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Budgeting as a Means for Communication of Business Ethics

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Budgeting as a Means for Communication of Business Ethics: the Case of the Tallinn City Government

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Abstract

This case study focuses on communication of business ethics via budgeting in the capital of Estonia during the last 75 years. Historically, Estonia was under the rule of Denmark, Germany, Sweden, and Russia for a long time. The first period of Estonian independence lasted for 22 years, beginning in 1918. In 1940, the Republic of Estonia was occupied by the Soviet Union. Estonia regained independence in 1991. The authors of the present article analysed and compared the annual budget books of the city government in all these three periods from the viewpoint of the concept of Corporate Social Responsibility and business ethics. As a result of the study an original model for measuring changes in CSR orientation was designed.

Keywords: accountability, budgeting, business ethics, Corporate Social Responsibility, public sector, social capital, sustainability

Introduction

Corporate Social Responsibility (CSR) promotes a vision of business accountability to a wide range of stakeholders. Key areas of concern are environmental protection and the well-being of employees, the community and civil society in general, both now and in the future. Thus CSR is about how companies conduct their business in an ethical way. The stakeholder approach was introduced by Freeman (1984) who emphasized the idea of ethical balance between the interests of the firm and the stakeholders in a perspective of strategic management.

The CSR concept started to attract increased attention with the work of Bowen (1953) focused on the obligations of business toward the expectations of the very society that permitted its existence and conferred on it legitimacy.

In the current exceptional circumstances, Corporate Social Responsibility is even more crucial than ever, said European Commission President José Manuel Barroso speaking at CSR Europe's General Assembly in Brussels on 11 June 2009 (Website of CSR Europe, 2009). Barroso said: "The crisis resulted, in part at least, from a failure by some businesses to understand their broader ethical responsibilities. Now all businesses must rise to the challenge." (*Ibid*).

How about accountability in the public sector? Even Weber represented bureaucracy as a threat to parliamentary democracy (Kolthoff *et al*, 2006). Once bureaucracy is established, he said, it becomes almost impossible to abolish. Moreover, it serves as a "power instrument of the first order – for the one who controls the bureaucratic apparatus" (*Ibid*). Kolthoff *et al* have found that sometimes the words *value*, *integrity* and *ethics* are non-existent in the capacious books directed to the New Public Service and they stress that we need to rethink what we mean by democratic accountability – today we only have accountability for *how* government does what it does but we also should care about *what* government does (*Ibid*). Already Wolf who published a far-famed Russian accounting journal in 1888-1904 says that it is not significant how to account – the most critical things are what we account for and why (Järve, 2009).

This paper examines accountability in the local government of Estonia. Our analysis is based on numerous annual budget books of the Tallinn City Government in 1934-2008 including all three periods of the Estonian state: the period of the first independence, the occupation period and the re-independence period.

1. Theoretical Background

According to Gray et al (1996) and Cornwall et al (2000) accountability involves two different (but linked) responsibilities:

1. the duty to undertake certain action,
2. the duty to provide an account for those actions.

Najam (1996) speaking about non-profit organizations identifies three categories of accountability concerns:

1. accountability to patrons,
2. accountability to clients,
3. accountability to themselves.

Corporate social responsibility is about the company's accountability to all of its stakeholders. For example, Tanimoto and Suzuki (2005) define CSR as a concept whereby companies fulfil accountability to their stakeholders by integrating social and environmental concerns in their business operations.

The concept of CSR does not have a generally understood meaning. In the European Union CSR is a part of the official policy as a factor improving competitiveness and the EU definition of CSR is: "A concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis". Although the concept of CSR dates from the fifties of the last century (Norris and Innes, 2005:10) and theoretical perspectives on CSR

have been developed for over two decades (Carroll, 1979, Freeman, 1984, Donaldson, Preston, 1995, Clarkson, 1995, McWilliams, Siegel, 2001), its practical implementation has increased in importance only in the last decade (Kawamura, 2004, Balmer *et al*, 2007).

CSR benefits businesses economic performance, their reputation and employee relations, improves their compliance with legislation and enhances their risk management (Freeman, 1984, Matten and Moon, 2004).

