Measuring corporate responsibility

Acting ethically – and being able to prove it

If the arguments about the benefits for companies to act – and being seen to act – in a responsible and ethical manner have largely been won, important now is credible measurement of these actions. Andrew Likierman outlines how to build a responsibility gauge

Formal corporate social responsibility programmes used to be confined to energy companies with obvious reputations to lose. But the past few years have seen most of the largest companies formalise corporate social responsibility, rather than rely on quixotic charitable contributions and ad hoc reaction to public pressure.

So are the programmes a success? Corporate social responsibility increasingly involves considerable resources, not just money, but also scarce senior management time. So questions about what is being achieved will become more pressing.

Performance evaluation is important in part to make sure objectives are understood (itself often a key measure of corporate responsibility success) and can be acted on. And as pressure groups engage and comparisons drawn with competitors, reputational risk is increasingly at stake.

So how would we know if a corporate social responsibility programme was successful? This article sets out the measurement difficulties and what can be done to tackle them.

Defining the issues

Companies can decide for themselves what social responsibility means and whether there is a moral dimension, and companies may differ in those judgments from shareholders or other stakeholders. And the frameworks set out by external bodies may be different again. Mismatches, and how to reconcile them, is one difficulty here.

Another is how to differentiate corporate social responsibility objectives from ordinary business. Many organisations include the way they treat customers and employees as part of the social responsibility agenda. With no agreed definition of social responsibility, this is rarely challenged, but the question here is what makes staff and customers so special.

It is simply good management to aim for low labour turnover and high customer satisfaction. It is part of strategy to recognise inter-dependency. As Coca Cola puts it, “If local communities suffer from water scarcity, so do we. If HIV/AIDS ravages the communities in which we operate, the people impacted are our employees, our customers and our consumers.”

A major private equity investor says: “If a company in which 3i has an investment acts irresponsibly on corporate responsibility issues, this may affect the monetary value of that investment and, as a shareholder in the company, raise reputational issues for 3i.”

Similar considerations apply to treating constraints as part of corporate social responsibility performance. Paying taxes and not unlawfully pumping toxic waste into the local river are obligations, not achievements.

Because measurement is seen to be so difficult, having no measures at all is sometimes taken as the way to get round the problems. Many corporate social responsibility reports are largely taken up with aspirational statements about cheerful but apparently random initiatives accompanied by pictures of cheerful and apparently random employees. Measures hardly feature.

If there are measures, these tend to focus on activity – numbers of programmes started, numbers of people seconded and amounts of money spent. This is not entirely surprising. If measurement is seen to be so difficult, best pick anything that is easily measurable.

The issue here is that success cannot be about activity. It must be about what is achieved by the people and the money in relation to the objectives of the programme.

Measurement is made yet more difficult by the need to identify the link between action and result. This is a problem even for less diffuse programmes. The objectives have to set out the expected impact, but charting the results of corporate social responsibility initiatives really is tough.

Finally, there is the issue of how to interpret the...
results. As with any set of objectives, success will depend on the choice of measure, the basis of comparison and the degree of stretch in a target. But it is rarely clear how these have been decided. Take targets. A 20% reduction in emissions? Why not 30%? And by 2008? Why not by 2007?

There may be very good reasons for the targets and timescales, but other than the inevitability of fatality targets being zero, the logic and link to overall company objectives and corporate plans are often obscure, perhaps even to the company itself.

It does not have to be. BT’s basis for the proportion of employees over 50 is that it should be “proportional to that which exists in the UK labour force”. Simple enough to explain, and much better than a figure that looks as if it has been plucked out of the air.

**Tackling the challenges – in four steps**

But how should these issues be met? Here is a four-stage process.

1 **Clarify the measurement framework**

The Prudential noted that in 2005 it “reviewed our CSR strategy to ensure that it continues to align our business objectives with our stakeholder concerns”. The process of defining the objectives in terms that reconcile external requirements with internal aims is the first element in clarifying the measurement framework. It is essential to make corporate social responsibility credible inside and outside the company. Yet, unlike the Prudential, many companies avoid the process, wrongly assuming that responsibility cannot be aligned in this way.

The reason for alignment is for employees to have the guidance for focused action. So objectives should not include actions that are normal good management practices or legal obligations.

Definition of objectives should also include an explicit statement about the connection between corporate social responsibility and financial performance, of the kind given by Land Securities, which says: “An effective CR programme can help to identify and manage business risks, generate operational effectiveness through resource efficiencies, and contribute to enhancing our reputation and achieving differentiation in the market place.”

While the objective of a corporate social responsibility policy can hardly be to destroy shareholder value, there are different views about whether, in making key choices, other stakeholders are to be taken as on a level with shareholders. This is a subject on which established indices take different views as well as measuring different aspects of corporate social responsibility (see box top right).

Clarification of the assumed costs and benefits is also essential. This does not mean squeezing them into an implausibly numerical straitjacket. Some of the direct costs will be quantifiable but many (including the opportunity costs of employee time) will not. Few of the benefits will be quantifiable either.

