

UNIVERSITÁ DEGLI STUDI DI MILANO-BICOCCA

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Corporate Social Responsibility in  
Global Diamond Markets

Relatore: Chiar.mo Prof. Silvio M. Brondoni

Tesi di Dottorato di:  
Michal Arkadiusz Bartosiak  
Matricola 709883

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# Corporate Social Responsibility in Global Diamond Markets

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# **1. Preface**

## **1.1. History and Industry overview**

*The international diamond cartel, controlling the extraction side of the industry, is believed to be the most successful and longest-lasting cartel in the history. The industry leader and primary supplier – De Beers, was formed in 1888 by the merger of the companies of Barney Barnato and Cecil Rhodes, by which time the company managed all diamond-extractions in South Africa. Up until recently, it controlled 80% by value of the approximately \$ 5.5 billion world market (Shor; 2005) – the supremacy that generated journalistic parlor games since at least the 1960s (Spar; 2004). As the only two elements of diamond equation are: "control of output" and demand, De Beers, by controlling both supply and demand, ensured that the price of diamonds would remain high and its position of leader untouched (if diamond supply grew too rapidly or too high, the allure of the stones would be damaged and the prices would fall, excess demand, on the other hand, could lead to speculation). Clearly, both sides of the equation are manipulable and manipulated in order to keep diamonds 'rare' and, thus, valuable (Montpelier; 2004). Moreover, by leveraging its single-channel marketing approach, formally introduced in 1935, De Beers managed to control the distribution of the majority of rough gems entering the global market (Shor; 2005).*

*In 2004, rough diamonds reached a record level of \$11.2 billion in global sales, while the diamond jewelry increased by 6 percent to a total of \$65.5 billion in sales worldwide. The same year, De Beers (actually privately owned and managed by Jonathan Oppenheimer, great-grandson of the company's founder) declared \$5.7 billion in sales of rough gems (constituting 48% of the global sales) and reported \$652 million in earnings. Today, 8 countries involved in the diamond mining (Russia, Botswana, South Africa, Canada, Angola, Namibia, Democratic Republic of Congo, and Australia) manage their production in function with expected demand, stockpile excess stones, and sell the body of their rough stones to the Diamond Trading Company (DTC), a De Beers-owned trading organization (Spar; 2004). Such conformity is the effect of over 100 years of*

*careful planning and negotiations, in which the organization has exercised successful efforts to govern the diamond trade and to optimize its long-term prospects. And despite the fact that producing countries have shifted rank over the last 20 years and De Beers has adjusted its operating formula, the industry's structure has barely changed shape (Spar; 2004). Nevertheless, the diamond cartel hasn't been wholly immune to change. In the recent years, the diamond trade as a whole (not only De Beers) had to face politically important events like the fall of apartheid in South Africa and of communism in Russia, horrors occurred in countries like Angola, Sierra Leone, Rwanda, Liberia, DRC and Cote d'Ivoire related to illegal diamonds trade (blood diamonds), as also discovery of new kimberlites' deposits in Soviet Union, Canada and Australia. Resultantly, the sectors' central players – De Beers above all – understood that they had to change the nature of their trade and, thus, also their operational formula, characterized by a greater openness and the sense of social, environmental and economical responsibility.*

*For example, for the first time producers have begun to brand their stones, integrate vertically to break the barriers that have long separated different operators of the value chain, adjust the cooperative structures that tie the sector players, and involve new ones, including the United Nations (UN) and large group of nongovernmental organizations (NGOs), into the game (Spar; 2004). Remarkably, even if these changes have not affected the core dynamic of the global diamond sector, undoubtedly the need of a new operational philosophy has emerged.*

## **2. Introduction – Understanding the Responsibility Concept in Diamond Sector**

*“The mystique of natural diamonds has been built by the industry. One hundred fifty million carats of mined diamonds are produced every year, so they are really not that special if you look at those terms”*

*- Lisa Bissel, CEO of Gemesis Corporation*

For centuries diamonds have been associated with supernatural qualities and as such symbolized power and grace. By appealing to the customers' sentiment, diamonds are considered one of the most luxurious products and historically enjoyed almost global acceptance. For example, De Beers “has designed one of the most unique and successful marketing strategies in history, using a carefully orchestrated marketing program in which all elements send a consistent, integrated message of romance, love, tradition, elegance and value creation” (Bergenstock *et al.*; 2001). But behind the glittery jewels shown off at celebrity gatherings and royal coronations is a definitely unglamorous and secretive business, promoting unjustifiably expensive jewelry and investment diamonds (Kretschmer; 1998), which happen to be used to evade taxes and to finance criminal organizations. Moreover, serious charges of speculation and price manipulation have been issued over years (for instance, in 1994 the United States accused De Beers and General Electric of violating the Sherman Antitrust Act by fixing the price of industrial diamonds; as a consequence the company was prohibited from conducting any activity in the United States) (McAdams *et al.*; 2008).

Lately, however, the customers' awareness and attention to controversial issues, recognition of diamonds' threat to regional and global peace, security and wealth, addressed operators' new behavioral patterns and, more precisely, a well-developed system of extra-legal certainty (Richman; 2009). Nevertheless, it is important to recall Walker and Howard's (2002) claim that generally the public opinion of the mining as a whole is poor and opinion of

gems extraction is influenced more by concerns over environmental and social performance rather than performance in areas like pricing, safety or quality.

Not surprisingly, new responsibility ideology provided a favorable climate in which the conflict diamonds issue could flourish (Bieri *et al.*; 2011). The relationship between blood diamonds and terrorist organizations attracted public's attention, providing further impetus for their international legal regulation (Morton; 2005) and triggering self-regulatory behaviors. More precisely, when the first report put conflict diamonds on the global agenda – 'A Rough Trade' (1998) – by describing De Beers as responsible of buying conflict diamonds from Angola (which constituted a violation of U.N. Security Council Resolution 1173 and of Lusaka Protocol), it became clear that the rules had to be dramatically changed. The challenge was to tackle this complicated and necessary process of change to drag the diamond industry into 21<sup>st</sup> century and guarantee that key issues of concern such as public scrutiny, accountability and ethical consideration would be enhanced. In doing so, the diamond sector embraced and implemented a new governance system - *Kimberley Process Certification Scheme* (KPCS), associated with a perceived decline in violence and representing one of the most interesting recent innovations in conflict prevention. What is particularly intriguing is the ambition of this initiative, that is, its objective to influence the course of war and peace through a multi-stakeholder approach that tries to harness the power of the private sector (Haufler; 2010).

Thus, keeping with new world-cultural model of responsible corporate citizen became necessary to contrast consumer awareness campaigns (i.e. boycotts) designed by NGO's in an effort to recast the symbolism of the diamond industry. While Littlewood (2014) draws upon the idea of a 'resource course' hidden behind the symbolism of the sector, Bieri and Boli (2011), for example, underlined how such symbolic de-legitimization was clearly linked to potential economic consequences ranging from declining sales and falling profits to permanent drop in demand. In other words, only by eliminating eco-political distortions and by attenuating negative effects of conflict diamonds on the society and local economy, the diamond industry could protect its interests, integrity and, more importantly, it's future.

A major concern with respect to the players like De Beers was that they didn't follow their home country's ethical standards while operating in countries, where rebel movements were seeking to undermine local legitimate governments. By operating in contrast with the concept of 'ethical imperialism' described by Buchholtz and Carroll (2008), the industry was shamed by the public agenda for being indirectly responsible for heinous acts - civilians' massacre and mutilation, especially women and children. The Sierra Leone war was particularly vicious, magnifying the moral responsibilities of the diamond sector (Bieri *et al.*; 2011). Interestingly, although De Beers had initially sued some NGOs for disseminating damaging or even false information, the company acknowledged the force of these groups, backed by careful documentation of horrors occurred in countries like Angola, Sierra Leone, Rwanda, Liberia, DRC and Cote d'Ivoire. As the diamond industry leader, De Beers risked serious repercussions on the bottom line, so driving away a damaging 'bottom-up' social movement campaigns was crucial.

On the other hand, other competitors representing Canadian, Australian and Russian diamond industry have capitalized on the symbolic delegitimization of African conflict diamonds (term *blood diamonds* was coined late in the 1990s and popularized in the 2000s) by certifying their gems as 'conflict free' – a process unrelated to the global *Kimberley Process Certification Scheme* (KPCS) designed in 2002 to combat the illicit diamond trade (Schlosser; 2012) and to retain confidence in globally traded diamonds. In recent years, however, a growing body of studies has called into question the political and ethical foundations for branding commodities as 'fair trade' or 'conflict-free', arguing that mainstream policies for promoting global commodity certification have rather reinforced and re-entrenched existing power inequalities that privilege mining multinational corporations and undermine social justice (Goodman; 2004; Schroeder; 2010; Spiegel; 2014). Schlosser (2012), for example, suggests that in promoting ethical consumption, Canadian diamond industry used the conflict-diamonds semiotics and, thus, encouraged what McClintock (1995) called a 'commodity racism' for business purposes.

Nevertheless, KPCS is still considered a major breakthrough in socially responsible diamond value chain supported by an array of partners: United Nations, mining companies, producing countries, importing countries, NGOs, the jewelry trade and rough dealers (Spar; 2006; Spiegel; 2014). It includes a complex certification system, where commitment and full compliance play a fundamental role. More specifically, KP is a global voluntary, industry-based certification scheme wrapped inside an export/import regime that is implemented through domestic legislation in member states (Haufler; 2010). All the individuals handling a diamond – from the miner to the jeweler – embrace ‘system of warranties’, aimed at ensuring the sources’ legitimacy through rough diamonds tracking and preventing those from conflict zones from flocking to legitimate global markets. As specified by Haufler (2010), unlike many similar efforts the Kimberley Process (KP) involves a degree of enforcement through state border control and has enhanced procedures to end the membership of violators.

Interestingly, Spar (2006) raised an intriguing point. Considering that De Beers was a central proponent of Kimberley Process (KP), why, after all, would the company endorse a protester with a vision that was originally oriented at smearing its reputation and image? Why would the firm that prized secrecy welcome a large number of interlopers into its business? Paradoxically, the author suggests that KP revealed itself beneficial for De Beers; “recall that the company has been devoted throughout its history to keeping excess supply off the market and preventing new suppliers from entering the business [...] this is precisely what Kimberley accomplishes”. Neither for Mostovicz et al. (2007) the KP’ success in boosting consumers’ confidence is obvious – “De Beers has been publicly ambivalent about the usefulness of the approaches in reassuring consumers”. On the other hand, as underlined by Haufler (2010), the sanctions imposed by United Nations did not impose sufficient costs on either rebels or government leaders to convince them to negotiate the conflicts’ conclusion, but imposed their harshest burden on ordinary citizens. The public agenda also expressed serious concerns regarding KPCS, after one of the founder members of the Kimberley Process - Ian Smillie representing Partnership Africa Canada (PAC), resigned his position accusing the regulator of failing to



supervise and claiming he could no longer "pretend that failure is success". At the same time, another founder member of KP added: "despite having all tools in place, the Scheme is failing effectively to address issues of non-compliance, smuggling, money laundering and human rights abuses in the world's diamond fields" (see Figure 1).



Fig. 1 Kimberley Process

The creation of the Kimberley Process took a record-breaking 3 years from start to finish and it was propelled forward by the intersection of a number of global norms with hierarchical industry structure and important market incentives (Haufler; 2010). Despite the some critics advanced in years by the public agenda and scholarship, KPCS is credited with a significant increase in the level of legitimate diamonds traded in international markets (it estimates that over 99% of traded diamonds today are conflict-free gems). In other words, there has been a significant decrease in diamonds circulating in illicit transactions, even if smuggling has still remained an issue. We have to remember that, in the moment when the threat of gemstone market collapse was overpowering, KP managed to provide and encouraged standards and guidelines necessary to rebuild the industry following the horrors of the civil

war. In fact, worldwide, there appeared to be increasing consensus on the need of the sector to take action on illicit diamond trade.

The maximum expression of this intent was a creation of World Diamond Council (WDC), whose mandate was to design a new international regime that would address a tracking system for export and import of rough gems and an sector-designed system of warranties and chain-of-custody policies. As recalled in Haufler (2010), in 2001 the industry began to implement a voluntary system of certification and began to establish internal controls in order to prevent conflict stones' purchasing and their distribution. It is true, however, that only with the support of governmental institutions acting as controllers and guarantors, such system could be successful. It required specific rigorous policies that would enforce legitimate diamonds trade through the customs systems and would protect local economies from smuggling and tax evasion effects. Nevertheless, the system showed some inefficiency related to vulnerabilities in the diamond industry, but also related to the product's characteristics.

### ***2.1. Threats and Risks Related to Vulnerabilities in the Diamond Industry***

Yet classical economists - Adam Smith above all - were wondering how come diamonds, despite their little value in use, have such high value in exchange (Smith; 1776; White; 2002). While nature introduces exogeneity on the supply side, determining diamonds characteristics and consequently their value, it may seem that it is the rarity to justify their price and high exchange rates (Scott, Yelowitz; 2009). It is true, however, that the diamonds supply is historically controlled by tight cartel upstream, and as a consequence - so do the price (Epstein, 1979). For years, diamond industry had been forcefully driven by one-supplier choices, de-legitimizing efforts of smaller producers till the late '60's. Since new kimberlites' deposits in Soviet Union, Canada and Australia have been discovered, the overall supply of rough diamonds on the market increased significantly (source: Bain Report, 2011) and De Beers monopoly suffered (see Figure 2).

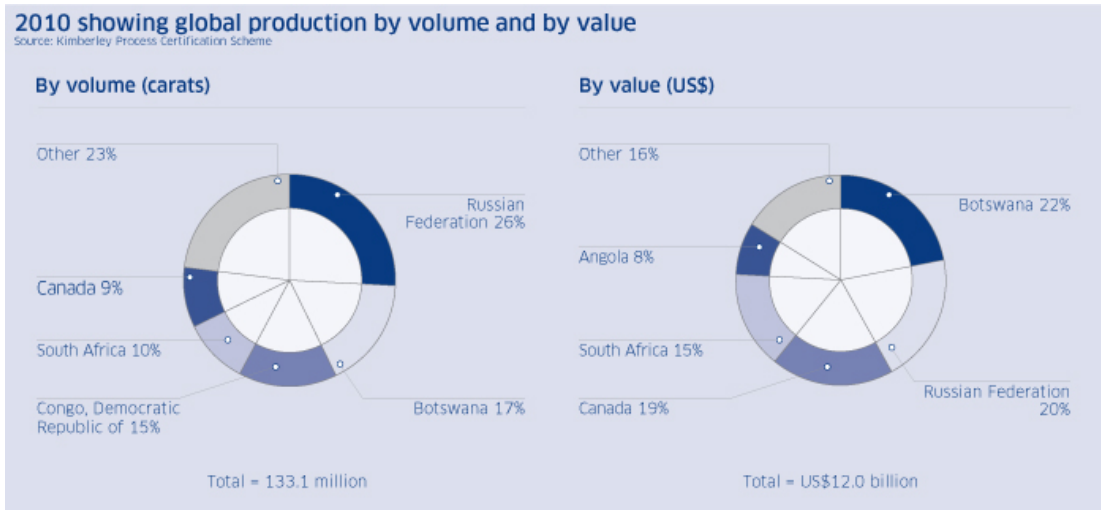


Fig. 2 Global Diamond Production by Volume and Value in 2010

Second, synthetic gems and emergence of new norms regulating the global diamond trade (i.e. *Kimberley Process Scheme* actively promoted by World Federation of Diamond Bourses and by the International Diamond Manufacturers Association) revolutionized the industry and imposed on suppliers a regulatory regime in terms of production, marketing and trade (Shor; 2005).

Third, as the stakeholders' position became stronger, diamond-mining companies had to expand their Performance Measurement Protocols (PMP) over reputation improving environmental and social performance measurements (i.e. protocols developed for tailings management, water and energy use, crisis management planning, external outreach) and self-reporting systems. The proliferation in CSR reports, as evidenced by Porter and Kramer (2006), has been paralleled by increasing role of CSR ratings and rankings.

Nevertheless, in the international debates the ethical outcomes of diamonds' exploitation have been widely criticized by activists, public agenda and even academics, who blamed the industry for much of the violence and bloodshed in Africa (Haufler; 2010), threat of demand-side speculation (Spar; 2006; Renneboog *et al.*; 2012), lack of transparency on the market (Mostovicz *et al.*; 2007), exploitation of workers and the natural environment (Bergensstock *et al.*; 2006), excessive use of power (Claasen *et al.*; 2012) and price manipulations (Gupta *et al.*; 2010). Moreover, as pointed out by the Financial Action Task Force (FATF), diamond trade system is now one of the

main methods by which criminal organizations and terrorist financiers move money in order to disguise its origins and, secondly, to integrate it into the formal economy.

In reference to the latter one, we decide to better address the threats and risks related to vulnerabilities in the international diamonds' transactions by reviewing characteristics, which make the diamonds vulnerable to fraud, speculation, price-manipulations, money laundering and terrorist financing:

- ***Very high value and high durability with stable pricing*** – as diamonds have the ability to earn, move and store value, their reward-to-volatility increases demand from high-net-worth individuals for safe haven investments, especially in times of crisis (Renneboog *et al.*; 2012). In fact, fairly stable price appreciation of tangible but easily storable assets like high-quality, flawless diamonds and, thus, their resilience to economic downturns has already streamed billions of dollars from the financial sector. Underscoring this, with financial institutions refusing to increase their founding of the diamond industry, new sources of cash, like diamond investment funds constitute an opportunity to generate a new capital flows and to reinvigorate the entire diamond pipeline (i.e. pressures to develop new regulations and introduce a greater transparency). On the other hand, however, a very high value increases the asset's vulnerability to mechanisms of money laundering and terrorist financing.
  
