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An Inquiry into the Accountability of the State-Owned Financial Institution versus Privately Owned Financial Institution

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Abstract: *The purpose of this research is to analyze whether State-Owned Financial institutions are giving more attention, in their integrated report, to stakeholders, that among the most important find the civil society, than Privately-Owned Financial institutions. An in-depth content analysis of the analyzed financial institutions' Integrated Reports has been carried out, through the employment of MAXQDA, whit the extent to answer research questions proposed. Evidences outlined a higher stakeholder engagement by State-Owned Enterprises. Further research are required for a better understanding of Stakeholder engagement of SOEs.*

Keywords: *Integrated reporting, financial institutions, public sector, private sector, accountability, stakeholders, content analysis*

JEL Classification: M41

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1. INTRODUCTION

In 2007-2008, the financial sector encountered a collapse, requiring involvement by governments to bail out financial institution (e.g. Lehman Brothers, Citigroup, HBOS, Royal Bank of Scotland, UBS) (Erkens et al., 2012; Pwc, 2015); such operations employed public resources in order to avoid bankruptcy.

In this regard, organizations which after the financial crisis became owned by States are now facing a different status, as they are considered State-Owned Enterprises (SOE). These entities include, according to the Organisation for Economic Co-operation and Development (OECD), ‘any corporate entity recognised by national law as an enterprise, and in which the state exercise ownership […] statutory corporations, with their legal personality established through specific legislation […] if their purpose and activities, or parts of their activities, are of a largely economic nature’ (OECD, 2015: 16).

SOEs are considered organisations which are facing ‘(officially and unofficially) extended lines of ownership and accountability’ (Luke, 2010: 160), instruments (Mishra, 2014) for different purposes such as privatisation, access to other markets, protecting or developing economies (OECD, 2015), bailout (Flores-Macias, 2009; Christiansen, 2011; G.D. Bruton et al., 2015) and for transition in economies like ex-communist countries (Tan, 2005).

Moreover, public sector organizations are feeling the pressure to justify their environmental and social activity in in economic terms (Gray et al. 2009) due to higher accountability expectations and obligations in the public sector and, also, higher in the case of SOEs compared to the private sector (Greiling & Grüb, 2014). Also, these organizations are facing a wider range of stakeholders than private organizations (Cormier & Gordon, 2001).

Given the previous assertions, SOEs and public entities have been drawn by different types of report (Guthrie & Farneti, 2008) in the recent years in order to inform their stakeholders; since they are the reason for reporting sustainability information (Farneti & Guthrie, 2009).

In spite of the fact that principal guidelines for Sustainability Reporting (SR) are delineated for private sector organizations (Dumay et al., 2010), it is noteworthy that SOEs have been publishing SR and embracing new type of reports, such as Integrated Reporting (<IR>).

<IR> includes financial and non-financial information relevant to the company in a single connected report (Eccles R.G., Krzus M.P., 2010; Eccles R.G., Saltzman D., 2011; Paternostro S., 2016). In particular, <IR> ‘should provide insight into the nature and quality of the organization’s relationships with its key stakeholders, including how and to what extent the organization understands, takes into account and responds to their legitimate needs and interests’ (IIRC, 2015; p.17).

Analysing the International Integrated Reporting Council (IIRC) Database, a wide range of private organizations, SOEs and public agencies seems embracing the <IR> movement; but, among these there is a high presence of financial sector institution.

The elevated presence of banks and insurance companies is supported by the need of the private financial markets of information, reporting and disclosure toward market operators, regulators and supervisors in order to function properly (Acharya & Richardson, 2009). Nonetheless, the financial crisis led to a loss of confidence by the society towards banks, as these organization are expected to attend the process of society’s development though their business activity (Krasodomska, 2015) financial institutions seem responding to the loss of confidence by

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civil society and the increasing demand of information from their stakeholder, through the employment of IR.

In this perspective, the present paper aims to analyse and compare the Stakeholder Engagement (SE) between State-Owned Financial Institution (SOFI) and Privately-Owned Financial Institution (POFI), based on the framework provided by Manetti (2011).

Prospective results shall strengthen insights to the SOFI commitment toward stakeholder, which as other scholars outlined (Cormier & Gordon, 2001; Greiling & Grüb, 2014) are expected to be higher than POFI. The present study, also, outlines that <IR> is also used to inform stakeholder not only shareholder; as, on average organizations analysed demonstrate a wide number of stakeholder.

