Chapter 2

Sustainable organisation

Learning outcomes

After reading this chapter, you should be able to:

- understand the opportunities and complexities related to adopting a strategic, proactive approach to sustainable development in the business context
- familiarise yourself with the debates surrounding the role of business in sustainable development, including various related concepts such as corporate social responsibility and bottom of the pyramid
- identify the key principles and themes associated with sustainable organisation, with an emphasis on the link to core business
- understand the business case of sustainable organisation and to identify the business-related risks and opportunities associated with diverse aspects of sustainable development, emphasising a strategic approach
- appreciate the complexities and opportunities of adopting a strategic approach to sustainable organisation, be it at the level of a small enterprise or multinational corporation
- understand key elements of a sustainability management system and in particular the importance of internal and external reporting
- appreciate the need for, and challenges of, cross-sector collaboration in addressing many of the complex social and ecological challenges facing organisations.

Overview

- This chapter introduces the notion of the sustainable organisation as a key element of business strategy.
- The notion of sustainable organisation is related to a broad array of other concepts, such as corporate social responsibility and stakeholder engagement, which are discussed in the chapter.

2.1 Introduction

- Discussions which focus on strategic decisions regarding a company's interface with its social and environmental context, are becoming increasingly common in company boardrooms and among senior managers.
- In the early 1990s, for example, Shell executives realised that such issues were becoming key determinants of business success when public opinion turned against the company with the murder of Ken Saro-Wiwa and his colleagues in Nigeria, and the decommissioning of the Brent Spar oil rig.
- Not only did these controversies contribute to consumer boycotts of Shell service stations, they also had a profound effect on recruiting top-level employees when talented managers or engineers balked at the prospect of working for a company with a tarnished reputation.

2.1 Introduction (cont.)

- More recently, in 2005, AngloGold Ashanti faced similar problems when an international non-governmental organisation (NGO), Human Rights Watch, published a report accusing company personnel in the Democratic Republic of Congo (DRC) of paying a bribe to a local militia known to have committed terrible human rights abuses. Compromising headlines appeared in newspapers around the world.
- This example highlights the risks associated with doing business in what some refer to as 'weak governance' zones, where the government is not willing or able to fulfil its responsibilities in providing public services and establishing and enforcing common rules.

2.1.1 Strategy, stakeholders and strategic direction

- *Sustainable development* is not only about improved risk management, and avoiding or mitigating negative impacts.
- Important business opportunities may also be identified and direct benefits may be realised.
- Example: Wal-Mart – Target of civil society activism as a result of negative social and environmental impacts associated with its low-cost supply chain strategies.
  - Guided by committed leadership – The company adopted a range of new policies to reduce waste, pollution, and energy usage associated with its products, as well as in its stores and logistics.
  - This has significant environmental and social benefits as a result of the company's size, and the large number of suppliers and customers. For instance, the company stated that in 2008 it achieved a 38% improvement in efficiency of its United States fleet.
  - Such efforts have had the effect of not only improving the company's reputation, but have also led to significant direct cost savings.

