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Communication at the Edge: Voluntary social and environmental reporting in the annual report of a legitimacy threatened corporation

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ABSTRACT

This paper examines the voluntary social and environmental disclosures made in the annual reports of Rothmans Ltd between the years of 1955 and 1999. The first part of the paper focuses on defining legitimacy theory as it has been used in accounting research and discusses the potential of a resource based approach to testing the theory. The study then considers legitimacy theory in light of the disclosures made by Rothmans. An initial qualitative analysis certainly provides examples of expected attempts to legitimatize the corporation given the threat posed by the smoking and health debate. Initial quantitative findings contradict those expected when compared to previous studies. However, it is concluded that when the fairly extreme circumstances faced by the tobacco industry are taken into account, legitimacy theory does provide a good explanation to both the nature and amount of the disclosures observed.

INTRODUCTION

In the effort to understand the motivation of corporations in providing voluntary social and environmental disclosure a number of theories have been employed. This paper continues this theme of research through a longitudinal case study conceived as a test of Legitimacy Theory as it has been described in accounting research. Instead of focusing on a range of organisations and industries, the examination of a single company compliments previous broader based studies. This may mean the findings loose some of their 'generalisability', but it also allows for a much richer analysis. Despite the potential for Legitimacy Theory to explain a broad range of corporate behaviour, there has been relatively little research to date into Legitimacy Theory except in the context of environmental disclosures.

It has been said that the best way to know someone is to see them under stress; in much the same way, in science it is often the extreme that help us understand the mundane. Focusing on the voluntary social disclosures made in the annual reports of a publicly listed Australian tobacco corporation, an organization that has faced increased government regulation, heightened community hostility, and threats to its income stream and long term survival, provides the potential to observe Legitimacy Theory in action under extreme conditions.

The paper starts with a discussion of the definition of Legitimacy Theory employed. There follows a brief discussion of the tobacco industry in the context of an increasing threat to its organisational legitimacy. Longitudinal context analysis techniques and statistical correlation are then used to examine the nature of disclosures and how they have changed over time. These changes are interpreted in the context of a Legitimacy Theory grounded explanation, to establish whether for this organisation the theory can provide a good fit for the observations.

The paper is not intended to address the ethical or health issues associated with the tobacco industry. Instead it provides an opportunity to focus on the appropriateness of Legitimacy Theory for understanding the nature of the annual report, and to further develop our understanding of accounting as a communicative practice.

This research adds to existing literature in three ways. First, the study looks at a range of social disclosures, not just the environmental disclosures that have been the traditional focus of such research, to test for legitimacy motives for disclosure in the annual report.

Second, the explicit focus of this research is a firm at the very 'edge of societal legitimacy'. This will provide much richer data than in many previous studies. Third, the tobacco industry has been seldom examined by accounting academics (other than a recent paper by Campbell *et al.* (2003) discussed later). Further examination of this significant (in terms of both economic and political power) industry seems warranted.

LITERATURE REVIEW

AN OVERVIEW OF LEGITIMACY THEORY

"***Legitimacy** is a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions.*" (Suchman, 1995, p. 574, emphasis in original)

One of the problems of legitimacy theory has been that the term has, on occasion, been used fairly loosely. This should not be seen as a problem of the theory itself and the observation could be equally applied to a range of theories in a range of disciplines (see for example Caudill (1997) on the abuse of Evolutionary Theory). A failure to adequately specify exactly what is being considered has been identified by Suchman (1995, p. 572, emphasis in original), who observed that "Many researchers employ the term *legitimacy*, but few define it". Hybels (1995, p. 241) comments that "As the tradesmen [sic] of social science have groped to build elaborate theoretical structures with which to shelter their careers and disciplines, legitimation has been a blind man's hammer." Legitimacy theory does provide the foundation for this paper, and in an attempt to address some of these concerns of 'fuzziness' a definition of the legitimacy theory being examined will now be provided.