The present paper unfolds as follows: the second section presents a brief overview of relevant literature, including three subsections: a theoretical framework analysis (tackling both legitimacy and stakeholder theories), a conceptual construct delineation (mainly oriented towards the approach on stakeholders from <IR>) and a linkage between stakeholder engagement and the concept of public accountability. The third section presents details about the sample used in the present study and the respective methodological steps used in our research. The fifth section outlines and discusses the results obtained from the analysis, while preliminary conclusions and future developments are presented in the final section.

2. 2. A REVIEW OF THE RELEVANT LITERATURE AND FRAMEWORKS

2.1. Theoretical Framework: Insights on Legitimacy and Stakeholder Theories

As our research tackles aspects concerning multiple interactions between actors in the extension of financial institutions, we frame it between the outlines of two main theories, namely: legitimacy theory and stakeholder theory. According to Suchman (1995), legitimacy manifests itself as a perception on the general level (or even an assumption) that the actions of an entity 'are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions.' Such is the case within the financial system, where the actors and institutions participate with the inherent understanding of financial fair-play.

However, it is highly debatable to which extent the degree of manifested legitimacy manifested by the involved entities is measurable (especially, when we make assessments of accounting disclosures) (Tilling, 2004). Instead of pursuing this measurable trait, other researchers used models derived from legitimacy theory to pinpoint relevant stakeholders in close connection with the organizations and their respective flow of resources (Hybels, 1995), such as: the state, the public, the financial community, and the media. Hence, this theory offers the means to modulate a starting point for unpacking organizational disclosures (and their respective information users) (Tilling, 2004).

The employment of the legitimacy theory in the framing of stakeholders within systems of reporting with non-financial traits occurs in the literature as it offers a proxy for assessing the respective relationships between the organization and interested parties. We notice this mainly for social disclosures (Grey et al, 1988; Archel et al, 2009) – as they show a strong emphasis on the relationship with the general public, but also for Integrated Reporting (Beck et al, 2015; Dumitru & Guse, 2017).

The stakeholder perspective provides insights from the users of the reports. The respective managerial theory also emerged in the private sector, in the mid-80s, stating that a 'business can be understood as a set of relationships among groups that have a stake in the activities that make up the business' (Freeman et al, 2010; Phillips et al, 2003; Freeman, 1984). The range of stakeholders may differ between organizations, so does the process of stakeholder management (Donaldson & Preston, 1995), as their interests are to be mitigated in such a way to ensure proper serving of each category (Ogden & Watson, 1999; Mitchell et al 1997).

Although – to some extent – it is descriptive, stakeholder theory has become very popular in the accounting research. Due to the complex relationship structure which it involves, it contributed to the development of studies concerning non-financial reporting (Hahn & Kühnen, 2013; Tagesson et al, 2009; Cooper & Owen, 2007; Freeman, 2004; Heath & Norman, 2004; Roberts, 1992). This evidence supports our claim that stakeholder engagement (with its entire network connections) was present in the focus of the reporting set from the precursor models (leading to the <IR>). After the emergence of <IR>, it was included as a guiding principle, as the interested parties became increasingly important for report issuers.

The stakeholder theory steadily migrated towards the public sector, as well, with evidence gathering on how this perspective is embedded in these types of organizations (Flak & Dertz, 2005; Freeman, 2004; Scholl, 2001; Burrit & Welch, 1997), within a broader range of interactions. The stakeholder perspective in the public sector is subject to a slight shift as 'public interest' and the 'public good' need to be accounted by public sector organizations in their operational activities and strategic focus. This provides an incentive of using an intelligible tool (or, otherwise said, a readable outlet) to provide information on how stakeholders are regarded and included in the public sector organizations' plans. Conversely, stakeholders (of all sorts) need to be engaged in the process of developing this tool (both on a guideline issuance process, and on a practical level).

2.2.Conceptual Construct Encompassing Stakeholders within Integrated Reporting

The natural evolution of the reporting system was to a template outline for <IR> which would be based on 'the story of an organization's journey towards reaching its vision', by the <IR> principles, its fundamental concepts, and its content elements. Moreover, <IR> is viewed as a prospect for the reporting parts to be summed up in a single holistic construct, presenting information about the 'web of interactions and implications of financial, social, environmental, and governance-related organizational activities for stakeholders' (Abeysekera, 2013).