2.1.2 Defining the term 'sustainable organisation'

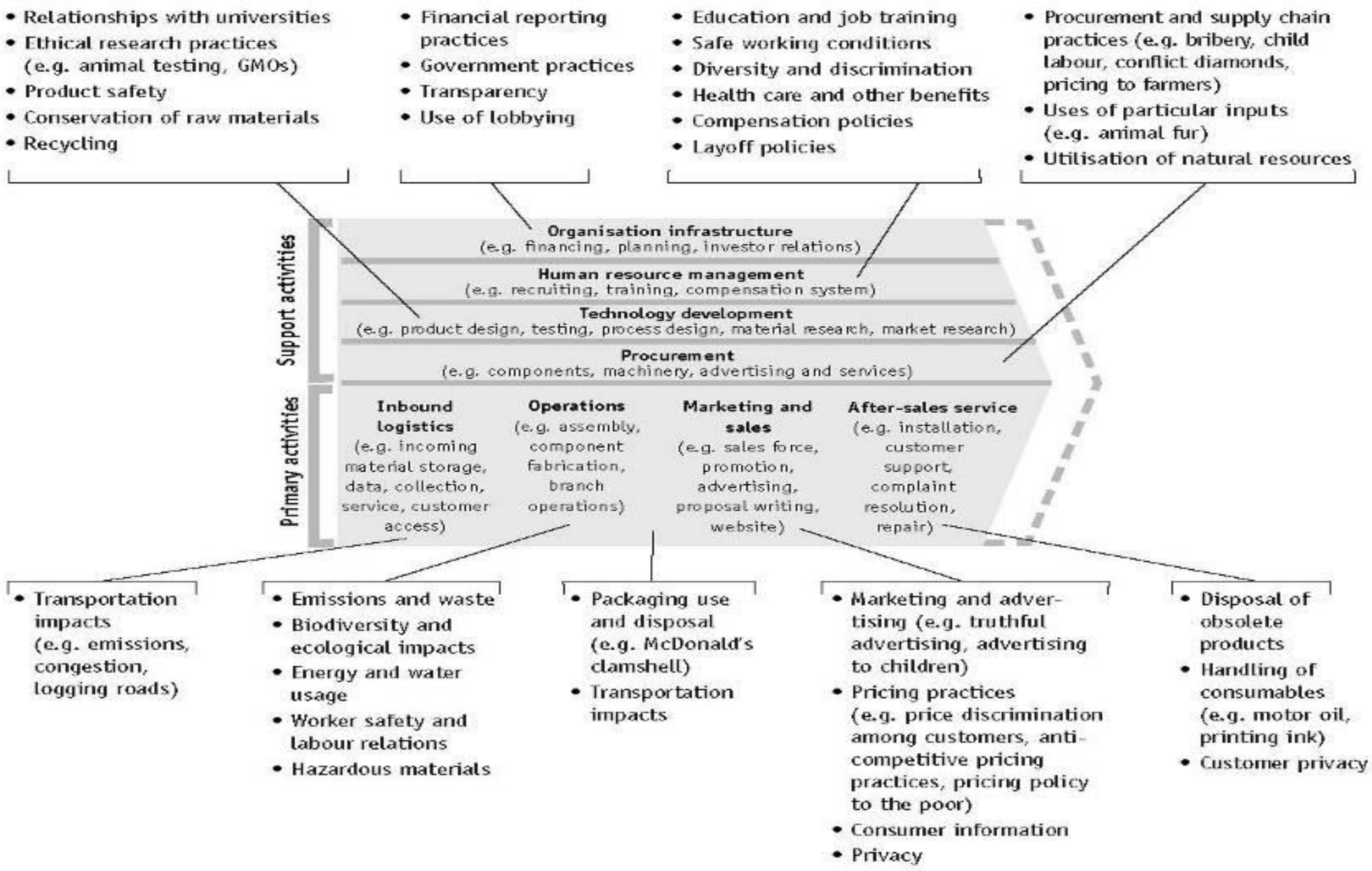
- Sustainable organisation is used here as an umbrella term for proactive efforts to design and implement financially viable business models that simultaneously contribute to solving some of the complex social and environmental problems we face.
- It encompasses and goes beyond some of the other prominent terms used in this field, such as *corporate social responsibility* (CSR), *corporate citizenship*, and *social entrepreneurship*.
- Sustainable organisation is particularly pertinent in Sub-Saharan Africa, where more than 40% of the population continue to live in extreme poverty.

2.1.3 A strategic approach to sustainable organisation

- Instead of philanthropy or legal compliance, the overarching approach to the relationship between a company and its social and environmental context should fundamentally be about organisational strategy.
- The organisational strategy identifies the key opportunities and challenges for the company and it is at this level that the interface between organisation and society must be understood and responded to.
- This is because social and environmental factors such as poverty, crime, food security, water scarcity and climate change, present a company in any sector with important risks that need to be adequately understood and responded to.
- They also provide a company with potentially important opportunities, if innovative means for addressing these problems can be developed.

A strategic approach to the sustainable organisation

Figure 2.1 Possible social and environmental issues associated with core business activities in the value chain[7]