There are in fact a number of layers to the theory which need to be examined. These are graphically presented in *Figure 1* on the following page. The macro theory of legitimation, known as Institutional Legitimacy Theory, deals with how organisational structures as a whole (business for example, or the government) have gained acceptance by society at large. "Within this tradition, *legitimacy* and *institutionalization* are virtually synonymous. Both phenomena empower organizations primarily by making them seem *natural* and *meaningful*" (Suchman, 1995, p. 576, emphasis in original). This conception is not unproblematic. It takes legitimate institutions to create legitimacy. This creates a 'chicken and egg' paradox, i.e., which came first, the institution or legitimacy. This however is not an issue this paper can address (this problem is explored by Hybels (1995, esp. p. 241)). In terms of accounting research given the time frames and questions generally being considered to take the current business environment, including capitalist structure, type of government, etc. as a given, a static context within which the research is situated.

Insert Figure 1 about here

One step down from the Institutional Level is what in *Figure 1* is called "Organisational Legitimacy" (sometimes referred to as Strategic Legitimacy Theory or Instrumental Legitimacy Theory, see Driscoll and Crombie (2001)). "Underlying organizational legitimacy is a process, legitimation, by which an organization seeks approval (or avoidance of sanction) from groups in society. Legitimation may be necessary to ensure an organization's continued existence" (Kaplan and Ruland, 1991, p. 370). It is from this level that most accounting research tends to draw its understanding of legitimacy (although in a moment we will see one final layer of resolution that is useful to consider). Mathews (1993, p. 350) provides a good definition of legitimacy is at this level:

> Organisations seek to establish congruence between the social values associated with or implied by their activities and the norms of acceptable behaviour in the larger social system in which they are a part. In so far as these two value systems are congruent we can speak

> of organisational legitimacy. When an actual or potential disparity exists between the two value systems there will exist a threat to organisational legitimacy.

At its simplest, within the Organisational view "legitimacy [is] an *operational resource* ... that organizations extract - often competitively - from their cultural environments and that they employ in pursuit of their goals" (Suchman, 1995, p. 575 - 6, emphasis in original). Legitimacy, just like money, is a resource a business needs to operate. Certain actions and events increase that legitimacy, and others decrease it. Low legitimacy will have particularly dire consequences for an organisation, which could ultimately lead to the forfeiture of the right (or licence) to operate.

This simple view deserves to be further developed. Although we can describe a firm as being legitimate, and conceive of levels of legitimacy, it becomes a very subjective exercise to try and directly measure legitimacy. This is because although it has concrete consequences, legitimacy itself is an abstract concept, given reality by multiple actors in the social environment. For a researcher to try and directly establish, or even rank, the legitimacy of various organisations (called 'Moral Legitimacy' by Suchman (1995, p. 579)) would seem to be a necessarily subjective undertaking, preferencing the researcher's own views. As Hybels (1995, p. 243) argues, "I reject this view because it is based on a conflation of the roles of observer and participant in social science".

As an alternative, rather than trying to subjectively measure a firm's legitimacy directly it can instead, arguably more objectively, be inferred from the fact that being legitimate "enables organizations to attract resources necessary for survival (e.g., scarce materials, patronage, political approval)" (Hearit, 1995, p. 2). Hybels (1995, p. 243) develops this in some detail:

> Legitimacy often has been conceptualized as simply one of many resources that organizations must obtain from their environments. But rather than viewing legitimacy as something that is exchanged among institutions, legitimacy is better conceived as both part of the context for exchange and a by-product of exchange. Legitimacy itself has no material form. It exists only as a symbolic representation of the collective evaluation of an institution, as evidenced to both observers and participants perhaps most convincingly by the flow of resources. … resources must have symbolic import to function as value in social exchange. But legitimacy is a higher-order representation of that symbolism – a representation of representations.

Hybels (1995, p. 243) argues that good models in legitimacy theory must examine the relevant stakeholders, and how "Each influences the flow of resources crucial to the organizations' establishment, growth, and survival, either through direct control or by the communication of good will". He identifies (p. 244) four critical organisational stakeholders, each of which control a number of resources. These are summarized in *Table 1* below.

Insert Table 1 about here

The last of these has received considerable attention. The power of the media has been noted by a number of researchers, including Patten (2002, p. 153), who states "that while increased media attention can certainly lead to the potential for increased pressures from any of the three sources [dissatisfaction of public; new or proposed political action;

increased regulatory oversight], increases in pressure can also arise, particularly with respect to regulatory oversight."