Nevertheless, the implementation and use of <IR> have much more complex ramifications within the activity model of an organization and its relationship with stakeholders than simply a mean to provide a more extensive view of the (created, preserved or depleted) value and the business model. Also, <IR> is considered a significant proxy for the overall level of quality of the management (emphasizing the growing interest intangibles and revealing the 'externalities' on the environment and society). 'Integrated thinking' – as a distinct concept – is seen as a mechanism to achieve 'balance between short-term imperatives and ongoing value creation' (Churet & Eccles, 2014).

The concept of integrated reporting, which involves disclosing financial and nonfinancial information about governance mechanisms, performance levels and risk management in a holistic

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manner within the same document, is considered a necessary, forward-looking upgrade of sustainability reporting. In his sense, <IR> guidelines have been argued to provide a ground for meeting information needs of long-term investors (favored to, but not excluding other groups of interested parties), by emphasizing the wider range of social and environmental externalities on the long run within the managerial process of decision-making. Nonetheless, <IR> puts strategic financial and non-financial information at the same level of importance for performance disclosure and stakeholder accountability (Synergiz, 2014).

Ensuring transparency in the reporting process is seen as an emphatic factor leading to the consolidation of public trust. This process reveals the way in which an organization perceives itself and its scope in the social context. Reporting secures the communication of the organization's performance (either good, or bad), but the most important trait is that it commits to the improvement of future performance and is a borderline in the context of accountability for meeting objectives (Halachmi & Greiling, 2016; Krzus, 2011).

Within the Conceptual Framework, the IIRC clearly states within its scope that <IR> is supposed to have provide an explanatory trait on the value creation process and that the report itself should work in the benefit of all stakeholders (among which we encounter local communities, customers, employees, suppliers, business partners, legislators and regulators, as well as policy makers) (IIRC, 2015: 2).

Also, in the body of the Framework, IIRC dedicates a full section (namely, 3C to stakeholder relationships). It provides an argument that stakeholders have an active role in the value creation process. Their perception and information requirements are deemed as significant for the reporting entity (and accounted for when addressing materiality, strategy, risk management and activity implementation). Last, but not least, stakeholder engagement is directly linked to concepts such as accountability and stewardship relationships (given the fact that the ownership of the six capitals does not always belong to the organization, but to interested parties, as well) (IIRC, 2015: 17-18). This argument consolidates the importance of the stakeholder relationships in the context of <IR>.

2.3.Stakeholder engagement – an enabler of public accountability for financial institutions

The emergence (and successful implementation – to this point) of the Integrated Reporting system is proof that organizations are responding to changes in paradigm, accepting the fact that becoming more transparent in relationship with their stakeholders would enable a discharge of accountability. This could work as a powerful motivation and incentive, in particular for organizations which have a broad range of stakeholders.

The relationship with a higher range of stakeholders and the myriad of interactions created within the economic environment of a public sector entity provides justification for a prospective implementation process on a large scale. This research direction has also been emphasized in the case of private sector entities (Morros, 2016; de Villiers et al., 2014; Cheng et al., 2014), intending to reveal the status quo of interested parties engaged in the reporting entity's organizational model. Stakeholders are (or should be) highly prioritized by decisional factors within the activity of entities (especially those who interact with the general public), as they include a multitude of actors involved in public accountability relationships (which are to be discharged by higher transparency levels enabled by <IR>).

We notice that – over time – stakeholders' demands concerning the quality of governing, transparency and accountability of reporting entities which interact with the general public have significantly increased. Hence, <IR> is an instrument able to provide a proper level of insight into how the reporting entity is managed and which are the main sources of information for decision-making, respectively how governing structures are held accountable in connection to their performance levels (KPMG, 2012).

Stakeholder engagement (which is also an essential principle in the <IR> construct) is also viewed as a key accountability mechanism, driving organizations to involve their stakeholders in revealing, understanding and responding to sustainability concerns, but also to issue reports, and provide explanations and answers to stakeholders concerning their actions, decisions and performance (AccountAbility, 2011: p. 6, found in Steyn & de Beer, 2012: p. 61).