- ***Subjected to poor regulatory framework*** – in most countries, credit and financial institutions (if not specialized diamond banks) don't apply specific procedures to diamond dealers (i.e. CDD - Customer Due Diligence) and, thus, rarely put into practice measures of extensive monitoring. It entails that diamond dealers are usually treated as any other customer when providing credit, followed by employees without technical knowledge. Governmental institutions, on the other hand, unwillingly enforce export and import controls as the rough diamonds change hands and are transferred among middle-men, distributors, polishers and retailers. In fact, some member countries struggle with high level of corruption and erratic commitment to the KPCS (i.e. the

certificates from these countries may be dubious, as corrupt officials can be richly compensated for ignoring the source legality).

- ***Difficult Traceability*** - once the items enter the legal market they are extremely difficult to trace, in terms of both their original ownership and value. Moreover, once the gems have gone through the processes of beneficiation and secondly rough gems are cut and polished, it becomes hardly possible to determine or to authenticate the origin of a diamond, since Kimberley Process Certification Scheme (KPCS) originally referred only to rough stones. For this purpose, the World Diamond Council (WDC) has created a System of Warranties endorsed by all KPCS participants (including all buyers and sellers of both rough and polished stones) and aimed at better monitoring of the sourcing system. Additionally, some big industry operators developed two self-regulation procedures – certification and hallmarking – in order to guarantee the quality and source, providing a unique selling proposition that attracts premium prices and to help the companies to add value. In case of small artisanal miners, on the other hand, it is Development Diamond Project (designed by DDI - Diamond Development Initiative) to promote traceability mechanisms and social/environmental standards. In addition to documentation systems and hallmarking, the industry is testing new technologies in order to support chain-of-custody systems and as such, enable physical product to be tracked through mechanisms of radio-frequency identification (RFID), inscription, digital imaging of stones and material fingerprinting. Necessary to say, individual technologies are enablers of the broader chain-of-custody system and do not constitute the system itself.
- ***Ability to go Undetected***– refers to the material properties. Diamonds are non-metallic, odorless and remain difficult to be detected by x-rays.
- ***Subjectivity of the evaluation process*** - there are no official or agreed tariffs for rough or polished stones as their value is a function of four parameters: cut, color, clarity, carat (4 C's). It means that for rough stones there may be thousands of prices as different professional evaluators may provide

reasonably different judgments referred to the same gem. This may enable manipulations in the pricing system, all the more so if we consider that prices directly affect the final tax burden. Furthermore, this may also cause difficulties in investigation procedures since it is complex to establish the price of a diamond where there is no 'one and only' value.

- ***Changeability*** – illegally gained stones may be cut, polished and, consequently, having the hallmark removed (constituted with four compulsory marks containing the following information: who made the article, what is its guaranteed standard of fineness, the Assay Office at which the article was tested and marked, the year in which the article was tested and marked). Logically, it inhibits law enforcement from pursuing criminal charges and authenticating the ownership.
  
- ***Vulnerable on the Retail Level*** – a big challenge for the industry is assuring that precious stones are not mixed or substituted for (cheaper) inferior or even synthetic diamonds. For example, Jewelers Vigilance Committee (JVC) and Responsible Jewelry Council (RJC) assist and educate companies to be compliant with the law in their business practices and promote more strenuous responsible sourcing activity. It is true, however, that standards for diamonds are limited to simple code-of-practices, rather than referred to robust chain-of custody standards like in case of gold and platinum market. In other words, diamond-mining companies should invest more efforts in developing mechanisms of control and stewardship.
  
- ***Record-Keeping Obligations*** (imposed by law and by rough gems' suppliers) for dealers are often limited, due to specific business practices where the gems' trade is based on trust and verbal agreements and, consequently, diamond dealers may not fully record transactions since they know each other. It results in vague and inconsistent records, complicating financial investigations for law enforcement. Interestingly, while a false record is retained illegal, lack of detail is not and, thus, without sufficient detail it becomes difficult to determine the extent of criminal activity. Additionally, lack

of information often stops financial institutions from reporting suspected transaction to institutions like *Financial Intelligence Unit* (FIU).

Once the threats and sources of vulnerabilities in the international diamonds' transactions are cleared, we proceed by analyzing the concept of responsibility in diamond industry from a global company perspective.

## **2.2 Diamond Industry, CSR and Global Markets**

Throughout the last two decades, one of the few congruous themes of marketing theory was the endorsement, espousal and commendation of strategic policies that enhance market orientation (Narver *et al.*; 1990; Harris *et al.*; 2002; Brondoni; 2003; 2012). In fact, aided by seminal developments in both, conceptualization and operationalization, market-driven strategies offered the potential, as stated by Kumar (2000), to “revolutionize an industry and reap vast awards”. In particular, a company is market-oriented when its culture is systematically and entirely committed to the unstoppable adopting of means of boosting value creation in international competitive environments (Zucchella; 2007). In approaching strategic decisions, the requirement of customer orientation has been flanked by the parallel need of orientation on social and environmental issues (Maloni, Brown, 2006). As noticed by Zucchella (2007) “those arise from different motivations: the most important one probably is represented by a growing demand from customers of socially responsible firms and products (demand-pull motivations), even though also some companies have pursued this behavior as a ethical conduct of business (organization-push motivations)”. Logically, also environmental forces had a significant influence, like the pressure of political movements, NGOs, public opinion, regulators, etc.

In this regard, many have suggested that the world of the 21st century faces problems for which *Corporate Social Responsibility* (CSR) is part of the answer (Salvioni; 2003; Buchholtz; 2008; Horrigan; 2010, Idowu *et al.*; 2011). So, it is not surprising that CSR is achieving dominance as a central issue also where monopolistic behaviors have been reported. Specifically, there is a lively

debate about the effects of competitive intensity (i.e. monopoly, oligopoly, perfect competition), as a context in which social and environmental sustainability may translate into competitive advantage and greater profits. For example, McWilliams, Van Fleet and Cory (2002), in attempt to analyze the techniques of resource monopolization, underlined how beneficial for the bottom-line may be gaining control over resources through long-term contracts and differentiation to secure unique reputation as also public acceptance and recognition. Clearly, public relations activities entailing philanthropic endeavors, communities' and NGOs involvement are often used to obtain and maintain good reputation that may consequently translate itself into a greater *social-license-to-operate* (SLO). Therefore, we posit that in today's markets it is easier for the organization to gain control over the resource and raise rivals' costs by investing heavily in CSR activities, constituency building policies and lobbying. In reference to the latter one, it is interesting to notice that in slow-growing industries the firms may lobby for stricter regulations and standards (i.e. De Beers's lobbying for strict rules imposed on the industry by the Kimberley Process), but only to the extent that they can meet them. In other words, the extent to which a firm pursues a lobbying strategy should be equal to the excess of benefits over costs it expects to obtain by implementing more restrictive standards and policies. Furthermore, by increasing their efforts to reshape legal and extra-legal regulations the organizations may empower their positive reputation (Porter *et al.*; 2006), enhance capacity to innovate (Jones *et al.*; 2009), build trust and, more generally, enforce firms' competitive advantage (Salvioni; 2003).

Nevertheless, the trust – 'a fundamental value in effective leadership and social necessity to overcome limitations of rationality' – is not the true purpose of CSR activities, but rather an opportunity to demonstrate the responsibilities that a global company is ready to assume (Mostovicz *et al.*; 2011) in front of increasing moral obligations and expectations of all stakeholders' groups. Parallel to the same rhetoric, the reputation even if retained to act as a fundamental driver to implement CSR and to generate opportunities for innovation within organizations in terms of corporate branding (Vilanova *et al.*; 2009), only partially justifies efforts in CSR activities. From business



perspective, as recalled by Porter and Kramer (2006), to justify firms' investments in CSR is also pursuance to the objectives of sustainability (long-term view) and license-to-operate (micro view) that needs to refer, however, to a coherent strategic framework. It consequently addresses the necessity of a new leadership model applicable to global companies – always more conscious of the ethical imperatives embedded in modern economies.

For example, one of the greatest challenges that global business face operating in different countries is achieving some kind of reconciliation and balance in honoring both the cultural and moral standards of their home and host countries (Buchholtz *et al.*; 2006). In fact, the business ethics is much more complex at the global level than at the domestic level. Such complexity stands in the fact that corporate value systems, standards of ethical behavior, cultures, socioeconomic conditions, forms of government and legal frameworks vary throughout the world. Some diamond mining companies, in fact, have been harshly criticized in the past for operating with divergent ethical standards in different countries, thus giving the idea that they are trying to take advantage of local circumstances (i.e. weak lobbying regulations, opaque norms on the relationship with employees, corruption). Exactly for this reason, there are specific *corporate global codes* (CGC) that individual mining companies have recently developed and applied, often actively supported by several NGOs. Important to say, in addition to individual corporate codes, a number of international organizations have developed their own global codes (i.e. UN Global Compact, Caux Roundtable Principles, Ceres Principles) in hope that the companies will adopt and follow them (Buchholtz *et al.*; 2006). All of this fits within a global CSR framework of corporate responsiveness to governance beyond government, regulation beyond law, and responsibility beyond sanctionability (Horrigan; 2010).

Let's take 'Good Citizenship Principles' developed by Anglo-American and supported by non-profit organizations like Technoserve and International Alert. Its main purpose is to set out the standards that guide the conduct of all the businesses the company is involved in, empowering in this manner corporate governance.

- *“We are committed to supporting the sustainable development of the societies where we work [...] Whilst we operate in many countries and in widely differing conditions, our values and principles have universal application. They apply to every business we manage, to everything we do and to every part of the world in which we operate or procure from. We will ensure that they are properly understood and observed and will review them periodically in the light of experience”*

*Sir. John Parker, Chairman of Anglo-American*

Although the world remains in the early stages of developing a comprehensive global platform for corporate responsibility, governance and sustainability, the international legal community is already taking significant steps in that direction (Horrigan; 2010). Such progress is visible in the nascent development of standards and principles of international legal responsibility, creation of nation-state supervisory obligations and business-related regulations oriented on the enforcement of selected areas of law, which are particularly sensitive to harmful effects of corporate activities (i.e. companies ignoring human rights, polluting mining companies, tax evasion). As suggested by Horrigan (2010), it gains even more power by embracing ‘bottom-up’ approach to international law that offers a framework for better understanding the importance of self-regulatory policies for international legal scheme.

In this sense the *Kimberley Process Certification Scheme* (KPCS) surely contributed to developing mechanisms for subjecting diamond-mining companies to some level of international scrutiny, nevertheless it only partially managed to create solid groundwork for the next level of international CSR architecture for the diamond sector. It is true, however, that despite the absence of a comprehensive international legal framework on corporate responsibility, KP mechanisms sponsored by United Nations are actively being used to scrutinize how well states monitor and remedy off-shore corporate abuses by organizations located within different jurisdictions. More

specifically, single nations are required to submit data on production, import and export of rough diamonds. The risk, however, stays in the fact that actual enforcement efforts regarding diamonds' trade are oriented more on ensuring compliance with the *Kimberley Process Certification Scheme* rather than issues like prevention of smuggling, fraud, or money laundering (i.e. lack of transparency for controlling officers at the border, lack of a universal standard for the format and/or specifications regarding the certifications). Moreover, in some cases the legal enforcement in some jurisdictions is still very low while the State's control over government marketing mechanisms is becoming an important tendency (i.e. Governments of Namibia, Russia, Angola and Botswana control now diamonds marketing channels).

To this point, it is evident that the role of global mining companies is not limited to a simple adherence to existing legal regulations, but also to call for a greater legal enforcement in order to protect the industry as a whole. Throughout the last years, in fact, the diamond-mining companies have developed their value networks in which they operate in concordance with rigorous alliance guidelines. Indeed, a myriad of changes have led to the larger business becoming larger, and the small and medium-size operators are struggling. There are fewer importers, exporters, brokers and wholesalers operating in the diamond sector, while joint ventures and vertically integrated operations are becoming more dominant (Sela; 2003). It's about networks of relationships in which organizations are connected to each other in complex and invisible patterns, offering potential for setting up trust and commitment platforms, which are mandatory for internationalization processes (Rao et al.; 2012).

For example, Alrosa's guidelines 'are based on the highest global business policies, internationally accepted corporate governance standards and key international instruments that regulate ethical principles of business practices, financial transparency, human rights, ensure security, social and economic stability and protection of the environment'. The obligatory adherence to these rules pushes firm's long-term rough diamond-buying and

trading clients to implement sophisticated responsible business practices to ensure the future cooperation.

Another important player – Rio Tinto, has developed a Chain of Warranty Program in conjunction with a particular marketing plan to appeal to consumers' sense of social responsibility (Michelle; 2014). Chain of Warranty (COW) is a mine-of-origin program creating a series of checkpoints in place in order to ensure the tracked transit of the stone throughout the supply chain, that is from the mine to the cutter and jewellery manufacturer and, finally, to the retailer. Rio Tinto provide a proof of a segregated supply chain under the form of COW documentation, certifying the origins of stones used for the jewellery. From the operational perspective, it requires a rigorous tracking system put in place by an independent third party, which is usually a consulting company specialized in supply chain tracking and new tracking technologies (the one developed specifically for Rio Tinto required 18 months of team work). At this point, we underline how important for global mining companies is partnerships development with third parties (i.e. consulting groups, NGOs) and their role in achieving a better social responsibility image and in generating moral legitimacy (Bieri *et al.*; 2011).

To understand a value network, it is necessary to explore how network structures and relationships create value and according to which logic they meet market members' requirements. In this sense, we can speak of *Network Global Codes* – codes of conduct extended over all the actors involved into the value network creation and managed according to the corporate stewardship logic. As recalled by Zucchella (2007) “a value chain shifts the emphasis from the practice of corporate social responsibility to the one of *network social responsibility* (NSR) [...] it means that network partners are progressively aligned to some shared values and corresponding “good practices” of social responsibility”. Thus, assessing what constitutes the success of the network for the benefit of its members as a whole occurs also on ethical basis.

From the operational perspective it entails acting in four areas of commitment to strategic value creation (Herribey; 2011): image challenge

(classical corporate communication; societal challenge and integrated communication; reporting systems), risk management (strategic risk, information risk; regulation risk; crisis management), governance challenge (employee engagement; high quality connections; creative engagement), competitiveness challenge (cost economy; market opportunities; competitive advantage). Managing successfully four areas translates into better evaluation of all risks that the company must be able to appreciate in order to anticipate crises and estimate potential negative impacts on its activity. Clearly, such risks are usually related to the firms' incapacity to embed biocentric (environmental) and anthropocentric (socio-cultural) into corporate governance, while concentrating on purely plutocentric (economic) type of values (Ketola; 2005; 2008). As a continuation of the risk to reputation, a lack of communication about the recognized impact of the company's activity on its social environment and nor about eventual corrective, compensatory actions may have negative reputational effects.

Remarkably, there is nothing more precious for the diamond industry than the reputation. Sentimental values that people place on diamonds origin a fundamental challenge for the industry: as the underlying demand is deeply rooted in sentiment and reputation, ethical outcomes of sector's activity could theoretically undermine the prices stability and, thus, bring about dangerous price fluctuations. Furthermore, especially in case of small stones the potential for permanent substitution is particularly high as other precious gems like rubies or emeralds, make perfectly good jewellery. Thus, we posit that in hypothesis of equal price, the customer will choose the stone that better addresses not only his personal taste but also his sentimental values. In this sense, by controlling reputational outcomes of its activity and by implementing sophisticated leverages of marketing (i.e. branded diamonds like De Beers's Forevermark), the organization may mobilize ethical consumption discourse and successfully differentiate from its competitors, constituting what Sela and Hennig (2003) called 'an antidote to commodity value destruction for polished diamonds'.

For example, Schlosser (2012) noticed how Canadian diamond industry depicted 'white, pristine and peaceful' northern landscapes of Canada in juxtaposition to 'violent African blood diamonds' in order to construct what Appadurai (1986) calls a "regime of value" (Appudarai argues that the value is not directly inherent in commodities but rather results from the act of exchange). Paraphrasing Goodman (2004), the material-semiotic story of commodity networks is changing between structures and meanings of 'ethical consumption' markets, where the commodity 'ethicalization' became a part of competitive strategy.

The literature on responsibility and ethical outcomes (Aguilera *et al.*; 2007, Rao *et al.*; 2008; Claasen *et al.*; 2012) investigated also on their contribution to legitimacy and social license-to-operate (SLO). The question is, thus, whether more ethical behaviour has positive effects on company's reputation and legitimacy. Generally, in the scholarship seems to prevail the belief that engagement in Corporate Social Responsibility (CSR) positively influences a firm's reputation, protects its license-to-operate, contributes to its legitimacy (Claasen *et al.*; 2012) and encourages a multistakeholder dialogue approach (Bieri *et al.*; 2012). Similarly, generating awareness and promoting collaborative platforms with stakeholders and interested parties, translates into major social acceptance and greater transparency on the market. Nevertheless, the diamond mining companies have been largely criticized for not doing enough to increase the confidence inside and outside the industry. As a reaction, World Jewellery Confederation (CIBJO) and World Diamond Mark (WDM) – both representing jewellery producers and retailers – launched their own programs in order to "increase the confidence [...] and ensure the health and future growth of the diamond and jewellery industry in the luxury market sector". The future challenge for the industry is, thus, establishing a better dialogue between mining companies, cutters, jewellery producers and retailers through an integrated industry stewardship plan.

### **2.3 Managerial Implications: De Beers**

It has already been underlined how global diamond companies fail to report their activities in terms of social and environmental investments. Thus, it becomes extremely complex to evaluate those efforts, as the information deficit is evident. Moreover, since the architecture of CSR activity systems is not a standardized process but rather a tailor-made 'creature' (designed in function of widely conceived vision, mission and strategic policies), it is difficult to generalize the sector's approach towards sustainability only by analyzing few companies. To be of value, our research progress from being descriptive to being explanatory, ranging from large companies' evaluation to small and medium-sized companies' one.

The basic assumption of this dissertation (supported by quantitative research illustrated in the chapter 4) is that there is a significant attitudinal gap between small/medium and large organizations. Clearly, the extent to which small companies contribute to local economies, social development and environmental protection is deeply rooted in their finances. Nevertheless, the important point is that those organizations don't follow any guidelines or specific strategy, but rather limit themselves to ad-hoc initiatives and occasional philanthropic giving. At this point no CSR innovation is contemplated and any spending on CSR is seen more as a cost than as an investment. Conversely, larger organizations are more successful in addressing social needs and expectations with means of innovative social and environmental programs. In other words, the grade of responsiveness is greater together with general attitude towards CSR innovativeness.