Companies try to manage their legitimacy because it "helps to ensure the continued inflow of capital, labour and customers necessary for viability… It also forestalls regulatory activities by the state that might occur in the absence of legitimacy... and pre-empts product boycotts or other disruptive actions by external parties... By mitigating these potential problems, organizational legitimacy provides managers with a degree of autonomy to decide *how* and *where* business will be conducted" (Neu *et al.*, 1998, p. 265). This is significantly different from the view of Stanton and Stanton (2002, p. 491) who think that legitimacy theory is "corporations [being] controlled by community concerns and values".

Thus instead of trying to directly measure legitimacy, it has been argued that it can be measured in terms of the resources relevant stakeholders provide. A problem with this view needs to be acknowledged. If it is argued that a decrease in legitimacy will lead to a reduction in the flow of resources to the company, and at the same time the resources available to the company are used as a measure of its legitimacy, then this is obviously a circular argument.

- *Hypothesis: Reduction in Legitimacy Reduces Resource Flows to Organisation*
- *Where: Legitimacy is Measured in Terms of Organisational Resource Flow*
- *Therefore: Replace Legitimacy with its Definition*
- *Hypothesis: Reduction in Organisational Resource Flow Reduces Resource Flows to Organisation*

To overcome this problem researchers have tended to implicitly look for circumstances that (drawing on the definition of legitimacy given by Mathews (1993) cited earlier) create an obvious disparity between the firm and the expectations of society. An example is the case of the Exxon Valdez Oil Spill (Patten, 1992). As Deegan *et al.* (2002, p. 319) have observed "when significant events such as a major environmental disaster occur, or when there is sustained mass media interest, then it is reasonable to assume that most managers would perceive that the organisation's ongoing legitimacy is threatened". This begins to look a lot like Moral Legitimacy which has already been criticised in this paper, but what is needed (and perhaps hasn't been done enough yet) is to examine more of these events and measure their effects on resources.

As shown in *figure 1* there is a final level of resolution within Legitimacy Theory that is simply a refinement to Strategic Theory. At this level the theory suggests that a firm will go through various phases with regard to its Legitimacy. There are four generally accepted phases within the process of Strategic legitimation.

Establishing Legitimacy This first phase represents the early stages of a firm's development and tends to revolve around issues of competence.

> Competence concerns organizational effectiveness - the ability of a corporation to 'deliver the goods'. A corporation must produce a product or deliver a service that meets with some success in the marketplace; one that does not break even, and hence fails to meet its obligations, understandably loses legitimacy with suppliers, bankers, and customers. Financial viability, however, is not the sole arbiter of competence; more critically, a corporation must meet socially constructed standards of quality and desirability as well as perform in accordance with accepted standards of professionalism (Hearit, 1995, p. 2).

Maintaining Legitimacy "Attempts to maintain legitimacy occur when the organization has attained a threshold of endorsement sufficient for ongoing activity. Maintenance activities include: (1) ongoing role performance and symbolic assurances that all is well, and (2) attempts to anticipate and prevent or forestall potential challenges to legitimacy." (Ashford and Gibbs, 1990, p. 183)

However the maintenance of legitimacy is not as easy as it may at first appear. Legitimacy is a dynamic construct.

> Community expectations are not considered static, but rather, change across time thereby requiring organisations to be responsive to the environment in which they operate. An organisation could, accepting this view, lose its legitimacy even if it has not changed its activities from activities which were previously deemed acceptable (legitimate). Because community expectations will change across time it is argued that the organisation must also make disclosures to show that it is also changing (or perhaps to justify why it is not changing). Changing activities without communicating such changes is considered to be insufficient (Deegan *et al.*, 2002, p. 319 - 20).

Extending Legitimacy. "Attempts to extend legitimacy occur when the organization is becoming established or is entering a new domain of activity or utilizing new structures or processes. Legitimation activities are apt to be intense and proactive as management attempts to win the confidence and support of wary potential constituents" (Ashford and Gibbs, 1990, p. 180).