The concept of CSR is underpinned by the idea that corporations can no longer act as isolated economic entities operating in detachment from broader society. Traditional views about competitiveness, survival and profitability are being swept away. Organisations begin to recognize that their role goes beyond a purely economic one, and that it has certain other duties and obligations (Reidenbach and Robins, 1991). Juščius and Snieška (2008) claim that only the companies, which aim to save all universally accepted ethical standards of social behaviour, can expect a positive attitude and support in the modern society. Nowadays corporate social responsibility is an integral part of the business vocabulary and is regarded as a crucially important issue in management (Cornelius *et al*., 2008; Humphreys, Brown, 2008).

The attention to the relationship between CSR and social capital is recent but it is starting to assume a significant relevance (Andreas *et al*, 2009). The reason for that is that CSR can be understood as the business contribution to sustainable development and according to Coleman (1988) social capital is definitely one of the pillars of sustainable society (Ibid).

According to Putnam (1993) the forms of social capital are general moral resources of the community, and they can be divided into three main components: first, trust (and more generally positive values with respect to development); second, social norms and obligations; and third, social networks of citizens' activity, especially voluntary associations.

Coleman (1988) claims that the forms of social capital are self-reinforcing and cumulative by nature: the more social capital is used, the more it grows.

Additionally, Bourdieu (1986) asserts that a bureaucratic organization is an effective administrative tool in concentrating social capital and transforming quantity (the number of members) to quality (the organizational effectiveness).

In last ten years, multiple studies are available that analyse the relationship between CSR and culture. Some authors (Hillman and Keim, 2001, Wieland, 2005, Rooney, 2007, Thornton and Jaeger, 2008) have found that there has to be congruence between organizational culture and CSR, and they claim that in general CSR should be seen as an embodiment of organization's culture and values. Many empirical studies have confirmed that individual and organizational values are significant predictors of CSR managerial behaviour (Branzei *et al*, 2004, Vitell, Paolillo, 2004, Hemingway, 2005, Waldman *et al*, 2006).

Developing a CSR orientation is possible only if a supportive organizational culture emerges within the organization (Lyon, 2004). This statement highlights that an organization must achieve a deep comprehension of the ethical and cultural developments associated with CSR if it wants to reach a genuine CSR orientation (De Woot, 2005). Developing CSR initiatives thus often demands the cultural evolution of the organization. Moreover, organizational cultures can represent of information, knowledge, and know-how that may support or spoil CSR efforts (Doppelt, 2003).

Some researchers have analysed impacts of national culture on CSR. Waldman et al (2006) have showed that while institutional collectivism predict the values of CSR in a positive direction, in-group collectivism had no significant effect on CSR. Additionally, Ringov and Zollo (2007) have found that cultural differences with respect to individualism had no significant effect on CSR. Chen *et al* (2001) claim that individuals with communal orientation demonstrate greater socially acceptable views and norms, which means that they link power with responsibility goals. Ringov and Zollo (2007) and also Scholtens and Dam (2007) have concluded that masculinity has a significant negative effect on corporate social performance and ethical policies. Husted (1999) has proved that managers in countries with high power distance, masculinity and uncertainty can easily engage in corrupt business behaviour.

2. Background of the Study

Kolthoff et al (2006) stress: “Do not assume that the public sector is more ethically aware than the private sector. In other words: developments in the business sector can contribute toward making the public sector more ethical.”

According to Kooskora (2008) the modern business environment in Estonia is relatively young and companies are still coming to understand new methods and new paradigms as CSR. Estonian CSR Index 2009 indicated that reporting on CSR is weak even among the companies that already practice CSR. The average index score for companies was 60% of the maximum 100% while the score obtained by the Tallinn City Government was 58% (Roostalu, 2009).

According to Hofstede (The Website of Hofstede’s works, i.e.) there are considerable differences between Estonian and Russian national culture (see Figure 1).

In Russia the highest cultural dimension is avoiding uncertainty indicating the society’s low level of tolerance for uncertainty. Making an effort to minimize or reduce this level of uncertainty, strict rules, laws, policies, and regulations are adopted and implemented. There is also a very high power distance that is indicative of a high level of inequality of power and wealth within the society (Ibid).