Large companies like De Beers, despite numerous critics that triggered the erosion of support from different domains of social interactions, seem to acknowledge the strategic dimension of CSR and move towards highly articulated CSR activity system's architecture. Additionally, media exposure and high level of controversy embedded in the industry push large businesses beyond traditional sustainable development rhetoric towards more innovative solutions. First of all, it is evident how in the recent years the reporting (i.e.

SA8000) and self-regulatory systems have evolved. Since the global crisis has peaked in 2008, large diamond companies became more active in leveraging their sustainability policies to 'win the game' in struggling economies (just think about 'ethical' Canadian diamonds), where the diamond as an item begun to have its (not necessarily cheaper) substitutes. Also a significant erosion of trust in the industry has been reported since in the early 2000's the 'blood diamonds' scandal has broken out. Therefore, it became clear that better reporting and self-regulation systems (introduced on both voluntary and obligatory basis) were a necessary step towards a greater transparency in the sector and future stewardship establishment in the industry.

Despite some conspiracy theories raised by its opponents, first step of De Beers was becoming a central proponent of Kimberley Process (2003). Considered a major breakthrough in socially responsible diamond value chain, KP revealed beneficial for De Beers even if the vision endorsed by the protesters was originally oriented at smearing its reputation and image (Spar; 2006). The company's strategy was thus based on the active participation in processes of enforcement of KP policies and of complex certification systems in order to convince the public opinion about its 'good will'. Pure PR strategy or not, the importance of De Beers in establishing new rules in the sector is undeniable. Since then the company has actively promoted the System of Warranties designed by the World Diamond Council (WDC) that has been endorsed by all KPCS participants. Resultantly, De Beers started requiring that it's each and every supplier operates within KPCS, which necessitates that, a written guarantee accompanies every stone to certify that its is not from illegitimate sources. Moreover, stringent procedures of protection have been introduced by De Beers (i.e. stones are microscopically branded with logo, unique diamond number which is logged in the De Beers Register of Diamonds and sold with unique, counterfeit-proof certificate of authenticity) in order to fight not only with so-called 'blood diamonds' but also with synthetic gems sold as natural stones.

Also rules for authorized bulk purchasers of rough diamonds (so-called 'sightholders' and other accredited buyers) have changed. A full compliance



with Best Practice Principles (BPP) is now required in order to “provide evidence to supply chain partners, consumers and other interested stakeholders that the exploration, extraction, sorting, cutting and polishing of Diamonds, and the manufacture and sale of Diamond jewellery by entities that are owned or controlled by the De Beers Group of Companies or by Sightholders and or De Beers Accredited Buyers, are undertaken in a professional, ethical and environmentally friendly and accountable way” (source: De Beers Group). The BPP Assurance Programme embraces a managerial system and a set of evaluation tools that constantly and systematically provide means of checking compliance with requirements related to anti-bribery, anti-money laundering, terrorism financing activities and, more generally, with KPCS principles. Thus, compliance with Best Practice Principles (BPP) became an integral part of all firms’ contractual arrangements and as such may constitute a breach of contracting entitling the company to suspend and/or terminate rough diamonds supply to contractor who acts in contrast with BPP Assurance Programme or who doesn’t ensure that also its business partners comply with BPP Programme.

Specifically, adherence to BPP Assurance Programme comprises a framework for the electronically submitted self-assessment as also for the independent on-site verifications made on annual basis (De Beers provides assurance as to independence and quality of its verifiers). In reference to the first one, non-submission or submission of false information on the self-assessment workbook may result in sanctions against the defaulting organization, including termination of contract. When it comes to the independent verifier, the entity must prove itself to be independent to De Beers and other entities subject to BPP Programme (in ensuring it, De Beers periodically requires an independent review process in order to confirm the verifier’s independence). In addition, the verifier can’t be involved in projecting the assurance program and nor in undertaking any particular training linked to BPP Programme. During the inspection the verifier examines company records, facilitation payments registers, policies, procedures, and, where applicable, company’s compliance with internationally recognized

standards (i.e. certifications ISO14001, SA8000, OHSAS18001). Finally, evidence of best endeavours (letters, minutes from meetings and trainings) gets checked.

De Beers introduced a set of generic policies that help their contractors to better respond to BPP requirements and promote more proactive behaviors among its sightholders/accredited buyers. Naturally, these policies are suggestions only (i.e. suggestions on general guidelines, monitoring system implementation, awareness building mechanisms) whereas the elements that address actual BPP are mandatory and constitute a core commitment to the Assurance Programme. For example, some suggestions regard the way the management systems are being designed; De Beers encourages its contractors to integrate business, social and environmental issues into decision-making processes and risk-review processes, fostering an awareness of shared responsibility and accountability. Importantly, those key-points addressing 'responsibility policies' are continuously encouraged to support national laws and regulations which are often subject to low or no set standards. For example, where the anti-bribery and anti-money laundering regulations are poor, De Beers' recommendations and requirements may reveal crucial for a greater transparency on the market.

From the organizational perspective, De Beers covers the costs related to primary Best Practice Principles (BPP) Assurance Programme development, investigation of any reported material violation of the Agreement, annual monitoring of self-assessment workbooks, annual independent verification of up to 10% of assessable entities. Conversely, both sightholders and accredited buyers are expected to cover the costs related to the annual self-assessment activity, any kind of consultancy linked to self-assessment, any independent verification requested by De Beers Group Company, any corrective activities necessary in hypothesis of non-compliance with BPP, any repeated independent verification required by De Beers, further downstream training at the corporate level, statements carried out by a properly qualified auditor to international accounting standards.

Also through diamond-branding strategies (Forevermark initiative first launched in 2008) De Beers carries a promise of a responsibly sourced gem, “originated at a carefully selected mine that benefits people, community and countries” (source: De Beers). To accomplish that, De Beers work together with SGS – a Geneva-based global certification and auditing firm, on subjecting its suppliers to periodic reviews and spontaneous audits to guarantee strict adherence to firm’s standards. A nicely architected marketing campaign enabled the Company to successfully sell its first branded diamonds (with unique identification number, certificate and the Forevermark icon inscribed) and thus distinguish themselves from their competitors. In fact, as from the demand side there is more attention to the responsibly sourced gems (so-called ‘ethical diamonds’), the companies extended their control of the source over the way the mine is actually managed (spillover analysis). In fact, the consumers seem to be more demanding for products that create value not only for them as consumers, but also for local communities (i.e. infrastructure, education, health system) and environment (i.e. water consumption, tailings management, lowering CO2 emissions, hazardous materials management). Specifically, De Beer’s community objective is to ‘secure and to maintain social license to operate from local communities for all its operations and activities, based on the principles of informed consent and mutual benefit’.

The reputational benefits of compliance with environmental management systems standards (i.e. ISO 14001, Greenhouse Gas Protocols) encouraged De Beers to develop necessary skills and to implement guidelines for the stewardship of environmental resources. It is therefore about responsibly managing national assets and working systematically across the diamond value chain in order to prevent/reduce the negative impacts of the firm’s operations. It also translates into a proactive response to stakeholders’ claims by investing in innovative solutions for environmental stewardship (i.e. energy and climate care programmes, water management technologies, research on biodiversity, conservation projects). For example, EPRA – Environmental Performance Reporting Application, is used for rigorous collection of strategic environmental data. EPRA facilitates data capture of the

firm's environmental indicators on a monthly basis, which enables a systematic analysis and verification of both current and past information. It also helps the company to measure its performance against stakeholder engagements and issues and assess the environmental impact of mining projects (Van Wyk's et al.; 2009) using criteria developed for the Dow Jones Sustainability Index for sustainability benchmarking. All the data is processed by De Beers' Environmental Peer Group – the environmental leadership team whose input serves for recommendations to the De Beers Environment, Community, Health and Safety Committee (ECoHS) and to the Executive Committee. The basic idea is to guarantee a direct line of communication to the firm's board of directors as also with NGOs and national institutions (i.e. De Beers has a partnership with WWF and SANBI – the South African National Biodiversity Institute, in order to develop a network for the conservation for South Africa's offshore biodiversity).

Social and environmental data evaluation by ECoHS leads to a suite of guidelines to support decision-making processes across the diamond value chain; the guidelines are consistent with international best practice, including the Good Practice Guidance for Biodiversity and Mining designed by the International Council of Mining and Metals (ICMM). For example, the Exploration ECoHS Guideline is used by the exploration staff in managing environmental, health and safety, community issues and provides suggestions on a range of issues like camp planning and management, negotiating access to land or exit strategies. On the other hand, the Projects Environmental and Social Guideline provides necessary information towards more efficient guidance on environment and community. More specifically, De Beers' community strategy (coordinated by the Group Community Relations Manager and delivered by community relations practitioners) is subject to regular evaluations and its overall impact on the local communities is assessed (Social Impact Assessment). At the Group level, the long-standing approach to community management is aligned with Anglo American's 'Social Way Management Framework' – a set of 24 criteria to be met by the group's

members and assessed every three years by SEAT – Socio-Economic Assessment Toolbox.

A core-element of SEAT are activities that actively engage local stakeholders and are less formal however, than IBAs or SLPs. SEAT regard activities of engagement laid out in each operation’s annual stakeholder engagement plan. Where possible, De Beers aligns its social investments with national, regional and local development programmes. On the other hand, some of De Beers’ community engagement operations and social investments (SI) are governed by formal regulatory agreements with local communities and authorities (i.e. Impact Benefit Agreements in Canada; Social and Labour Plans in South Africa). Specifically, IBAs are formal contracts that outline the impacts of the project and specify commitments and responsibilities of both parties.

### **3. Innovative CSR: from Risk Management to Value Creation**

*“In the last few years, companies have begun to move beyond traditional philanthropy and basic compliance into a new kind of corporate and social responsibility”*

*Jane Nelson, Director of the CSR Initiative,  
Harvard Kennedy School of Government*

#### **3.1 Introduction to Sustainability**

Sustainable development (SD), broadly explained, encompasses firms' desire to simultaneously sustain, enhance and promote environmental, societal and economic dimensions of corporate workability. In practice, however, striving towards sustainability in all these areas may trigger conflicts, mismanagements, wrong evaluations or even bad investments, making the corporate stability shatter (Lélé; 1991; Eggert; 2000). In fact, the conceptual shift from 'eco-developmental paradigm' (Lélé; 1991) or 'eco-modernism' (Hajer; 1995) to more complex and rigorous framework (breaking definitively with neoclassical view of a firm as a closed system only concerned about its shareholders), led to the studies on tools measuring sustainable development (SDI's – sustainable development indicators), often coordinated by supra-national bodies (ex. UNEAP).

Historically, the first benchmark definition was given by the Brundtland report (1987), but since then no method of measuring SD has gained a similar globally widespread level of support and consensus (Mitchell; 1996; Corniani; 2014). Considerable effort is currently made by systems of supranational institutions, national governments, non-governmental institutions (NGO's), but also – by the companies themselves. In fact, while SD policies come from governments and often imply some sort of regulatory force, management systems (ex. ISO 14001, SA 8000) are applied more or less voluntarily by a company's management (Steurer *et al*; 2005) and actively integrated with

corporate strategies (Sharma, Vredenburg; 1998; Hoffman; 1999; Bansal; 2005; Brondoni; 2014; Lambin; 2014). Furthermore, substantial advances in managerial sciences have proven the important role of 'management systems' in value and competitive advantage generating, as also in improving the reputation. Nevertheless, some researchers argue that the concept of *Sustainable Development* and consequently its measurement are useless (Beckerman; 1995) and notice that '*sustainable growth*' is an oxymoron, diverting attention from imminent environmental limits to economic growth (Daly; 1996).

Generally speaking, *Sustainable Development* is by its very nature a 'corporate-centric' concept in the sense that it deals with how firms interact with stakeholders in order to secure important resources provided by them and to them (Welford; 1997; Frooman; 1999). In other words, SD is seen more as a tool rather than as an end state. In fact, corporations are still being accused (mostly by NGO's) of perusing the issue of sustainability with unclear strategies and rather opportunistic behavior, often in concordance with political agenda (i.e. putting human and economical development at the center; lack of regulations; corruption). It may happen, however, that a company gets involved indirectly in political affairs, appearing to be responsible for internal conflicts. For instance, oil companies operating in Angola addressed huge payments (so-called 'signature revenues'), to the local Government, much of which served to finance their war against 'Unita' - the rebel opposition. Whereas, the diamond industry, operating in the territory controlled by Unita, channeled payments to Unita in contravention of a United Nations' embargo on the sale of diamonds from Angola. Interestingly, all these companies claimed in their annual reports to be politically neutral.

In general, studies of the communication of corporate ethics have pointed how the oil and mining companies fail to tackle the fundamental issues of sustainability by providing poor or no information regarding their socially responsible investing (SRI), its environmental footprint or even their plan how to generate 'win-win situations' (Clarke, Gibson-Sweet; 2002). As the following study (Table 1) shows, only 25% of the biggest diamonds producers actually acknowledge the disclosures' performative function in generating major public

trust, activities' legitimization and in establishing a new type of competitive advantage source. It is not the objective of this paper, however, to analyze this finding, but rather to highlight the problem of poor self-reporting policies in the diamond industry as also their defensive character.

In fact, a first premise for this study is that although companies are accustomed to setting up compliance mechanisms in relation to a whole raft of regulatory requirements (i.e. laws regulating gas emissions or minimum wage), there are aspects of *Corporate Social Responsibility* (CSR) that still lack a compliance framework (i.e. regulations on social investments, philanthropy, involvement in politics). It can be claimed, that this regulatory function was assumed by voluntary codes of conduct, measured by inter-corporate evaluations and reported by non-financial disclosures. According to Frankental (2001), 'an indicator of the real value that companies attach to CSR is where they locate this function within the organizational structure'. On the other hand, some authors suggest that the extent to which the regulatory function is perceived and reported varies among the countries, national cultures (Dore; 2000; Maignan *et al.*; 2002; Aguilera *et al.*; 2003; Van der Laan Smith *et al.*; 2005; Oriij; 2010), industries (Cooke; 1992) and times (Campbell; 2007).

A second premise for this paper is that regulatory tools should be constantly redefined to serve changing needs of the society and the sector. In order to capture this dynamicity, some organizations started applying algorithmic principles to make constant adjustments to their business models, strategies and structures, bringing together capabilities and assets to create advantageous positions (Reeves *et al.*; 2015). From CSR perspective, it entails deploying a nested set of strategic processes (i.e. new social/environmental investment strategies, strict rules of conduct, new corporate culture, business models' modifications, coordinated CSR programs), to which the organization gives more visibility and transparency, engaging, for example, NGO's into social/environmental investments' evaluation. Consequently, we postulate that building organizational capacity to invest the time and the energy to explore sustainability trends and emerging issues (Laszlo; 2008; Brondoni; 2014; Lambin; 2014) may anticipate future expectations (ex. new legislations



affecting the industry, consumers' preferences) and, at the business level, move CSR from reactive to a proactive dimension.

**Table 1. Disclosure Policies in the Diamond Industry**

Company	Ownership Structure	Annual Sustainability Report	GRI disclosure	Environmental and Societal Impact Reported?
BHP Billiton	private	✓	✓	✓
Alrosa	state-owned	✓	✓	✓
Rio Tinto	private	✓	✓	✓
De Beers	private	✓	✓	✓
Petra Diamonds	private	✓	✓	✓
Lucara	private	✓	✓	✓
Diamcor	private	✗	✗	✗
Endiama	state-owned	✗	✗	✗
DDC	private	✓	✓	✓
Firestone Diamonds	private / state - owned	✗	✗	✗
Botswana Diamonds	private / state - owned	✗	✗	✗
Kimberley diamonds	private	✗	✗	✗
Gem Diamonds	private	✓	✓	✓
Alexkor	state-owned	✗	✗	✓
Rockwell Diamonds	private	✗	✗	✗
Lucapa Diamond Co.	private	✗	✗	✗
Peregrine Diamonds	private	✗	✗	✗
Kennady Diamonds Inc.	private	✗	✗	✗
North Arrow Minerals	private	✗	✗	✗
Mwana	private	✗	✗	✗
Mountain Province Diamonds	private	✗	✗	✗
Stornoway Diamond Corp.	private	✓	✗	✓
Archon Minerals	private	✗	✗	✗
True North Gems	private	✗	✗	✗
Lonrho Mining	private	✗	✗	✗
Paragon Diamonds	private	✗	✗	✗
Tsodilo Resources	private	✗	✗	✗
Global Diamond Resources	private	✗	✗	✗
Trans Hex	private	✗	✗	✓
Merlin Diamonds	private	✗	✗	✗
Octea Diamond Group (BSG)	private	✗	✗	✗
Zimbabwe Mining Development Corp.	state-owned	✗	✗	✗
Pangolin Diamonds Corp.	private	✗	✗	✗
Letseng Diamonds	private / state - owned	✗	✗	✓
Stellar Diamonds	private	✗	✗	✗
DiamondCorp PLC	private	✗	✗	✗

A third premise for this paper is that defining the value proposition for stakeholders is a starting point for the organizations' value creation architecture and the very first step in creating complex exchange relations with actors operating along the supply chain. Generally, the complexity of these relations stands in the network component (Brondoni; 2014; Corniani; 2014), strategic alliance system, new ethical investments' patterns as also in the product stewardship concept. On the flipside, the overly frequent use of mediated power (Boyle *et al.*; 1992), excessive information asymmetries and lack of transparency may damage normative commitment between the parties

and cause increased channel conflict (Brown *et al.*; 1995) with immediate negative effects on the value creation process.

