AUD008 Social and governance disclosure by Lonmin Plc pre and post Marikana: A research note

Maroun, W
University of the Witwatersrand

Abstract

This draft paper is grounded in an interpretive epistemology. It uses thematic content analysis to identify social and governance disclosures to explore the possible relevance of legitimacy theory for explaining changes in social and governance disclosures by South African corporates. The focus of the preliminary study is on Lonmin Plc and changes in the extent of the social and governance disclosures found in its' annual reports one year before and after the events taking place at Marikana.

The results suggest that the company responded to this significant labour unrest by increasing non-financial disclosure dealing directly with the incident. It includes the majority of this information in a specific section of the 2012 annual Report. The company also reduces the extent of social and governance disclosures specific to other sections of the organisation. Collectively, these results point to a legitimation strategy designed to imply that the strike action was an isolated event and not indicative of the corporate social environment at the company as a whole. Related to this, it may also be the case that less specific non-financial disclosure can, paradoxically, bolster legitimacy by avoiding additional scrutiny.

Key words: Corporate governance; Legitimacy theory; Marikana; Social disclosure

1. Introduction

Studies dealing with the value relevance of corporate social responsibility (CSR) disclosures frequently report a lack of statistical significance between environmental, social and governance (ESG) disclosures and financial performance (Hassel, et al, 2005; Jones et al., 2007; De Klerk & De Villiers, 2012). These findings stand in stark contrast with the arguments of the International Integrated Reporting Council (IIRC) and the Integrated Reporting Committee of South Africa (IRCSA) that, for organisations to be sustainable in the short-, medium- and long-term, effective disclosure of non-financial information is paramount (Institute of Directors in Southern Africa [IOD], 2009; IRCSA, 2011; IIRC, 2013). The results are also at odds with the documented proliferation of ESG information being included in the annual or integrated reports of contemporary organisations (KPMG, 2012; Hughen, et al., 2014). As such, the absence of a definitive economic case for ESG reporting begs the question: are other forces at work explaining the increased emphasis being placed on non-financial reporting?

From a neo-institutional perspective, the growth in the sustainability reporting movement cannot be ascribed only to rational economic processes. Instead the nature and extent of ESG information being communicated by organisations to their stakeholders is influenced significantly by powerful social and political pressures (for examples, see Patten, 1992; O'Donovan, 2002; Burritt, 2012; Higgins & Walker, 2012; Gray, 2013). In other words, changes in ESG reporting can be interpreted from a social constructivist viewpoint[4] (Tregidga, et al., 2014). The objective of this research note is to offer initial evidence in support of this assertion from a South African perspective.

Although there is a considerable body of work on ESG reporting in a South African context, much of this work is fairly descriptive (for example, see Marx & Dyk, 2011; Hindley & Buys, 2012; PwC, 2014) and is limited to examining changing trends in non-financial reporting by companies listed on the Johannesburg Stock Exchange (JSE). With some notable exceptions (De Villiers & Barnard, 2000; De Villiers & Alexander, 2014), the majority of the prior local research is also grounded in finance paradigms (see, for example, De Klerk & De Villiers, 2012) which overlook the relevance of socio-political stimuli for the evolution of ESG reporting (Carels, et al., 2013).

Consequently, this draft paper makes use of a neo-institutional[5] theoretical framework to portray South African ESG reporting in a different light. Instead of an exercise in direct value creation, non-financial reporting is presented as an exercise in social legitimation (Tregidga, et al., 2014). Based on the work of Patten (1992; 2002) and De Villiers and Alexander (2014), the research argues that ESG reporting is a social construction designed to appeal to the interests of stakeholders and secure organisational credibility in times of crisis. To do this, the study examines the changes in the frequency of certain social- and governance-related disclosures in the annual reports of Lonmin Plc (Lonmin) before, during and after the wildcat strikes[6] at Marikana on 12 August 2012.

The study deals specifically with this example of industrial unrest in South Africa due to the unusually violent nature of this post-Apartheid strike (Cawadas & Mitchell, 2012; Sorensen, 2012). Although possibly indicative of wide-spread socio-economic ills which plague the country, the strike action is commonly associated with the world's third largest producer of platinum group metals. Its employees were directly involved in the events taking place on 12 August 2012 and the company reported significant decreases in metal output and revenues as a result of the unrest (Lonmin, 2012; Reuters, 2012). Almost three years after the tragic loss of life, the Marikana incident also offers an established case for exploring how an organisation's ESG reporting responds to a social crisis. This is not only important for academics and practitioners wanting to understand the relevance of ESG reporting in the contemporary South African capital markets; the research is expected to contribute to the

[4] According to this viewpoint, corporate governance systems are seen as the product of multiple and conflicting experiences of individuals and not just a rational technical development. The purpose of research is, therefore, to explore the relevance of different views or opinions and avoid reducing the subject matter as is the case with positivist research (Creswell, 2009).