Estonia freed itself from a foreign power almost 50 years after annexation. Lagerspetz (1996) has found that even if Soviet doctrine never reached the position of ideological hegemony in Estonia, the legacy of the previous regime is often still visible in Estonian public organizations — mostly in people’s behaviors and mindsets.

Since public administrators’ values and attitudes directly affect the processes and outcomes of public administration — often more than the structures and processes themselves — Estonian local administration is still rather far from “good public administration” (Drechsler, 2004).

Tõnnisson (2006) believes that the Estonian public sector lacks a clearly established system of values and thus the formation, propagation, and reinforcement of the values should be initiated.

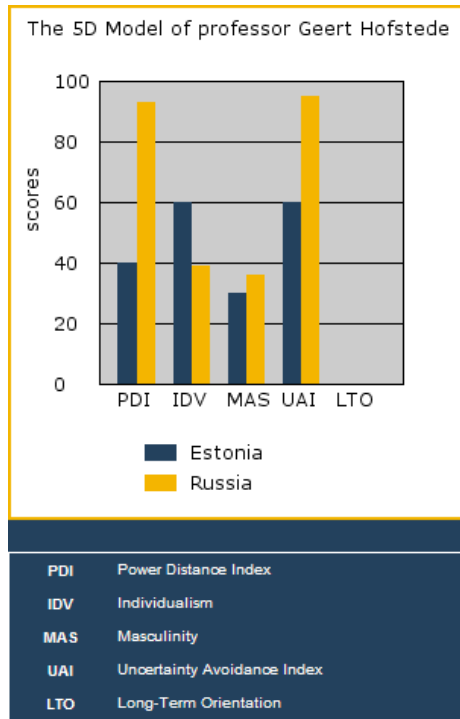


Figure 1. Comparison of Estonian and Russian national culture

According to Vinkel (2008) the prevailing organizational culture in Estonian municipalities is a clan-like culture, where family-like affairs, good relations between workers and the lack of competitiveness are valued, while in other countries the prevailing organizational culture for the institutions in the public sector has traditionally been the hierarchical one. Übius and Alas (2009), according to their study in 8 countries, have proved that three organizational types – clan, hierarchy and adhocracy culture – predict two facets of CSR (i.e. organization performance concerning social issues and organization respects the interest of agents), and the 4th organizational culture type – market culture - predicts one facet of CSR (i.e. organization performance concerning social issues).

The Legatum Prosperity Index 2009 shows that Estonia holds the 31st place among 104 respondents but our results in social capital, which is a part of the index, are very bad – we are holding the 94th place (Legatum Prosperity Index, 2009).

3. Purpose and Methodology of the Study

Our purpose was to find out how the budget books of the city government portray the city’s ethical behaviour and CSR orientation and whether there have been better times for social capital in Estonia. There are no data on such studies in Estonia – some

authors have studied the use of management accounting information both in the private and public sector but not from the viewpoint of CSR. Moreover, the authors of the present article have no information about any studies focused on CSR communication via budgeting all over the world although there are several studies devoted to various responsibility reportings.

The content analysis as a qualitative study method was used for analysing the body of annual budget books. Using quantitative content analysis in CSR researches is not new. We could not use quantitative methods of content analysis for counting some phrases or words because these budget books did not include any primary phenomena of CSR – they were rather hidden in the background of the content and we needed to read between the lines. Thus, first the Critical Discourse Analysis (CDA) was used. Fairclough's (1989, 1995) model for CDA consists of three inter-related processes of analysis tied to three inter-related dimensions of discourse. These three dimensions are:

1. The object of analysis (including verbal, visual or verbal and visual texts),
2. The processes by means of which the object is produced and received (writing/speaking/designing and reading/listening/viewing) by human subjects,
3. The socio-historical conditions which govern these processes.

According to Fairclough each of these dimensions requires a different kind of analysis:

1. text analysis (description),
2. processing analysis (interpretation),
3. social analysis (explanation).