As the recent studies show (Baumann-Pauly *et al.*; 2013; Rangan; 2015), many large and medium size companies are hampered by poor coordination and a lack of logic connecting their CSR programs with core-business functions, even if they are proved to possess several traits enhancing an effective communication and reporting practices. In this paper we critically analyze the corporate perceptions of CSR lingering in the diamond industry, highlighting how the concept of ‘responsibility’ is no longer only of the manufacturers’ domain. We particularly focus on the explicit efforts of some companies to transit from ‘defensive’ to ‘pro-active’ CSR strategy, summarizing these efforts and attempts with a conceptual framework (*Pro-Active CSR Model*). This model, not only explores new managerial CSR strategies, but also reflects on the inefficiencies and self-regulation concerns of the upstream players.

The study contributes to the understanding of the *Corporate Social Responsibility* in the mining industry in multiple ways. First, it provides an interesting insight into the industry, which till the late 60’s had been forcefully driven by one-supplier choices, de-legitimizing efforts of smaller producers. Secondly, it provides in-depth empirical evidence of the current implementation status of CSR in the diamond industry, highlighting the problem of poor reporting practices and historically ‘defensive’ character of its communication patterns. Thirdly, with means of a new conceptual framework (*Pro-Active CSR Model*), calls the businesses to provide extensive commitments to CSR, recognizing its competitive dimension and its role as a differentiation factor.

### **3.2. Corporate Sustainability as a Competitive Advantage**

Since 1987, when the United Nations’ report “Our Common Future” (so-called ‘Brundtland Report’) gave the most cited definition of Sustainable Development (“Development that meets the needs of current generations

without compromising the ability of future generations to meet their needs and aspirations”), the conceptual boundaries of the term have been significantly expanded. Regarding its thematic breadth, the sustainability agenda, by definition, addresses the implications of ecological dependency and planetary wide social impacts of economic behaviors (Moon; 2007). While some authors discussed the importance of internalization of the environmental concerns into governance practices (Robinson; 2004; Redclift; 2005), the literature seem to suggest that even if initially economic and social issues were addressed only as far as they were perceived to be relevant for environmental concerns, they evolved with time into equally important dimensions of *Sustainable Development* (Steurer *et al*; 2005). Thus, the former view suggests a balance between those three pillars of SD, pointing to ‘win-win-win’ solutions for the society, environment and businesses (Elkington; 1994; Backer *et al*; 2008).

Although in the 80’s some scholars claimed that SD is an ‘intellectual oxymoron’ (O’Riordan; 1985; Redclift; 1987), the concept of sustainability gained a lot of attention in the literature, giving an interesting insight into traditional concepts of the stakeholder theory, legitimacy theory and finally – to the agency theory. In fact, the conceptual extension of Freeman’s theory (1984), according to Steurer (2005), addresses more complex business-society relations established in post-Keynesian age and regulated by ‘second-order requirements’ of transparency, participation, reflectivity, integration and intergenerational equity. From a transaction costs economics perspective, leveraging these principles in answer to duties imposed by highly formalized compliance mechanisms (i.e. governmental institutions’ regulations, supra-national regulations and inter-sectorial agreements like *Mining and Mineral Sustainable Development Project*) and, less formalized, self-regulation mechanisms (i.e. corporate policies, management systems) may result into lower transaction costs and greater competitive advantage.

In concert with the idea that SD is extremely ‘corporate centric’ (Welford; 1997; Frooman; 1999), Porter and Kramer (2006) claim that it’s all about ‘pragmatism’ – the organizations make decisions in respect to the issues (societal, environmental, financial, legal) that matter to their stakeholders in

order to foster constructive dialogue with regulators, local citizenry and activists, whose consent is vital for the corporate existence (*license-to-operate* approach). If corporations lack the ability to establish such relationship with stakeholders, it may result in the company's alienation from the rest of society, reduced reputation, decreasing shareholder value triggered by the erosion of its license to operate (Steurer *et al.*; 2005; Hill; 2001). Sustainable development (SD) is, thus, defined not by ecological parameters but with the means of societal consensus-finding processes (*Social license-to-operate*) (Reid; 1995; Steurer *et al.*; 2005). In the mining business, for example, where the extraction projects have not satisfied the demands of civil society, shutdowns and slow-ups have been frequent (Prno *et al.*; 2011), even if (unfortunately) it is not always a rule (see Hines, Snow; 2007). Moreover, in case of mining multinational corporations (MMNC's), the reputational struggles in one business, caused problems with other businesses where the extraction companies were involved (ex. scandals regarding the diamond extraction have affected negatively the reputation of some companies operating also in coal, aluminum or iron industry).

For Waddock and Graves (1997), the companies, which were initially involved in posturing behaviors, discovered over time to have actually institutionalized cultural or strategic changes in what Mintzberg (1987) calls 'emergent strategy' (see also Brondoni; 2014). Specifically, recent scholarship in strategic management (in clear contrast with neoclassical mainstream) suggests that emerging influences on strategic decision-making are the result of a new conceptualization of the role of business in society and of how the relations between both are managed (Freeman; 1989; Gladwin *et al.*; 1995; Bansal; 2002; Moon; 2007). At the same time, the transformation of investment regimes and patterns of investment flows led to incremental improvements in processes' control and optimization, with a continuous monitoring of firms' ethical outcomes (*Integrated Sustainability Assessment*). In this sense, corporate social responsibility (CSR) provides an effective vehicle for the contemporary notion of SD (that is, going beyond the tripartite core of economic, social and environmental issues). Said differently, while SD is

acknowledged to be a normative societal concept<sup>1</sup>, CSR represents organizations' voluntary contribution (management approach) to better address stakeholders' claims.

Evidence suggests, however, that many companies struggle with transforming corporate commitment to sustainable development into operational reality. The diamond industry, for instance, was accused in the past of marginalizing issues of safety on micro and macro-level that led to illegal trading and smuggling procedures. This also contributed to an exclusionary form of capitalism, where certain classes of small-scale producers were systematically excluded due to national 'securitization' processes (Spiegel; 2014) while the industry was forcefully driven by one-supplier choices.

This specific concern, regarding the unclear relation between the companies and governments, has attracted increasing interest of scholars (Eggert; 2000; Jenkins; 2004; Shor; 2005; Kemp; 2010; Littlewood; 2013), fostering a debate about the patterns of avoiding taxations and royalty payments and, consequently, questioning industry's ethical outcomes. Bracking and Sharife (2014), in pursuit of investigating the contribution of diamond mining to the economic development of South Africa, analyzed volumes and values of exported and imported diamonds. Given the fact that value of sales (and thus the pricing system) predetermines the rate of tax paid, the authors posit that import / export price manipulation caused an import value inflation of USD 3,9 billion for the years 2004 - 2012. Accordingly, they claim that some companies externalize the price difference to another subsidiaries in a different (lower) tax jurisdiction like Botswana, taking advantage of weak legal framework in South Africa. Necessary to say, the valuation exploitation occurs more often in case of diamond parcels rather than single gems.

To avoid such situations, in Israel, for example, all rough diamonds imported to or exported from the country are examined and evaluated with the objective of collecting due taxes and receiving proper documentation by a

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<sup>1</sup> Its meaning is determined through societal consensus finding processes and, thus, it strongly relies on the concepts of participation, integration and transparency (see Steurer et al.; 2005; Moon; 2007; Ebner et al.; 2006)

special diamonds customs stations located within the diamond exchange and operated by gem specialists. Similarly, in Belgium and in Russia every shipment is checked, verified and assessed by sworn experts and subjected to the government inspection. Generally, however, in the most of the jurisdictions there are no specific import / export customs controls, which facilitates tax evasion and diamonds' under-grading procedures not only by the mining companies but also by cutters, polishers and retailers. Moreover, in some countries (i.e. Switzerland) there is no legislation for declaration requirements regarding cross-border transportation of currency related to the diamonds' trade, which may potentially facilitate criminal phenomenon of money laundering and putting 'conflict diamonds' into circulation. For example, in 2014 Swiss bank headquartered in Geneva – HSBC, was accused by public agenda of low standard of due diligence by holding some high-risk accounts named in connection with illicit diamond trading activities ('blood diamonds').

Thus, it becomes evident, that lack of global and uniform legal framework (i.e. weak national and international regulations, lack of record-keeping obligations and reporting responsibilities in most of jurisdictions, lack of license and registration requirements for business activity in the diamond trade, poor guidelines for monitoring the import/export of diamonds by the Customs Departments) is damaging the Kimberley Process Certification Scheme's (KPCS)<sup>2</sup> effectiveness. The risk states in the fact, that current enforcement efforts (i.e. System of Warranties created by the World Diamond Council) are directed more at ensuring to block 'blood diamonds' rather than preventing money laundering, smuggling or frauds. Interestingly, also some companies still tend to control more the source of the gem rather than the legality of its use across the 'diamond pipeline'. Nevertheless, in the recent years, an important commitment by the sector's players has been formalized with the means of detailed guidelines, manuals, standards and network-regulation rules. For example, Rio Tinto set up a *Business Integrity Standard*, which defines responsibilities, requirements and behavioral obligations applied to employees, contractors, consultants and service providers in virtue

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<sup>2</sup> The Kimberley Process (KP) is a joint governments, industry and civil society initiative to stem the flow of conflict diamonds – rough diamonds used by rebel movements to finance wars against legitimate governments.

of *'responsible corporate citizenship'* concept, while Lucara Diamonds Corporation and De Beers, in addition to their guidelines, encourage whistle blowing, where suspicious activities are suspected.

Again, whilst the negative impact of poor legislation and ineffective self-regulation policies on financial and political agenda result evident, social and environmental dimensions shouldn't be ignored. In pursuit of achieving all three forms of legitimacy (cognitive, relational, moral) proposed by Suchman (1995), the companies must not only conform to the rules and beliefs systems prevailing in the physical contexts (Scott; 1995), but also to proactively embed environmental and societal issues into corporate objectives. Remarkably, mining stakeholders constantly execute such isomorphic pressures on the industry players, forcing them to undertake notable shifts in governance and, generally, in modalities the organizations relate with the external environment. On the organizational level, it entails that new performance measurement protocols had to be developed in reference to social investments, biodiversity, tailings management, energy use, gas emissions, external outreach and crisis management planning. Additionally, a new challenge of addressing aboriginal relations has sprung, after some controversies dominated public agenda (i.e. Marengo diamond fields' conflict). The mainstream stakeholder literature, however, seem to neglect the question of what actually fosters a greater / lower sense of corporate responsibility.

In attempt to fill the gap in the stakeholder theory literature, Campbell (2007) reflected on the conditions under which organizations are more likely to act in socially responsible ways. First of all, exactly like Galaskiewicz (1991), he recognizes that institutional constraints and, normative institutions in general, mitigate or even discourage opportunistic behaviors. In reference to our research, the absence of these elements, as discussed before, may induce the mining industry's players to behave irresponsibly (i.e. money laundering, terrorism financing, bribing, frauds, mixing undisclosed synthetic diamonds with natural gems, under/over-grading procedures, polluting, weak post-closure mines' monitoring programs, controversial company-owned mining towns closures, use of child labor, no labor rights innovation, poor social investments). It follows that the institutionalization of certain norms is

essential in affecting the degree to which diamond sector actors operate in socially responsible ways.

Secondly, among different firm-level attributes affecting organization's CSR participation, the literature identifies the size as an important but relatively unexamined variable (Madden *et al.*; 2006; Campbell; 2007; Udayasankar; 2008; Muller *et al.*; 2010; Chang *et al.*; 2012). Generally, it has been argued that there is a positive impact of the firm size on the CSR and consequently also on the Corporate Social Performance (CSP). In fact, some researchers believe that size may affect strategic motivations (i.e. institutional pressures, greater need of obtaining legitimacy) and determine the scale of CSR activities considering the presence of more advanced and sophisticated internal systems as also of greater financial and non-financial resources (Brammer *et al.*; 2006). By comparison, studies by Meznar *et al.* (1995) rejected the hypothesis of positive link between the size and CSP. The third chapter of this dissertation we prove that there is a positive correlation between the revenue and investments in CSR, but no correlation between the firm size and conjoint variables. Neither for Chang *et al.* (2012) this link is obvious. The study suggests that the relationship between both - size and CSP, is mediated by corporate governance structure, in particular by the presence of outside director representation. It follows that board structure and top manager's agency behaviors, even more than the firm size, enhance stronger commitment to CSR and build a positive relationship with environmental constituents.

Thirdly, Campbell (2007) suggests that 'corporations will be more likely to act in socially responsible ways if there is a system of well-organized and effective industrial self-regulation in place to ensure such behavior, particularly if it is based on the perceived threat of state intervention or broader industrial crisis and if the state provides support for this form of industrial governance'. From perspective of this preposition, it becomes even more evident the importance and regulatory force of 'chain-of-custody' (CoC) applied to the diamond industry and its role in the establishment of a social-licence-to-operate (SLO). For example, Responsible Jewellery Council (RJC), which efforts are best articulated by RJC's '*Code of Practices*', launched the only



CoC standard applied to the diamond sector (and other precious metals like gold or platinum) in 2012. The CoC standard promotes the concept of responsible sourcing referred to metals produced, processed and traded through jewellery supply chains and thereby monitors if all participants act responsibly. Remarkably, out of more than 600 members only three of them are actually diamond producers, which constitute less than 0,5% of all companies involved.

The literature on sectorial analysis, corporate governance and stakeholder management has stressed that the way managers adjust their efforts in CSR depends also on the degree to which the corporations are engaged in institutionalized dialogue with NGOs, social movement organizations, investors, press as also with labor unions and employees (Jenkins; 2004; Brugmann; Prahalad; 2007; Campbell; 2007; Littlewood; 2014). It entails incorporating certain 'participatory models' into governance processes, where monocratic leadership is absent and traditional activities of coercion, command and control are no longer sufficient. It follows, that CSR's pro-activeness stands in including processes of negotiation, cooperation and support aimed at creating formal and informal policy networks, where operators are bound together by common interest in ongoing interaction (Hessing *et al.*; 2005).

Moreover, the stream of studies regarding the relationship between the companies and their stakeholders suggests that a greater competition reduces the complacency effect and addresses more pro-active character of CSR programs (i.e. projects developed collaboratively with De Beers, local foundations and the government of Namibia: Community Sustainable Development Project, Whole School Development Project, Education and Training Sector Improvement Program). For example, Fernàndez-Kranz and Santalò (2010) empirically studied the link between the level of competition and CSR performance. Their findings show that firms operating in more competitive markets have better social and environmental ratings, with a corresponding larger within-industry CSR variance. Along the same lines Fisman *et al.* (2006) note that CSR can be a product differentiation tool where the output would be otherwise homogenous (think about polished diamonds

which differentiating characteristics are usually non observable with a naked eye). Thus, CSR activities highlight the firm's aversion to sacrificing unobservable quality (Fisman *et al.*; 2006; Fernández-Kranz *et al.*; 2010) and may potentially translate into increases in market share (Porter, Kramer; 2006). However, there is a lot of controversy in the literature about this claim. Some researchers, mostly from the field of economics, believe that in periods of intense competition the firms, in order to survive, are more willing to reduce altruistic behaviors (i.e. philanthropy) and to give less importance to ethical outcomes (Schneiberg; 1999; Bagnoli, Watts; 2003). At the interpretation level, the same logic stood at the basis of Schumpeter's (1944) theory of negative link between competition and innovation.

Finally, Littlewood (2013) argues that a greater interest in CSR engagements may be attributed to continuing controversial nature of many mining investments, even if the actual state of integration of CSR into core business activities remains dubious (Hamann *et al.*; 2004). In other words, organizations' engagement in CSR could depend on the level of controversy embedded in the mining activity. Nevertheless, Hamann and Kapelus (2004) questioned, if some mining companies weren't using CSR only for 'green-washing' their reputation and for constructing corporate legitimacy. Interestingly, involving symbolic and rhetorical framing (often in contrast with substantive behavior) into CSR is a common practice in public image management (Campbell; 2007), being a part of what Porter and Kramer (2006) described as a 'cosmetic corporate response'.

Generally speaking, the literature and public agenda express serious doubts concerning the CSR effectiveness in the diamond mining and provide evidence that the engagement only partially translates into legitimacy. Reflecting on the contribution of CSR to a greater cognitive, pragmatic and moral legitimacy, Claasen and Roloff (2011) noticed that, the legitimizing power of diamond producers is limited due to serious concerns regarding the quality of CSR projects, stakeholders' doubts about how target groups were selected as also due to extremely high level of secrecy regarding economic and environmental impact. Moreover, the analysis of 42 semi-structured interviews allowed the authors to raise serious concerns about overall

reputation of the industry, trust and transparency issues. Also Spiegel (2014) reported how the diamond producers actually fail to conceptualize what Butler *et al.* (2007) call 'equity-sensitive interventions', generating serious environmental, social and political struggles. Exactly like Perez and Sanchez (2008), Claasen and Roloff (2011), Fonseca *et al.* (2013), Spiegel recognizes the importance of honest reporting policies in minimization of risk related to the legitimacy establishment. His particular concern, regarding the gap between the truth and what is actually reported, provides an interesting insight into the actual state of CSR programs lingering in the diamond industry and constitutes a dramatic testimony of their inefficiencies.

### **3.3. CSR: the Way towards Innovativeness**

At this point, once external (i.e. poor legal framework, weak international and national regulations, lack of registration and reporting requirements, small number of competitors) and internal (i.e. top-managers agency behaviors, lack of institutionalized dialogue with stakeholders, weak self-regulation policies, the size-effect) sources of mismanagements in CSR have been discussed and pointed out, we return to our initial research question on the pro-active CSR workability in the diamond sector. In doing so, we follow a stepwise approach to construct a better understanding of CSR's 'pro-activeness' with means of a conceptual framework, which constitutive elements are called by the author 'arenas'. The term 'arena' is used here on purpose. Leaving behind convictions deeply rooted in neoclassical economy, we argue that responsible organizations operating in modern economy are forced to compete with each other on different levels (arenas) and only the supremacy on all levels constitutes a competitive advantage. It follows that corporations are seen as a nested set of strategic CSR processes, continuously evaluated not only by the enterprise itself but also by a large number of stakeholders. Thereby, the nature of the 'engagement premium' (i.e. reputation, earnings, market share, brand equity) is determined by a positive result of such evaluations.

