

Sustainability: Environmental, Social and Corporate Governance Performance in Czech SMEs

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ABSTRACT

The paper focuses on environmental, social and corporate governance performance in relation to business sustainability in small and medium enterprises in the Czech Republic. Corporate Governance is understood as a key element when achieving economic performance as well as growth enhancing the investors' trust. It also makes it possible to create structures supporting the determination, checking and achievement of the objectives of the enterprise. It creates suitable initiatives for the members of the administrative bodies and the management. In the integration with sustainability, featured as the business strategy, the long-term corporate objectives, efficiency, performance, competitiveness are pursued through the inclusion of economic, environmental and social aspects to the corporate management. The sustainability of small and medium enterprises in the Czech Republic may bring about its effects in practice through the analyses of environmental, social and corporate governance performance, increased interests of uninvolved groups in the issues, competitiveness, increased market share etc. The inclusion of sustainability in the corporate management of an enterprise calls for a change in business. The target of the paper is the empirical analysis of the environmental, social and corporate governance performance in small and medium enterprises in the Czech Republic.

Keywords: sustainable development, sustainability, environmental performance, social performance, corporate governance

1. INTRODUCTION

In the Czech Republic, the sustainable development was defined in 1992 by Act No. 17/1992 Sb., on the Environment. From the original definition accept as a key element the theory of sustainable development meaning that the present generation should live in a way that does not restrict the life of the generations to come. These restrictions stem mainly from the

depletion of restricted resources. These may be economic, environmental and also social resources. Currently, the sustainable development is understood in a comprehensive way and „three pillars“ are considered: **society, economy and the environment**. Regardless the context, the crucial idea remains the same - people, environment and economic systems are interlinked [5].

2. SUSTAINABLE DEVELOPMENT AND BUSINESS ENVIRONMENT IN THE CZECH REPUBLIC

It can currently be observed that there is a growing importance of the support of sustainable development on the part of enterprises in the Czech Republic. The business sector, particularly small and medium enterprises, plays an irreplaceable role in terms of employment.

The importance of the business sector in market economy is quite obvious. However, an important role is also played by the business support. Research and empirical data demonstrate that the small and medium enterprises sector has a major share in the employment, in general. At the same time, small and medium enterprises are highly sensitive to the quality of the business environment. Small companies are mainly characterized by a weaker financial background. The basic task of such an enterprise is to keep or increase its own market value and to generate (reasonable) profit [15].

What is therefore of importance for the enterprise is that the market system should provide enough incentives and possibilities to make it behave in accordance with sustainable development. In order to make an enterprise competitive in the domestic and foreign markets, it should develop the principles of sustainable development. The enterprises are required, similarly to all other social stakeholders, to strongly boost the productivity of resources, while creating at least the same values, to reduce the consumption of materials, water, energy, to optimize services and products required by the customer.

An enterprises setting out sustainable development as

a strategic objective will sooner or later encounter a question of how to *measure sustainability of the enterprise, how to set the objectives* and what measures and procedure should be applied to meet the objectives. Therefore, it is necessary to collect, record, analyze and hand over information on the economic consequences of environmental and social activities. This information need must be satisfied and new tools must be developed to support the decision-making processes. Indicators, management analysis tools, communication and information system are employed by the enterprises to determine the sustainable development objectives.

What is emphasized is the use of existing tools in the enterprise, support of strengths and reduction of weaknesses [4].

Indicators used to measure sustainable development in enterprises are continuously developed by various international organizations in order to achieve an internationally recognized standard intended to ensure mutual comparability of national economies, individual fields of industry and individual enterprises

The most important international activity is Global Reporting Initiative-GRI focusing on standardizing the sustainable development report (Sustainability Report).

The objective of these voluntary activities is to win or strengthen the trust of a business entity with investors and other stakeholders.

The enterprise is under the pressure of *economic, environmental* and currently also *social* legislation, ethical codes and conditions of consumers, suppliers and therefore profit maximization ceases to be the only criterion. The decision-making must also include voluntary approaches related to sustainable development. The objective is to achieve a balanced relationship between the environmental, economic and social pillars - to ensure sustainable management at the level of the enterprise. It is also necessary to define the sustainable corporate governance, i.e. such management that results in the sustainable development of the enterprises as well as the whole society.