Next we applied a content model to the results of CDA which we had designed on the example of the Portes' model of social capital where both positive and negative categories or so-called outputs of social capital are taken into account (Portes, 1998; Portes and Landolt, 1996). In our model some categories of CSR are similar to outputs of the Portes' model. Additionally, according to the results of CDA we added several new categories and grouped all of them to the various phenomena of CSR and finally we grouped these phenomena to the three main groups describing three dimensions of CSR (see Appendix). These three dimensions form our three-part model. As the number of the analysed budget books for each period was not equal (there were 6 books for the 1st period and 9 for the other two periods) we could not use absolute values for results of the content analysis. Thus we used a homogenized scale with rates of densities where „-1“ was the biggest negative value used by negative categories and „+1“ was the biggest positive value used by positive categories. These values can be classified as performances of categories. For example, if a positive category existed only in three budget books of total 9 we calculated for its performance $3/9=0.33$ (or -0.33 if it was a negative category).

4. Empirical Data and Analysis

In this section we present the results of our model and some of the best examples of the city's activities during the three periods under our investigation related to the model.

The 1st part of the model - the economic dimension of CSR

Here we selected and assessed three phenomena of the economic dimension of CSR: balanced budgets as a keyword for economic stability, transparency of budgets and technical level of budgets. The latter two include many categories (see Appendix). An aggregated overview of the results of this dimension is given in Figure 2. The figure shows that in the 1930s the city government had the highest transparency of budgets. In the Soviet time transparency decreased while technical level increased. Today these two phenomena are slowly increasing.

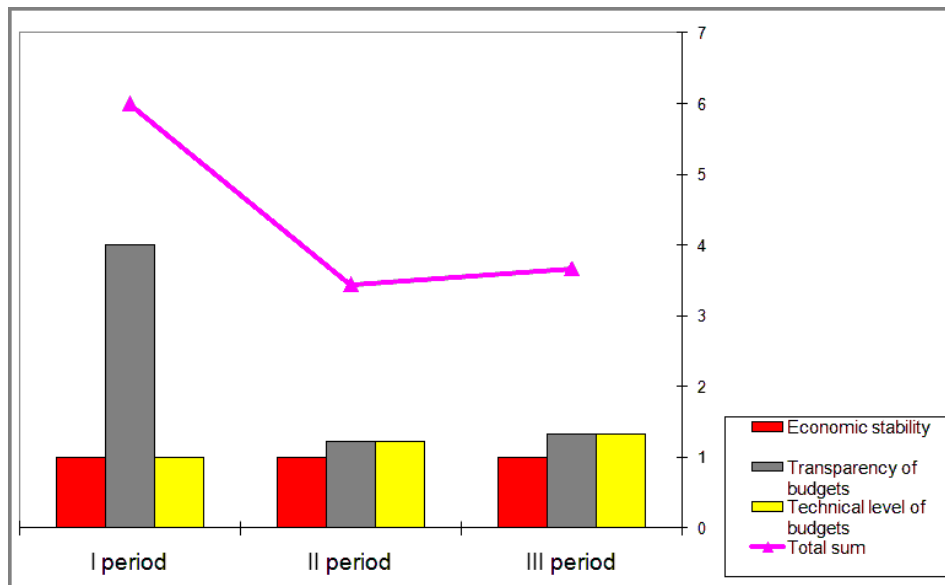


Figure 2. Changes in the economic dimension of CSR

Example 1

The city's budget books from the 1930s include several long tables in the appendixes that take 2-3 times more space than the budget itself and offer a lot of useful information on the priorities and operation modes of the local government related to the community and other stakeholders. The largest table (49 pages!) describes the labour costs of all officials and other workers providing their first names, surnames, positions, monthly wages, wage groups (or levels), job tenures, flat rents and other costs where applicable (Tallinn, 1934: 195-243).

Example 2

Immediately after the Soviet occupation, the so-called nomenclature of the new local government took for granted that they deserve better wages. In the first budget book of the time 24 pages are filled with argumentations for each post (names were no longer specified) that the wages must be increased "because there was a growth of work load" or – in case the rise in wages was much higher – "because there was a growth of work load and work responsibility" (Tallinn, 1940: 11-34).

Example 3

In the introduction of the first budget book dating after the re-independence, the financial department has written that "this book is addressed to all interested people in- and outside the city organization because in the conditions of democracy a bigger

openness is needed while at the Soviet time only 20 pages were covered with explanations on occupational work”¹ (Tallinn, 1993: 3).