The contribution of corporate social responsibility to reputation (or damage to it) will ultimately be a matter of judgment, as will the benefits of community involvement or impact on the environment. But all costs and benefits must be at least identified so that a commentary on progress can be provided, even if a formal financial analysis cannot.

Finally, there should also be a statement about the risks involved in pursuing the corporate social responsibility agenda, which should be a subset of the company’s main risk analysis. Ideally this should include a statement of the risks of not pursuing the corporate social responsibility agenda. Shell, for instance – and understandably in view of its problems over recent years – makes it clear that risk analysis operates across the full range of its activities.

2 **Find better measures**

Measures and related targets, linked clearly to corporate social responsibility objectives, need to be chosen with care. Work practices in a recycling workshop in Bangladesh or a textile plant in Burma may meet local criteria but be quite unacceptable in Britain.

An example of how to find a better measure is given by Unilever, which teamed up with Oxfam to assess the impact of its operations on reducing poverty in Indonesia. Their report identified the complexity of the economic impact. One aspect was unexpected – the importance of the distribution chain. Another aspect – less unexpected – was that the impact on people living in poverty depended on how the benefits of the value created were spread.

The importance of this study for measurement is that simplistic measures of economic impact, such as wages or taxes paid, are not sufficient to make the connection to the underlying aim of reducing poverty.

The Unilever/Oxfam example provides the general lesson that any proxies chosen need to be appropriate. If the purpose of a diversity programme for black and other ethnic minority employees is to improve the quality of company decision-making, the measure should be of those employees linked to decision-making. If most of the relevant staff are nowhere near the decision-making process, tracking their proportions in the company as a whole is not good enough.

Breaking down overall figures to provide relevant detail in this way is another method of improving the quality of measures. Roche, for example, had “regretted losses” (people

**Different indices, different coverage**

The Dow Jones Sustainability Indices define sustainability as “a business approach that creates long-term shareholder value by embracing opportunities and managing risks deriving from economic, environmental and social developments”.

The UK’s Business in the Community defines corporate responsibility as managing a company’s impact “so as to add value to the company and increase wider social and economic well-being now and over the longer term”.

The FTSE4Good index, taking a rather different approach from the other two, excludes certain industries such as tobacco and nuclear power and, “reflecting a broad consensus on what constitutes corporate social responsibility”, looks for evidence of behaviours in five areas – “working towards” environmental sustainability, relationships with stakeholders, human rights, the supply chain and bribery.
Performance credibility league table

In ranking order, credible success requires measurement of performance against:

- externally established measures and targets (best);
- comparison to peers;
- last or previous years;
- internally set targets;
- lists of activities (worst).

Definition of objectives should also include an explicit statement about the connection between corporate social responsibility and financial performance

the company would have wished to retain) of 2.2% within an overall employee turnover of 6.7%.

Turning the focus from activity to outcomes is also part of devising better measures. Evidence of the difference made on the ground is a crucial element here, just as lack of any evidence leaves open the question “what’s this all for?”

Examples of outcome measures are the effects on work practices in a country whose local standards are unacceptable in a company’s home country or sourcing raw materials from targeted poor communities.

Though process and activity measures should generally be avoided, some may be relevant in providing signals. An example might be evidence that managers are including corporate social responsibility objectives in their day-to-day work and how that improves, or otherwise, their ability to achieve their own objectives.

Where possible, measures involving comparisons need to be with a peer group or an externally recognised standard, not with purely internal measures, or based on an arbitrarily set target. The Business in the Community Corporate Responsibility Index, for example, compares companies with the sector and with a wider index of more than 120 organisations.

Such measures might also cover meeting industry guidelines or national requirements. Sony’s television recycling rate in 2004 was 86%, compared with a legal requirement of 55%. This is very different from meeting a requirement that is part of normal business. BAA makes it clear that permission for a third runway at Heathrow is dependent on its meeting requirements for European Union air quality standards by 2010.

Not all external measures are necessarily credible. A high ranking in Stonewall’s Equality Index carries greater weight as a measure of gay and lesbian diversity than relying on those in the organisation who have voluntarily declared their sexual preference to the company. Similarly, anonymous returns from a high proportion of employees in surveys across years will be a better indication of trends than inclusion and ranking in the “Great Place to Work” table, where competition is confined to those companies that apply to be judged.

Finding better measures means taking account of best practice elsewhere. There is an increasing body of information in this field, much of it public because it is not seen as commercially sensitive and because companies are keen to demonstrate that they are taking action. Outsiders, including representative groups, and insiders with wide experience, such as non-executive directors, can help to give context here.

Finally, it should be recognised that measures should be appropriate to the impact of the organisation on the corporate social responsibility agenda and choices should be explained accordingly. When “Corus recognises that steel and aluminium industries are significant contributors to man-made greenhouse gas emissions”, it is easy to put the measures chosen by the company in a different context to those of a small service company.

3 Ensure that measurement is credible

Credible measures of achievement start with credible data. This is often a serious problem on the ground – contributions to HIV/AIDS in sub-Saharan Africa will be difficult enough for those on the spot and the definition of “cure” for less lethal diseases may well vary. This also applies inside the organisation.