Over the last three decades, since CSR has emerged as a central business agenda, new conceptual contents and business practices have been gradually codified, developed and applied in the organization's strategy (Brugmann *et al.*; 2007). Going beyond Friedman's (1970) Kantian perception of CSR (with a dominant role of shareholder's figure), numerous authors like Freeman (1984) and Porter & Kramer (2006) studied the relations between corporations and their stakeholders in the context of corporate strategic management (CSM). In fact, the recent scholarship (Donaldson, Preston; 1995; Mitchell *et al.*; 1997; Phillips; 2003; Steurer *et al.*; 2005; Brondoni; 2014; Lambin; 2014) stressed that managing such relations is vital for businesses and constitutes an essential vehicle for CSR policies design, implementation and innovation. As stated repeatedly in the literature, civil society engagement in controversial issues (i.e. pollution, deforestation, indigenous peoples rights, child labor, corruption) accounted for the upsurge in CSR activism and the involvement of NGOs in advocacy, economic and regulatory activities (Utting; 2005). For Midttun (2009), this entails a radical change in strategic focus, introducing the paradigm of serving both societal and business needs, thereby transcending the traditional dualist approach based on division between private and public goods. Admittedly, since a single-minded focus on economic sustainability is no longer considered a winning approach, CSR support function has been extended over first-order (economic, social, environmental issues) and second-order (transparency, participation, reflectivity, integration, intergenerational equity) issues (Steurer *et al.*; 2005). The assumption of this paper is that every company has its social responsibility and therefore it is the extent to which the organization uses those issues to design, introduce and innovate CSR strategies, which will vary.

From the 'defensive' and 'reactive' CSR perspective, firms' engagement lays in a safeguarding support function and in eliminating malpractices in selected parts of the organization in virtue of new social and environmental expectations, while in essence remaining strategically focused on business as usual (Midttun; 2009). It follows that fundamental value creation drivers regard exclusively first-order issues, without embracing the operational innovation that anticipates the projected evolution of external regulations,

laws and social trends. In fact, once compliance requirements (i.e. legislative pressures) are satisfied, the companies have neither interest nor resources to invest in more pro-active CSR programs. Within this perspective, the organizations empower initiatives that catalyze social and/or environmental transformation only in presence of stakeholders, who possess attributes of power (legal, financial, media, ethical), legitimacy and urgency of claim (Prno *et al.*; 2012). CSR strategic management, on the other hand, is limited to 'reactive' policies answering to claims of the most powerful stakeholders, whose consensus is necessary for the corporate legitimacy and for access to fundamental resources. Finally, we postulate that reactive approach is a spillover of multiple factors among which: legal inefficiencies, top-managers' agency behaviors, condition of monopoly or oligopoly, indigenous peoples without attributes of power, market secrecy, lack of 'watch-dog' activism.

Despite a substantial body of CSR literature, there is no all-embracing definition of CSR (Van Marrewijk; 2003). In fact, although many definitions have been created (i.e. strategic CSR (Porter *et al.*; 2002), transforming CSR (Mirvis *et al.*; 2006), 'extended perspective on the corporate citizenship' (Matten *et al.*; 2005), Kyosei principles (Kaku; 1997), triple-bottom line), none of them seem to represent a more holistic approach, but would rather concentrate only on one or few aspects of CSR. In answer to van Merrewijk's (2003) call to create more 'all-embracing' notion of CSR that wouldn't be, at the same time, too vague we decide to work on the concept that have already been described in the literature – pro-active CSR.

Generally, authors used different terms and concepts describing the passage from reactive to more pro-active policies, recognizing undeniable shift occurred in the firms' social and environmental behaviors in the last twenty years. For Torugsa *et al.* (2013) "proactive CSR is represented by a pattern of responsible business practices adopted voluntarily by firms that simultaneously support sustainable economic, social and environmental development at a level above that required to comply with government regulations". Yet, we believe that this definition needs to be integrated with second-order issues proposed by Steurer *et al.* (2005) and particular concerns

that dominated recent debate regarding CSR effectiveness (Frankental; 2001; Porter *et al.*; 2002) (table 2).

**Table 2. Differences between Reactive and Pro-Active CSR**

	Reactive CSR	Pro-active CSR
<b>CSR output</b>	Philanthropy, Code of Conduct, Legal Compliance	CSR Innovation and New Patterns of Social/Environmental Investment
<b>Managerial Agency Approach</b>	Limited to Claims of the Most Powerful Stakeholders	Visionary
<b>Engagement Policies</b>	Defensive Exclusive	Transforming Inclusive
<b>Transparency Compliance Requirements</b>	Public Relations Answer to Legislative Pressures	Full Disclosure Answer to all the Stakeholders' Pressures
<b>Strategic Intent</b>	License to Operate	Social Change

First, CSR pro-activeness stands in the organization's ability to engage various groups of stakeholders in decision-making and operation processes, defining the way the value proposition strategies address the parties involved (engagement culture). By increasing the perception of the other's party level of commitment with means of formal (i.e. contractual constraints) and informal (i.e. information sharing) mechanisms, the responsible organizations boost ex ante their stakeholders' confidence (Brown *et al.*; 1995; Rindfleisch *et al.*; 1997) and effectively attract value-seeking investors (i.e. banks, investment funds, insurance companies). An influential body of business and academic opinion seems to embrace the concept of interaction as a central component of the governance perspective (see also Kooiman; 2003) and underlines that high-profile corporations are becoming always more aware of benefits related to symbiotic linkages. For instance, Brugmann and Prahalad (2007) posit that smart corporations, recognizing the emergence of joint regulatory frameworks

(that is, co-presence of the State and NGOs as corporate sector's de facto regulators) have build the ability to actively participate in global and local policy networks and to define new standards through negotiations with their stakeholders. Conversely, some authors (Frooman; 1999; Calton *et al.*; 2003) emphasize how increasing diversity and number of stakeholders has decreased firms' capacity to focus on the companies' primary objectives (*the stakeholder paradox*).

Secondly, responsible companies are those who apply continuous learning processes, based on systematic evaluations of internal and external context and investigating changing perceptions and needs in society (Steurer *et al.*; 2005). It follows that reflectivity refers to firm's ability to predict the evolution of legal framework and social trends, mitigating the risk related to negative events and, on the other hand, maximizing the realization of opportunities. Following this line of reasoning, Mintzberg (1993) suggested that the companies should aim at building institutional capacities, competencies and first of all – resources to understand, confront and respond to unexpected changes in the market. Naturally, as he noticed, it requires a major operational flexibility and, thus, more dynamic governance strategies keeping pace with changes that occur or may occur. As to why more systematic evaluations get started, a snapshot of current thinking seems to identify their rationale as based on a rational argument (i.e. stability), strategic argument (i.e. competitive advantage) and economic argument (i.e. financial risk mitigation). Oftentimes, authors apply cause-related approach to study situational triggers of the 'learning processes' phenomenon like changing market conditions, greater competition, greater stakeholders expectations and 'watchdog activism'. It follows, that a company's capability to deal with those variables is the mirror image of its strength, culture and competitiveness.

Thirdly, CSR pro-activeness is reflected in firm's orientation on the intergenerational equity rather than single-minded focus on short run economic sustainability typical for reactive approach. Despite some decision makers may unscrupulously seek to serve their self-interests in the short-run (Parkhe; 1993; Rindfleisch *et al.*; 1997), market-oriented corporations have started to abandon the opportunistic and heavy-handed use of power (Brown

*et al.*; 1995), shifting their strategies towards more collaborative and future-oriented policy networks. In other words, the integration of pro-active CSR into organizations' long-term strategies and decision-making criteria entails a transition from an utterly economy-driven culture to a more value-laden culture and from negative duty-based morality to positive-duty morality that embraces institutional, organizational and individual levels (Maon *et al.*; 2009; Hine *et al.*; 2009). Specifically, responsible leaders are concerned with ensuring integrity with means of advanced accountability processes, where the demands, needs, interests and values of employees, customers, suppliers, communities, shareholders, NGOs, the society and the environment are being continuously aligned and reconciled (D'Amato *et al.*; 2009). Interestingly, Rangan, Chase, Karim (2015) underline that smart companies deliver social or environmental benefits in ways that support firm's operations across the value chain, often improving efficiency and effectiveness, increasing revenue and/or decreasing costs. For instance, sustainability initiatives that reduce the use of emissions or that invest in optimizing employee education may result in a substantial costs reduction and in boosting the productivity. Nevertheless, a relevant point raised in some critical reviews has to do with actual conditions of managerial agency in terms of CSR pro-activeness. For example, Hine *et al.* (2009) in their study on the perceptions of CSR in different managerial groups, found – exactly like Roberts (2001) - that generally for senior managers CSR is a 'manipulative attempt to protect shareholder value' and, thus, a manifestation of corporate pragmatism rather than of positive-duty morality. Concomitantly, Frankental (2001) questions whether CSR is not an invention of PR and if a truly responsible organization can actually adopt self-serving definitions of responsibility ignoring at the same time the whole development of formal and informal frameworks (see also Hamann *et al.*; 2004).

Moreover, pro-active CSR aims at strengthening drivers of moral legitimacy by eliminating inconsistencies between company's strategy and CSR engagement and differences regarding the treatment of stakeholder groups (Claasen *et al.*; 2011). In doing so, the companies may decide to formulate new transparency policies and establish a convincing oversight authority, whose primary objective is to contribute to future-oriented value nets creation.



Therefore, as suggested by Claasen and Roloff (2011), the firms used to minimize their risk related to lost of legitimacy with tools of comprehensive, transparent and honest reporting systems, regularly evaluated by both profit and non-profit institutions. The business relations are, thus, no longer trust-based but rather based on radical transparency and financial disclosures, dealing with horizontal shifts in traditional roles of governing (legal requirements by government actors are now flanked by non-governmental institutions requirements, for example in terms of reporting) (Eckerberg *et al.*; 2004). Paraphrasing Morgan and Hunt (1994), to be an effective competitor in the global economy requires one to be a trusted cooperator of all the stakeholders groups (relationship commitment), whereas marketing activities should be directed toward establishing, developing and maintaining successful relational exchanges.

Remarkably, as the expectations from institutionalized corporations evolved out of the liberal market system are higher (Chamberlain; 1982), the strategic use of corporate power and firms' assets for ethical, other-regarding actions became a fundamental element of corporate legitimacy. Breaking with the heavily individualistic and self-regarding perception of value has led, thus, to rethinking of revenue-sharing model from the strategic marketing perspective (Porter *et al.*; 2002) and gave more space to new patterns of social investment that goes beyond a mere philanthropy. Specifically, pro-active CSR focuses more on innovating and reforming the patterns of producing environmental and social value, shifting both tangible and intangible resources towards areas of higher yield for the society. Since the literature and public agenda have critically analyzed the link between tax laws and philanthropy (Clotfelter; 1985; Navarro; 1988; Campbell; 2004), many firms have been accused of manipulations in charitable giving processes. Peculiarly, some authors suggest that businesses often use philanthropy for tax deduction purposes rather than with objective of peer-driven value creation. Conversely, pro-active CSR empowers complex and highly coordinated (by both project managers and project sponsors) charitable initiatives that include donations of money, equipment to civic organizations (i.e. hospital supplies and equipment), financing community initiatives and projects (i.e. raising funds for

schools or hospitals), employee volunteering support, employee health and housing programs, microfinancing programs, launching natural resources conservation programs (i.e. forest protection policies). It is not however, as suggested by Rangan, Chase, Karim (2015), about collecting the greatest number of activities but rather about strategic selection of initiatives consistent with the firm's business purpose and with major potential for corporate legitimacy and bottom-line strengthening.

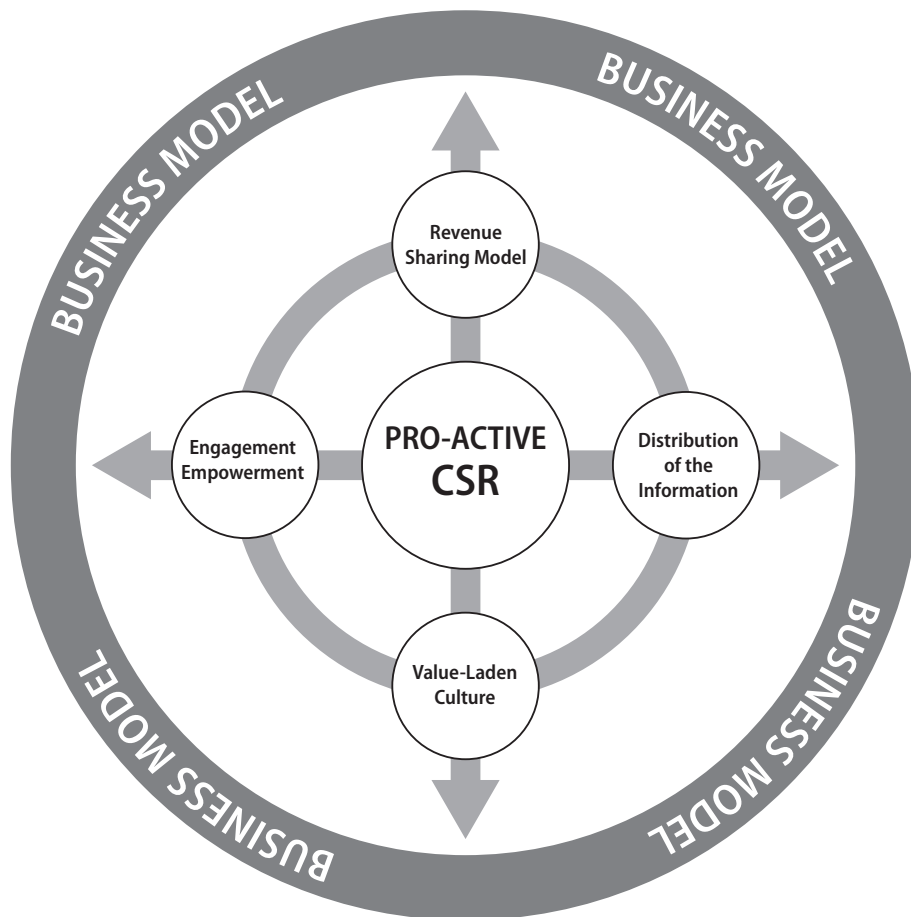
Finally, the recent scholarship also deals with the organizational developments required to integrate CSR principles into business models (BM) and processes activated by the 'front-runner' companies (Zadek; 2004; Lüdeke-Freund; 2009). Remarkably, oftentimes the BM is interpreted as a determining factor of corporate behavior (Elkington; 2004), and as such, is subjected to strategic innovation processes (Schaltegger *et al.*; 2012). In fact, the basic assumption of this research in some way evokes Weber's (2008) claim that, moving from value-supporting to value-driving policies may address business model transformations in order to secure sustainable operations in the long term (Fig. 2). Using Ballon's (2003) distinction between four domains of business modeling (value network, functional model, financial model, value proposition), we suggest four underlying BM parameters that are directly connected to the issue of CSR pro-activeness: engagement empowerment, distribution of the information, revenue sharing model and value-laden culture.

As to the first parameter, a thoroughly developed research on future-oriented business models has resulted in concepts and frameworks centered on the ideas of 'openness' (Chesbrough *et al.*; 2007), stakeholders' involvement (collaborative advantage) and on building engagement platforms (Martin; 2002) addressing a number of hybridized governance arrangements (Prno *et al.*; 2012). For example, some diamond mining companies formalized specific agreements (IBAs) with local communities in northern Canada, meant to address territorial economic development and ensure socio-economic reporting for mining projects (i.e. De Beers's IBA with Daninu Kuè First Nation, Rio Tinto's IBA with Yellowknives Dene First Nation, BHP Billiton's IBA with Lutsel K'e Dene First Nation). At this point, we disagree with Ballon's

definition of the actor in value network as a strictly 'commercial entity'. In congruence with modern stakeholder theory literature, we decide to speak rather about commercial (i.e. cutters, jewelry retailers, financial institutions) and non-commercial entities (i.e. NGOs, aboriginal communities, research centers), actively participating in value creation processes.

The second parameter refers to systems of information distribution between the firm and its interlocutors (functional model domain). For example, reporting systems and transparency policies vary among the businesses and industries, being often reduced to simple statements and mostly financial performance indicators, all the more so where the legal framework is weak. The accuracy of the reports, on the other hand, is rarely certified by independent actors like NGOs but rather by for-profit consulting companies, journalists and professional writers (Adams; 2002), rising in some cases serious concerns about the reports' objectivity. Moreover, as emphasized by Basu and Palazzo (2006), the trend of rising homogeneity and near standardization in CSR reporting makes it difficult to reveal real differences among the organizations. Thus, truly responsible companies are those who not only publish accurate reports, but also adopt policies, frameworks and standards (i.e. ISO 26000, SA8000) developed and controlled by independent organizations, often with a non-profit mandate like Global Reporting Initiative (GRI). Moreover, the pro-active nature of their CSR policies pushes the organizations towards sharing-information solutions in efficiency-seeking practices. It entails, that smart companies keep coherent portfolio of initiatives that offer operational and bottom-line targets improvements achieved with means of information and know-how exchange (i.e. collaboration with the Universities in order to develop more efficient solutions in manufacturing processes).

**Fig. 1. Pro-Active CSR Model**



The third parameter – the revenue sharing model (referred to financial model domain) summarizes firm's efforts in undertaking charitable initiatives and in supporting financially important causes for both society (i.e. social investments) and environment (i.e. gas emissions reduction) (Kanter; 1999). Hence, in reference to the organizational side, managers can determine the appropriate level of investment in such initiatives by conducting cost-benefit analysis in the same way that they analyze other investments (McWilliams *et al.*; 2001). Interestingly, Porter and Kramer (2002) underline how philanthropy is increasingly used rather as a form of investment in PR and advertising ("the myth of strategic philanthropy"), while, as they claim, true strategic giving stands in addressing relevant social and economic goals simultaneously, targeting areas of competitive context where the business and society both benefit because the firm brings unique assets and expertise (ideal citizenship interpretation).