The 2nd part of the model - the environmental dimension of CSR

The phenomena that belong to this group include environment protection and control over natural resource consumption where the uses of both natural and financial indicators were assessed (see Appendix).

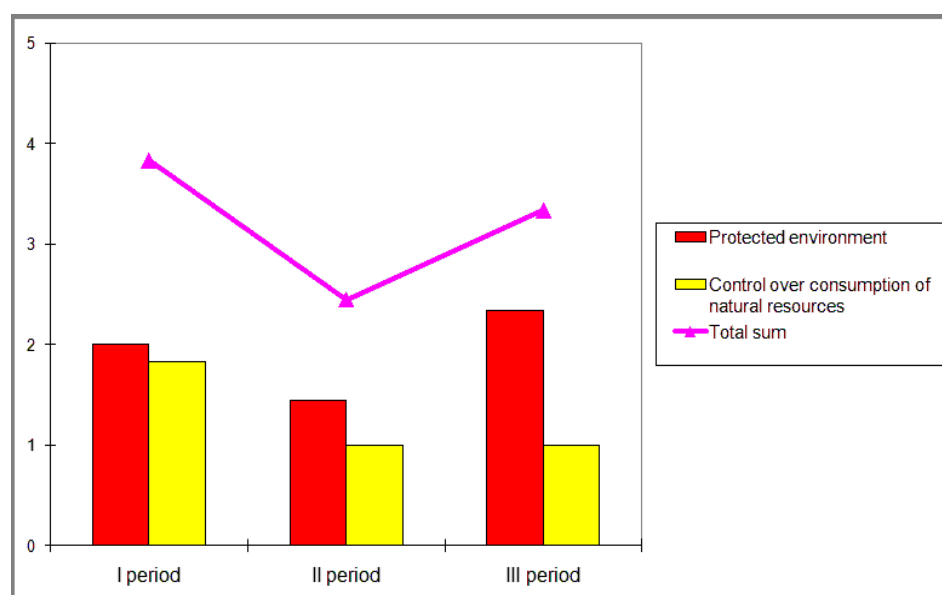


Figure 3. Changes in the environmental dimension of CSR

We can conclude that in the 1930s managing this issue was a little bit better while in the Soviet time it was significantly weaker (see Figure 3).

Example 4

In the 1930s the dog tax was 15 crowns per year but for blind and deaf-and-dumb persons it was only 1 crown. The members of sport clubs were freed from the water vehicle tax “if these vehicles were not used for increasing incomes”² (Tallinn, 1936: 28).

The 3rd part of the model - the social dimension of CSR

In this dimension we had 20 categories (see Appendix), which were grouped to the three phenomena (see Figure 4). As the other parts of our model include altogether 18 categories, the score chances here were bigger, too.

¹In the 1950s instead of budget books and budget project books we can only see brochures including financial numbers without explanations. These brochures are both in Estonian and in Russian while before only Estonian language was necessary.

² In 2009, the Tallinn City Government also validated the boat tax but without any exception.

Unfortunately in the Soviet time the city government's score of the social tasks was much lower than that of the other two managing issues at this time. Moreover, in the field of education and culture the results were negative. Thus in the second period, a rapid fall occurred.