Enterprises that wish to succeed in the advanced international as well as domestic markets declare the quality of their business management by introducing relevant environmental management systems (ISO 9000, ISO 14 000, EMAS, Cleaner production, LCA, BOZP, SCR, etc.) and the ownership of applicable certificates. This guarantees the business partners, as well as other stakeholders (public administration, the general public) a certain standard of

corporate culture and the level of development of the relevant enterprise.

To measure the sustainable development at the corporate level abroad, a number of economic, environmental and social indicators are available, documenting the development of changes in the care of the enterprise in the individual environmental domains over the defined period of time. The indicators may be absolute and relative, financial parameters may be used for the indication.

The evaluation of sustainable development keeps being developed at the international level by various international organizations in order to achieve an internationally recognized standard aimed at a mutual comparison of national economies, the individual branches of industries and individual enterprises.

Micro enterprises, small and medium enterprises form an important part of every economy, as they account for a majority in the structure of companies. Over the past two decades, their number has been on the rise and their influence in the business environment, as well as social environment where they act as an element strengthening the social stability has been increasing. In relation to the environmental aspects the research indicates that the environmental management systems can also be introduced in small and medium enterprises. The environmental management system is a highly motivating voluntary tool for small and medium enterprises. A great incentive for the enterprises is the obtaining of a certain certificate in order to make their efforts at improving the management of the enterprise and its stance to the environment more visible.

The small and medium enterprise sector is a driver of the business domain, growth, innovation as well as competitiveness. It is also an important tool when creating job opportunities. As of 31st December 2010, there was a total of 1 029 871 small and medium enterprises in the Czech Republic, representing 99.83 % of all economically active entities. They had a 62.33 % share in the total employment rate and a 36.22 % share in the GDP.

The SMEs also have a major share in the total export and import where both these values reach a minimum of 50 %. A detailed view of the small and medium enterprise development in the Czech Republic in 2000 - 2010 is provided in Figure 1. It also provides a division into natural persons and legal entities.

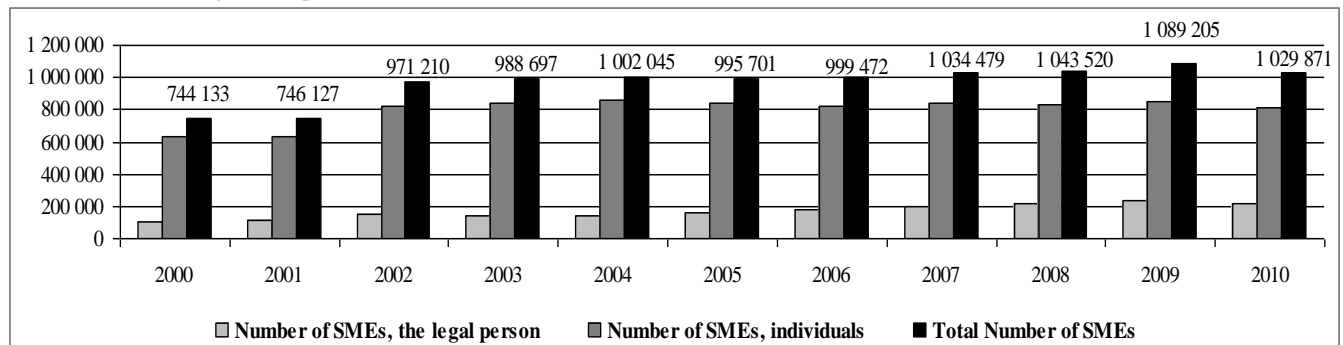


Figure 1 Development of the number of active SME in the CR
(Source: our own processing of data at the MPO [16])

The importance of small and medium enterprises in the economy is not challenged by anyone. Their ability to react fast to changed conditions or ability to absorb free labour is irreplaceable. As regards their functioning (their number, share in the employment rate and added value), the Czech economy is

standard.

