

Chapter 2

Background: Social Role of Companies and Success Indicators

Abstract The basic function of any organization, i.e. that which legitimizes it socially, is to create value for society as a whole; however concern for the economic and financial factors involved in all trading activities has resulted in the development of accounting focused on these instrumental issues. The successful development of this accounting has led to results concerned with the actual purpose of organizations being relegated or overshadowed. This chapter analyses the different theories that make economic results a good indicator or social value: transaction cost theory, contract theory, agency theory, etc. These are contrasted with a system-based outlook taken from stakeholder theory, seen as a more suitable paradigm for understanding the inherent nature of organizations and their consequent function in society. Finally, the main indicators being developed are reviewed in an attempt to visualize the social value generated fundamentally by companies.

Keywords Social value • Stakeholder theory • Social accounting • Monetizing social value • Value for stakeholder • Theory of the firm • CSR • Corporate social responsibility

Ever since companies as we now know them first emerged in the Industrial Revolution they have been seen as generators of economic value (Groth et al. 1996), and their social functions have been relegated to a secondary level with indeterminate effects (Fernandes et al. 2011). The economic approach adopted from the outset has led to economic results, and more specifically financial results, being overvalued, and to social outcomes being considered as a mere extension of those results consisting even in the best cases of a mere distribution of the economic value generated. Economic theorists have, more or less explicitly, taken on board the argument that the “invisible hand” (Smith 1776) socially redistributes the economic value generated. As a result better and more and more sophisticated accounting systems have gradually been drawn up that enable us to capture a “true picture” of companies. However that picture refers only to their economic functions (Gassenheimer et al. 1998). In recent years calls have been made, with some degree of success, for the role of companies as generators of not only economic but also social value to be considered (Argandoña 2011; Jensen 2001; Melé 2002, 2009; Retolaza and San-Jose 2011; Retolaza et al. 2015), and for these two values to be

combined into a single integrated or blended value (Prahalad 2006; Porter and Kramer 2011; Emerson et al. 2003).

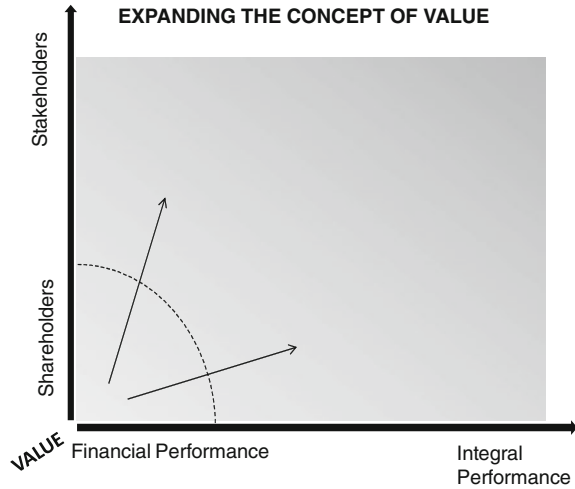
Is worth pointing out that the idea of production activities having a social value is not new (Dood 1973); it can be found in publications dating from long ago (Aquino 1954). However, it was in the wake of the Industrial Revolution that the idea gathered strength (Smith 1776), in both classical economics (Smith 1776), and Marxist thinking (Marx 1844). The earliest modern examinations¹ of the concept of social value consider it clearly from a subtractive perspective (Coase 1960), highlighting the social costs linked to negative externalities, especially in regard to the environment. Subsequently there has been a shift towards a more positive approach to the generation of social value by organizations, with the emergence of the social and non-profit sectors leading, in mercantile affairs, to concepts such as CSR (Carroll 1979; Husted and Allen 2007), corporate citizenship (Néron and Norman 2008), and stakeholder theory (Freeman 1984), where economic value is limited in the worst-case scenario and in other cases becomes merely instrumental, as in the ontological stakeholder view (OSV).

To date, the traditional view has focused exclusively on the value generated by companies for their shareholders, so the basic value indicator is profit after interest and taxation. However, based on the ontological view of stakeholder theory (San-Jose and Retolaza 2012; Retolaza and San-Jose 2011; Retolaza et al. 2015), a broader concept of value needs to be considered. The concept needs to be broadened in two directions: on one side there is a need to integrate economic value distributed to stakeholders as a whole, whether at the end of an operating period (taxes, dividends, reserves) or throughout the process of conducting economic activities (wages, social spending, taxes, R&D, etc.). On the other side there is a need to consider the not-directly-economic effects of an organization's actions on its various stakeholders. Such effects may be positive or negative (see Fig. 2.1).