Defending Legitimacy. "Attempts to defend occur when the organization's extant legitimacy is threatened or challenged. Legitimation activities tend to be intense and reactive as management attempts to counter the threat" (Ashford and Gibbs, 1990, p. 183).

It is this last phase that has tended to be the main focus of accounting researchers and, as mentioned earlier, provides us with an opportunity to examine the crucial link between legitimacy and resources. Even barring a major incident it is likely in the Western Capitalist system that almost every corporation will regularly need to defend its legitimacy, by the mere fact that "corporations must fulfil both a competence and community requirement to realize legitimacy… Satisfaction of stockholder interests often occurs at the expense of community concerns (e.g., the despoiling of the environment, the use of labour) while, conversely, responsibility to the larger community often occurs at the expense of the stockholder" (Hearit, 1995, p. 3).

Social and Environmental Accounting Theory papers focusing (either explicitly or implicitly) on the defence of strategic legitimacy have tended to draw on Lindblom (1994) who identifies four strategies that a company can use to defend its legitimacy:

1. Change itself - The organisation seeks to inform and educate the 'relevant publics' about actual changes within the organisation.
2. Change the Public - The organisation seeks to change the perceptions of the relevant publics, but does not see a need to change its own behaviour.
3. Manipulation - The organisation seeks to deflect attention from issues of concern to other issues. For instance, highlighting links with charity.
4. Misrepresentation - The organisation may go as far as not being totally truthful about its activities that are of concern to the 'relevant publics'.

These last two strategies, which appear to have been particularly relevant to the tobacco industry, are discussed generally in more detail by Ashford and Gibbs (1990, especially p. 180). Also Harte and Owen (1991, p. 59) note "The need for such an enhancement of credibility is suggested by earlier research indicating that social information provided within annual reports tends not to be directly related to quality of actual performance and can indeed by positively misleading".

Some interesting additional observations can be noted particularly in light of their potential relevance to the tobacco industry. Abrahamson and Park (1994, p. 1302) have identified that in terms of the 'negative event' which has led to the threatened legitimacy, at least one (if not both) of the following communication strategies can be expected from management: "First, officers interpret the negative outcomes that they do reveal to shareholders in ways that shift the blame for those outcomes away from themselves", and "Second, officers may conceal negative outcomes entirely."

Hearit (1995, p.6) observes that "re-ligitmation… typically require[s] a dual strategy of a positive and a negative rhetoric. Corporations seek to distance themselves from their illegitimate behaviours and then create identifications with the public values they are reputed to have violated". The paper goes on "One way to deny wrongdoing is through the use of an opinion/knowledge dissociation, which challenges the validity of the charges by redefining them as groundless. Here a company asserts that critics' claims are mere opinions and do not represent fact" (Hearit, 1995, p. 7). He goes on to say that this can be much more effective than a mere denial. Both concealment of negative outcomes and knowledge dissociations have been regular techniques employed by the tobacco industry in dealing with the smoking and health issue (for a very detailed analysis see Pringle (1998)).

LEGITIMACY, ACCOUNTING AND THE ANNUAL REPORT

The link between Accounting Research and Legitimacy Theory revolves around the annual report and related disclosures. Gray *et al.* (1995) discuss the use of this focus on the annual report in some detail and conclude that the focus is justifiable. Their argument is that the annual report is not only a statutory document but is in fact "the most important document in terms of the organization's construction of its own social imagery" (p. 82). The annual report "uses the tools of management, marketing and communication theory to construct a picture of the organisation" (Stanton and Stanton, 2002, p. 478). This 'picture' is viewed by a wide audience and "provide[s] organizations with an effective method of managing external impressions. Annual reports are a primary information source for investors, creditors, employees, environmental groups and the government" (Neu *et al.*, 1998, p. 269). This view is also supported by Mangos and Lewis (1995, p. 56) who state that "corporate social responsiveness as demonstrated within the content of corporate annual reports is both a visible and measurable social influence". They also argue, in terms that could be seen as supportive (or at least suggestive) of Legitimacy Theory, that:

> corporate social responsibility is a form of corporate social responsiveness by the managers of a firm to pressures which they perceive and the managers then attempt to influence the social environment. Managers' accounting choice and literate response in annual report form part of the corporate social responsiveness within the economic activity (Mangos and Lewis, 1995, p. 54)