The corporate governance of small and medium enterprises needs a procedure to measure, control and improve the performance of the enterprise. Such a procedure for effective and efficient management should be simple and

efficient and it should integrate these various viewpoints of the performance in environmental, economic and social terms [3].

3. EMPIRICAL ANALYSIS OF ENVIRONMENTAL, SOCIAL AND ECONOMIC PERFORMANCE IN SMALL AND MEDIUM ENTERPRISES IN THE CZECH REPUBLIC

Sustainability of small and medium-sized businesses in the Czech Republic may bring effects in the capturing the practice in the form of analyses of the environmental, social and economic performance, increasing the interest of stakeholders in the issues, etc. Surveys in small and medium-sized enterprises focused on the mapping of sustainable development situation in 2010. A total of 280 companies from the processing industry, construction, trade and services selected from a corporation database were contacted. Of the total, 27.4 % were companies with under 250 employees, 28.2 % with under 50 employees and 17.7 % companies with fewer than 10 employees. In the sample of companies analyzed, the most frequently represented industries were the processing industry, trade, construction industry and services.

Among small and medium-sized enterprises, differences in the interest in, and intensity of response to, the issue of sustainable development were expected. It follows from the survey that 57% of companies include a reference to sustainable development, and include it into their strategic goals, and 43% of companies do not include a reference to sustainable development and it is not a part of their strategic goals, either.

In the survey, respondents were offered a choice of four statements describing sustainable development and were asked to choose the one that best described their experience and practice. There may be a number of explanations why the content of the concept is not well-understood in small and medium-sized enterprises, e.g., employees are inadequately informed about sustainable development, failure to include strategic and social goals, etc. A small percentage of respondents from small and medium sized enterprises agreed on the basically textbook definition of sustainable development, the best-know definition is that sustainable development will provide for a "balance between three pillars" (8.6 %), and the "future generations" definition was second (18.5 %) best characterizes

Table 1 Link to different areas of sustainable development

	Definitely Not	Rather Not	Rather Yes	Definitely Yes
in environmental field	5.6%	6.4%	16.9%	13.7%
in economic field	3.2%	6.5%	15.3%	21.0%
in social field	4.8%	7.3%	16.9%	12.9%

(Source: own processing of empirical research)

In their opinion, the small and medium enterprises contribute most to sustainability in the economic field. On the other hand, they view their contribution as smallest in the social field.

Implementation of sustainable development in small and medium-sized enterprises may be advantageous for several reasons, most importantly because it may enhance eco-efficiency of technological processes, mitigate negative impacts on health and the environment, lead to an economic success of the company, facilitate negotiations with state authorities, local

governments and other stakeholders, enhance positive attitudes of employees towards their company and thus achieve significant economic effects, increase attractiveness for would-be investors and for international cooperation, etc.

The Czech Republic is quite successful in joining in the worldwide efforts at sustainable development of human society. As regards small and medium enterprises in the Czech Republic, there is an effort to mitigate the negative impacts on the environment by introducing more environment-friendly technologies aimed at reducing the volumes of waste to the minimum. There is a very strong involvement of voluntary initiatives and activities focusing on environmental protection in these companies by introducing voluntary tools in the environmental and social fields.

The effort of the enterprises is to focus on sustainability. Thus, sustainability is a strategy of the sustainable development process. Sustainability combined with the business environment has become known due to the environmental approaches in the enterprises. Sustainability has three important dimensions for the enterprises: economic growth, social responsibility, and responsibility for the environment. The sustainability of the enterprise is a strategic approach concentrating on the efficiency, efficacy and performance of the enterprise as well as on the creation of values for the owners (competitiveness) resulting from the environmental, economic and social dimensions. The definition of sustainability is related to the conception of strategy marked as sustainable development strategy in relation to the enterprise [11], [12].

The sustainability strategy of an enterprise currently encompasses a broad approach related to the integration of environmental, social and corporate governance, understood as key elements to achieve economic performance and to enhance investors' trust.

4. ENVIRONMENTAL PERFORMANCE

The vision of the sustainable development of an enterprise is currently introduced as a broad approach concerning the integration of economic, environmental and social characteristics.