The social dimension is also of significant importance as it involves a shift in accountability relationships from a 'vertical' structure to a 'horizontal' one between stakeholders. The interaction and communication processes between instances of public administration and the taxpayers are ensured by intermediate agents. This leads to a better distribution of power and a more balance establishment of relations (Bovens 2005; cited by: Bartocci & Picciaia, 2013: 194). This leads to a 'flattening' and downward enlargement in relations, introducing a horizontal dimension of accountability.

As our research is targeted towards analysing financial institutions, we make a clear distinction between the privately-owned financial institutions (POFI) and state-owned financial institutions (SOFI). One aspect in need of mentioning is that the financial crisis triggered a series of instruments enabled by states to support (or, rather, prevent the fall of) large POFI, such as takeovers and capital injections. Thus, some of them morphed into state-owned entities. In terms of sector membership, state-owned entities (SOEs) are placed at the borderline between public and private sectors, acting as hybrid organizations (Bruton et al, 2015). With regards to their function, they are owned by state agencies or bodies, but they work and are organized by corporate rules (Stan et al, 2014), in the service of the general public. Evidence from the literature is inconclusive (to this point) concerning a unitary terminology and delineation of the SOE concept (Roper & Schoenberger-Orgad, 2011; MacCarthaigh, 2010), but conveys the alignment to theoretical frameworks connected to stewardship and stakeholders.

In this sense, the inference of public accountability and interest shown by the SOEs, deriving from the theoretical underpinnings, provide a layout for these types of entities to mimic the experience from the private sector implementation of <IR> and transpose initial evidence within the public sector. In other words, they act as a cross-sector, as the range of stakeholders is specific to the public sector, but the reporting practice and governance mechanisms are connected to the private sector (Roper & Schoenberger-Orgad, 2011; MacCarthaigh, 2010).

Therefore, accountability holds the spotlight within many studies, but it remains a very complex concept (not yet fully understood). Also, public accountability has been widely debated as the new trends in reporting are reaching the public sector, as well (Grossi & Steccolini, 2015). For <IR>, this is particularly interesting because – regardless of the different levels of complexity, public accountability manifests itself in both private and public sector entities, through their actions. This concept remains a fundamental principle for public sector entities and it will become increasingly important when restructuring the reporting system as it may serve as an instrument of know-how transference for <IR>.

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3. METHODOLOGY

The sample analysed for the present research has been gathered from the IIRC Database for the European zone, as the European Union is undergoing regulations on non-financial information began through the EU Directive 2014/95/EU. A list of 186 organizations has been fulfilled and analysed with the extent to define the sector of activity and the ownership of financial organizations; this operation has been pursued through the employment of Thomson Reuters EIKON. Insurance and bank entities have been merged together, as done by other scholars (Kolk, 2003; Venturelli et al., 2017).

Based on the analysis of the database, the sample is composed by 27 European financial organizations, which are divided in 5 SOFI and 22 POFI.

Table 1. Sample presentation

Country	Total	SOFI	POFI
Austria	1	1	0
France	2	0	2
Italy	6	0	6
Netherlands	7	0	7
Spain	2	0	2
Sweden	3	3	0
UK	1	1	5
Total	27	5	22

Authors' projection, using data are gathered from Thomson Reuters EIKON

Reports required for the analysis has been downloaded directly from the official site of each entity for the year 2016, as it is the last year in which all reports were available; and, as reports are considered for their high credibility (Guthrie & Parker, 1989; Willmshurst & Frost, 2000); despite, companies are hardly disclosing negative aspects of their activities in their reports (Hahn, 2014).

The research method employed for the present study is content analysis, which is 'a research technique for making replicable and valid inferences from texts (or other meaningful matter) to the contexts of their use' (Krippendorff, 1980; p. 18). It 'uses a set of procedures to make valid inferences from text' (Weber, 1990; p. 9), reports are extensively used in corporate disclosure research (Guthrie et al., 2014); the analysis is conducted with the extent to answer questions proposed by Manetti (2011), below exposed in Table 2; moreover, the present study outlines the average number of stakeholder recognized for the two analysed categories in Table 3. We considered the methodology applied by Manetti (2011) as replicable given the use of a framework for another system of reporting (IR) which derives from the conceptual pillars of sustainability.

