing the financial, not social or moral interests of shareholders, in practice given the tangible and intangible benefits associated with CSR activity, any perceived illegality of CSR is mistaken, and therefore granting safe harbour is unnecessary. Undertaking CSR as a risk management tool, is by its nature in the best interests of the corporation. RepuTex does however support an expansion of directors duties in order to better promote CSR and sustainability principles, for example via the implementation of mandatory reporting requirements.

RepuTex would like to comment specifically on the CAMAC Terms of Reference that question:

- *How might corporate responsibility be usefully described for working purposes?*

It is RepuTex's contention that Corporate Social Responsibility (CSR) has historically been ill-defined in the Australian context. This has led to confusion among sections of the business community, regulators and key stakeholders which has ultimately skewed debates concerning the merits of effective CSR strategies.

This stems from the perception in some quarters that CSR is merely profit sacrifice via the improvement of various social ills. In practice the adoption of CSR has a much wider application and may be more appropriately defined as a form of risk management. From this perspective:

Corporate Social Responsibility (CSR) is best defined as a management tool or strategy which organisations can employ to address key governance, environmental, social and workplace risks, while capitalising on opportunities which add value to the organisation and its stakeholders.

- *What are the incentives or disincentives for a company to conduct its business in a socially responsible manner?*

There are clear incentives for a company to 'conduct its business in a socially responsible manner' as suggested in the above definition.

In recent years RepuTex has seen a shift as leading organisations both in Australia and internationally have begun to appreciate the positive implications of 'sincere' CSR and recognise the fundamental importance of addressing stakeholder concerns to both the long-term viability of the corporation and the community. As the concept is further developed – and adopted as a mainstream management tool – it is expected that CSR strategies will be more widely adopted to drive innovation and enterprise value as well as incorporated into operational risk management procedures as competitive pressures drive take-up due to the benefits of an integrated approach. Evidence of this can be seen in the incremental improvement in performance of Australian and New Zealand companies in the RepuTex Social Responsibility Ratings between 2004 and 2005.

Nonetheless disincentives remain an impediment to full scale take-up of CSR across the Australian market. This can be attributed to a number of key factors:

- i) Not all companies recognise the business case for CSR or perceive issues linked to governance, environmental, social or workplace factors as an immediate material risk to the company and its shareholders.
  - ii) There remains a focus on short-term indicators, eg. share price, at the expense of the long-term sustainability of the company. In sections of Australian corporate culture this tends to hinder the ability of some corporate decision-makers to recognise long-term costs and externalities.
  - iii) While the Federal Government has actively promoted CSR through the Prime Minister's Community Business Partnerships (PMCBPs) there has been a lack of coordination between government departments and agencies to nurture the mainstreaming of CSR. Greater governmental coordination and advocacy has thus far occurred in other jurisdictions such as the United Kingdom where CSR has moved from a fringe activity to one increasingly seen as a mainstream corporate governance tool used by directors of publicly listed companies and government owned enterprises.
- *Do different or additional implications arise depending on the nature and size of the enterprise?*

While 'different or additional implications arise depending on the nature and size of the enterprise' certain sectors continue to lag behind others in their efforts to integrate CSR into their operations. Research by RepuTex indicates that companies in sectors including Banking and Materials have tended to more readily adopt strategies which address key social risks and maximise associated opportunities, while other sectors such as Media, Hotels and Leisure have tended toward a compliance based approach.

There are obvious reasons for this. Industries such as Banking have been subject to significant stakeholder scrutiny stemming from a perceived lack of concern for the communities in which they operate. This has led some Banks to become CSR leaders in Australian (and global) markets. Similarly companies in the Materials sector, particularly the extractive industries, have attempted to adopt a more sustainable profile following various NGO and social movement actions around issues stemming from environmental degradation and indigenous rights.

Cynics may argue that these organisations are attempting to placate their critics and remain wedded to irresponsible practices. However it is increasingly recognised that CSR has matured beyond its early public relations phase and can be seen as a new way of doing business. It

creates competitive advantage through driving efficiency, innovation, lifting employee, productivity/quality/retention and enhanced enterprise value through maximisation of human, reputation and social capital. These are benefits that than can accrue to any organisation, and while a company's approach will invariably be influenced by the nature of its operations and the sensitivity of the markets in which its operates, it can be argued that CSR remains an integral business strategy.

- *In practice, to what extent is corporate decision-making driven by stakeholder concerns?*

Clearly decision-makers make distinctions between different classes of stakeholders. Nonetheless, as noted above, leading corporate entities recognise the benefits of managing broader stakeholder expectations and the benefits that this can have on shareholder value. These include an enhanced capacity to manage and control risk associated with new or altered demands from corporate regulators, employees, the community, shareholder activists and consumers, and ultimately, the long-term preservation of the communities in which they operate. From this perspective recognising stakeholder concerns is an emerging business imperative, but it should be noted that corporate decision-makers do not uniformly prioritise stakeholder interests.