In the Czech Republic, the environment-oriented management system is based on the ČSN EN ISO 14 000 standard represented mainly by the ČSN EN ISO 14001 standard. The ČSN EN ISO 14 000 standard series govern the implementation of the environmental management systems and their audits. The basic idea behind these international standard is to encourage the enterprises in all aspects towards active and independent dealing in environmental matters. The ČSN EN ISO 14 001 standard may be applied in enterprises of all types and sizes, while respecting internal and external conditions.

To evaluate the environmental performance, information about the environmental profile of the enterprise is necessary. The environmental profile evaluation (EPE) according to ČSN EN ISO 14 031 is yet another important internal tool providing continuously reliable and verifiable information to the corporate governance, which makes it possible to determine whether the environmental profile of the enterprise meets the criteria set by the corporate governance.

Attention should mainly be paid to environmental operations that contribute to the steady growth of values for the owners; therefore, it is necessary to concentrate on the future and long-term effects supporting sustainable development of the enterprise.

The empirical research indicates that the priority aspect for small and medium enterprises in environmental area is the consumption of energy and heat (41.5%) followed by waste (34.7%), see Figure 2.

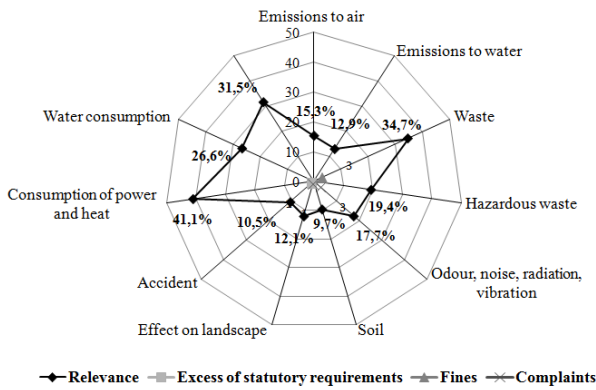


Figure 2 Significant environmental aspects (Source: own processing of empirical research)

The SMEs most often improve their environmental profile by minimizing waste (35.5%), improving the environment (31.4%). On the contrary, they pay least attention to sustainable traffic, see Figure 3.

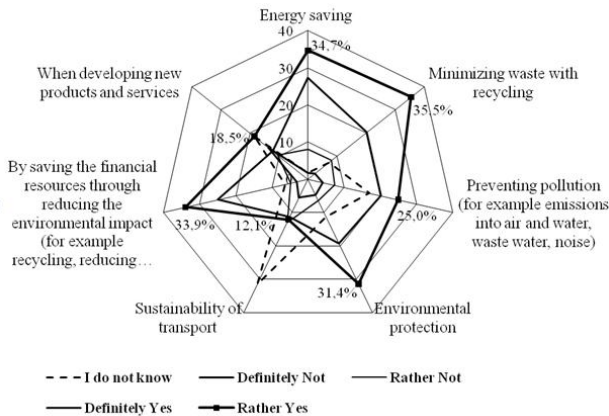


Figure 3 Ways of reducing the environmental impact (Source: own processing of empirical research)

Czech SMEs have a number of voluntary environmental tools. A total of 37.9% of the contacted companies uses the Quality management system according to ISO 9000, 26.6% use the environmental management system; acc. to ISO 14000, 17.7% of companies have introduced cleaner production. The least applied is the Environmental management accounting and Environmental management systems based on EMAS.

5. SOCIAL PERFORMANCE

Social performance of the enterprise is another important component of the economic and environmental performance of the enterprise. Conversely, it could also be said that good economic performance forms solid foundations for ecological and social aspects. Therefore, it is generally good for an enterprise to process and adopt principles in the field of health

and safety of the employees, human resources and ecology. Corporate social performance could be considered as employee care.

An important element of the social pillar of sustainable development is occupational health and safety (OHS). The right to the protection of health is one of the fundamental human rights guaranteed in the developed countries by the constitution and the charter of fundamental human rights and freedoms. To this end, the EU has adopted a number of directives. For the corporate governance of each enterprise this indicates the need of permanent creation of such conditions at work that guarantee a high degree of safety for the employees of the enterprise as well as its customers and surroundings. The trend underscoring the social aspects of sustainable development is the concept of corporate social responsibility (CSR).