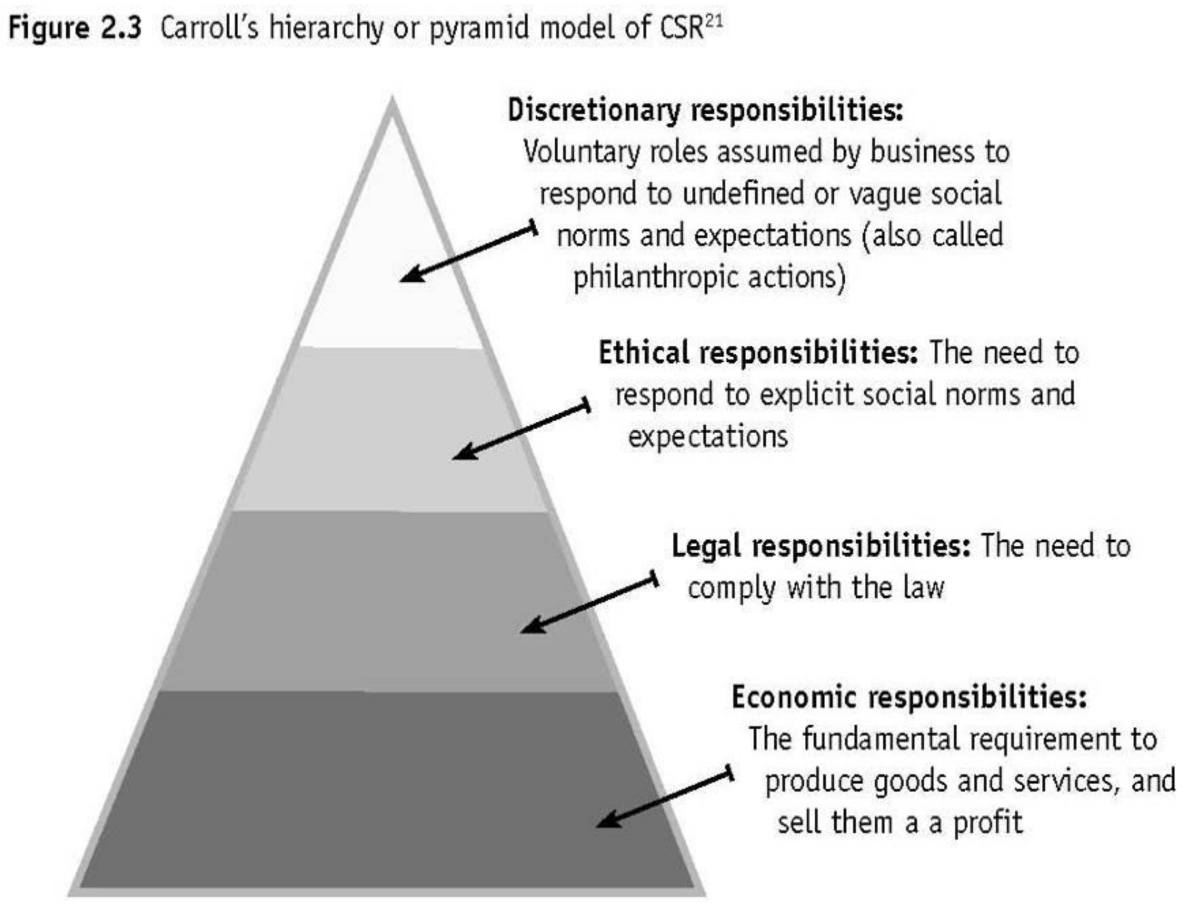


2.2 From CSR to sustainable development & human rights

2.2.1 Defining corporate responsibilities

- A range of terms, and a variety of historical trends, pertain to the link between business and its social and environmental context.
- One of the earliest terms used was *corporate social responsibility* (CSR) – published in a book in the United States (US) in 1953.
- CSR was defined 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'.
- In South Africa business leaders decided after the 1976 Soweto riots that continued neglect of black townships was not in the interests of business.
- The result was the formation of the Urban Foundation, which contributed to health, education and housing projects in black townships.
- Many efforts were philanthropic in nature (termed *corporate social investments* in South Africa) and were not linked to core business.
- The term CSR has not been particularly popular in South Africa.

Figure 2.3 Carroll's hierarchy or pyramid model of CR



2.2.2 Enter sustainable development

- In the 1980s and 1990s there were revitalised scholarly discussions on CSR, business ethics, and stakeholder engagement .
- In 1992, the Earth Summit in Rio de Janeiro, Brazil argued that 'the policies and operations of business and industry, including transnational corporations, can play a major role in reducing impacts on resource use and the environment'.
- The Earth Summit also called upon business leaders to contribute decisively to sustainable development by changing their strategies and decisions.
- Since then, this link between CSR and sustainable development has become increasingly prominent.
- In 2003 Hart and Milstein motivated for a shift from the established concept of CSR to sustainable enterprise, with an emphasis on the business opportunities that this may offer:
  - 'A sustainable enterprise is one that contributes to sustainable development by delivering simultaneously economic, social, and environmental benefits – the so-called triple bottom line.'

2.2.3 The United Nations Global Compact principles and human rights

- Former UN Secretary-General, Kofi Annan, established the UN Global Compact in 2000.
- The Global Compact asks companies to embrace, support and enact, within their sphere of influence, a set of core values in the areas of human rights, labour standards, the environment and anti-corruption.
- The emphasis of the UN Global Compact and others on the need for companies to 'embrace, support and enact' a range of principles, including 'internationally proclaimed human rights', has strong links to the concept of *corporate citizenship*.
- The notion of corporate citizenship creates an important link between the role of organisations and human rights.
- Human rights are a core component of understanding the role of business in society.

2.2.3 The United Nations Global Compact principles and human rights (cont.)

- As pointed out by Crane and Matten, ‘citizenship’ relates to the rights and responsibilities of members of a community.
- Although corporations are not ‘real’ citizens, they are juristic persons and powerful actors in society, so they arguably have duties to respect, uphold and further the social, civil and political rights of citizens.
- This duty is all the more pertinent because ‘the failure of governments to fulfil some of their traditional functions, coupled with the rise in corporate power, has meant that corporations have increasingly taken on a political role in society’.
- The notion of corporate citizenship creates an important link between the role of companies and human rights.

2.2.4 The bottom of the pyramid and the call for alternative business models

2.2.4.1 The notion of the bottom of the pyramid

- A particularly prominent part of this new frontier is the argument that important opportunities are related to the creation of new markets.
- Prahalad and Hart argue that large corporations can make substantial profits in marketing to the poor at the 'base of the pyramid' (BOP):

"Contrary to popular assumptions, the poor can be a very profitable market – especially if MNCs [multinational corporations] change their business models. Specifically, [the poor are] not a market that allows for the traditional pursuit of high margins; instead, profits are driven by volume and capital efficiency"

- This notion is popular with big business, because it suggests that innovation in product development, supply chain management and business model design can b beneficial both for the innovating company and for poor people.
- Example: Vodacom phone shops as a means of reaching BOP customers in urban and rural communities in South Africa.