- *In practice to what extent do stakeholders consider a company's social responsibility performance when making assessments about a company?*

Again distinctions remain between different stakeholders and the nature of the company's business. However RepuTex has seen a range of internal and external stakeholders – be they investors, consumers, community groups or employee publics – gradually take a greater interest in the extra-financial aspects of a company's operations. This interest will invariably gather pace as the corporation assumes a more prominent role in society. We have already seen NGOs and other pressure groups monitoring the activities of corporate entities and often basing their assessments about a company on its performance against defined social and environmental targets. Yet, in recent years this has moved beyond the interest group sphere to include individuals, potential employees, supply chain partners and increasingly, investors.

The most cogent example of this is the growth in the Socially Responsible Investment (SRI) market. We have seen a steady increase in the number of investors who look to non-financial concerns when making investment decisions. This shift has been driven by an increasing awareness of issues such as environmental degradation, social and economic inequality and human rights abuses, coupled with a growth in financial literacy. Such investors now account for a growing proportion of the investment market in Australia and as of June, 2004 there was over AUD\$21 billion in Funds Under Management (FUM) in SRI products. While this clearly remains a comparatively small proportion of overall FUM, many in the investment community anticipate that SRI will make a move into the financial mainstream within the next decade as increasingly savvy and informed investors allocate superannuation payments to SRI products. Indices, such as the RepuTex SRI Index, are a further reflection of this trend and play an important role in providing information to investors, while sending a signal to companies about the importance of CSR.

Similarly there is evidence to suggest that employees are increasingly taking into account the social and environmental profile of potential employers. This is acting as a key driver of CSR take-up within Australian companies as they strive to attract and retain talent in increasingly competitive and globalised labour markets.

- *Are there any changes that could enhance triple bottom reporting, sustainability or like reporting including:*
  - *whether any aspect of this reporting should be mandated and, if so, for what companies and what respect(s)*

In encouraging non-financial reporting, governmental support is crucial and a consistent approach needs to be taken to ensure that reports are both adequate for stakeholders and comply with legal requirements. The Global Reporting Initiative (GRI)'s sustainability reporting guidelines are perhaps the most globally applied reporting standards and Australian companies should be encouraged to utilise the G3 guidelines (to be released in October 2006) in the preparation of their sustainability or Triple Bottom Line reports (TBL).

The current situation in Australia where companies' main environmental disclosure requirements are the National Pollutant Inventory and the *Corporations Act s 299(1)(f)* has resulted in a situation where stakeholders cannot always accurately compare the performance of two similar companies due to different approaches taken to the reporting of non-financial information and different understandings of what constitutes a 'particular and significant environmental regulation'.

Comparisons are further complicated when contrasting social performance indicators. Few companies have adopted uniform standards by which social performance can be reported creating issues for stakeholders, external assessors and ratings agencies. While it is often more difficult (and contentious) to quantify a company's social performance which is largely a qualitative exercise, it has become evident that Australian companies have fallen behind their OECD counter-parts.

It is RepuTex's contention, therefore, that the Federal Government should implement mandatory TBL reporting for listed companies. Some critics have put forward the argument that mandatory reporting would promote a compliance based approach. They note further that this would stymie innovation and lead to a 'tick box' culture. However it is RepuTex's contention that mandatory reporting – particularly if material risks were effectively factored into disclosures – would create competitive pressures that would lead to innovation as organisations attempted to outperform sector and market peers. Moreover, at its most basic level reporting would require companies to consider the impact, positive or otherwise, that their operations have on the community. This requirement for heightened transparency would potentially act as a driver for companies to develop systems to capture data on their performance and introduce strategies to manage and mitigate their impacts.

- *increasing the level of clarity and comparability of these reports –*

There is a need to promote a greater degree of consistency and comparability between CSR, TBL or sustainability reports. Globally recognised benchmarks such as the GRI offer a useful model which balances the need for flexibility while promoting a globally uniform approach. Where implemented effectively benchmarking against GRI indicators also enables stakeholders to efficiently establish the CSR profile of a particular entity.

- *any suggested changes to external verification of those reports*

There is clearly a space for mandating independent verification of CSR reports. As noted in the Discussion Paper there is a perception among sections of the community that CSR reports can become instruments of 'Greenwash' as companies attempt to fashion reports as brochures or extensions of PR campaigns. Verification by established auditing firms and consulting companies adds credibility and integrity to these reports, and where conducted by an independent, third party, an additional layer of accountability.