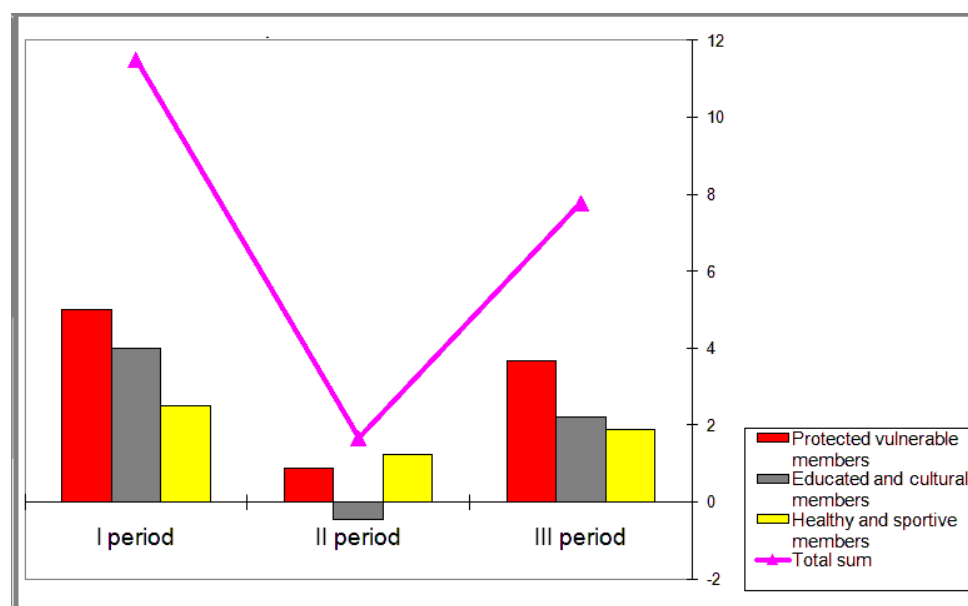


Figure 4. Changes in the social dimension of CSR

Example 5

In 1937, when the city government had planned to increase wages of all workers via the so-called tenure wages it was decided that low-paid workers need a higher rise in wages (6,5 % - 32,5% from the basic wage) than high-paid workers (4% -20%)³ (Tallinn, 1937:78).

Example 6

In the 1930s, retired or long-time workers as well officials with their families received one-time or permanent benefits. All the beneficiaries with the data including their names, positions, job tenures, benefit sums and remarks about the real beneficiary (to himself, his widow, etc.) were listed in the appendix. In 1934 the list of beneficiaries included 129 persons and most of them were ordinary people such as builders, stokers, street-cleaners (Tallinn, 1934: 264-266).

Example 7

In 1945-1970, taxes from community included the following two taxes (Tallinn, 1950:12): the income tax and “the tax of the citizens of the Soviet Union who are unmarried, single, or having few children⁴”. According to an appendix of the budget book 25% of the taxpayers had no children, 42% had one child and 33% had two children (Tallinn, 1950, 286).

³ Unfortunately this nice tradition has not been followed anymore and in fact, using equal coefficients, which is quite common increases differences between high- and low-paid workers' wages.

⁴In the 1970s Soviet statutory law became slightly milder: all married women and all men even very young and single who did not have any children had to pay this childless tax.

Example 8

In the 1950s the rates of VAT (actually the tax from turnover, not the value added tax) were very different and most of them were unbelievably high. Probably these rates or rate ranges were validated in Moscow but we are sure that the city government also had some freedom to validate them because for example the leather shoes manufactured in two different factories had different rates of VAT: in Kommunaar where the production had a higher quality and was not on open access (i.e. reserved for white-collar workers with high positions) it was only 13% while in Artell that made common shoes VAT was 20% (Tallinn, 1950: 196-206). Moreover – in Pohjala, where rubber boots were made for ordinary people, taxes to men's galoshes were 69.5%, 72.3% to women's galoshes and 74.4% to child's galoshes (Tallinn, 1950: 196-197). Additionally, other basic commodities such as food were also highly taxed: cereals with 90%, meat with 80%, sugar with 78% and milk with 57% (Tallinn, 1950: 177-190) while nonessentials were not: for example stationery were taxed with 24% (Tallinn, 1950: 224). It is important to point out to the credit of alcohol policy of this time that vodka had the highest tax rate – 1000% (Tallinn 1950: 178).

Example 9

According to the budget of the Estonian Soviet Socialist Republic (ESSR) from 1945, all kindergartens and most of the orphanages were funded by local governments and in orphanages food costs per child were 1.5 times higher than in kindergartens (Eesti NSV, 1945: 32-33). The food calculations of the city government show that five years later this difference was 1.3-1.4 (Tallinn, 1950: 94-96). Additionally, there were big differences in the norms of milk, butter and fresh fruit. In orphanages, fruit was totally lacking while in kindergartens fruit norm was 100 grams and in two special kindergartens for children with weak health conditions it was 200 grams. The norms of butter were 17 grams in orphanages, 30 grams in kindergartens and 50 grams in special kindergartens. The norms of milk were 250 grams in orphanages, 300-350 grams in kindergartens and 500 grams in special kindergartens. In orphanages, the norms of potato, vegetable, fish, cookies and candies were slightly higher (Ibid).