2.2.4.2 Criticisms of the BOP concept

- There are, however, a number of criticisms of the BOP concept.
  - Pertinent risks in focusing on the poor as consumers are not limited to the business, but more importantly, also involve the poor.
  - The poor often do not have disposable income and one suggestion is that BOP strategies might involve close links to microfinance arrangements.
  - Microfinance is indeed a crucial aspect of many anti-poverty initiatives.
  - Arguably, the most famous such initiative is the Grameen Bank, which started in Bangladesh and facilitated the distribution of small loans through a network of women's groups in villages.
  - One of the key requirements for obtaining a loan, however, was that it would be put to productive use, such as buying a sewing machine or paying for education.
  - In the absence of such requirements and the crucial social networks that tie the Grameen Bank participants into a way of doing things, there is a danger that marketing to the poor exploits their vulnerability, increases indebtedness, and further entrenches their poverty trap.

2.2.4.3 A revised model of BOP strategy: co-creation

- One response to criticism of the BOP model has been the development of a revised model of BOP strategy, which emphasises the 'co-creation' of value involving a close cooperation between the company and communities that are meant to benefit.
- This call for the co-creation of value between business and communities is aligned with what some call the emergence of a new form of business organisation, indeed a new form of organisation.

"Over the past few decades, the boundaries between the public (government), private (business), and social (non-profit) sectors have been blurring as many pioneering organisations have been blending social and environmental aims with business approaches... While the mission and method of many organisations in the business, government and nonprofit sectors are becoming steadily more similar something more than simple blurring of the boundaries is occurring. Pioneering organisations in the three sectors are in fact converging toward a fundamentally new organisational sector that integrates social purposes with business methods: a Fourth Sector"

2.3 The business case and institutional drivers

2.3.1 The business case as a response to critics and sceptics

- Key challenge is persuading chief executives and finance directors of the business case for sustainable organisation.
- Business leaders are likely to query the need for any business activities that may be perceived as being ‘non-core’.
- The best-known critique of the notion that the role of business goes beyond making a profit has come from liberal economists, led in particular by the Nobel laureate, Milton Friedman.
- Economists’ concern is that business decision makers are neither mandated nor capacitated to devote attention and resources to anything other than the company’s core purpose of making money.
- CSR proponents or related terms argue that that contributing to sustainability objectives will also benefit a company’s financial performance in the long term.

Table 2.2 Key elements of the business case for CSR and sustainable organisation

- Better anticipation and management of an ever-expanding spectrum of risk
- Improved reputation management
- Enhanced ability to recruit, develop, and retain staff
- Improved innovation, competitiveness, and market positioning
- Enhanced operational efficiencies and cost savings
- Improved ability to attract and build effective and efficient supply chain relationships
- Enhanced ability to address change
- More robust ‘social licence’ to operate in the community
- Access to capital
- Improved relations with regulators
- A catalyst for responsible consumption

2.3.2 The business case is multifaceted

- North American academic literature has a long history of studies that aim to identify a correlation between companies' social performance and their financial performance.
- For instance, Margolis and Walsh surveyed 127 studies on this topic published between 1972 and 2002.
- They write that 'a simple compilation of [these studies'] findings suggests that there is a positive association, and certainly very little evidence of a negative association, between a company's social performance and its financial performance'.
- However, they also note that these studies are plagued by diverse methodological shortcomings, which leaves the debate over the business case unresolved.

2.3.3 Ethics and institutions as drivers of the sustainable organisation

- A key concern is that the business case alone is not a sufficient motivation for responsible business practices.
- Avery argued:
  - 'While there is a strong "business case" for respecting human rights, companies are obliged to respect human rights at all times, not just when it suits them.'
- In many instances, such arguments have been made on ethical grounds.
- In South Africa institutional drivers are:
  - National legislation e.g. BEE
  - The King Reports
  - JSE Socially Responsible Investment (SRI) Index
  - International CSIR initiatives of relevance in South Africa

2.3.4 An overview of pertinent institutional changes in South Africa

2.3.4.1 National legislation

- South Africa's transition to democracy in 1994 brought with it significant and far-reaching changes in government policy and regulations, many of which have played a crucial role in the development of South Africa's sustainable organisation agenda.
- Table 3 provides an overview of some of the relevant legislation and policies.
- This list suggests that the South African government has done more than many other states to legislate on social issues.
- This is most clearly evident in legislation relating to Black Economic Empowerment (BEE), which includes a number of dimensions closely aligned with the sustainable organisation agenda.
- Although South Africa's policy framework is widely respected, crucial concerns remai with regard to the implementation of this legislation, which has important implication for business.
- CSR should therefore not be seen as being relevant to 'beyond compliance', but it needs to be seen as also contributing 'towards compliance'.
- Limited government capacity has also been identified as a potential driver for CSR in South Africa, in that businesses take on developmental or regulatory responsibilities because the state is not fulfilling them.

2.3.4.2 The King Reports

- State policies and legislation has been complemented with the emergence of increasingly important market-based incentives and pressures.
- One of these was the publication in mid-2002 of the second *King Report on Corporate Governance for South Africa*, colloquially known as the King 2 Report.
- It is significant in that it explicitly defined and motivated for concepts such as 'corporate citizenship,' 'social responsibility,' 'triple bottom line' performance, and 'sustainability reporting.'
- For instance, it advocated an inclusive 'stakeholder approach', which 'recognises that stakeholders such as the community in which the company operates, its customers, its employees and its suppliers, amongst others, need to be considered when developing the strategy of a company'.
- It also required that 'every company should report at least annually on the nature and extent of its social, transformation [including black economic empowerment], ethical, safety, health, and environmental management policies and practices' and that this ought to take into consideration the guidelines of the Global Reporting Initiative.