[5]From a neo-institutional perspective, accounting and governance systems are seen as one of the means of legitimising an organisation by creating the appearance of rationality and structure and not just a technical financial development.

[6] A strike begun by workers spontaneously or without support of a union.

limited body of local interpretive corporate governance research in African settings (Brennan & Solomon, 2008; Maroun & Jonker, 2014). It also offers evidence in support of the theorisations of Patten (1992; 2002) and De Villiers and Alexander (2014); highlighting how ESG disclosures change in response to a challenge to legitimacy.

The remainder of this paper is organised as follows. Section 2 provides the theoretical frame of reference and summarised prior research dealing with ESG reporting from a neo-institutional perspective. Section 3 discusses the method. Section 4 presents and discusses the results and Section 5 concludes and identifies areas for future research.

2. Theoretical framework and prior research

According to Suchman (1995), the term 'legitimacy' is a 'generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions'. He goes on to identify three 'types' of legitimacy: pragmatic, moral and cognitive.

Pragmatic legitimacy rests on the organisation being perceived as valuable or aware of the interests and needs of stakeholders (Dowling & Pfeffer, 1975) and is based mainly on 'self-regarding utility calculations' (Suchman, 1995). Moral legitimacy is more normative and arises from the entity following processes and producing outputs which are consistent with the moral values of its constituents (Dowling & Pfeffer, 1975; Suchman, 1995). Finally, cognitive legitimacy is dependent on the extent to which an organisation or its functions become institutionalised or so integrated in day-to-day life that its existence is simply taken for granted (DiMaggio & Powell, 1983; Powell, 2007).

2.1. Maintaining and repairing legitimacy

Being socially constructed, organisations can often find that their standing in society is threatened by either their own activities or exogenous events (DiMaggio & Powell, 1983; Powell, 2007). To this end, Suhman (1995) and Dowling and Pfeffer (1975) outline different strategies for repairing and preserving legitimacy:
In the first instance, the organisation offers a normalising account of the delegitimising event by denying, excusing or justifying it. The aim is to separate the threatening revelation from the rest of the organisation creating a type of 'firewall' which prevents a significant depletion of the organisation's legitimacy reserve (Suchman, 1995).

Similarly, an organisation faced with a threat to legitimacy can attempt to stress that the issue is limited to a specific sector and agree to remedy stated faults. The aim is to acknowledge shortcomings and appear responsive to the concerns of stakeholders while pre-empting additional scrutiny. This often goes hand-in-hand with the organisation inviting more monitoring and review, effectively providing assurances to stakeholders that future occurrences of the event in question are unlikely (Suchman, 1995).

An entity can also make use of disassociation, attempting to create a clear line of demarcation between the threatening event and the rest of the firm (Suchman, 1995). This can be achieved using symbolic displays with the entity making public statements, participating in forums and encouraging active debates on how to best deal with the delegitimised action or event (Ashforth & Gibbs, 1990). It can also depend on formal restructuring of the organisation, relying on moving or closing problematic divisions, charismatic employees to defend a particular position or changes in the executive structure of the firm. The aim is to signal its allegiance with societal expectations and distance the entity from those identified as responsible for the questionable act (Dowling & Pfeffer, 1975).

2.2. Legitimacy theory and ESG reporting

There is a large body of research which deals with the link between ESG reporting and organisational legitimacy (for examples, see Patten, 1992; O'Donovan, 2002; Burritt, 2012; Higgins & Walker, 2012; Gray, 2013). De Villiers and Alexander (2014), for example, describe the development of CSR reporting as an institutional process influenced heavily by isomorphic pressures and the need to secure a sense of pragmatic and cognitive legitimacy. In this context, an organisation faced with additional public scrutiny as a result of a poor environmental track record can use additional disclosure to signal an awareness of societal interests (De Villiers & Van Staden, 2006). For example, Deegan, et al. (2002) examined the environmental disclosures of BHP, and found that the company publishes positive social and environmental information in response to unfavourable media attention. Similarly, Patten (1992) – while examining the effect of the Exxon Valdez oil spill on corporate reporting – argues that changes in the nature and extent of environmental disclosures can be ascribed to perceived changes in the perceptions or expectations of stakeholders. More specifically, the quantum of disclosure dealing with environmental disasters is found to be directly proportional to the perceived significance of the relevant incident (Patten, 2002). These findings are consistent with research suggesting that, due to added political pressure and public interest, large firms are more likely to prepare separate or more detailed CSR reports (Thorne, et al., 2014).

