

Sustainable development

What challenges for SME?

This document is a product of the “sustainable development and SME” working group, created on the initiative of ORSE and which, between the end of 2003 and the middle of 2004, brought together about thirty specialists.

Debates and eyewitness accounts, as well as the analysis of documents, permitted this group to identify three factors of change likely to incite SMEs to become involved in sustainable development:

- The new expectations of contractors (corporations and local authorities).

- The change in attitude of financial partners (bankers and insurers).

- The availability of CSR rating systems.

In order to make all this work convincing to SME managers, the group has attempted, as far as possible, to present real-life situations experienced in all the areas explored.

→ Sustainable development and value creation ←

- Does sustainable development create wealth for companies which commit to it or, conversely, does it destroy it?
- Does sustainable development strengthen companies, in particular SMEs, or, conversely does it weaken them?
- Can, and should, a manager commit to this procedure alone or does he run the risk of penalising himself if he does?
- Consequently, should he take the initiative on his own or wait for it to be imposed on him by means of a ruling, for example?

These few questions sum up reasonably well the concerns of economic players and observers on the subject of sustainable development. Its implementation and the pace of its integration into companies depend on the replies provided.

Understanding what makes value creation
From a financial viewpoint, the value created by a commercial company is the difference between the profitability of the capital invested and its cost. Another way of presenting value creation involves linking it to the price of the company in the sense that the more a company is profitable, the higher its price.

Nevertheless, this relationship is not always systematic. Thus, for example, a company's market price may fall despite good profitability because of a problem involving its reputation, a future risk identified by investors, etc.

In reality, two aspects are involved when valuing a company:

- net book value,
- goodwill.

The existence of goodwill signifies that investors agree to pay more for a company than its book value because they are banking on its ability to generate profits in the future.

Various research works in the field of finance have shown that the “invisible” assets in the company's financial reports, called intangible assets, constitute an

important and even a vital part of its value. These assets vary greatly in nature, but, nevertheless, may be organised into four main categories: clientele, staff, the structure itself, suppliers.

Intangible capital, a subset of sustainable development

An entrepreneur who leads his company with the desire to increase its long-term prosperity and its overall value will look to develop its customer capital, its human capital, its supplier capital, etc. Therefore, the search for long-term economic performance is linked to the values of sustainable development. Intangible capital is a subset of sustainable development, focused on value creation in the company through its first level partners (customers, suppliers, employees) as illustrated in the diagram below.

Question of the link between responsibility and profitability

One of today's limitations to the analysis of the economic performance of sustainable development comes from the fact that it restricts itself to wanting to establish a direct link between CSR and value creation.

However, this relationship has not been verified as being something which is positive or negative¹, with “responsible management” only being a necessary condition but not something which is enough to create value. This link between sustainable development and value creation can be made easily when CSR is combined with intangible capital.

Evaluating a company's overall policy requires an analysis based on 3 approaches:

- the financial approach: helps to understand its financial health,
- the CSR approach: assesses its behaviour with regard to its stakeholders,
- the Intangible Capital approach: takes account of the value and contribution of its first level partners.

The key to sustainable value creation for a company is based on its current financial health, its CSR and the quality of its intangible assets

¹ Study «les stratégies de développement durable nourrissent-elles la performance financière » (Do sustainable development strategies feed financial performance?) ORSE - 2003

→ The new expectations of SME partners ←

Evolutions in the practices and expectations of SME's natural partners – contractors, bankers, insurers – give rise to new demands which companies must anticipate. It is true that these evolutions involve temporary discomfort, when changing habits and ways of thinking, but they also offer one great virtue, that of reconciling professional activities with humanist and ecological aspirations

Contractors

One result of a corporation's sustainable development policy is a change in the behaviour of their purchasing departments with regard to suppliers..

To date, there are no exhaustive studies on the recent changes in purchasing practices and policies. However, initial analysis shows that these practices are very unequal, depending on the companies involved, and may be summarised by the following four remarks:

1. Product quality and safety have been long-term preoccupations for companies. However, the environment and conditions for manufacturing and product retailing are subjects which are still very much in their infancy.
2. The vigilance of buyers with regard to the overall social and environmental policy of suppliers is a subject of interest to a growing number of companies. This evolution is related directly to the affirmation of the CSR concept.
3. Ethical purchasing codes are not greatly used and involve widely varying levels of responsibility from one sector to another. Only a minority of groups have formalised their practices on this subject in a rigorous manner. In most cases, purchasing procedures prove themselves to be globally responsible, but are informal and not secure. Unfortunately, many companies are unaware of the importance of purchasing procedures
4. Measures to support, train and assist suppliers are recent initiatives, even more visible because they are exemplary.

The 4 main areas covered by a "responsible" purchasing policy

The characteristics of the product/service bought: quality, customer safety, degree of respect and protection for the environment, etc. Assessment concerns the object itself, but also the manufacturing and retailing conditions.

Eligibility criteria for the supplier: the purchaser's vigilance includes, in particular, aspects concerning the act of selling: marketing ethic, transparency, loyalty, respect for commitments, etc.