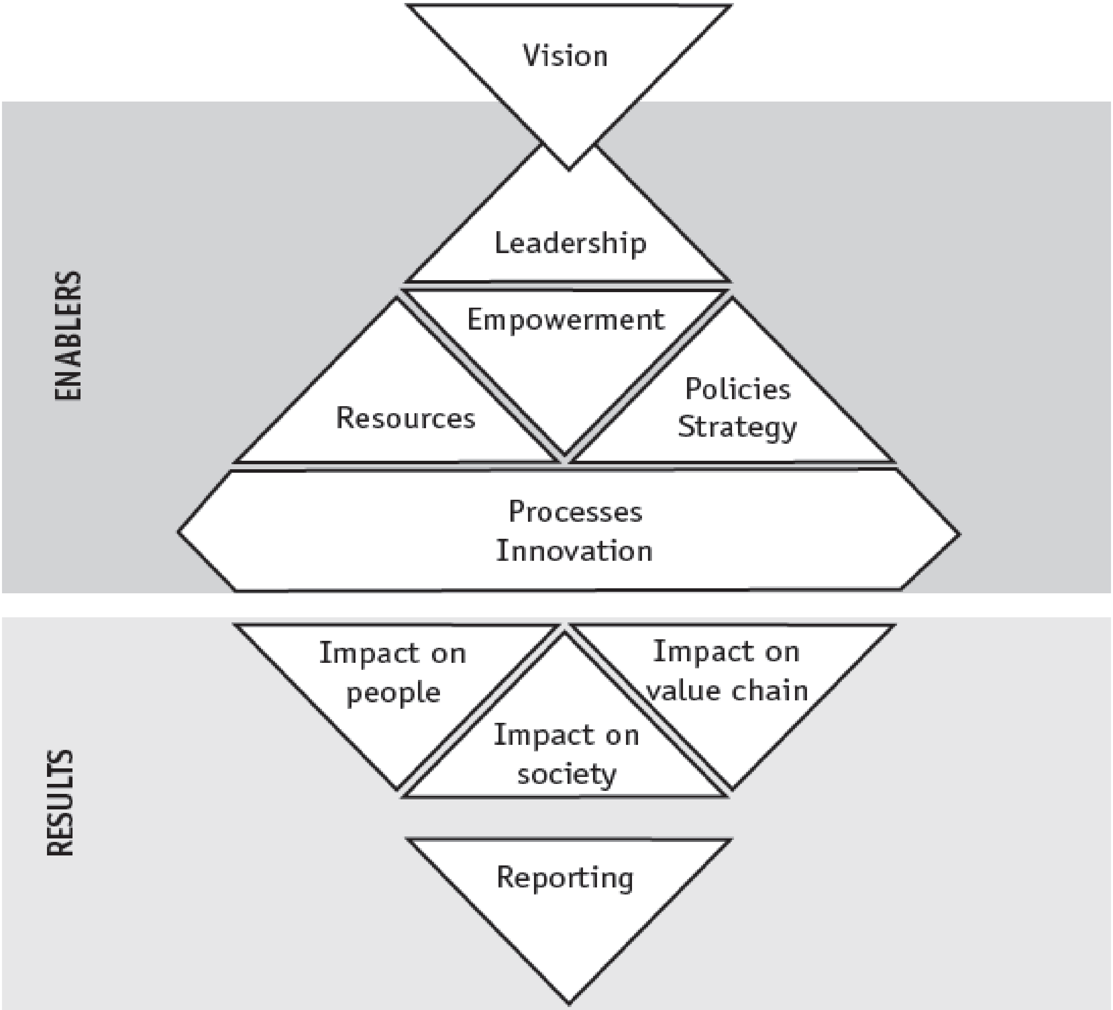
2.3.4.3 The JSE Socially Responsible Investment (SRI) Index

- A further market-based development relates to the role of investors in pushing the CSR agenda, a driver frequently mentioned by corporate managers, as illustrated above.
- The London and New York stock exchanges, in particular, have significant amounts of investment funds allocated to so-called socially responsible investments (SRI).
- Primary mechanisms for these are the Dow Jones Sustainability Index in New York and the FTSE4Good in London.
- In South Africa, however, SRI represents only about one per cent of investments under management, and there is relatively little awareness of and support for SRI, though it is growing rapidly.
- To provide a benchmark for SRI investors, as well as an impetus for CSR more generally, the JSE Securities Exchange launched a sustainability index in 2004 called the JSE Socially Responsible Investment (SRI) Index.
- This made it the first bourse in an emerging market to develop a sustainability index.
- The Index is centred on a set of approximately 70 criteria or indicators (originally more than 90), grouped in terms of the four overarching categories of corporate governance, society environment, and economy

2.4 Business management systems and public reporting
2.4.1 The United Nations Global Compact Performance Model

- This model, shown in Figure 2.5 below, focuses on diverse enabling factors and the kind of results that are to be achieved and monitored.
- The model provides for two broad categories of performance elements, as highlighted in Figure 2.5:
  - the enablers
  - the results.
- Underlying all of these elements, however, is an emphasis on the role of stakeholder engagement and partnership.