Through the lens of legitimacy theory, additional reporting plays an important role in demonstrating that the organisation acknowledges prior shortcomings and is taking steps to address society's concerns (Laine, 2009b; Brennan & Merkl-Davies, 2014). ESG reporting can also be used to symbolic ends, appealing to the assumptions and beliefs of stakeholders in order to garner support and limit additional scrutiny (Tregidga, et al., 2014). By constructing the image of a sustainable organisation in annual or integrated reports, it also possible for ESG disclosure to be used as a type of legitimacy-buffer, relying on the appearance of effective CSR to immunise the entity form isolated failures (Laine, 2009a; Tregidga, et al., 2014). In this way, non-financial reporting often depends on content, structure and diction to de-emphasise negative ESG actions or deflect attention (O'Donovan, 2002). A resulting sense of sustainability as a 'natural' part of day-to-day operations is combined with references to competency, experience, transparency, accountability and responsibility, personifying the organisation and entrenching a sense of cognitive and moral legitimacy (Higgins & Walker, 2012; Tregidga, et al., 2014).

Attempting to repair or defend claims to legitimacy when faced with a significant ESG crisis can, however, have unanticipated consequences. As explained by Suchman (1995), explicit appeals designed to win credibility can, paradoxically, lead to stakeholder circumspection. As such, effective management of non-financial communication with stakeholders does not necessarily require the provision of more information (Ashforth & Gibbs, 1990). O'Dwyer (2002), for instance, notes that CSR reporting has the 'potential to engender rather diminish societal scepticism in an environment where public pressure is keenly felt by many organisations'. De Villiers and Van Staden (2006) reached the same conclusion. Companies with high environmental impact tend to find generic disclosures less threatening (Solomon, et al., 2013). They also tend to 'decrease specific disclosures when they perceive them to be potentially more damaging than helpful to maintain legitimacy' (de Villiers and van Staden, 2006, p. 426). The same logic may apply to Lonmin's reporting of social and governance-related information in the context of the events unfolding at Marikana.

On the date of the Marikana incident, Lonmin reported that industrial unrest had resulted in an immediate loss of 15 000 ounces of platinum production and resulted in a significant decline in share price on the date of the incident (Reuters, 2012c). In addition to the economic implications, the Marikana incident is considered a significant event in South African history with parallels drawn between the Marikana shootings and the Sharpeville and Soweto uprisings of 1960 and 1976 respectively[7] (Sorensen, 2012). The event attracted significant attention from local and international media due to the number of casualties, as well as the historical sensitivity associated with the South African Police Services' (SAPS) use of force[8] (Marinovich, 2012). Marikana also evoked a response from the investor community, with many questioning whether the industrial unrest was indicative of wide-spread labour problems and the beginning of the end of the South African mining industry (Cawadas & Mitchell, 2012). In line with the arguments of Patten (1992; 2002) and Deegan, et al. (2002) one would expect this to result in an increase of social and governance disclosures from 2011 (one year before the incident) to 2013 (one year after Marikana). At the same time, the company may rely on more generic disclosure to signal its commitment to effective CSR practices and avoid dealing with specific metrics which, as per De Villiers and Van Staden (2006), may simply result in more negative press.

3. Method

This study subscribes to a social constructivist worldview. Language and imagery found in annual or integrated reports does not just describe corporate activity but plays an important role in constructing and reconstructing varying realities (Laine, 2009b). As such, an interpretive textual analysis was relied on to analyse the social and governance-related disclosures in Lonmin's annual reports[9].

[7] These are two well-known uprisings against the Apartheid Government during which police opened fire on protestors. The events attracted significant international media attention and were widely condemned.

[8] The Apartheid Government relied on the South African police to suppress worker rights for almost 60 years (Welsh, 2011).

[9] This is in keeping with the fact that these are the primary reports used by the company to communicate with its stakeholders (see IOD, 2009; Lonmin, 2012a).