The last parameter, the value-laden culture (referred to value proposition domain), designs the firm's ability to generate and distribute value inside and outside the corporate system by the strategic use of firm's assets and competences. It is also a fundamental driver to empower innovative business models built around opportunities where there is potential for significant congruence between social/environmental and economic value creation, logically susceptible to particular ethical and ideological interpretations. Interestingly, Heimans and Timms (2014) suggest that blending new business models with new values, gives life to 'new powers' – more open, peer-driven and participatory, the power that instead of being hoarded gets channeled. It favors more informal and inclusive network approaches to governance, submitted to rules of strategic and innovation management.

### 3.4 Pro-Active CSR Model

A key assumption underlying the figure recalls the claim that a strong business model is built around opportunities where there is potential for significant congruence between social and economic value creation. From pro-active CSR activity system perspective (Zott et al.; 2009), designing a strong BM starts, thus, from the identification of the groups of stakeholders, their expectations, claims and the rules they are subjected to. This knowledge is a starting point for further evaluations and strategic decisions leading to innovative, cost-effective and bottom-line-strengthening ways to address social and environmental problems, even more so where the governmental institutions fail to solve them and to protect the citizenship ('extended view of corporate citizenship') (Ansoff; 1980; Matten *et al.*; 2003).

The second point raised is that optimizing four parameters of pro-active CSR traces new trajectories in development of existing analytical units of strategic management, such as company, organization or the industry. As such, CSR's activities and attributes may be examined through underlying strategic purposes (differentiation strategy (McWilliams *et al.*; 2001), competitive and leadership strategy (Porter *et al.*; 2006), sustainability and resources usage strategy (Marshall *et al.*; 2005), corporate legitimacy strategy (Suchman; 1995), entrepreneurship strategy (Brugmann *et al.*; 2007)) or through their substantive content (ethical, legal, discretionary, economic – Carroll; 1991). In this paper we decide to follow Porter and Kramer's (2006) point of view and, in doing so, we decide to call four parameters of pro-active CSR "arenas", where the corporations compete with each other in order to gain major legitimacy, leadership and to achieve bottom-line-strengthening targets. It follows that, BM's CSR strength is a result of overall efforts of both managers (project managers) and CEOs (project sponsors) in all the arenas, the way they are perceived, developed and internally controlled. At this point we decide to recall Rangan's et al. (2015) finding that CEOs frequently do not engage in CSR programs, leaving their be-or-not to be to internal managers, who often run them in an extremely uncoordinated manner and without any consistent logic

embedded in a vision that would articulate the direction and the ambition of the organization as a whole. In fact, as suggested by Waldman et al. (2006), the role of CEO in CSR coordination process is extremely relevant but often mined by personal characteristics (i.e. lack of intellectual stimulation) or by existing conditions on the market (i.e. during financial crisis expenditure on CSR is generally considered unwise).

Thirdly, our model explicitly acknowledges that the optimization of corporate social responsiveness requires the inclusion of a more coherent base to managerial decision taking processes, where specific capabilities equally support strategic development of all the 'arenas' in virtue of a greater isomorphism among CSR practices. In operational terms, it entails that an interconnected system for assigning CSR decision rights referred to a particular arena must be crafted and roles must be designated and allocated to the different members (or team of members) operating along the organizational ladder. Furthermore, the objective of coherency and consistency empowers more inclusive, flexible and cooperative forms of governance, resulting in widely shared and coherent mind-set that enables the firm to deliver superior value. It is essential to observe that still many companies struggle with a consistent selection, development and communication of all the activities arising from four arenas of pro-active CSR. For example, in many cases public agenda expressed serious concerns regarding the actual integrity between what is reported and what the organization really does (Perrini *et al.*; 2006).

Finally, we posit that in highly dynamic and competitive markets also CSR systems require mechanisms of adjustment. To start, from the perspective of viable system theory (Beer; 1984), the arenas are nothing but subsystems originated and subordinated to one supra-system, which codifies firm's attitudinal variables related to socially and environmentally responsible behaviors (it possess its own problem solving capacity). As such, the subsystems establish necessary conditions for healthy growth of effective relationships with all the groups of stakeholders, empowered above all with the means of high interconnectivity between the managerial units and high level of reactivity to changes occurring within the environment. Specifically, in

order to respond more quickly to those, effective policy-makers adopt more coordinated, synergy-seeking positions and crosscheck, in the main, intelligence and control issues. This has significant implications for designing multi-function workgroups that articulate the direction and the ambition of the organization to become a visionary front-runner in solving emerging social/environmental problems. Clearly, four subsystems reinvent themselves, giving the whole structure (supra-system) a strength, integrity but also flexibility and robustness necessary to successfully compete in fast-changing environments as discussed by Porter and Kramer (2002; 2006) (strategic CSR).

### **3.5. Innovation, CSR and the Diamond Sector**

As previously claimed, the literature and public agenda express serious doubts concerning the CSR effectiveness in the diamond mining and provide evidence that the engagement only partially translates into legitimacy. The diamond business, where the academics have long recognized sets of control mechanisms attributable to oligopolistic practices of few suppliers (Zimisky; 2013), is consequently constrained to rethink its CSR policies (Mostovich *et al.*; 2007) and strategically reassess its interaction models as a result of legal (i.e. imperative of a greater transparency, new regulatory regimes and legislations, more stringent enforcement of anti-money-laundering laws, sustainability reporting requirements, a growing number of regulatory actors, ineffectiveness of public courts), ethical (i.e. new patterns of social/environmental investments, need for more inclusive policies), structural (i.e. greater competition, sector stewardship, globalization processes, greater importance given to strategic alliances and value nets, innovative engagement platforms' requirements) and economic (i.e. shrinking profit margins, flat prices, weaker credit sale, banking industry-wide restructuring, progressive introduction of Basel III rules, increased need for working-capital financing, sharp increase in credit risk) developments.



Generally, these changes affect systems of legal and extra-legal<sup>3</sup> certainty (Richman; 2009), pushing the arbitration procedures towards an enforcement system that employs social norms, equal distribution of coercion value between stakeholders as also sharp reputation and transparency mechanisms. For example, in the wake of financial crisis, the purchase financing and the diamond middle-market's access to bank liquidity in general, has become extremely challenging and complex. Specifically, Diamond Banks, financial and insurance institutions enhance procedures for appraising inventories (processed, for instance, by *enterprise resource planning* (ERP) software) but also request improved reporting systems referred to firms' sustainability scheme. Accordingly, the following proposition is advanced:

*P1: There is a positive link between pro-active CSR activities and access to financial assets.*

Existing studies on the tradeoff between investment in CSR and financial performance lack of substantial consistency, suffering from contrasting conclusions (McWilliams *et al.*; 2000; Scholtens; 2008). Little has been said, however, about the relationship between CSR activities and access to financial assets, which are fundamental for the firm's economic viability. As recalled in Scholtens (2006), a well-developed financial system affects the size, growth and the timing of economic operations, having positive effects on resource allocation and resulting in market interest rates that fully reflect the relative attractiveness of different investment opportunities. In reference to the latter one, financial intermediaries use key actions of brokering like screening, monitoring and enforcement in order to minimize the risk of the investment (safe savers' resources allocation) and evaluate firm's general efforts in value creation processes. The objective of an appropriate benchmarking of sustainability-driven funds and derivatives over the long term is also obtained with the means of specific indices like Dow Jones Sustainability Index (DJSI). Following a best-in-class approach, the indices measure the performance of

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<sup>3</sup> A non-state system of contract enforcement that rests on personal exchange and reputation mechanisms.

the world's sustainability leaders, who share the same vision of being global citizens and visionary sustainability supporters (Mirvis *et al.*; 2008).

As to the diamond mining companies, one outcome of CSR agenda is the increasing need to justify their existence (Jenkins *et al.*; 2006) and document their sustainability performance in answer to more variegated shareholders' and investors' claims. Thus, the perception of relationism has become more articulated and based on specific expectations referred to firms' level of commitment in sustainability programs, delineating firms' ability to keep the volatility low, to reduce the risk of investment and, indirectly, to contribute to equity cost reduction (see also Eggert; 1997; El Ghaul *et al.*; 2011). Specifically, funding agencies, banks, private and public sector providers of insurance have increasing reason to evaluate firm's efforts in minimizing risks related to credit (i.e. delayed payment), position (i.e. company's devaluation), security (i.e. divestiture), legal aspect (i.e. liabilities) and funding (i.e. depreciation) (Warhurst; 1998). Spar (2006) explained that while other industries are more prepared to handle price fluctuations, for diamonds, by contrast, the potential for permanent substitution is very high and, thus, it becomes more difficult for the companies to ensure that prices stay steady and commerce relatively unobtrusive. Exactly for this reason, in a capital-intensive industry *par excellence* like the diamond industry, the biggest mining companies invest heavily in advanced reporting systems, in order to successfully attract and maintain venture capital. After all, the basic assumption of *Capital Asset Pricing Model* (CAPM) is that investors are concerned with two relevant aspects - the mean and variance of portfolio returns (Hawley; 1991), expressing the organizations' ability to bring a greater certainty and value into the marketplace. Paraphrasing Matten and Moon (2008), corporate governance reforms tend to extend the function of controller from banks and major block holdings over capital markets, resulting in 'creative destruction' of defensive reporting policies. In doing so, the organizations avail of trusted auditors and consultants, actively engaged in bringing a greater transparency into corporate activities. In this sense, the underpinnings of the arenas of 'information distribution' and 'engagement empowerment' underwrite the strategic dimension of pro-active CSR.

Our study, analyzing 40 nonfinancial reports and different sustainability indices and rankings (i.e. DJSI, Stoxx Sustainability Index, Global Compact 100), identified three common characteristics of the companies endorsed for exemplar corporate governance and reporting policies (i.e. transparency, adherence to GRI's sustainability reporting guidelines and to standards of Social Accountability International (SA8000), adherence to Financial Accounting Standards (FAS), management of standards like ISO 26000, integration of mine closure toolkit ICMM 2008, general capacity to build trust). First, the firm's size seems to have a positive effect on the reporting operations' integrity. In fact, while no small-size diamond company has published annual sustainability report, all large companies result to have always more advanced reporting systems as confirmed by their rising Bloomberg's Social Disclosure Score (SDS) in years 2009-2014. Secondly, organizations with revenues higher than \$500mln result to be more precise, transparent and skillful in communicating their *Socially Responsible Investment* (SRI) activities. Thirdly, as all the biggest diamond companies are listed, we conclude that the extent to which the firm perseveres in developing the arena of 'information distribution' is influenced by the presence or not on the stock exchange. Specifically, there are numerous examples of more extensive, meaningful disclosure requirements and new frameworks for a better assessment of the perception of risk and stability (i.e. Sustainable Stock Exchange Initiative, ACCA, Australian Securities Exchange, CERES, World Federation of Exchanges) in order to improve the quality of information available to providers of financial capital and to enable a more efficient, productive and ethical allocation of capital. Moreover, Chamberlain (1982) noticed that, as the expectations from an institutionalized corporation evolved out of liberal market system are higher, corporate management has to respond affirmatively to the shareholders' ethical position and, thus, also the corporate strategy has to change (see also Epstein and Pava; 1993). More recently, Laszlo (2008) argued that mainstream publicly traded companies are now playing a leading role in solving the world's toughest problems since a new competitive environment and regulatory pressures has emerged.

Some authors rightly claim that generally self-regulations tend to be preventive and remedial rather than innovative (Chamberlain; 1982). In fact, historically diamond merchant groups used to create tailored substantive, self-oriented contract regulations and private arbitration procedures to govern their transactions, confirming indirectly the ineffectiveness of state-sponsored courts (Richman; 2009). Today, however, in front of structural changes occurred in the diamond industry (de Waal *et al.*; 2013), firms are becoming more conscious of the role of commitment, strategic partnerships, policy networking, smart volatility-minimization solutions and, thus, they introduce more innovative and articulated self-regulations. In doing so, large companies introduce specific principles and programs, extended over their long-term clients, constraining them to work towards a greater compliance with International Financial Reporting Systems (IFRS) in order to receive rough supply. For example, De Beers moved away from the contract proposal questionnaire (CPQ), which was obligatory in sightholders' application process, towards new contract's requirement guidelines, including a greater focus on financial governance and transparency in spirit of IFRS framework. Furthermore, more the trade demonstrates its transparency and adherence to financial regulations, the greater is its chance to get additional credit for rough diamonds purchases (Krawitz; 2015).

It is true, however, that by investing in development of arenas of 'information distribution' and 'engagement empowerment', the firm attracts not only investors but also a whole range of different actors. Resultantly, a following proposition is being made:

*P2: The presence of pro-active CSR policies enforces the social license-to-operate in the diamond industry.*

Since full legal compliance with state laws and regulations is no longer sufficient to satisfy society's expectations regarding mining issues (Prno; 2013), mineral developers' activities are subjected to more complex arbitration procedures. In fact, general state of legal uncertainty and regulatory inefficiency (Richman; 2009) induced the diamond mining

companies to innovate their self-regulations according to the world citizenship logic and, from the other hand, to recognize the prominent role of non-state parties (i.e. civil society, NGOs, local communities). According to Rowley (1997), as the density of the stakeholder network increases (see also Brondoni; 2014), the focal business becomes less and less capable of hiding information or even of ignoring the importance of the stakeholder issues. It implies that new concepts of moral and legal imperatives (encompassing ‘voice of society’ concerns, new requirements for public accountability and supply chain pressures) (Warhurst; 1998) shape innovative guidelines for responsible business practices (i.e. Alrosa Alliance Guidelines, De Beer’s Best Practice Principles), support horizontal governing mechanisms (Eckberberg *et al.*; 2004) and create new links between business innovation and social development (Brugmann *et al.*; 2007). For example, in 2015 the major diamond mining companies launched the Diamond Producers Association (DPA), following the trailblazing partnership model launched in 2012 under the World Federation of Diamond Bourses (WFDB) – the World Diamond Mark. The decision indulges requests from within the industry to create a body that would not only drive consumer demand with joint category marketing initiatives, but would also become an institution where to develop hybridized governance arrangements referred to best practices in environment management, social investments, license-to-operate and supply chain integrity. The element of innovation in this case stands in the ‘openness’ to other market players (acting as the unified voice of the diamond producers) and non-industry institutions (i.e. NGOs) in order to promote the interests of the sector.

Generally speaking, however, there is a lot of controversy about the effectiveness of such programs and, thus, about the firms’ capacity to successfully obtain and sustain cognitive, pragmatic and moral legitimacy (Suchman; 1995; Claasen *et al.*; 2011). In fact, authors like Hamann (2004), Claasen and Roloff (2011) and Spiegel (2014) acknowledge that despite engagements in CSR in diamond mining industry have evolved over time, there are still a lot of concerns regarding the depth of CSR adoption and how CSR practices have been actually integrated in core business activities and

decision-making processes. Resultantly, social responsibility performance (SRP) measurements like ISO 26000, ISO 14001 and adherence to GRI's Sustainability Reporting Standards have become valid indicators of the company's effective efforts in obtaining an additional 'social license to operate' (SLO). Analogously, Claasen and Roloff (2011) suggest that "companies can minimize the risk of losing legitimacy by reporting in an honest and comprehensive manner on their activities and policies, by collaborating with other legitimate actors [...] and assuming responsibility and accountability for their activities and their effects". Again, from our study results that only 8 out of 39 companies under analysis, use such measurement standards, which partially explains very low level of trust in the diamond industry.

As discussed previously, the combination of three factors – the lack of transparency, the absence of a solid oversight authority and the exclusiveness of regulatory power – undermines organizations' legitimacy that cannot be easily moderated by only well-drafted reports and smart communication activities (Porter *et al.*; 2006). The construction of moral, cognitive and pragmatic legitimacy is, in fact, an extremely complex process aimed at eliminating contradictions and differences between what is reported and what is the actual CSR performance. For instance, the gap between CSR engagement and the way the aboriginal communities are treated may result in weaker moral legitimacy. Exactly for this reason, a number of hybridized governance arrangements have loomed in the mining sector in recent years, mostly out of acknowledgment that some sustainability issues in the globalization era are too complex to be managed only by one party (Lemos *et al.*; 2006). Clearly, the globalization of societal problems has contributed to creation and development of new behavioral models applied to corporate governance, fostering solutions like co-management, public-private, private-social arrangements and, in some cases, shaping innovative business models. An emblematic example of this phenomenon comes from Canada. Denendeh Investments Limited Partnership (DILP) – entirely owned by Dene First Nations in the Northwest Territories (NWT) – aims at long-term value creation for aboriginal communities through equity building in northern resource development, growing local businesses, creating employment and training

opportunities for the locals. DILP's business model (centered on co-management solutions) is explicitly designed to recognize and incorporate local knowledge systems and to encourage the community involvement through power-decentralizing procedures. It entails that aboriginal people are engaged indirectly (i.e. discussions) or/and directly (i.e. equity investment) in decision-making and regulatory processes, which gives them a greater control over their territories and natural resources.

More inclusive governance regime addresses, thus, new supra-regulatory tools meant to ensure that the benefits are delivered to Aboriginal communities (Prno *et al.*; 2012) and consequently to reduce opportunistic behaviors *ex ante*. Although not legally required, the Supreme Court of Canada, for example, has affirmed that the companies are obliged to consult with Aboriginals who may be affected by projects occurring on or near their traditional land. Specifically, so-called 'Impact and Benefit Agreements' (IBAs) are formal contracts that outline the impacts of the project and specify commitments and responsibilities of both parties (i.e. assure the respect, recognition and support) (Caine *et al.*; 2010). From the resource dependency theory perspective (Pfeffer *et al.*; 1978), IBAs are essentially countervailing initiatives meant to secure legitimacy and access to minerals, while from the local community point of view, IBAs constitute an opportunity to negotiate royalty-type payments, employment and education opportunities, additional cultural and environmental protection measures (Prno *et al.*; 2012). Interestingly, Gibson (2008) observed how the models of negotiated agreements in the diamond sector have changed in the recent years. While all agreements continue to enhance economic and employment benefits, the more recent constructions call for a greater community involvement, greater investment in social and cultural programs, dispute resolution mechanisms, new revenue sharing schemes, and environmental restrictions (Gibson; 2008; Caine *et al.*; 2010). Therefore, we conclude that by strengthening supra-regulatory tools like IBA, the diamond mining companies may effectively gain an additional SLO, reduce transaction costs and avoid potentially costly conflicts with local communities and non-governmental organizations (NGOs).