While, Manetti (2011) exposed the results of the research as the whole sample, without comparing results from nation or industry; the present study compares the obtained results between SOFI and POFI, for the selected industry, as public entities are considered to be more accountable (Cormier & Gordon, 2001; Greiling & Grüb, 2014) the division of organization in the present research aims to understand the involvement of stakeholder in organization and reporting decision. Moreover, to pursue the present research MAXQDA, a software for qualitative analysis, has been employed with the extent to improve the objectivity of this study.

In order to assure credibility and avoid subjectivity the reports have been analysed by all the authors and results have been compared with the extent to provide an objective result of the research, as differences have been discussed and analysed per single case.

4. REZULTATE ȘI DISCUȚII

Results of the analysis presents a favourable situation for SOFI, while POFI appear to be less interested in SE in their reports; the present section unfold with discussion per each point outlining differences among the two categories proposed.

Based on the evidences, SOFI disclosed more information about the degree of stakeholder engagement, representation, involvement, as well as methods and channels of engagement. A shared behaviour among the two categories is the lack of disclosure about difficulties in met SE, as any company recognized difficulties about it.

Table 2. Comparative analysis of results

	SOFI		POFI	
	n°	**%**	**n°**	**%**
1. GENERAL INFORMATION				
1.1. Has a proper section been devoted to the SE in the report?				
Yes	5	100%	14	64%
No	0	0%	8	36%
1.2. Aims and objectives of SE				
- setting or reviewing strategic objectives	0	0%	1	5%
- setting the content of the report (defining what information are relevant)	1	20%	3	14%
- both of the previous elements	3	60%	7	32%
- no reference to the previous elements	1	20%	11	50%
2. DEGREE OF REPRESENTATION OF STAKEHOLDER				
2.1. Have all the stakeholders identified in the report been engaged?				
Yes	5	100%	10	45%
No	0	0%	12	55%
2.2. Among the groups engaged, have representatives been appointed?				
Yes	4	80%	10	45%
No	1	20%	12	55%
3. DEGREE OF STAKEHOLDER INVOLVEMENT				
3.1. Simple consultation, monitoring, and information gathering?				
Yes	5	100%	12	55%
No	0	0%	10	45%
3.2. Direct involvement in the reporting process?				
Yes	3	60%	8	36%
No	2	40%	14	64%
3.3. Proactive role and appointment of representatives in the governing bodies?				
Yes	0	0%	2	9%
No	5	100%	20	91%
3.4. Preventive engagement accomplished in the earlier stages of planning and accounting (information gathering) or stakeholders are addressed to review the final document ready to be released?				
- only preventive	2	40%	8	36%
- only final	0	0%	0	0%

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- both	0	0%	1	5%
- not declared	3	60%	13	59%
3.5. Is there stakeholders' perception on the previous edition of the sustainability report?				
Yes	2	40%	7	32%
No	3	60%	15	68%
first report	0	0%	0	0%
3.6. If so, are stakeholders required to express their opinion on the materiality and reliability of the information displayed?				
Yes	2	40%	8	36%
No	3	60%	14	64%
there is no perception of previous report	0	0%	0	0%
4. ENGAGEMENT CHANNELS AND METHODS				
4.1. Are the channels and methods used to reach the stakeholders identified?				
Yes	5	100%	15	68%
No	0	0%	7	32%
5. ADDITIONAL ELEMENTS				
5.1. Are difficulties met in SE stated?				
Yes	0	0	0	0
No	5	100%	22	100%
5.2. Are the commitment and objectives to report continuous improvement declared?				
Yes	3	60%	7	32%
No	2	40%	15	68%
5.3. Are specific guidelines used in SE?				
Yes	3	60%	8	36%
No	2	40%	14	64%

Sursa: Analysis using the questions and methodology from Manetti (2011)

On average, SOFI appear to be more oriented toward stakeholder than POFI; all SOEs have in their report a section dedicated to SE and 60% of these organizations have relations with stakeholder in order to establish or reviewing strategic objectives and the contents of the report.

Moreover, the difference on the representation of stakeholder in SOFIs' reports demonstrating the high degree of representation of stakeholder compared to POFI; as these organizations do not engage all their identified stakeholder in the reports, just 45% of entities engaged and appointed their stakeholder.