Traditional theories of the firm incorporate the assumption that the only production factor that assumes residual risk is capital (Coase 1937), since other factors or resources have remuneration that is agreed on a contractual basis (Williamson 1979, 2002). Accordingly, residual profit and decision-making rights concerning management correspond exclusively to capital. However, these assumptions no longer seem to be entirely correct. On the contrary, capital can be considered as just one more production factor in regard to the generating of value, and the fact that its returns are variable does not entail any qualitative shift in regard to other stakeholders, a large part of whose remuneration may also be variable in the present or, undoubtedly, in the future since it depends largely on the results of the organization. The current economic crisis has also shown without a shadow of a doubt that residual risks are certainly not borne exclusively by shareholders but are rapidly transferred to other stakeholders: employees are fired or go unpaid, suppliers must put up with delays in payment and growing default rates, customers find themselves unable to claim on warranties, amounts owed to the public administration cannot be paid, and

¹We consider this to mean events from the mid 20th century onwards.

Fig. 2.1 Concept of social value. Financial versus blended results



costly bailouts must be funded by the public as a whole. These are just some of the residual risks externalized by capital holders. If the activities of the company entail the transfer of risks to a broad group of stakeholders, then why not examine what value is generated for them, even if it is only to determine whether that value offsets the potential costs entailed by the risks run. We might even consider that each individual stakeholder is capable of valuing their own risk/benefit matrix, given that public administrations (and through them the general public) are stakeholders in all organizations, and may therefore legitimately seek to learn the balance between creation and destruction of value at each individual organization. Indeed, the contractualist view (Donaldson and Dunfee 1994) holds that social value is the only moral justification for the existence of trading companies.

To date there has been little research into the monetizing of social value, and most of the papers published have focused on quantifying impacts (Barraket and Yousefpour 2014; Murphy and Ackermann 2014). The few publications that refer to the monetizing of those impacts are mere ad hoc justifications or are still at a very early stage of development. Although the concept of social value dates back a long way in economics (Schumpeter 1909; Tool 1977), there is as yet no standard way of evaluating it. Today's CSR frameworks are an attempt to establish a set of standards and regulations to objectify the concept (Gawel 2006); however, there are presently more than 300 such frameworks (Mazurkiewicz 2004). Although expectations have grown up that GRI may be a step towards standardization in regard to accounting (Tapscott and Ticoll 2003), the truth is that so far no regulations have been established in regard to monetizing indicators, and given that GRI is being developed as a framework for presentation rather than valuation such regulations are unlikely to be created. It is true that GRI4 and integrated reporting seemed to be heading towards some degree of homogenization and standardization of indicators that will, at some point, require a modernization of units of measurement, i.e. the monetization of social value (GRI 2013).

Explicit recognition for the social function of firms leads to concern for determining the quality and quantity of the social value generated by organizations as a whole and by each individual organization (Vancaly and Esteves 2011). Just as there is a need for an accounting system capable of showing and managing the economic value of trading companies, a system is required that can enable social value to be objectified, valued, and compared so that different organizations in particular and stakeholders as a whole can manage their actions in a way conducive to the optimizing of that value for the whole of the society in which organizations operate. Such evaluations were initially based on a dichotomy, with positive and negative valuation criteria to determine whether an organization generated or destroyed social value. This approach, which was influenced to a great extent by the view of externalities, was validated in practice by well-known indices such as the FTSE4Good and the Dow Jones Sustainability Index, and by actions such as “ethical investments” and “fair trade”. Subsequently, it was realized that progress needed to be made in identifying and quantifying the social value created by organizations, and the preparation of social reports or balance sheets was proposed (Bebbington et al. 2014; Fifka 2012). This required progress in terms of unifying regulations and criteria for preparation and presentation. The GRI (www.globalreporting.com) is perhaps the most highly structured example of this.

In spite of the progress entailed by the second type of feedback, there are still major shortcomings such as the following: (1) there is a great deal of room (too much) for interpretation in regard to the value generated depending on the interests of the managers of the organization itself; (2) no objective analysis of the social value generated by firms is provided, so no comparative analysis of that value is possible; and (3) the information on social value is not combined with the information on financial value, or at least does not use the same language (one is qualitative/quantitative and the other is monetary), which means that they are considered as two linked but clearly distinct subsystems.

This being so, further progress seems necessary towards standardizing a relatively homogenous, universal accounting system that can enable the social value generated by organizations—or at least a Industrial Revolution that the idea gathered strength significant part of it—to be monetarized, so that economic value and social value can be combined as two complementary areas of a broader concept of overall, integrated, expanded or blended value.

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Social Accounting for Sustainability

Monetizing the Social Value

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2016, VIII, 75 p. 23 illus. in color., Softcover

ISBN: 978-3-319-13376-8