Other key issues related to the corporate social responsibility are: human rights, employees' rights, involvement of municipalities and relationships with suppliers, information policy including issues such as releasing information, transparency, educating the consumers and anti-corruption measures. The importance of the corporate social aspects is mainly linked to the human resources. From the economic point of view it is possible to evaluate the performance of a person by e.g. the volume of work made over a certain time, the work performance may be measured by productivity of labour. From the social point of view, the person is willing and able to achieve an optimal performance (i.e. achieve optima work performance), if s/he uses his/her full potential, feels self-fulfillment and satisfaction and develops his/her personality.

Based on the conducted research, 48.4% of all contacted companies take care about the feedback with their customers, suppliers and other partners. It comes as a surprise that the SMEs do not support the local labour markets and do not provide work for people from the community. The employment in this way is offered by as little as 4% of the companies. 29% of companies provide funds to support public activities and projects, particularly for charity purposes. On the other hand, as little as 5.6% of companies, encourage their employees to participate in public activities and projects. Only 12.9% of companies are able to employ the ecological parameters of their products and services to gain competitive advantages although 26.6% of companies consider the environmental impacts of their products in the course of their development, see Figure 4.

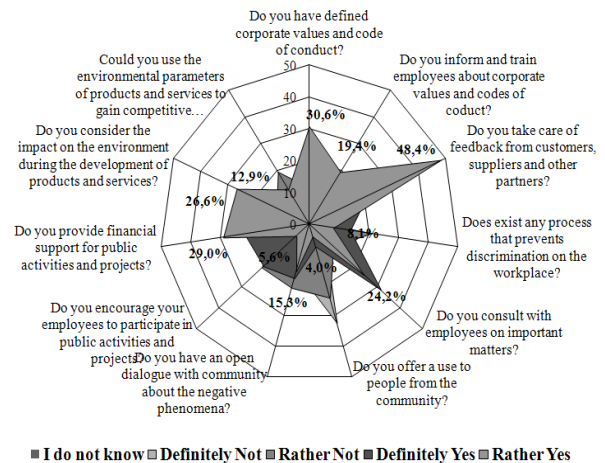


Figure 4 Responsible corporate behavior in the social field (Source: own processing of empirical research)

The most frequently used tool is occupational health and safety, this tool is implemented in 78.2% of cases. This is followed by safe company (16.9%), checklist for the safety of suppliers (14.5%) and Corporate Social Responsibility (13.7%), while the CSR will become a priority tool in the future, see Table 2

The previous text clearly indicates the effect of the corporate social performance on the economic performance. Despite that, there is still a lack of theoretical and empirical knowledge dealing with the relations between the social and

economic performance.

The common rule applicable to most enterprises is that improvement in the field of social performance is only acceptable if it pays off. To pay adequate attention to social performance and its management, it is first necessary to identify the linkage between the economic and social performance. If it turns out that the linkage is strong enough, the social performance will start being perceived as a major competitiveness factor.

Table 2 Tools used in the social field

	Used	Will be implemented	Implementation in the future	Now important	Barriers to implementation
Social Responsibility of Companies – CSR	13.7%	8.8%	10.5%	10.4%	6.5%
Occupational Health and Safety Management System (HSMS)	78.2%	4.0%	2.4%	4.8%	4.0%
Check-list for security of contractors (SCC)	14.5%	8.8%	7.3%	31.5%	8.1%
Safe company	16.9%	14.6%	3.2%	33.0%	5.6%

(Source: own processing of empirical research)

The remaining key question is whether social performance may mean a competitive advantage. The answer depends on the current and future competitive standing of the enterprise.