Example 10

In 1992, the city government and all city's district governments established their reserve funds where in 1993 lot of payments were made to theatres, choirs, handicapped sportsmen association and other handicapped people associations, child associations, sport clubs etc (Tallinn, 1993: 53-56).

The Final Results of the model

Figure 5 gives an aggregated overview of the results.

Hence, although there were no differences in financing social and environmental tasks during the three periods, i.e. the rates of the money for these tasks were constantly between 88% and 90% from the budget sums (Tallinn, 1934-1940, 1949, 1950, 1959, 1969, 1979, 1989, 1990, 1991, 1993, 1995, 1998, 2001, 2003-2005, 2008) we can see big changes in the CSR orientation.

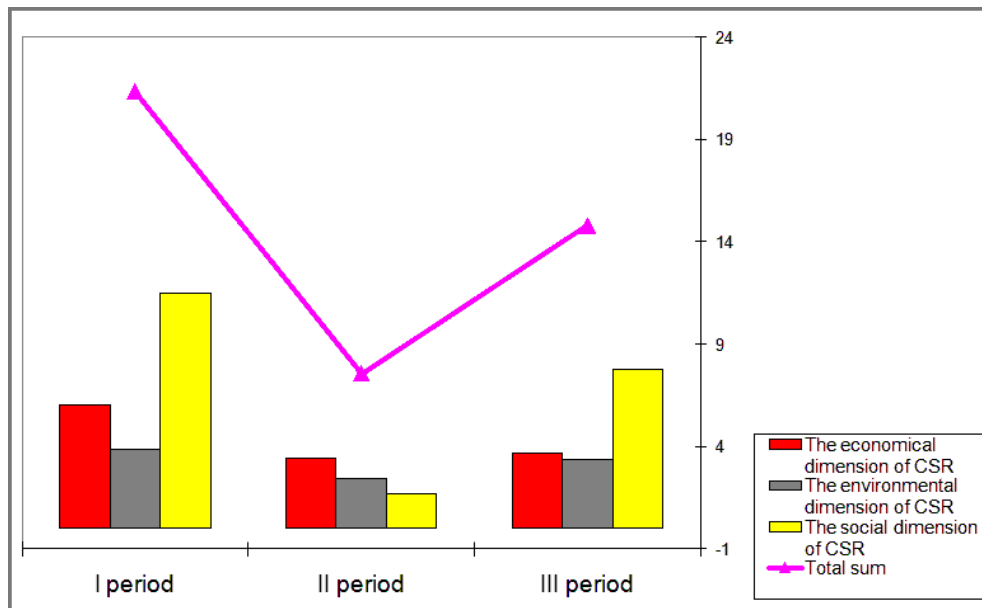


Figure 5. Changes in the CSR orientation of the city government

As CSR is related to social capital we can suppose that there was a decrease in social capital, too.

Conclusions

Habermas (1981) defines communicative action as a form of social interaction in which the plans of action of different actors are co-ordinated through an exchange of communicative acts, that is, through the use of a language orientated towards reaching an understanding. This paper observes the communication of business ethics via budget books of the capital of Estonia during the last 75 years including all three periods of the Estonian state: the first independence period, the occupation period and the re-independence period.

Our approach is based on content analysis of annual budget books of the city of Tallinn. As a result of the study a model for measuring changes in CSR orientation was designed. As we have no data about papers presenting such a model we are sure that we can pretend to originality in our modelling.

The results of the study show that regardless of equal financing tasks in all three periods there were big differences in the essence and aims of social and environmental tasks of the local government.

The study indicated that in the 1930s, the city government had the highest ethical behaviour and CSR orientation, which means that in the Estonian public sector some CSR principles were used 15-20 years before Bowen's famous work. The authors found that in the 1930s, the budgets were very detailed and transparent. Moreover, the budget policy of the city government was directed towards the well-being and supporting the community as a whole, especially its most vulnerable members. There are also several examples about voluntary activities of the city.

Developing CSR orientation and business ethics was interrupted by the occupation although the level of general accounting tools increased. It can be said that the local government executed its tasks in the frames of the law.