It must be acknowledged, however, that this focus is not universally accepted. Zeghal and Ahmed (1990, p. 51) have criticised the narrow approach taken by many researchers as their "research indicates that the description provided by the annual reports of social information disclosure by a company may not be complete". They claim that companies use many different media to make disclosures, and the selection of media and message are very targeted. By only focussing on one document source researchers may be drawing incomplete conclusions. Zeghal and Ahmed (1990, p. 39) state that "one cannot judge corporate performance on social responsibility solely on the basis of information disclosed in the annual reports. Social information disclosure may also take place through company staff newspapers, press releases, paid newspaper, television and radio advertising and company brochures". Robertson and Nicholson (1996, p. 1099) also express concern about the focus on the annual report, their concern being that "Cynics of corporate intentions may consider all corporate social responsibility disclosure as 'lip service' or 'window dressing'. Cynicism seems justified when descriptions of corporate social responsibility across a range of annual reports from different companies read as though they were written by the same person, and are so general as to be meaningless."

In terms of Legitimacy Theory, however, the researcher is not assuming any link between the annual report disclosure and actual performance. The annual report is a document where the organisation communicates the information it wishes to have publicly available. "In legitimising its actions via disclosure, the corporation hopes ultimately to justify its continued existence" (Guthrie and Parker, 1989, p. 344). Also, the author acknowledges that examining a range of corporate communications from a legitimacy perspective would be useful, however this paper is intentionally limited in scope.

SOME SPECIFIC STUDIES OF LEGITIMACY THEORY AND CSD

Only a few researchers have specifically undertaken detailed studies examining evidence of the operation of legitimacy theory in the annual reports of companies. Fewer still have used specific measures of resource flows to establish quantifiable measures of legitimacy. The conclusions have been generally (but not always, see below) affirming. One recent study was Neu *et al.* (1998) who examined the disclosures of Canadian mining companies and concluded that "Although organizations utilize a variety of textually-mediated communication media such as brochures and advertising in an attempt to, *inter alia*, sustain legitimacy, the annual report appears to be the preferred method for communicating with the … relevant publics as opposed to the general public" (p. 269). Buhr (1998) examined a 28 year history of the Falconbridge foundry in Canada and its struggles in managing Sulphur Dioxide emissions. She concluded that "an evolution in disclosure [in the annual report] supports legitimacy theory" (Buhr, 1998, p. 186).

In an Australian study (Deegan *et al.*, 2000) five major incidents (including the Exxon Valdez oil spill and the Bhopal Disaster) provided a context in which to examine the annual reports of related (in industrial terms) Australian firms to see if there had been a significant change in their social or environmental reporting. They concluded:

> The results of this study are consistent with legitimacy theory and show that companies do appear to change their disclosure policies around the time of major company and industry related social events. … These results highlight the strategic nature of voluntary social disclosures and are consistent with a view that management considers that annual report social disclosures are a useful device to reduce the effects upon a corporation of events that are perceived to be unfavourable to a corporation's image (Deegan *et al.*, 2000, p. 127).

Two studies have been undertaken into BHP's annual report disclosures. The first is one of the earliest studies into the connection been legitimacy theory and the annual report.

Guthrie and Parker (1989) examined the correlation between specific types of annual report disclosures and a detailed history of significant events at BHP. They concluded that "The evidence examined in this historical case study has failed to confirm legitimacy theory as an explanation of BHP's CSR over time. In general, little correspondence was found between peaks of BHP's CSR disclosures and key socio-economic events affecting BHP during its operating history" (Guthrie and Parker, 1989, p. 350).

This became the trigger for Deegan *et al.* (2002), which given the success of other papers in finding support for legitimacy theory considered "whether there [was] something different about BHP, or whether Guthrie and Parker's measure for community concern was mis-specified" (p. 313). They argued that the original Guthrie and Parker paper (1989), by focusing on historical events without contextualisation of community awareness had not provided a good measure.