6. CORPORATE GOVERNANCE

The importance of Corporate Governance consists in its contributing to not only corporate prosperity, but also to responsibility. Along with the development of global markets investors' activity increases, with them demanding higher standards of responsibility, conduct and performance. Investors tend to seek opportunities outside their domestic markets ever more often. The companies trying to gain resources on the international capital markets, however, often find that capital is only available for those who conform to the internationally accepted standards of Corporate Governance and publishing of information. These are only some of the reasons leading to the worldwide improvement of the Corporate Governance standard and, in some degree, to its convergence. The defining of Corporate Governance is not a matter of unified terminology. In the evaluation of the corporate governance is described with the following quotes: a system through which companies are managed and controlled [10].

The statutory bodies are responsible for corporate management. The responsibility of a body covers the setting of a company's strategic goals, the management keeping check on realization of the goals, supervision of the management and informing shareholders about the performance of duties of a steward [1]. According to another description of Corporate Governance it is a process through which companies respond to the rights and requests of stakeholders [2].

Corporate Governance is understood as the key element in the effort to reach economic efficiency and a growth

justifying increase in the investor trust. It encompasses a broad range of problems arising from the relationships between the corporate management, the administrative authorities, shareholders and the other stakeholders [6].

In the Czech Republic, on the other hand, the dualistic model is used; it consists of the board of directors as the executive body and the supervisory board as the body of supervision. Based on the KPMG research a board of directors in the Czech Republic typically comprises three members, followed by a five-member setup. A typical supervisory board comprises three or six members. An average number of members of the administrative bodies (9.6) does not reach the numbers common in the EU with the average equalling (12.5) members [9].

In the Czech Republic a Code of supervision and management of companies based on the OECD principles was introduced as early as 2001 and was last updated in 2004.

The KPMG survey addressed 500 largest Czech companies. The objective of the survey was to understand some procedures of corporate governance and working methods used by the Boards of Directors and Supervisory Boards of companies in the Czech Republic. A special emphasis was placed on the ability of the members of the corporate bodies to gain information and work with it efficiently. The results of the survey indicate that most interviewed companies have only set the corporate governance rules to an extent meeting the basic statutory. This minimalist approach means that some procedures and practices are a far cry from the recognized best practice [8].

According to the conducted SMEs research, the most frequently published information is environmental and social information, not in the form of separate reports but as a part of another summary report, such as, for example, a chapter in the annual report (16.9%). The least frequent form is a sustainable development report, see Table 3.

Table 3 Forms of voluntary reports published

	I do not know	Definitely Not	Rather Not	Rather Yes	Definitely Yes
Environmental Report	9.6%	34.7%	14.5%	6.5%	8.1%
Health, Safety and Environmental Report	14.6%	36.3%	12.1%	2.4%	8.1%
Corporate Social Responsibility Report	18.6%	33.9%	14.5%	1.6%	4.8%
Sustainable Development Report	15.4%	37.9%	12.1%	5.6%	2.4%
Accrued report	12.1%	27.4%	8.9%	8.1%	16.9%

(Source: own processing of empirical research)

Corporate Governance is a system through which business companies are managed and controlled. The structure of corporate governance defines the division of rights and duties between the individual stakeholders in a company and lays down detailed rules and procedures for the decision-making on business matters of a company. On this basis a structure is created that establishes the company goals and the means of reaching the goals and monitoring performance“.

7. CONCLUSIONS

The enterprise is thus exposed to the pressures of economic, environmental and currently also social legislation, ethical codes and conditions of the consumers, suppliers and the profit maximization therefore stops being the only criterion. The decision-making must also include voluntary approaches related to sustainable development. The target is to achieve a balanced relationship between the environmental, economic and social pillars- to secure sustainable management at the corporate level. As it has been stressed several times in the article, sustainability has three important dimensions for an enterprise and although there may be compromises between these dimensions , social responsibility (towards the employees and other stakeholders) and environment-friendly behavior lead generally towards the strengthening of trustworthiness, and therefore this approach also makes sense from the business point of view.

The crucial element in achieving the targets in all the aforesaid areas is the Corporate Governance. Corporate Governance should consider the interests of the stakeholders and affect the development of the business strategy through its activities and its implementation in order satisfy the justified interests of these parties. Simply speaking, Corporate Governance should integrate the efforts of all three areas – environmental, social and economic and bring them to life through a suitable strategy and means.

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