Finally, it is argued that since the Republic of Estonia regained its independence the Tallinn City Government has been rehabilitating its ethical face.

We found that accountability of the local government of Estonia was suppressed by the Soviet occupation but nowadays it is increasing again. Accountability is related to the process of lawmaking and legitimacy (Stahn, 2004). Coming back to Habermas we stress that for him legitimacy is first of all creditworthiness (*Anerkennungswürdigkeit*) (Habermas 1976: 271). Habermas defines his famous discourse as a procedure where all actors having equal rights and using communicative actions reach consensus as the truth, which is the only legitimate one (Habermas 1992: 138). Thus Habermas claim that only these norms of behaviour are legitimate, which are accepted by all actors of discourse. Moreover Habermas' discourse can be interpreted as the only means for democratic law making (Käärik, 2009 & 1998, Dy, 1994) although many authors have criticised this viewpoint of Habermas (Ibid). Here we agree with Dy, who claims that Habermas' ethics of discourse provides us with a foundation or standard for discussing and judging what is right or wrong in the context of society (Dy, 1994).

There are also limitations in this study connected with the used methodology. Namely, as our selection of categories as well as phenomena for this model was a subjective process in its nature we do not pretend to the absolute truth of our results. It is not only our problem – content analysis always includes some subjective moments and there is no absolute truth for making such models.

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APPENDIX

CSR Content Analysis Model

FENOMENA OF CSR ORIENTATION	POSITIVE CATEGORIES	NEGATIVE CATEGORIES	I period	II period	III period
1. The economic dimension of CSR			6,0	3,4	3,7
Economic stability	Balanced budgets		1,0	1,0	1,0
Transparency of budgets	Detailed view of costs and revenues		1,0	0,3	0,4
	Detailed explanations of costs and revenues		1,0	0,3	0,3
	Budgets of each organizational entity		1,0	0,1	0,3
	Labour costs by each worker		1,0	0,1	0,2
	Bilingual budgets		0,0	0,7	0,0
		Dissembling	0,0	-0,3	0,0
Technical level of budgets	Product based budgeting		0,0	0,0	0,3
	Analytical accounting tables		1,0	0,6	0,4

	Cost accounting and cost prices of services		0,0	0,3	0,1
	Financial ratio analysis		0,0	0,3	0,1
	Accrual based accounting		0,0	0,0	0,3
2. The environmental dimension of CSR			3,8	2,4	3,3
Protected environment	Public parks and beaches		1,0	1,0	1,0
	Tallinn Botanic Garden		0,0	0,4	1,0
	Supporting environment protection organizations		0,0	0,0	0,3
	Boat tax		1,0	0,0	0,0
Control over consumption of natural resources	Measuring consumption of natural resources in financial indicators		1,0	1,0	1,0
	Measuring consumption of natural resources in non-financial indicators		0,8	0,0	0,0
3. The social dimension of CSR			11,5	1,7	7,8
Protected vulnerable members	Kindergartens, orphanages, hospitals		1,0	1,0	1,0
		Discrimination of orphans	0,0	-0,2	0,0
	Supporting child organizations		0,7	0,0	0,3
	Child benefits		0,0	0,0	0,6
		Tax on childless and other discriminatory taxes	0,0	-0,9	0,0
	disability allowances		1,0	1,0	1,0
	Supporting disabled people's organizations		0,8	0,0	0,6
	Supporting retired employees and their families		1,0	0,0	0,2
	Bonus for low-paid employees		0,5	0,0	0,0
Educated and cultural members	Supporting schools of ethnic minority		0,7	0,0	0,3
	Primary, secondary and vocational schools		1,0	1,0	1,0
	Supporting poor students in primary schools		1,0	0,0	0,0
	Scholarships in universities		0,7	0,0	0,4

		Study fees in secondary schools	0,0	-0,6	0,0
	Supporting culture and education organizations		0,7	0,0	0,4
		Taxes from public organizations	0,0	-0,9	0,0
Healthy and sportive members	Sport enterprises		0,5	0,8	1,0
	Supporting sport organizations		0,7	0,0	0,4
	Tax benefits for sportive and young people		0,7	0,0	0,4
	Alcohol policy		0,7	0,4	0,0
TOTAL SUM			21,3	7,6	14,8