For this paper, the emphasis is on the annual reports published in 2011, 2012 and 2013. This is to ensure that there is a 'base' (determined before the outbreak of violence in August 2012) for evaluating changes in the extent of ESG information being included in the reports in the year of and one year after the Marikana incident. It should also be noted that reports prepared before 2011 were specifically excluded due to the possible effects of the, then, recently released discussion paper on integrated reporting and the transition from King II to King III (see IOD, 2009; IRCSA, 2011).

The aim was to examine the content and themes of social-related disclosures, their frequency, and how the information is presented to readers (Laine, 2009b). Due to the fact that the research is concerned with how Lonmin is using social-specific disclosures in its communications with stakeholders to manage legitimacy, articles published by third parties (which may not reflect the company's position) were excluded from the analysis.

Overall, the approach followed is subjective with the data collection and analysis progressing in a hermeneutical manner which was not restricted by a rigid methodological framework (Llewelyn, 2003; Laine, 2009b). In the first stage, the researcher read the 2011, 2012 and 2013 annual reports and identified passages with references to social and governance issues and to the Marikana incident in particular. Relevant excerpts were organised thematically to provide a comparison of the nature and frequency of social and governance-related disclosures from 2011 to 2013. The research uses the same procedure as Solomon and Maroun (2012) and Carels, et al. (2013). The aim was not to follow a scientific approach by counting words and testing for changes in disclosure trends which were statistically significant. Instead, an interpretive approach is followed where the researcher constitutes the data collection and analysis 'instrument' (Merkl-Davies, et al., 2011).

The researcher relied on a systematic analysis of each report to identify main disclosure themes or categories (theme codes) and the specific sections of the annual reports in which these themes were discussed (adapted from Solomon & Maroun, 2012). These themes were interpretively derived from the analysis of the annual and sustainability reports informed by the guidelines provided by Sustainability South Africa and, due to its widespread application, the GRI G3. In addition, the final theme register specifically took into account the disclosure categories identified by similar studies examining reporting trends in South African integrated reports (Marx & Van Dyk, 2011; Solomon & Maroun, 2012; Carels, et al., 2013; PwC, 2014). Duplicated disclosures were eliminated and disclosure themes which were very similar were merged. As an additional validity check, the theme codes were re-examined by the researcher and a research assistant one month later to ensure that the register was accurate and complete.

The final result of the analysis was a simple matrix which disaggregated each annual report into sections and recorded the frequency of social and governance-related disclosure per section. These sections were the main components of the annual reports and were largely consistent with those used in similar prior studies (see Solomon & Maroun, 2011; Carels, et al., 2013). The matrix was then used to compute (1) the cumulative disclosure of social and governance information in the 2011, 2012 and 2013 annual Reports; (2) the frequency of disclosures per theme; and (3) the change in disclosure frequencies over time. These statistics were not intended to 'quantify the social disclosure found in the reports or provide measure of the quality of disclosures. Instead, they were used to gain a sense of the change in the extent of social and governance-related disclosures one year before and after the Marikana incident (Patten, 1992; Patten, 2002).