*P3: More pro-active CSR policies enhance new patterns of social and environmental investment.*

Third proposition is based on the assumption that empowering engagement practices and value-laden business cultures leads to more innovative patterns of social and environmental investment, all the more so in globalized and highly competitive context. In fact, CSR activity systems, exactly like general corporate activity systems, became more complex, shaped by three 'design elements': content (strategic choice of activities), structure (the way the activities are linked), governance (who performs them) and four 'design themes': novelty (innovative contents and structures), lock-in (the way the stakeholders are involved), complementarities (bundled activities to generate value) and efficiency (activities reducing transaction costs) (see also Zott, Amit; 2009). As the architecture of CSR activity system is not a standardized process, the companies tailor their choices in function of their widely conceived vision and mission, as also in function of more specific strategic policies. For example, in 2006 De Beers launched its HIV/AIDS programme (DMP – Disease Management Programme) in consultation with government and NGOs, recognizing negative financial impact of the disease on corporate operations (i.e. costs related to absenteeism, lost productivity, training and replacement, medical interventions). In doing so, De Beers wants to provide a holistic workplace program, enhancing the quality of life for HIV-positive employees and communities where the company operates, while minimizing the economic impact of HIV/Aids on the organization and increasing, on the other hand, the corporate reputation.

For Tilton (1992), the extent to which mineral production contributes to local economies is determined by three elements. First of all, mineral wealth needs to be developed. Second, national and local governments should consider potentially negative macroeconomic consequences of mining booms (i.e. 'Dutch disease'). Third, to sustain the benefits of mining activities once the reserves are depleted, a portion of income must be reinvested (i.e. investments in local development, infrastructures, education and sanitation systems). In reference to the latter one, Littlewood's (2013) study on the 'Company towns'



(communities owned and administrated by mining industrial employers) endorses how challenging is the sustainability support after mining and how the decline of a community represents a significant reputational risk on national and international levels, with possible repercussions on the company's current social license to operate (SLO). As confirmed by Littlewood's research, the mining companies should develop more pro-active behaviors that would trigger interventions occurred as a part of a long-term strategy and clearly articulated vision for community sustainability, and that would assist communities in becoming self-sufficient. In particular, some operators in Namibia collaborated with town councils and other key-stakeholders (multi-stakeholder partnership) in launching Community Sustainable Development Projects (CSDP), engaging issues of competitiveness and developing alternative purpose for the town beyond its relationship with the mining industry. Nevertheless, the author raises serious concerns about the gap between sustainable development (SD) rhetoric and companies' actual engagement in addressing more sustainable closure policies and a greater assistance for aboriginal communities. Van Wyk's et al. (2009) conclusion is similar. Their study revealed that in some cases no evidence of facilities declared in the firms' annual reports (i.e. gymnasiums, convenience stores, guesthouses, fuel stations, tourism and transport services, infrastructures) was found, which triggered the erosion of support from different domains of social interactions.

As the opaque character of the negotiation process strengthens the perception that most of social and environmental agreements lack of effective normative enforcement and coordination, a new idea of incentive that would prompt the individuals to actively participate in institutional arrangements is required. The vast literature (Lemos *et al.*; 2006), indeed, upholds that traditional rhetoric of centralized control has been substituted by distinct governance decentralization, which Hutchcroft (2001) calls "a fashion of our time". Embracing strategic pro-activeness (Steurer *et al.*, 2005) is, thus, likely associated with advancing strong claims about the imperative to set and strengthen a tripartite alliance of civil society, governments and the private sector. The establishment of trust between those three groups, however,

revealed itself extremely strenuous and required new verification efforts – that is, tools certifying firm’s commitment in generating stability, perseverance and a greater responsiveness to social and environmental issues. Adherence to legal codes and performance standards is the price of legitimacy and acceptance. For example, the reputational benefits of compliance with environmental management systems standards like ISO 14001 or Greenhouse Gas Protocols (GHGP) encourage mineral developers to implement environmental guidelines and skills relevant to the each stage of the diamond value chain. In doing so, they find innovative ways of collecting environmental data through special informative systems and applications (i.e. De Beers’s EPRA - ‘Environmental Performance Reporting Application’) that, with third party verification where appropriate, assess the environmental impact of all new mining projects and whenever significant changes are made at existing operations level (i.e. review of CO<sub>2</sub> and SO<sub>2</sub> emissions, energy and water consumption, tailings management) (Van Wyk’s *et al.*; 2009). In line with this reasoning, large-scale diamond companies are currently working to standardize their energy and climate change measures and integrate them into sustainability programs on daily basis under control of specific committees, panels and auditing groups. As reported in Van Wyk *et al.* (2009), De Beers established Water Steering Committee, whose main objective is to create a culture of sustainable water management by focusing on key aspects like assurance, promotion of innovative ideas, knowledge sharing, continuous improvement and relationships with academia to enhance research on water management. Also Rio Tinto gathered leading thinkers and specialists from IUCN (International Union for the Conservation of Nature) and the University of Queensland to debate how to increase and share understanding of the monetary and non-monetary values of water and how to incorporate such values into decision-making processes.

The studies of Hilson (2002) and Amankwah *et al.* (2003), however, confirm our position that small mineral mining companies and the ad-hoc nature of their operations generated a myriad of concerns regarding environmental (i.e. atmospheric and water pollution, deforestation, land degradation) and social (i.e. safety, health) issues. As the small-scale mining

companies cannot survive on the basis of current reserves only, the objective of maintaining and increasing existing levels of diamond extraction is accomplished often at the expense of social and environmental concerns (adverse social/environmental impact). Thus, despite some prominent examples of CSR pro-activity in large companies, small diamond producers seem to be less successful in responding to stakeholders' expectations. First, small companies don't embrace key international instruments that regulate ethical principles of corporate activities, financial transparency, human rights and guarantee major social, environmental and economic stability to the same extent that large companies do. On the other hand, national regulations have been traditionally less demanding when it comes to the environmental impact assessment required for the small-scale companies applying for new licenses or renewal of the old ones. Second, small companies find it more difficult to involve all the business partners (i.e. backward linkages with some local industries and forward linkages with long-term rough diamond-buying clients, jewelry retailers) in developing and strengthening business guidelines, as they usually fail in creating successful value-nets. Third, their business models facilitate less the technological, organizational innovations and, thus, jeopardize reconfigurations of the underlying value chains or value networks (Schweizer, 2005; Wirtz, 2011). Finally, small producers find it more difficult to bring together capabilities, information systems, culture and financial assets to create advantageous positions in terms of social and environmental value creation (assessed by principles-based methods like SROI – *Social Return on Investment*).

#### **4. Corporate Social-Financial Performance Relationship**

*“Depletion of mineral resources should be compensated by generation of new wealth, which, in the form of useful lasting capital, can benefit present and future generations”*

*L.E. Sánchez<sup>4</sup>*

Since Milton Friedman’s (1970) seminal work added some intellectual challenge to the discussion on CSR with his famous claim that “the only corporate’s social responsibility is to make profit”, there has been additional interest in either proving or disapproving the link between social (CSP) and financial performance (CFP) (Griffin *et al.*; 1997). Despite a number of scholars have empirically explored this relationship no definitive consensus has been actually reached. In fact, the recent scholarship tried to explore the inconclusive nature of the debate and study the sources of such incongruence, analyzing, for instance the ‘industry effect’ (indeed, every sector is unique; it has its own internal competencies, different degrees of activism and deals with specific external pressures that create a ‘specialization’ of social interests) (Carrol; 1979). Other scholars, for example, recognized that firms’ size or even different accounting measuring tools of financial performance (i.e. net income, ROI, ROE, earnings per share) as also different data sources might generate contrasting results in making large cross-sectional comparisons across industries (Davidson *et al.*; 1990; Griffin *et al.*; 1997).

Nevertheless, most of researchers do agree that the CSP-CFP relationship is rather positive (Bowman; 1978; Wood; 1984; Freeman; 1984; Spencer *et al.*; 1987; Waddock *et al.*; 1994), supporting the popular claim that organizations generating negative ethical outcomes experience declining stock prices. Therefore, the mainstream literature claims that engaging in symbolic and rhetorical framing of CSR translates into public image and

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<sup>4</sup> In “Industry response to the challenge of sustainability: the case of the Canadian nonferrous mining sector”; 1998

bottom-line strengthening (Hirsh; 1986; Campbell; 2007), but at the same time, the effects of CSP on CSF may vary between industries.

The dominant belief in the scholarship is, thus, that pressures coming directly from concerns about social issues in management empower more complex allocation of strategic resources (Waddock *et al.*; 1997). According to Bowman (1977), social and environmental problems should be taken into consideration even if it entails a reduction in profits. Importantly, positive consumers' perceptions towards firm's sustainability policies, and thus its environmental awareness and patterns of relationism with local communities and governments, are increasingly becoming bases of competition. Further, since evaluating organization's performance on a range of social and environmental dimensions has become a widely shared policy, successful companies invest heavily in activities and add-on social spending measures that embrace philanthropy, workforce conditions improvement, pollution control systems optimization, water and energy management etc. (*good management theory*).

Nevertheless, further investigations showed that some organizations (especially the large ones) were accused of externalizing some CSR-related costs (i.e. environmental damages, mining closure, financial risks) in order to maximize the profit to distribute among shareholders and managers (Claasen *et al.*; 2012). Indeed, proponents of the so-called 'contrarian view of the firm' (inspired by seminal works of Friedman) give a myriad of examples of how firms act in socially irresponsible manner in order to survive and to satisfy shareholders' claims. For example, in diamond mining some companies have been accused in the past of externalizing costs of mines' closure by abandoning the extraction site and by holding the State responsible for covering all the expenses related to the process of closure.

In sum, however, always more businesses have begun to embrace corporate responsibility, recognizing its positive effect on the bottom line. As noticed by Preston and O'Bannon (1997), the causation may run in both directions which means that there may be a simultaneous and interactive

impact of both variables (CSP-CFP), forming what Waddock and Graves (1997) called 'a virtuous circle'. In other words, higher levels of financial performance lead to higher levels of social performance, *ceteris paribus*. Hence, we assume that profitability in one time period may have positive effects on discretionary projects that include environmental and social investments, subsequently.

From *slack resources theory* perspective, it means that the availability of slack resources ("potentially utilizable resources that can be diverted or redeployed for the achievement of organizational goals" – George; 2005) strongly influence the way the corporations address stakeholders' needs (Preston *et al.*; 1991) and determines investments in social and environmental performance domains. According to Zhong (2011), these resources act as a buffering mechanism to counter threats and also as a facilitator to exploit opportunities. For Waddock *et al.* (1997), in hypothesis of slack resources' accessibility, better CSP arises from the way these resources are allocated in specific domains, and thus higher level of CFP predicts in some way a better *corporate social performance*. That is, organizations with higher revenues are expected to spend more resources on "doing good by doing well". Similarly, firms with less financial resources are believed to possess less ability to make discretionary investments in various CSR activities and, generally, are less likely to engage in socially responsible corporate behavior (Orlitzky *et al.*; 2003). It follows, that "firms whose financial performance is so weak that they risk suffering serious losses and jeopardizing shareholder value may be less inclined to meet even the minimum threshold of socially responsible behavior as the firms whose financial situation is stronger" (Campbell; 2007). Moreover, the management literature seems to agree that smaller, less visible companies are subject to a lower level of scrutiny from external agents (Jensen *et al.*; 1990; Brammer *et al.*; 2006) and, thus, are less motivated to innovate and invest in CSR than large companies.

Some authors hypothesized that *corporate social performance* is both a predictor and consequence of *corporate financial performance* (McGuire *et al.*;

1990; Waddock *et al.*; 1997). Clearly, most of the scholars seem to agree that the association between both variables is positive, but the strength of this relationship changes as the industry varies. The relationship between CFP and CSP is, thus, contingent on situational, industry-specific factors that become difficult to detect with means of traditional analytical approaches. For example, some studies rated considerably low (in terms of *corporate social performance*) the mineral extraction or pharmaceutical industries despite high incomes in both sectors. Interestingly, these evaluations were made in reference to industries where competition is virtually nil (i.e. monopoly, oligopoly) – context where the customers and suppliers have few if any alternatives and, on the other hand, state regulations and capacity of external actors (i.e. environmentalists, consumers, unions) are weak. Exactly for this reason, a number of economists have claimed that, the state should better regulate corporations in order to mitigate some of the market failures and negative spillovers in terms of corporate sustainability (Friedman; 1962; Campbell; 2007).

In reference to the mineral extraction industry, Tilton (1992) noticed that in order to sustain the benefits of mining a portion of the revenue must be re-invested in activities that would be beneficial for local communities and their territory (i.e. social infrastructure, electric-power systems, sanitation systems, education, trainings). Ideally, the executives in mining should actively address social and environmental issues even at the expense of reduction in profits distributed among shareholders and managers (Bowman; 1977). ‘Business exposure’ of the extraction industry, as broadly explained in the introduction, pushes mostly large organizations towards more innovative patterns of social investment, even if several concerns are being raised whether enough and the right people (and not only a small elite) benefit from organizations’ CSR activities and whether the projects are being run in a sustainable manner (Claasen *et al.*; 2012). As a result, it remains a mystery to what extent the diamond-mining companies are really beneficial for vulnerable stakeholders groups, including civil society and environmental groups. The situation is aggravated by the fact the actors operating in the

diamond sector are only transparent about scrupulously selected issues, being consequently accused by public agenda of 'green-washing' their reputation in order to protect their legitimacy and ensure future profits (Hamann *et al.*; 2004).

The objective of this chapter is, thus, proving or disapproving the hypothesis of positive link between financial performance (expressed by revenue and ROA) and investments in CSR in the diamond sector. Particularly, exactly like other empirical studies on *corporate social performance*, we focus on a specific area of social performance (SP) - on social investments (the only data included in all corporate annual reports) - as constructing a truly representative CSP measure is commonly considered extremely complex and difficult (i.e. access to the information, timing necessary for the data collection). The term of social investment indicates an investment in corporate governance activities aimed at solving societal problems, creating societal opportunities and empowering future-oriented relationships with local communities (i.e. professional staff development, charity work, health and safety programs, labor rights support, access to fresh water, education, local infrastructure). Thus, we want to verify if greater revenues translate into greater social expenses (hypothesis 1). Secondly, we want to test the correlation between ROA and social investments, in order to see if major profitability encourages the diamond-mining companies to donate a higher percentage of their profits for charitable purposes (hypothesis 2). Finally, we want to verify if the percentage of profits going to cover social expenses is the same for large and small/medium sized mineral developers (hypothesis 3).

#### ***4.1. Size and Revenue Effect on CSR***

While the effect of the revenue on investments in *corporate social relationship* (CSR) has been widely studied by the slack resources theory literature, the relationship between size and corporate social performance



(CSP) is a relatively unexplored. The assumption, at this point, is that size reflects and embodies a diverse range of corporate attributes (Brammer *et al.*; 2006). Generally, in the actual scholarship prevails the belief that bigger companies invest more in CSR activities, as they have more financial resources and they have a greater visibility. Brammer and Millington (2006) noticed that, in common with the economics literature, the social issues in managerial studies highlight the “role of visibility as an antecedent of a range of organizational behaviors that arise primarily because more visible organizations are subject to a higher level of scrutiny from external agents”. As the firm’s size is typically used as the measure of its visibility – or better, its ‘exposure’ as claimed by Miles (1987), the recent scholarship attributes greater administrative innovativeness in terms of *corporate social relationship* (CSR) activities (Bowen; 1999; McElroy *et al.*; 1985; Adams *et al.*; 1998) to larger, more visible companies.

Moreover, some scholars argue that organizational size is positively correlated with organizational power (Meznar *et al.*; 1995), even if the issue here is how this power is actually being used to address social and environmental concerns (evaluation of corporate performance in non-financial areas). In fact, the issue of power is important exactly because it affects the character of the relationship established between the society and the organization. From the structural perspective, it springs from organizational structures that include resources and interconnections between corporate positions and diverse stakeholders groups rather than from the actions of single executives (see also Cendon *et al.*; 2001). In fact, in large companies embedded in policy networks, hierarchy or monocratic leadership is less significant, if not absent (Van Kersbergen *et al.*; 2004) and therefore more inclusive, participatory behavioral models are promoted. At this point it becomes evident that measuring corporate power only with organizational size is an extremely approximate, simplified and, as noticed by Bowen (1999), “unsatisfactory” technique.

Among already discussed motivations that drive large organizations CSR choices - greater visibility, more articulated claims made by diverse

stakeholders groups and insufficiency of full legal compliance, the literature mentions also the need of obtaining cognitive, relational and moral legitimacy and gaining additional social license-to-operate as a valid reason. In short, an organization is considered legitimate if it acts in respect with societal expectations and perceptions that the society has regarding the organization, cultivating at the same time mutually beneficial relationships. An additional social license-to-operate (SLO), on the other hand, exists when a mining project is believed to have the broad and continuous society's acceptance and approval to run and develop its activities (Joyce *et al.*; 2000; Prno *et al.*; 2012). In coherence with Claasen and Roloff (2012), we posit that large companies necessitate stakeholders' trust and acceptance as they ascribe and deny legitimacy, whereas the companies themselves can influence legitimacy and social license-to-operate (SLO) by adhering to legal frameworks, empowering their credibility, building engagement platforms, developing appropriate behaviors and by day-to-day channel commitment addressing social and environmental issues. Moreover, large companies (controlling a number of exploration sites) are particularly interested in reducing social risk and risk of community conflict with means of formal (face-to-face agreements) and informal (satisfying society expectations embedded in wider cultural norms) activities (Prno *et al.*; 2012). By contrast, Lynch-Wood and Williamson argued that small and medium-sized companies (so-called 'junior exploration firms') rarely embrace the philosophy of social license-to-operate (SLO), due to the lack of societal and market-driven pressures typical for larger organizations. Thus, what changes is the degree to which a mineral developer matches a community's perception of sustainability and the extent to which it embraces community participation approaches (transactional, transitional and transformational forms) (Bowen *et al.*; 2010).