- *To what extent are voluntary initiatives leading to improvements in corporate social and environmental performance?*

As outlined in the Discussion Paper, 'voluntary initiatives by their nature lack sanctions, other than peer or market pressure'. RepuTex acknowledges that there is a growing recognition that

voluntary initiatives without adequate government support are insufficient in promoting CSR, and has found that corporate Australia's environmental and social performance has not significantly improved through voluntary mechanisms, although there has been an incremental improvement over time as innovative companies push forward.

A case in point is the target for Australian retailers to voluntarily phase out plastic bag usage by 2008. Rather than following the lead of Ireland in placing a levy on plastic bags – which resulted in usage being cut by 90% in the first five months alone<sup>1</sup> – the Australian Retailers Association and major retailers lobbied instead for a voluntary reduction plan. Under the plan, group one companies (including Coles, Woolworths and Kmart) set a target of 50% reduction by December 2005 (using 2002 figures as the baseline). However as of July 2005 participating retailers had managed only a 33.8 per cent cut, prompting calls for a mandatory levy to be reconsidered.

Another example of Australia falling behind others on the global stage is in the area of greenhouse gas emissions. While Australia is admittedly on schedule to meet its Kyoto target (despite not ratifying the Protocol), it should not be forgotten that Australia is in fact the only developed country allowed to increase its emissions over 1990 levels. In comparison to the European Union, which (in part through its use of financial incentives to reduce emissions) reduced its 2003 total emissions by 1.7% below the baseline<sup>2</sup>, Australia's 2003 total emissions increased 1.1% over the baseline levels<sup>3</sup>.

The lack of sanctions and/or mandated mechanisms to reduce emissions, such as the development of national carbon trading schemes, has significantly influenced the degree of action by companies to reduce greenhouse gas emissions in Australia. The lack of governmental support for significantly increasing the mandatory renewable energy target (MRET) can also be considered a major factor in the lack of innovation shown by utilities companies in investing in renewable energy developments and technologies.

- *What lessons might be derived from any experience with voluntary initiatives?*

Beyond mandating CSR reporting, RepuTex recognises that voluntary mechanisms – particularly those that rely on market-based instruments – remain the only feasible solution to broader take-up of CSR across the Australian market. The Federal Government could promote enhanced environmental performance of corporate entities through regulatory support of specific actions such as emission reductions as indicated above. Similarly it can continue to actively promote a culture of corporate giving through the PMCBPs which will gradually lift the philanthropic performance of Australian companies. However voluntary initiatives which lack adequate governmental support will not in themselves encourage the development of a sustainable corporate culture.

## **Recommendations**

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It is therefore our contention that government should take a leadership role. It needs to promote enabling policies which support CSR among Australian corporations. In this respect, RepuTex believes that there are a number of voluntary or market based options which would alleviate the need for overly prescriptive regulatory measures. These require commitment from both the public and private sectors:

- 1) *A whole-of-government approach to CSR.* Where not constrained by conflicting policy objectives governmental bodies should become CSR leaders. There is already evidence that this is taking place with GBes performing well in the RepuTex Social Responsibility

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<sup>1</sup> See for example <http://news.bbc.co.uk/1/hi/world/europe/2205419.stm>

<sup>2</sup> [http://themes.eea.eu.int/IMS/IMS/ISpecs/ISpecification20040909113419/IAssessment1118392868101/view\\_content](http://themes.eea.eu.int/IMS/IMS/ISpecs/ISpecification20040909113419/IAssessment1118392868101/view_content)

<sup>3</sup> <http://www.greenhouse.gov.au/inventory/2003/index.html>

Ratings relative to listed and privately-owned entities. However there is a space for greater information exchange between governmental bodies and coordination of policy objectives with respect to CSR. Similarly there is a need heighten the profile of CSR in the broader community and the private sector. The PMBCPs, while commendable, do not retain the profile required to fully mainstream CSR. RepuTex suggests examining the approach taken by the United Kingdom's Department of Trade and Industry and establishing a Ministerial portfolio with oversight of CSR policy.

- 2) *Introduction of ethical sourcing or CSR supply chain mandates by governmental bodies.* To reward sustainable business practices governmental bodies could implement policies which specifically stipulate that partners and contractors that meet high CSR standards (e.g. across governance, environmental, social and workplace practices areas) should be rewarded with preferential access to contracts and tenders.
- 3) *Promotion of the SRI market in Australia.* The growth of socially responsible investing – and the signals this sends to corporate decision-makers – offers perhaps the most important driver of CSR take-up across the Australian market.
- 4) *Mandatory CSR reporting.* RepuTex recognises that there are strong arguments in favour of maintaining the current policy mix of promoting voluntary measures and strategic partnerships through the PMBCPs. However while RepuTex supports an approach which favours market mechanisms and self-regulation we believe that mandatory reporting would help lift the CSR performance of Australian companies and heighten transparency of extra-financial and material risks.