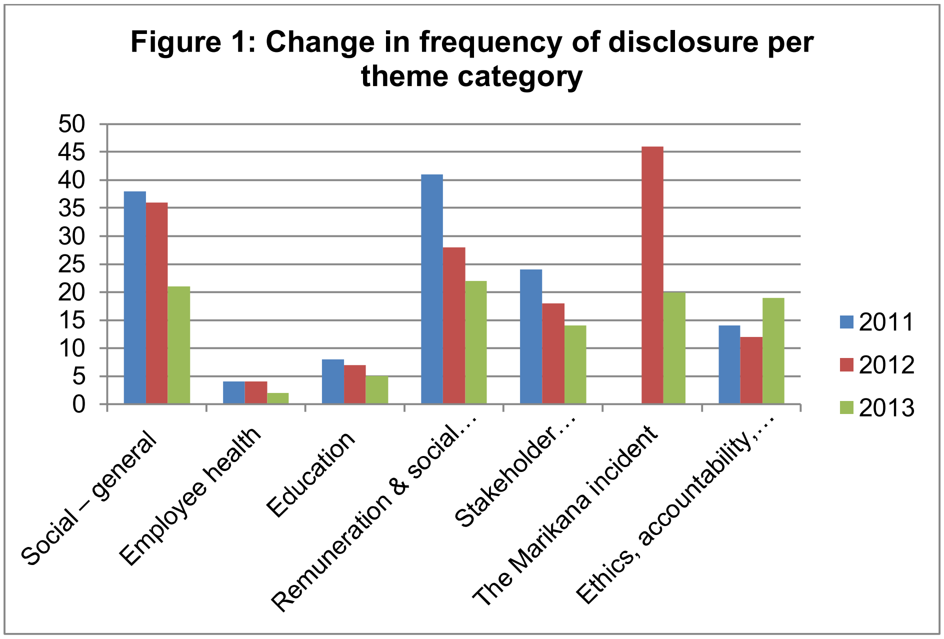
4. Results and discussion

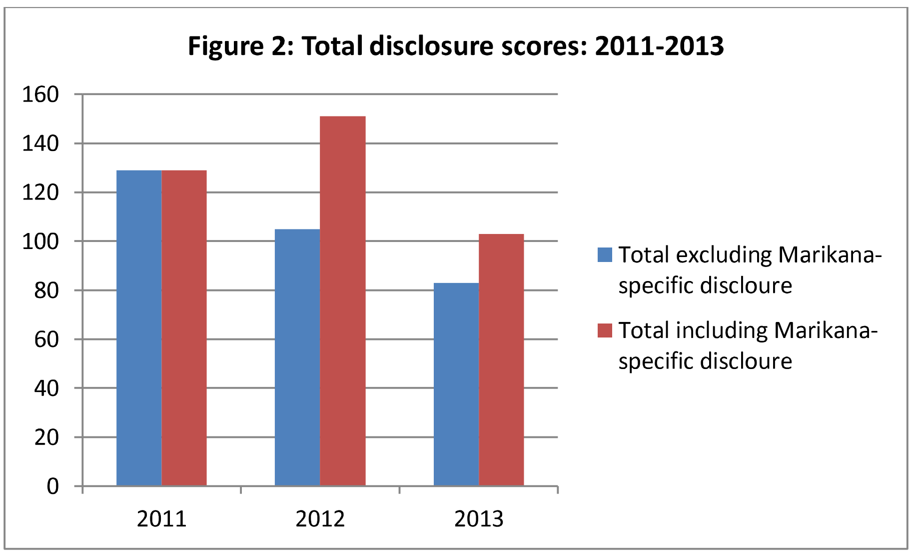
Preliminary results are presented in Table 1 and are consistent with the predictions of Patten (1992; 2002). In response to the events taking place at Marikana, Lonmin appears to have increased the extent of social and governance-related disclosures included in its annual report (2012). The total frequency of social and governance disclosures increases by 18% from 2011 (total score of 128) to 2012 (total score of 151) with most of this attributed to disclosure dealing specifically with the events taking place at Marikana. If, however, the changes in the frequency of disclosures are considered per category, a slightly different perspective emerges.

Table 1: Disclosure scores per theme category

	2011	2012	2013
Social – general	37	36	21
Employee health	4	4	2
Education	8	7	5
Remuneration & social investment	41	28	22
Stakeholder engagement/management	24	18	14
The Marikina incident	0	46	20
Ethics, accountability, transparency	14	12	19
Totals	**128**	**151**	**103**

The statistics in Table 1 above shows that contrary to initial expectations, Lonmin actually decreased the extent of ESG reporting per category year on year, with Marikana-specific information (which is included in a separate section of the 2012 annual report) and the 'Ethics, accountability and transparency' category (which shows a net increase from 2011 to 2013) as the only exceptions. The change in categories is also visually depicted in Figure 1 and Figure 2 below:





At first glance, these results are inconsistent with prior research which posits that companies include additional non-financial information in their annual reports when faced with a crisis of legitimacy (Patten, 2002; Tregidga, et al., 2014). The results, however, suggest that Lonmin adopted a different legitimation strategy. Faced with a crisis of confidence in the aftermath of the strike action, the company cannot simply ignore the implications of Marikana for investor confidence (see Suchman, 1995). In order to ascertain how the Marikana-incident was dealt with by Lonmin, the Author thoroughly scrutinised the 2012 annual report.

The information provided to readers includes are both qualitative and quantitative in nature data. For example, the company reported on lost production time and the direct cost of the strike. It also dealt with issues such the loss of life; the work of the Farlam Commission of Enquiry; and the role of the company's corporate governance systems for implementing any remedial action (Lonmin, 2012).This allows the entity to be seen as responsive to the interests of stakeholders according a sense of pragmatic legitimacy. In particular, multiple examples of the company expressing regret and offering condolences (found throughout the 2012 annual report) personify the organisation and highlight how it is functioning according to socially expected standards thereby securing moral and cognitive legitimacy.