In addition, studies of firm *corporate social responsibility* revealed that larger corporations are more likely to have specialized and bureaucratic administrative structures that facilitate greater social responsiveness and, thus, empower more innovative patterns of social and environmental investment. It can be partially explained by the fact that large companies

possess meaningful financial resources and they better recognize the importance of CSR as a competitive advantage. In other words, when profits and financial resources are high, executives are able to provide a part of funds (slack resources) from which to resource discretionary activities, better answer to stakeholders' claims (McGuire *et al.*; 1988) and guarantee a sustainable approach to mining activities since the first stages of exploration until post-mine closure (McAllister *et al.*; 2010). Moreover, financially healthy corporations are also less likely to be subject to pressures from creditors (i.e. banking institutions) and, thus, meet stakeholders' obligations more easily. For example, those corporations are more inclined to invest in charitable contributions with objective to improve external perceptions of the organization, persuade external decision makers and mitigate the risk of regulatory policies that may negatively affect the corporate governance (Brammer *et al.*; 2006). At the other extreme, when the profitability is low the executives try to give priority to creditors and shareholders' claims. Indeed, business literature confirms that in periods of low profitability and high competition some large organizations adopted some unethical behaviors in order to survive, despite risking negative publicity and discriminatory purchasing behaviors. Nevertheless, recent evaluation of socially damaging externalities by more and more frequent controls executed by governments, supra-national organizations and NGOs, discouraged unethical corporate behaviors of some mineral developers.

Thus, the scholars studying the link between the firm size and social investments (i.e. philanthropic expenditures) seem to agree that both variables are strongly correlated (McElroy *et al.*; 1985; Adams *et al.*; 1998; Brammer *et al.*; 2008). In the introduction we have already showed that large diamond-mining companies adopt more frequently highly complex and articulated reporting systems as also a variety of so-called voluntary initiatives, whose objective is to improve organizations' social, environmental and human rights' record (Utting; 2005). Particularly, we highlighted two important issues: first, only 25% of companies release information regarding their CSR activities; second, there is a significant qualitative gap in reporting

systems of large and small companies. It confirms previously cited claim by Brammer and Millington (2006) that large businesses with high exposure are more inclined to invest in influencing corporate perceptions. At this point, we argue that diamond-industry level factors like corporate reporting quality may play a significant role in stimulating greater innovativeness in CSR but only among companies with similar characteristics and relatively big dimensions. In fact, the big players operating on the market developed advanced reporting systems and they are strategically motivated in doing so. Small diamond companies, on the other hand, usually limit their CSR activities to simple adherence to national and global regulations and to modest philanthropic gifts, mostly due to the lack of financial resources to donate. Importantly, artisanal miners, who struggle with defining social and environmental standards in their mining operations, constitute a part of these diamond sector operators. In helping them, organizations and governments operating under the leadership of Diamond Development Initiative (DDI), commit to promote and provide a unique, transparent, independently verifiable system of standards, offering opportunities for better government oversight of artisanal producers and greater security in the sector. For example, in June 2012 DDI along with World Bank's Communities developed a program summarizing ideas on new regulatory structures, artisanal mining sector formalization, environmental protection, property rights and, generally, social welfare.

#### ***4.2. Diamond Industry Study Case: Quantitative data analysis***

Strategic managers working for mineral-extraction companies are continuously facing decisions of how to allocate financial resources and how many of these resources should cover social expenses. As recalled by Waddock (1997), decisions on financial resources allocation “have always been complex, but now they are even more so, since companies are assessed not only on the financial outcome of their decisions but also on the ways in which their companies measure up to a broader set of societal expectations”.

From the scholarship perspective, a further evaluation of these efforts has been widely recognized as problematic (Griffin *et al.*; 1997). First of all, the literature is inconsistent when it comes to financial performance measurement (i.e. net income, revenue, earnings per share, return on assets, return of equity, return to investors, return on sales, earning per share) and in the way social expenses are evaluated. Specifically, corporate social investment is a multidimensional construct, with behaviors that go across a wide variety of inputs (i.e. investments in infrastructure), outputs (i.e. charity programs and community relations) and internal CSR processes (i.e. workers training and education), which makes the assessment of these efforts extremely complex. Secondly, capturing the essence of this study is extremely challenging due to the lack of fully reliable data on both: financial performance and social investment. In fact, the methodology of collecting the necessary information (revenue, ROA, social investments) was based on the content analysis of documents (i.e. sustainability reports, financial disclosures) and sources like Bloomberg database.

The basic idea of this study stands in analyzing if revenue and profitability have a positive effect on social investments made during the year that follows. Specifically, we expect to confirm the basic assumptions of the slack resources theory. In doing so, we use financial data of nine diamond-mining companies for years 2009 – 2013 and information regarding social expenses for years 2010 - 2014. Subsequently, we want to verify Claasen and Roloff's (2012) concern that large companies efforts are believed to be a “proverbial drop in the ocean”. In doing so, we decide to study the effect of size and use it as an independent variable in regression analysis.

Based on the theoretical framework, following hypothesis were developed:

**H1:** There is a significant relationship between social investments and firm revenue.

**H2:** There is a significant relationship between social investments and ROA.

**H3:** There is a significant relationship between social investment and size.

The collected data:

YEAR (REVENUE)	REGRESSION R-SQUARE	P-VALUE
2009	0,7667	0,00437
2010	0,839	0,00137
2011	0,494	0,052
2012	0,8105	0,0009
2013	0,856	0,0035

YEAR ROA	REGRESSION R-SQUARE	P-VALUE
2009	0,266	0,19
2010	0,004	0,0028
2011	0,097	0,6494
2012	0,029	0,6598
2013	0,0226	0,6989

YEAR S.E	REGRESSION R-SQUARE	P-VALUE
2009	0,7048	0,1604
2010	0,3353	0,4209
2011	0,1032	0,678
2012	0,453	0,3266
2013	0,404	0,2235

YEAR S.E	REGRESSION R-SQUARE	P-VALUE
2009	0,9977	0,0023
2010	0,9814	0,009
2011	0,9356	0,007
2012	0,74	0,061
2013	0,65	0,09

### **4.3. Initial Results and Discussion**

This section presents the results of the analysis performed on the data collected on nine diamond-mining companies (representing more than 20% of the formal market) to test three hypothesis using statistical tools. By calculating the correlations between the variables, we managed to see whether there is any relationship between variables summarizing firms' financial performance (profitability and revenue) and social investments. Subsequently, we introduced the size as an independent variable in order to verify if large companies invest proportionally more than small and medium-size diamond miners. It needs to be pointed out that several scholars have found contradictory results on this relationship and, underlined that the relationship nature changes among industries (Griffin *et al.*; 1997). Thus, focusing on a single sector allows enhancing internal validity, studying the degree of activism in a specific context and, finally, recognizing specific patterns of social performance that may characterize only a given industry (industry-specific patterns).

Our sample is composed of nine firms within the same sector that are subjected to broadly similar regulatory constraints, stakeholder activism and enforcement policies. Particularly, four of them are large (>5.000 employees) and highly visible diamond-mining companies, already evaluated and present in global sustainability rankings. The distinction between large and small-medium sized companies will serve us later to analyze if bigger organizations' efforts are greater than the ones of smaller companies.

Initial results indicate that the first hypothesis (**H1**) evaluating the link between revenue and social investments in a specific year is confirmed by the statistics (p-value is always lower than 0,05), and is aligned with what we would expect following basic assumptions of the slack resources theory. Despite some scholars (Hunt; 2000; Seifert *et al.*; 2004) mentioned how soaring revenues in some industries translated into felling corporate philanthropy during the 1990s, slack resources theorists state that better

financial performance potentially translates into the availability of slack resources that provide the opportunity for the organizations to strategically invest in social performance domains (Waddock *et al.*; 1997). In other words, dominant claim is that more the company earns, more it can donate, as also, more it enhances a better public image as a 'socially responsible leader' (Waldman *et al.*; 2008) more it can attract investors that place a premium on sustainability.

By definition, the concept of responsibility lies on obligations and accountability (Seifert *et al.*; 2004) and, thus, large mining companies are particularly expected to be more efficient and innovative in managing new patterns of social contracts evolved from the revolution of rising expectations and rampant entitlement mentality (see also Buchholtz *et al.*; 2008). The evaluation of this claim occurs with means of qualitative analysis of existing documents (i.e. annual financial and sustainability reports) providing relatively accurate information regarding differences in social investments and general corporate engagement between best performers and businesses with lower revenues. In fact, we argue that better is the firm's financial condition, more it invests in innovative social programs and better it can address social needs and expectations. Specifically, our analysis suggests that better financial performance (in terms of revenue) leads directly to greater firms' capacity of response and reaction, which at that time may potentially translate into more articulated and innovative solutions to social and environmental issues. Finally, recalling the idea of 'responsiveness' suggested by Miles (1987), we argue that diamond mining companies with substantial revenues better manage their external affairs strategy (a function of top management philosophy) and their external affairs design (a function of business exposure) in relation to firm's investments in social issues.

Further results of our analysis, however, raised an intriguing point. While in the past scholarship the correlations between revenue and social expenses (**H1**) and ROA and social expenses (**H2**) have been both either positive or negative, surprisingly in this research only the first hypothesis has been accepted. In attempt to find a valid explanation for such result, we explored the



recent scholarship regarding CSR practices and investments in the diamond sector. In doing so, we concentrated on findings of Claasen and Roloff (2012) who acknowledge that despite engagements in CSR in the diamond mining industry have evolved over time, there are still a lot of concerns regarding the depth of CSR adoption and how CSR practices have been actually integrated in core business activities and decision-making processes. Specifically, their analysis of 42 semi-structured interviews revealed numerous concerns whether the diamond mining companies were doing enough to solve some of the most important social/environmental issues. General feeling was that the corporations could do more and that their efforts were not satisfactory for both local communities and NGOs. In this sense, our finding (refusal of **H2**) may be interpreted as a confirmation of such claim. More precisely, we argue that social expenses are covered by a flat percentage of firm's revenues, the percentage that doesn't increase exponentially, however, in hypothesis of soaring profits. In other words, a greater profitability doesn't necessary translate into firm's greater effort in terms of social investments.

Finally, by introducing the firm size as an independent variable (**H3**) we wanted to verify if the small and medium size mining companies' approach towards social investment is similar or rather divergent to larger organizations' one. In fact, the test showed that firm size influences the way the companies act in terms of social investments. Firstly, our result confirms Brammer and Millington's (2006) claim that larger businesses with high exposure are more inclined to invest in influencing corporate perceptions. Conversely, as already stated by Jensen et al. (1990), smaller, less visible organizations are less motivated to invest in CSR as they are subject to lower level of scrutiny from external agents. In fact, national regulations have been traditionally less demanding when it comes to the social impact assessment required for the small-scale diamond-mining companies applying for new licenses or renewal of the old ones. Secondly, we recognize that small businesses lack substantial resources necessary for a successful social investing (capabilities, information systems, culture and financial assets) (see also Orlitzky *et al.*; 2003). In fact, excessive jeopardization of shareholder value – typical for smaller, less profitable organizations, usually translates into poor ability to make

discretionary investments in various CSR activities. Thirdly, we argue that smaller companies are also less successful in empowering innovative engagement platforms and in designing articulated CSR strategies as the qualitative analysis of corporate reports has shown. Specifically, small mining companies usually place their commitment into sporadic charitable giving and philanthropy (generating much confusion in CSR objectives formulation) rather than into well-conceived strategic vision of CSR. Additionally, the lack of consistency in corporate self-regulatory systems discourages activities that engage the largest group of internal stakeholders -firms' employees (i.e. career planning and trainings, improvement of labor remuneration systems, medical and recreational facilities).

## ***5. Conclusions***

Our analysis of the diamond sector suggests that corporate social responsibility is playing an increasingly significant role in mining companies' narratives and practices, all the more so in the global market context. Clearly, as 21st century is witnessing the cycle of an explosion, fragmentation and rationalization of CSR standards in globalized economies (Horrihan; 2010), supra-national and intergovernmental initiatives (i.e. UN or World Bank initiatives), are no longer sufficient in monitoring and evaluating the ethical outcomes of diamond-mining activities (Bridge; 2004; Prno; 2013). Accordingly, in the last 10 years non-governmental organizations and the companies themselves have actively promoted and formalized initiatives embedded in the logic of a 'non-state market driven governance'. Those include ground-breaking CSR frameworks that, in attempt to solve the problem of non-harmonized corporate reporting, enhanced the universalization of standard-setting flows on to gathering, disclosure and verification of data (Horrihan; 2010).

Even if enhancing new requirements for CSR-sensitive disclosures (in virtue of the need for modern regulatory regimes for investment decisions, corporate reporting or stock exchange listing conditions) has become a

priority in some industries, this research shows that in diamond sector (accused by public agenda for implementing oligopolistic practices and unclear pricing policies) there is still a lot of resistance to corporate reporting harmonization. Moreover, some critics raised from the recent scholarship regard the real motivations that stand behind the reporting systems, and CSR in general. For example, Hamann and Kapelus (2004) question whether the diamond companies use CSR for 'greenwashing' their reputation rather than for value creation. The authors continue: "critics argue that CSR is primarily about projecting a suitable image in order to placate critics and ensure business as usual".

After having examined digital archives of 39 major diamond companies we conclude that only 25% of those release CSR-sensitive data (i.e. ethical conduct, social investments, health and safety systems, training spend, staff turnover, retention, security management, stakeholder engagement, water and energy usage, carbon emissions, mines' closure policies) under the form of media for social and environmental disclosure (i.e. annual reports, articles published detailing companies' activities, websites, press releases, community reports, environmental reports, booklets addressing the social and environmental activities of the company). 75% of the diamond companies, on the other hand, hide themselves behind the veil of secrecy. Not surprisingly, the diamond industry is struggling more with the public opinion's concerns over environmental and social performance, rather than over issues over the product pricing, quality and safety (Jenkins et al.; 2006). Interestingly, also funding agencies, private banks, commercial banks, regional development banks, providers of risk insurance have an increasing reason to evaluate and monitor ethical outcomes of the projects in which they invest (Warhurst; 2004). The future challenge is, thus, to promote the integration of various sustainability issues into reporting systems, even though social and environmental reports do not yet have definite rules concerning their form, structure and content (Jenkins et al.; 2006).

New imperatives of CSR, springing from the revolution of rising stakeholders' expectations, globalization mechanisms, ineffectiveness of public courts and the entitlement mentality (Richman; 2004; Buchholtz et al.; 2008),

brought to the extension of classical model of CSR that is traditionally articulated in three elements: legal responsibilities (observance of legal restraints, fulfillment of contractual obligations, adherence to all regulations), economic responsibilities (profitability, dividend policies, tax paying) and philanthropy (corporate contribution to provide support to the community). In this sense, the recent conceptualization of Corporate Social Responsibility (CSR) is also a 'story of progressive business sensitization to systems of governance beyond government, regulation beyond law and responsiveness beyond formal responsibility' (Horrigan; 2010). Now that international institutions, local governments, NGOs and aboriginal peoples inevitably position themselves as participants in remodeling the balance of power with their regulatory attempts (Harribey; 2011), the companies became global citizens actors in society. According to Crane et al. (2008) it means that the firm contributes to the life of the civil society and functions as a citizen, citizenship administrator and, finally, as a citizenship arena for stakeholders.

In the mining industry structural changes have led to major access to new territories for exploration, facilitated by the liberalization of mining regulations generating intense corporate-community disputes (Jenkins et al.; 2004). In fact, global mining companies had to recognize newly empowered stakeholders and, consequently, to accommodate interests of both the organization and its stakeholders (i.e. indigenous peoples). In the following dissertation we examined different studies on how the diamond mining companies actually embed the 'corporate citizenship' imperative into their policies, concluding that despite unquestionable progress recently made, the diamond-mining companies are generally not successful in balancing the diverse demands of stakeholders with the logical need to make profit. With means of quantitative research we also proved that large companies do not invest proportionally more (despite their resources and capabilities) than small diamond-mining companies. Interestingly, our discovery confirms Claasen and Roloff's (2012) claim that in the diamond industry, large companies could do substantially more. Specifically, their analysis of 42 semi-structured interviews revealed numerous concerns whether enough and the right people benefited from the projects (stakeholders felt that the poorest

people are usually being overlooked) as also whether De Beers-controlled Namdeb distributes the benefits from mining in a socially acceptable manner.

Finally, our study generated a myriad of concerns regarding the way the diamond-mining companies innovate their Corporate Social Responsibility (CSR) practices. Generally speaking, the diamond-extraction companies are still being criticized for the secrecy lingering in the industry, exploitation of workers and the natural environment, corruption, while managerial practices struggle to effectively address such issues. The major lesson learned from this study is that the organizations can minimize the risk of jeopardizing their reputation and losing their legitimacy (cognitive, rational and moral) by implementing more pro-active practices to CSR. It entails breaking with traditional defensive CSR patterns, where once compliance requirements (i.e. legislative pressures) are satisfied, the companies have neither interest nor resources to invest in more innovative CSR programs. Within this perspective, the organizations empower initiatives that catalyze social and/or environmental transformation only in presence of stakeholders, who possess attributes of power (legal, financial, media, ethical), legitimacy and urgency of claim (Prno et al.; 2012). Contrarily, pro-active CSR is associated with more innovative, participatory and future-oriented CSR policies, applied and required by the whole value network rather than only by a single firm. We argued also that such approach may have positive effects on the bottom line, legitimacy, social license-to-operate as on the competitive advantage.

From the operational perspective, integrating business and stakeholders' needs requires, however, more than good intention and strong leadership (Porter et al.; 2006) – continuous adjustments, reporting system development and incentives to more inclusive culture are required. As underlined by Porter and Kramer (2006), it's also about choosing on which environmental and social issues to focus on. In fact, pro-active CSR encourages the companies to apply highly articulated selection processes 'moving' parallel with firms' competitive strategies.

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