AstraZeneca reported that it was still working to standardise the reporting of accidents and incidents, with a database to be rolled out in 2006. If the figures cannot be properly verified, reservations about the integrity of the data need to be made clear, or there will be a danger that a campaign will be discredited by embarrassing revelations.

Credibility is also enhanced by a choice of measures that are clear, not seen as biased, reported consistently and with a run of figures. Spills by oil companies are of interest to environmental campaigners and BP reports the number of spills. It also reports the (arguably more relevant) amount of oil spilled and not recovered. Both figures cover five years and credibility is further enhanced by recent data showing that they were moving in opposite directions.

Improvements in data may well result in a short-term deterioration of performance. For Rio Tinto, a target to reduce the number of employees exposed to noise levels over 85 decibels was not met in part because monitoring improved with the implementation of new occupational health standards.

Questionnaires are essential for the less easily measurable factors, such as reputation or attitudes. So special attention needs to be paid to the way questions are framed and the whole questionnaire is constructed, sent out and returned, so that bias is avoided. (Everyone will be familiar with the invitation to fill in a questionnaire about service quality while the person being assessed is standing and watching.)

Credibility of the measures is also enhanced by transparency in setting out the basis by which the scope, objectives, measures, targets and timescales have been decided. Targets set against externally established targets are the most credible. Less credible come those compared to peers.

Next in the credibility league table (see box top left) come runs of figures over time. These provide a
context for performance but trends on their own are difficult to interpret. Next lowest in the table, but the most common, comes performance against internally set targets. They carry little clout unless good reasons are given for why the target level has been decided.

Bottom of the table come lists of activities. These may impress directors and employees but are likely to leave informed outsiders cold.

In its 2005 Corporate Citizenship report, Diageo recognised that some scores were lower than the average for a comparator group of high performing companies and that appropriate action was required. Similarly, Tate and Lyle admitted that there was a problem with contractor safety standards, but said the focus “in 2006 will be to bring contractor safety standards closer to the high standards of employee safety we are achieving at Tate and Lyle”.

Inclusion in one or more of the well-known indices (such as Dow Jones Sustainability Index, FTSE4Good or BITC Corporate Responsibility Index) will also add credibility. It is doubtful whether there is widespread understanding of the differences in coverage. But the very fact that organisations will be assessed against externally determined criteria will give them additional status.

This status is only likely to be short term, however. As inclusion in an index becomes the norm within any industry, failure of any prominent company to be included then becomes a matter of reputational risk. It will also always be worth tracking best measurement practice in the industry and indeed elsewhere.

4 Recognise limitations of the measures alone

Even after clarifying objectives, improving the measures and ensuring credibility, performance measurement challenges will remain. Corporate social responsibility is not a factory product and its measurement is not an exact science. Calls for a precise number for “the bottom line” or talk of the “ROI of CSR” are doomed, since many challenges are inherent to corporate social responsibility programmes, such as identifying the lags between action and result and taking account of quality. It is wise to recognise this, as does the Gulf-based airline Emirates, which uses “a wide variety of quantitative and qualitative evaluation techniques”, while Deloitte also conducts “some fairly extensive evaluations, which gives us a good feel”.

The reality of the measurement challenges needs to be acknowledged in a commentary. So, for example, if initial targets to hire ethnic minority groups are found to be unrealistic because of the lags in hiring, this should be acknowledged, not regarded as failure or a cause for apology. Similarly the company should not take credit for windfall improvements, such as a reduction in carbon emissions from less business travel when travel is reduced because business is bad. On the contrary, credibility will be enhanced if both setbacks and windfalls are explained in the commentary.

Among the very many corporate social responsibility targets achieved, Marks & Spencer will have reinforced its reputation for integrity by reporting the delay in “field to fork” self-assessment covering sustainability standards, especially combined with a commitment to introduce a database in 2006.

The commentary also needs to acknowledge the fact – already noted – that some costs and most benefits will not be measurable in numerical terms. Taking volunteering as an example, the opportunity cost of time is not just what people are being paid, but the benefit they might have given if they had not been away, less the long-term benefit to the organisation through the wider experience gained by the employee.

Similarly, any improvement in the company’s own motivation and morale as a direct result of a corporate social responsibility programme will be difficult to trace. So too will the improvement in the cost of capital from what might have been the cost of capital if the programme had not been in place. Rather than put dubious numbers onto these costs and benefits, the commentary should set out any assumed figures – and their limitations. This is not numbers territory.

The commentary also needs to reflect the relative importance of different corporate social responsibility measures. There is a tendency to treat all measures as having equal weight, when some will clearly be more significant than others.

Getting there

The journey to identifying corporate social responsibility success often starts with emotion and proceeds via ambiguity and technical problems to end with more emotion. This is a real challenge for those looking for a robust basis for constructing measures and interpreting them.

But if corporate social responsibility is to be an integral and credible part of that way an organisation works, a good measurement framework is essential. The four steps set out above will help to provide it.

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