Maintaining and repairing legitimacy, however, also involve the establishment of clear lines of demarcation between the delegitimised event and the remainder of the organisation (Suchman, 1995; De Villiers & Van Staden, 2006). To this end the social and governance disclosures dealing specifically with the Marikana incident are included in a separate section of the 2012 annual report. To further signal how the event was an extraordinary one – and not indicative of daily operations at Lonmin – other ESG disclosures were not increased. As explained by Suchman (1995), the aim is to protect past achievements Decreasing the extent of other ESG information is, therefore, used to signal subtly how - barring the events taking place at Marikana - the company continues to operate as a credible part of the South African mining industry.

A decrease in ESG disclosures in other sectors of the report also highlights how the company is possibly seeking to preserve and repair legitimacy by avoiding scrutiny (Suchman, 1995). As found in an earlier study by De Villiers and Van Staden (2006), South African mining companies frequently decrease the quantum of specific environmental disclosures in their annual reports in order to avoid the added attention of various stakeholders. As discussed above, the unprecedented nature of the strike action means that the company is probably compelled to deal with Marikana in detail in the report in order to avoid accusations and further negative publicity. As explained by Suchman (1995), denial or avoidance of a clearly significant social event is unlikely to be an effective strategy for preserving legitimacy. This must, however, be juxtaposed with the ESG reporting on other parts of the organisation.

It is possible that including additional ESG information on the remaining segments or business units could have acted as an unintended signal to the users of the annual reports that Marikana was indicative of a pervasive ESG challenge being faced by the organisation rather than an isolated issue. In other words, reducing the ESG disclosures in other sections of the reports acts as a subtle signal to stakeholders, allowing the organisation to build trust and preserve its legitimacy reserves. This also provides an explanation for the only other category which reported an increase in the frequency of disclosures.

Ethics, accountability and transparency information tends to be less specific and, as such, pose less of risk of stakeholders asking difficult questions on the basis of ESG metrics included in the 2012 annual report. At the same time, these disclosures often deal with the corporate ethos and, as such, play an important role in communicating the values of the organisation. By increasing the quantum of these disclosures, the entity is able to demonstrate how its values are aligned with generally accepted social standards which champion good governance and corporate transparency. This accords pragmatic legitimacy. At the same time these disclosures preserve the image of the organisation as a responsible actor ensuring that a general decrease in ESG disclosure (other than Marikana-specific information) goes almost unnoticed.

5. Conclusion

This draft paper provides initial evidence in support of the relevance of legitimacy theory for explaining changes in the extent of social and governance information being provided by companies to their stakeholders. In particular, the research deals with how Lonmin changes the extent of its social and governance information included in its annual reports following the widely publicised strike action at Marikana.

In line with expectations (Patten, 1992; 2002), the study shows that Lonmin increased the total social- and governance-related disclosures from 2011 to 2012, followed by a decrease in the following year. Most of this increase is, however, attributable to disclosure dealing specifically with the events at Marikana. Given the unusually violent nature of the strike – and significant public scrutiny – it is simply not possible for Lonmin to relegate the implications of Marikana to a footnote in its 2012 annual report (see Suchman, 1995). In order to create the impression of an organisation which is aware of societal concerns (and which empathises with the loss of life at Marikana) dealing with the strike action in the opening section of the annual report accords moral and pragmatic legitimacy. At the same time, the disclosure strategy is used to create a clear line of demarcation.

By including most of the social and governance information on Marikana in a separate section of the Annual Report (2012), the company is able to signal subtly that it regards the incident as isolated and not indicative of the ‘real’ organisation. This is supported by decreasing the ESG information (which is not Marikana-specific) in other sections of the annual report (2012). At the same time, the company – mindful of the added public scrutiny – can avoid drawing attention to the CSR activities at other operations which have gone largely unnoticed.

In order to examine exactly *how* the company is mobilising its ESG disclosures to maintain and repair legitimacy, additional research will be needed. This review note simply provides an introductory perspective. The data collection and analysis process has not been completed. In particular, discourse and interpretive text analysis is needed to explicate the functioning of specific legitimation strategies (see Jones & Solomon, 2013; Tregidga, et al., 2014). The preliminary results have also been limited to examining Lonmin’s disclosures. To understand better the relevance of legitimacy theory for non-financial reporting, future research needs to explore how other platinum mining houses altered their ESG reporting from 2011 to 2013. Finally, interpretive research making use of detailed interviews with primary stakeholders is needed to illuminate the social construction of South African corporate reporting and how annual/integrated reports are interpreted by their readers.

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