Figure 2.5 The UN Global Compact Performance Model



Source: C. Fussler, A. Cramer, and S. van der Vegt, *Raising the Bar: Creating Value with the United Nations Global Compact* (Sheffield: Greenleaf Publishing, 2004:58).

2.4.2 The enablers – from vision to innovation
2.4.2.1 Sustainable organisation values in vision and mission statements

- In terms of the enablers, the company's vision is at the very top of the model.
- The core of sustainable organisation is in how a company defines its purpose and the degree to which this incorporates broader society.

2.4.3 Measuring and reporting results

2.4.3.1 Reporting results with regard to impacts on people, the value chain, and society

- The lower box in Figure 2.5 shows the *results* achieved through continuous improvement of the company's enablers.
- 'Employees do not just expect material advantages from their job, but rather an enhancement of meaning and community in their lives.'
- In terms of results related to the value chain, it is important to understand how customers perceive issues related to corporate citizenship as this will influence their purchasing behaviour.
- It is also important for companies to better understand how they can influence suppliers and contractors so that they improve their social and environmental performance.
- In terms of impact on society, Fussler and his colleagues concede that assessing and managing a company's impact on society is complex and fraught with tensions.
- One of these difficulties is assessing the boundaries of a company's responsibilities up or down the supply chain.
- Another is the tension of conflicting expectations – while the term 'sustainable development' confuses some people because of its simultaneous emphasis on growth and limits, it ought to be seen rather as a requirement for creative thinking and innovation.
- Finally, there is the concern about a company's ability to make a difference when the broader framework conditions – market pricing, weak governments, etc. – present such powerful countervailing forces.

2.4.3.2 The standardisation of sustainability reporting – the Global Reporting Initiative

- Globally, sustainability reporting has become increasingly standardised particularly for large, publicly listed companies.
- Much of this has been due to the Global Reporting Initiative (GRI), a multi-stakeholder initiative that has developed a set of principles and indicators for such reporting, which is either integrated into a company's annual report or comes in the form of a stand-alone sustainability report, and it is generally also prominently represented on companies' websites.
- The GRI defines sustainability reporting as follows:

  "Sustainability reporting is the practice of measuring, disclosing, and being accountable to internal and external stakeholders for organizational performance towards the goal of sustainable development… A sustainability report should provide a balanced and reasonable representation of the sustainability performance of a reporting organization – including both positive and negative contributions"

- In South Africa, the King Report on Corporate Governance (its third version was published in 2009) emphasises the need for sustainability reporting and recommends adherence to the GRI guidelines

2.5 From stakeholder engagement to collaboration
2.5.1 The stakeholder model of the organisation

- Engaging stakeholders is a key component of devising and implementing a sustainable organisation strategy.
- Definition of stakeholders:
  - 'Stakeholders are persons or groups that have, or claim, ownership, rights, or interests in a corporation and its activities, past, present, or future. Such claimed rights or interests are the result of transactions with, or actions taken by, the corporation, and may be legal or moral, individual or collective. Stakeholders with similar interests, claims, or rights can be classified as belonging to the same group: employees, shareholders, customers, and so on' (Clarkson, 1995).
- *Primary stakeholders* are those stakeholders whose continuing participation is vital to the organisation, or those who have direct and well established legal claims on an organisation's resources.
- *Secondary stakeholders* are those groups that are affected by the organisation, but are not essential to its survival, or that do not have legal claims but rather rely on non-binding or ethical obligations