Further, the involvement of stakeholder is higher when SOFI are gathering information and involving stakeholder in the reporting process; but no presence of stakeholder in the governing bodies have been found in SOFI; while for POFI there has been two entities that appointed representative in the governing bodies. Few are the categories where POFIs disclosed more information rather than SOFIs, besides the one already mentioned, one private entity recognized that it engages with stakeholder preventively and after the report has been completed.

While the stakeholder perception from previous reports and the stakeholder's opinion can be considered similarly by the two categories, as both obtained similar results from the analysis.

All SOEs disclosed information about methods and channels used to reach stakeholders; while, just 68% private institutions disclosed their methods.

Additional elements outline the lack of disclosure about difficulties met in SE, as both categories had 0 references; but, again, SOFI, demonstrate more disclosure toward their commitment and objectives and specific guidelines used in SE.

Table 3. Number n° of Stakeholder Recognized

	nr
SOFI	8,50
POFI	5,91

Source: Authors' projection

Nevertheless, the number of stakeholder recognized by SOEs is higher despite these organization operate in the same sector; Table 3 above demonstrates that on average SOFIs recognizes 8.50 stakeholders while POFIs 5.91.

The results we obtained to this point provide a confirmation of the theoretical aspects from the literature claiming that entities belonging to the private sector have more public accountability and a wider range interactions with stakeholders. Moreover, when we address Integrated Reporting, this finding is even more emphatic as stakeholders are evidently prioritized within the entirety of its architecture. Also, higher disclosure levels towards stakeholders from SOFI show that they seek more often discharges in public accountability (which is enabled by the use of public funding within their activity).

On the other hand, some of the POFI – which do not disclose information about their interaction and regard to stakeholders might see some of this aspects as elements of competitive advantage (as their market position and capital structure are more vulnerable than in the case of SOFI).

5. PRELIMINARY CONCLUSIONS AND FUTURE DEVELOPMENTS

The flaws of the financial markets emerged in the wake of the financial crisis lead to a more emphatic consideration for the concept of accountability. As the states got more involved in the markets (mainly, to prevent them from complete failure), we notice a growing distinction between financial institutions (driven through the lens of their ownership).

Also, the public accountability trait manifests itself on all accounts when we discuss about entities which interact with the general public (such is the case of financial institutions). Hence, we have a high regard for stakeholders, as they enable a myriad of interactions with these types of entities. Both SOFI and POFI's accountability towards their interested parties counterparts enable – to some extent – a legitimacy for their actions (in close connection to the respective stakeholder structure). However, the extent to which the legitimacy and accountability differs between the two types of entities is highly debatable. In this sense, to be able to discharge accountability (in this case, to their stakeholders), they are required to provide a high level of disclosure.

Within our research, we analyse the level of this disclosure in comparison between SOFI and POFI which issue integrated reports (which are viewed as outlets with a more 'readable' trait). Our main results show that – overall – SOFI present more information concerning stakeholders than POFI within their integrated reports, especially regarding the principle of engagement, inclusion in governing bodies, technical reporting issues (such as channels of engagement and interaction), but many others as well. When we consider the number of stakeholders considered by the two

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types of entities, we can notice that SOFI have a higher average number of stakeholders then POFI – disclosed in their integrated reports (confirming the claim that the public sector has a more emphatic myriad of interactions with stakeholders than the private sector).

One limitation of our study is that the sample is unbalanced, as we have just five SOFI and twenty-two POFI (making it harder to outline solid patterns for disclosure concerning stakeholders). An increase of the sample is only possible when more SOFI emerge with published integrated reports in the respective <IR> databases. Another limitation is connected to the low comparability in expression of compliance with the <IR> principles, as each reporting entity structures its reports in its own way (due to the fact that the Framework is merely a set of guidelines) and identification of markers using content analysis is not always accurate.

As a future development, we intend to extend and pursue our analysis more in-depth, with a more complex breakdown of the stakeholder structure. Also, to what extent possible, we will attempt to identify new financial institutions to include in our sample and increase the significance of our results so far. Last, but not least, we will attempt to define a set of markers to use within our content analysis of the integrated reports, so that the degree of subjectivity in interpretation is minimized.

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