The method of managing the act of purchasing: referencing ethic, the management of calls for tenders, the fight against corruption, the fight against conflicts of interests, etc.

Measures for supporting, assisting and searching for winner-winner relationships with suppliers: equitable price policy, local purchasing policy, reduction in suppliers' turnover, education and support for suppliers, etc.

The initiative of the French purchasing department of the Accor Group

The work of this department, approved and supported by the group's development committee, has been organised in two phases:

Definition of a sustainable purchasing charter reflecting the group's desire to work solely with responsible companies, as much on a social level as on an environmental level. This charter was sent to all suppliers in June 2003.

Formalisation of a questionnaire in order to evaluate the social and environmental practices of suppliers and their desire to progress in these fields. This questionnaire, the same for all companies, was sent to all French suppliers, namely 460 companies working in both the food and non-food sectors. 3 types of criteria were taken into account and considered depending on the sector: environmental performance, social performance and the quality of the information communicated. The assessment also took into account the size of the companies.

The first CSR rating of suppliers provided Accor with a high quality monitoring tool to improve its policy of sustainable purchasing. The group has been able to concentrate its actions on 21 % of suppliers for which the results were unsatisfactory. It is not Accor's wish not to exclude partners, but, rather to enter into a process of continuous improvement and dialogue with them.

The work conducted by the AGF purchasing department.

The insurer has introduced an "**ethics and sustainable development**" clause in all its contracts with suppliers. At present, this clause, which includes a section on social issues and another on environment issues, is not very demanding because it is limited to enforcing the regulations in force. However, if the clause is breached, a contract may be cancelled without payment of compensation.

Also, a **questionnaire** focusing mainly on the environment and the sales relationship was sent to all referenced suppliers. It is intended that it should be submitted to suppliers on an annual basis thus leading to the creation of a grading system. This would make it possible to classify suppliers on the basis of CSR criteria in the event of similar replies being given to standard criteria for analysing calls for tenders (quality, price, etc.).

The approach adopted by AGF also includes an **ethical purchasing code** which has been signed by all its buyers.

Prosign, a SME which has succeeded in changing the behaviour of its suppliers, multinational groups

Prosign, a road marking company, is a SME with 380 members of staff which has voluntarily committed itself to a policy of sustainable development by eliminating the risks which its products (often toxic, harmful, irritant and inflammable) represent for people and the environment. Its work illustrates the opportunities which exist for providing support in the customer-supplier relationship.

The most symbolic example is that of the water-based paints developed by Prosign to replace Toluene:

To develop these products, Prosign wanted to create the first French Eco-profile* in order to evaluate, in an exhaustive manner, the environmental impact of water-based road paint. The company asked one of its main suppliers to jointly finance the process: the chemical product manufacturer, Rohm& Haas (17,500 staff members). The latter accepted and was also able to take advantage of the impact of this project on its image and its communication by distributing this study to all its installations throughout the world.

Another example, the replacement of a toxic lead chromate pigment by an organic pigment for yellow paint, initially resulted in an economic dead-end. After a new attempt by R&D and the provision by suppliers of an organic pigment which increased the cost of the final product only slightly, a satisfactory solution was found.

Prosign works in the same manner in all areas and tries to encourage its suppliers to change. Following the analysis of the life cycle of ecodesign packaging material, a high level of eutrophication (development of algae in the water) was found. It was quickly discovered that the cardboard was the cause of it. For a year, Prosign asked its supplier to pass its waste through water and its waste treatment systems before discarding it. These requests were in vain despite the fact that they were repeated several times. This supplier was dropped and, after an audit, it was Otor Picardie which was finally chosen as a replacement.

In all these operations, the customer and the supplier never lose sight of the inherent marketing logic and all these initiatives provide factors of differentiation which are promoted among Prosign customers (for example through the NF Environment certification)

*Eco Profile: according to the international standard 14025, this is an environmental "identity card" which describes the ecological impact of a product from its manufacture to its use including its distribution

Public authorities

The reform of public procurement contracts in France is a first attempt to reconcile sustainable development and the most rigorous principles of competition.

The 2004 public procurement contracts code authorises account to be taken of social and environmental considerations under certain conditions. In short, it is now possible to include in a public procurement contract:

- social considerations if there is no discrimination (all bidders, whoever they are, may present themselves as candidates, regardless of the number of bidders), if the procedure is transparent and if social

criteria are justified by the object of the market.

- environmental considerations, provided that there is no link between what is needed (object of the market) and environmental requirements, that the environmental criteria is clearly visible, that there is no discrimination (the procurement contract must be written in such a way that all bidders, whoever they are, may present themselves as candidates), and finally, that all demonstrations of quality are accepted (a company which is not certified ISO 14000 may provide proof that its policy meets the same quality requirements as those in the certification).

Financial partners

All companies, including SME, are faced with having to manage risks involving the environment (site cleanups, extended responsibility as a generator of waste, etc) social issues (strikes, social plans, etc.), ethics (uncertain origins of capital, risk of money laundering, etc.) and damaged customer relationships (complaints, loss of trust, court cases, etc.).