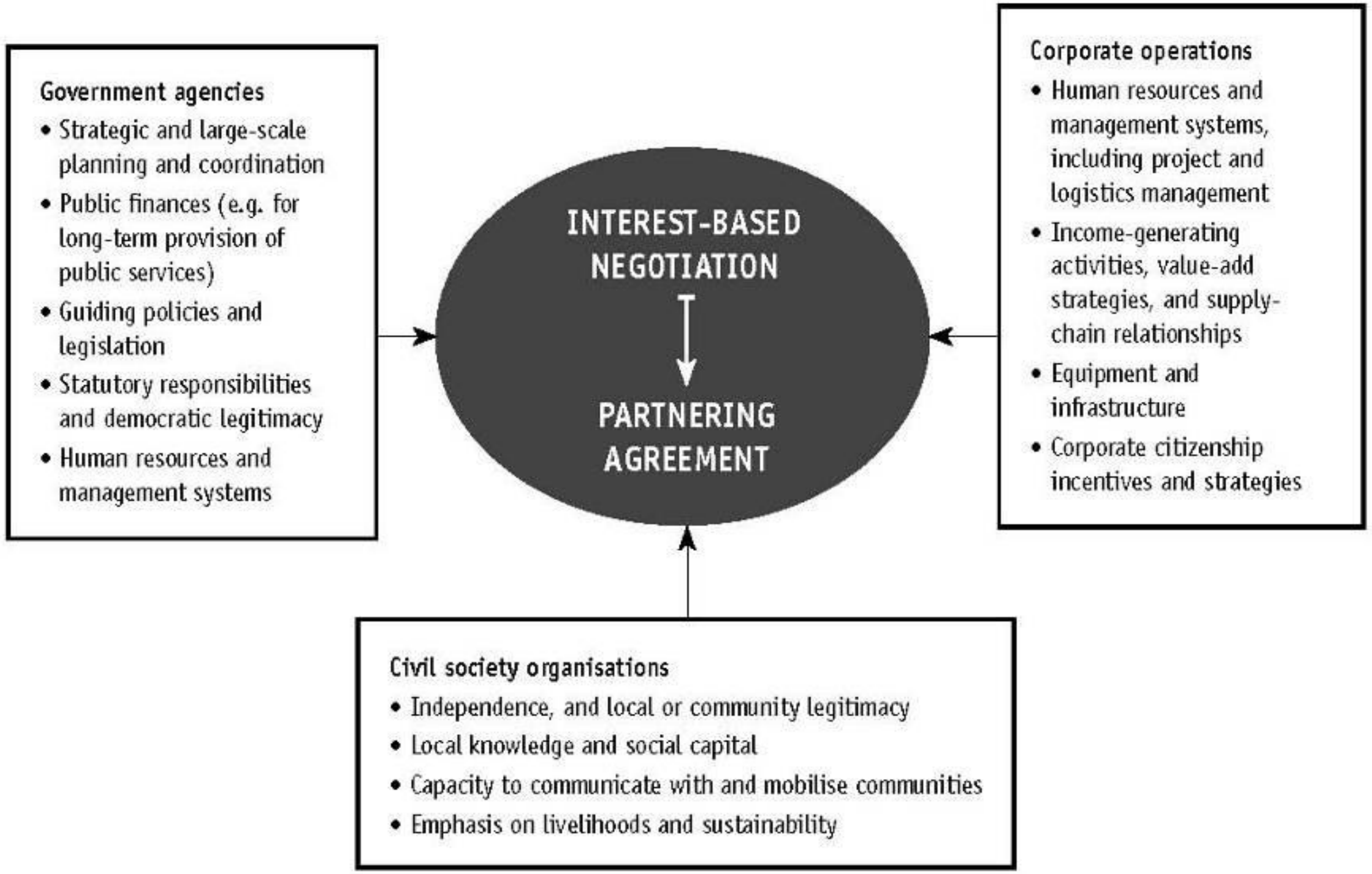
2.5.2 Stakeholders as part of a network or complex system

- There are, however, a few problems with the stakeholder model.
  - One is that it focuses almost exclusively on the relationship between the company and the stakeholders.
  - In other words, it implies neutral relationships between the stakeholders.
  - But stakeholders and stakeholder groups, particularly the local ones, are in fact embedded in a complex web of relationships.
  - Furthermore, it puts the company in the centre of these relationships, which potentially sidelines important processes that are outside the immediate ambit of the company but which nevertheless play a crucial role in an effective corporate citizenship strategy.
  - Consequently, it often places insufficient emphasis on the role of power in the relationships between the company and its stakeholders, as well as between the various stakeholders

2.5.3 Partnerships
2.5.3.1 A trisector partnership model

- Implementing sustainable organisation strategy effectively requires effective partnerships.
- The key principle in partnership formation is ‘complementary core competencies’.
- Capabilities and resources of the organisation are combined with those of other sectors for maximum effect, allowing each participant to concentrate on its strengths.

Figure 2.8 Schematic illustration of complementary core competencies in a trisector partnership model[126]



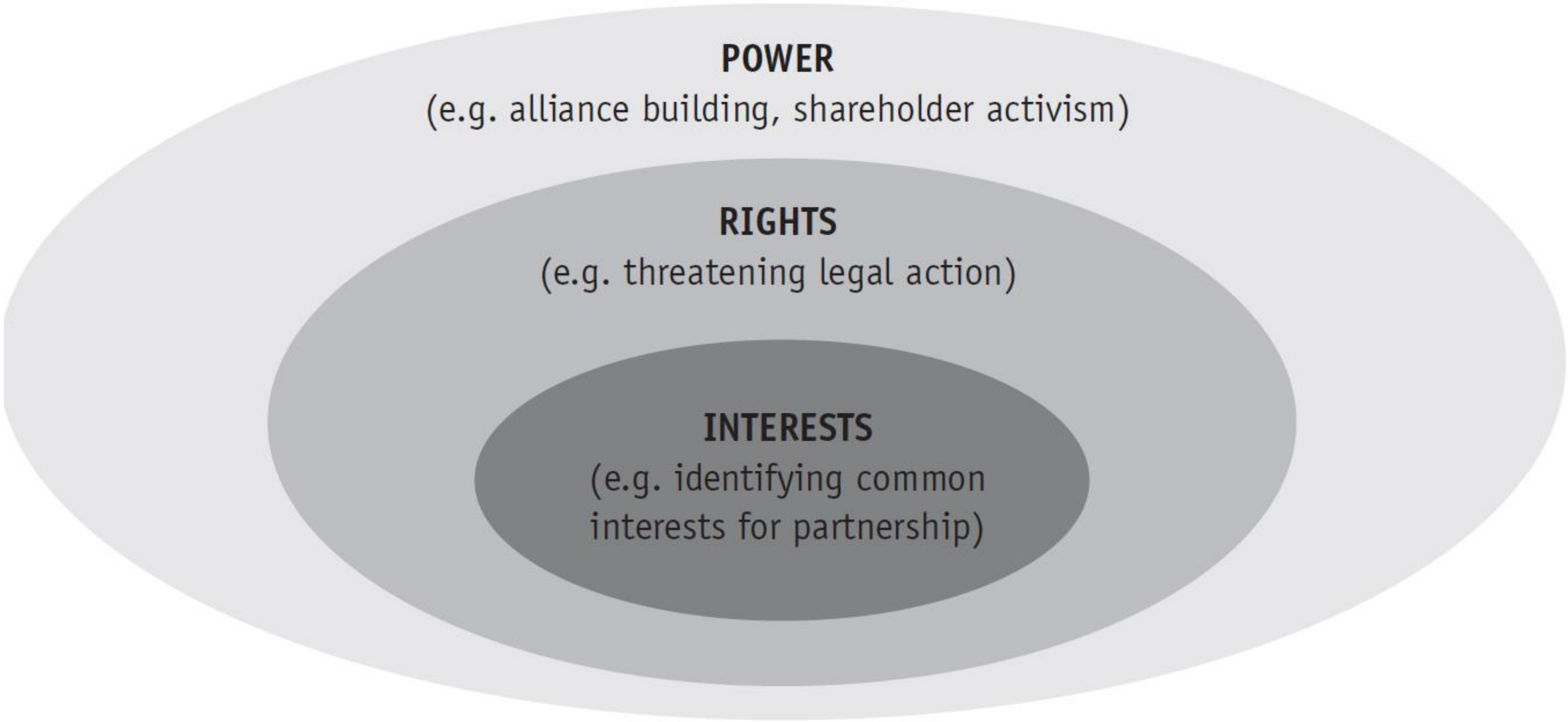
2.5.3.2 Challenges with regard to partnering

- Common practical challenges to the partnering process are an inadequate understanding by the potential partners' representatives of what the parties could offer each other:
  - an unwillingness to modify or compromise; ineffective attempts to institutionalise the partnership within the participating organisations; and insufficient orientation of newcomers to the partnership.
- Even where common interests can be identified, the partners' culture, working methods and organisational objectives are often very different.
- The kind of communication between people that underlies effective partnership cannot be taken for granted.
- Partnerships are no panacea.
- In particular, they may require certain circumstances and conditions. According to one critic, the notion of partnership assumes that 'both parties are relatively equal in their power and access to resources', an assumption that is rarely justified.
- Others maintain that a balance of power is not necessary, arguing that the partnership need only benefit each partner more than is possible by any other means.
- Most agree, however, that partnerships cannot succeed if companies misuse their considerable financial or human resources, or their undue influence over government officials, to systematically enhance their bargaining position.

2.5.3.3 Interest-based negotiation

- The concept of interest-based (or principled) negotiation was introduced by Fisher and Ury in their ground-breaking book, *Getting to Yes*.
- They argue that bargaining on the basis of entrenched positions does not produce optimal outcomes because more attention is paid to positions than underlying interests.
- It is also inefficient because opponents tend to start with extreme positions, and it strains the ongoing relationship between the parties.
- Their alternative – principled negotiation – requires negotiators to, inter alia, 'focus on interests, not positions', to 'invent options for mutual gain' and 'insist on objective criteria' for the process and outcomes of decision making.
- This approach is the basis of the following four requisite conditions for partnerships:
    - *Balancing power asymmetries, Acknowledging critical rights, Negotiating both converging and conflicting interests, Managing relations with stakeholder constituencies.*

Figure 2.9 A strategic approach to partnerships relies on reference to interests, rights and power



SOURCE: Adapted from A.L. Lytle, J.M. Brett and D.L. Shapiro, 'The Strategic Use of Interests, Rights and Power to Resolve Disputes', Negotiation Journal, 15, 1 (1999): 31–51.

2.6 Summary

- The concept of the sustainable organisation is a key element of business strategy.
- It is important for a business leader to understand both the risks and opportunities associated with an organisation's social and environmental context.
- There are direct economic benefits that can be derived from a proactive approach to sustainable development.
- Once the scope and drivers of the sustainable organisation have been identified, the next step is to understand how to define and implement a corresponding strategy.
- An important cross-cutting imperative is effective stakeholder engagement.
- The key is to develop partnerships based on mutual benefit.
- The sustainable organisation recognises that long-term business success is intimately tied to the success of the communities and societies in which it operates.

Discussion questions

1. Is it important to adopt a strategic approach to sustainable development, rather than one focused primarily on philanthropy or marketing? If so, why?

2. What are the social responsibilities of business?

3. Milton Friedman argued that the social responsibility of business is only to maximize profits, though he also added that this needed to be done within the law and the ‘rules of the game’. If confronted with this perspective, how would you respond?

4. Do you think there is a clear business case for the sustainable organisation? If yes, how would you describe and substantiate it? What is the role of ethics in this regard?

5. What does it take to devise and implement an effective sustainability strategy?

6. What is the role of internal and external reporting in the implementation of a company’s sustainability strategy?

7. Why is stakeholder engagement an important aspect of a sustainability strategy?

8. What are some of the possible challenges to effective stakeholder engagement and cross-sector partnership, and how can these be responded to?