Given the growing importance of these risks in a company's performance, financial partners (banks and insurance companies) are becoming increasingly interested in measures to reduce these factors for their customers in order to evaluate their own risks better.

Axa's "environmental impact" offering for SME

Following the development of an "environmental impact" offering especially for SME, AXA looked for ways to support its customers using its network of general agents. This led to the creation of a CD for diagnosing risks which, in a simple manner, takes a look at the risks which a company has to deal with in terms of its business, its awareness of the environment and its methods of environmental management. After having completed the questionnaire, the SME receives a summarised report presenting an image of the level of risk and the preventive measures which may be implemented

Identification of social and environmental risks by the Société Générale

The Société Générale has trained its staff to evaluate the risks involved in its customers' portfolios. A directive to take into account environmental and social risks, approved in 2001 by the bank's executive committee, describes all the procedures for examining files and the list of sensitive sectors in the field of the environment.

To inform and alert its staff, the bank also wrote environmental sheets for several industrial sectors, in particular the most sensitive ones, which are made available on its Intranet site. These are one page summaries of recommendations from the Plan environnement et entreprise 2000 (Environment and Business Plan 2000), written by Ademe and the Chambers of Trade and Industry.

After having collected the information distributed on the Internet by the DRIRE (Regional Office for Industry, Research and Environment), a team of consulting engineers uses a simplified environmental questionnaire which is completed during field visits and is attached to the final report transmitted to operators.

With this questionnaire, the consulting engineers are able to identify any likely problems and can suggest either to the company owner or to the bank that a more detailed audit be carried out by a specialist company.

To reinforce its approach, the Société Générale conducts a call for tenders to reference auditing companies. Applications have already been refused by banks on the basis of environmental issues alone.

Overview of the European offering (source Novethic)

For several years, SME have had access to self-rating tools allowing them to become involved gradually in a sustainable development approach. In view of the profusion of these tools, it appeared to us to be interesting to put them into perspective.

To simplify, it is possible to organise the different systems into three main categories:

- Flash self-rating systems: these are based on questionnaires and do not require any specific implementation within the company (global performance model, social performance assessment and RL Europe).
- Complete sustainable development management systems which involve the implementation of a complete process from strategy to the measurement and reporting system (for example SD 21000).
- The social and environmental rating system which consists of positioning a company in relation to standard thresholds, a task entrusted to an external assessor, such as Goodcorporation for example)

Name of tool	Country	Availability	State of advancement	companies involved
Denmark Social Index	Denmark	Tool available online	In force	About one hundred
Vastuun Askeleita	Finland	Available by ordering	In force	Several dozen
Sigma	United Kingdom	12 tools in the process of being put online	Under construction	N.A.
BS 8555 (Acom project)	United Kingdom	Unavailable		N.A.
IIPUK: Investors in People	United Kingdom	Available by ordering	In force	34,000 companies committed
Community Mark	United Kingdom	Guide and questionnaire available online		
UK Good Corporation	United Kingdom	Audit, but questionnaire available online	In force	70 companies certified
Q-Res	Italy	Available by ordering	Under construction	Fewer than ten
IMS	Austria	Consultants, no tool available for downloading	In force	12 SME
Albatros	Belgium	CD Rom available by ordering	In force	A dozen SME
Foretica	Spain	Audit, no tool available for downloading	In force	Several dozen
Value Management System	Germany	Available by ordering	In force	4 small companies 30 medium-sized companies 10 corporations
SME Key	CSR Europe	Tool available online	Experimentation	Several dozen
FRENCH TOOLS				
Social performance assessment	CJIDES	Summary and methodology available online	In force	100
Global performance	CJD	Self-administration version published by Editions d'Organisation (March 2004) – Educational version distributed within the network	Experimentation (2 nd phase)	300 + 400
Guide CSR-Alliances	Alliances	Summary available online	Experimentation (2 nd phase)	30 / year
Lignes SD 21000	AFNOR	For sale online (€57)	3 types of experimentation raising awareness, support, adaptation for local authorities	150 to 500

Main remarks:

- There are still relatively few companies experimenting with or using tools to rate their overall performance. Many more of them choose certifications or procedures on one specific theme or another: enhancement of human resources, environmental certification, etc. This is related, in particular, to the fact the many CSR tools are neither completely finalised nor, even more so, because they are not “in force”.
- The availability of tools is unequal: online, for sale, or confidential (because they are

an integral part of a consulting offering for example), not all tools are accessible free of charge.

- Their origins are mainly private (companies, but above all, research centres or universities, initiatives by associations or networks, generally greatly supported by public authorities). Only one tool from the panel is completely public: the Danish Social Index
- The public addressed is rarely microbusiness-SME exclusively. With the exception of SME Key, almost all the tools listed do

not make company size a discriminatory feature.

- The thematic basis is variable: tools may cover one, two or three sustainable development themes.
- Although, generally, the main component is a basic questionnaire, certain features include up to 12 different tools, thus greatly exceeding its role of rating to offer a real management system.