To establish community awareness Deegan *et al.* (2002) employed media agenda setting theory, which emphasizes the importance of the media in informing the public about specific issues. This is closely aligned with the importance of the media in the strategic conception of legitimacy theory discussed earlier. A study by Ader (1995), which specifically examined salience about environmental issues, but which has wider ramifications, concluded that "The public needs the media to tell them how important an issue the environment is. Individuals do not learn this from real-world cues" (p. 310). It is also interesting to note that this paper concluded there was not a strong link between actual environmental performance and media interest. Although this paper did not look at how firms reacted to the increased media attention, a number of papers have found a significant and positive relationship between media disclosure (both negative and positive) and both social and environmental reporting. See for example Cormier and Gordon's (2001) study of Canadian utilities type companies.

An earlier paper by Deegan *et al.* (2000, p. 105) had discussed the linkages between Media Agenda Setting Theory and Legitimacy Theory:

> How corporations maintain their legitimacy, perhaps through corporate social disclosure, is influenced by management perceptions of the threats to its legitimacy. The source of these threats to legitimacy can often come from the media … Evidence indicates that management react to adverse media coverage, and use corporate disclosures as a strategy to alleviate the potentially adverse effects caused by negative media coverage.

Based on an examination of BHP's Social and Environmental Disclosure and comparison with newspaper reports Deegan *et al.* (2002) concluded that their results showed that higher levels of the print media coverage were associated with higher levels of specific social and environmental disclosures (and *vice versa*) made by BHP in its annual reports and that management did indeed release positive information in reaction to unfavourable media attention. They conlcuded with the observation that "These results, then, lend support to legitimation motives for a company's social disclosure" (Deegan *et al.*, 2002, p. 333). It is this last study, linking media disclosure with Social and Environmental Disclosure in the annual report which provided the initial inspiration for the current study.

Special mention deserves to be made of Campbell *et al.* (2003), which in many ways presents an antithesis to this paper. A longitudinal study (20 years) of three sectors (including Tobacco) is presented, and whilst similar disclosure patterns to those found in this study for the Tobacco Industry are observed in the English context almost opposite conclusions are reached. "L[egitimacy] T[heory] is difficult to defend as a possible explanation of social disclosure" (Campbell *et al.*, 2003, p. 574). However the conceptualization of Legitimacy

Theory is based on a normative gauge of legitimacy as opposed to a more objective measure as per the work of Hybels (1995) already discussed. This would deal with the concerns of "perceptions" raised by Campbell *et al.* (2003, p. 562). In addition as shown later in the paper the fall in disclosure by the tobacco industry, seen as so damning of Legitimacy Theory is no real surprise and is in fact expected.

THE TOBACCO INDUSTRY AND LEGITIMACY

There can be little doubt that the Tobacco Industry has faced a consistent threat to its legitimacy worldwide since the original negative link was established between smoking and health. The two watershed documents were the 1962 British Royal College of Physicians report and the 1964 Surgeon-Generals Report (USA), which both concluded that cigarette smoking was directly related to Lung Cancer and a number of other diseases. Both received wide ranging publicity, and both had an immediate impact on cigarette sales (Taylor, 1984, see esp. pp. 9 - 11). This was the starting point for an increasing range of legislative measures aimed at regulating tobacco use around the world. In the American context Miles (1982, p. xiii) observes that:

> The smoking-and-health controversy posed one of the most significant threats in the U.S. business history to the well being of an established industry. It exposed members of the domestic tobacco industry not only to an unprecedented wave of unwanted scrutiny and publicity, but to a long and cumulative series of government regulations restricting their ability to do business. It hurt their pocketbooks. It took away their access to the public broadcast media. It put warning labels on their products. It forced them into unfamiliar domains. And it threatened the careers of their senior managers. Just as important, it tarnished their image and wounded their pride.

He goes on to add that "In short, the smoking-and-health controversy amounted to a *legitimacy crisis* of fundamental proportions for the tobacco Big Six" (Miles, 1982, p. xiii, emphasis added). This view is echoed by Davidson (1991, p. 49) who states that "Perhaps no industry has been subjected to such serious erosion of its legitimacy as the tobacco industry". Both Miles (1982) and Davidson (1991) also discuss in a management context the processes by which tobacco companies attempted to meet this threat, within the broad framework of legitimacy, though no mention is specifically made of the annual reports of the companies.

"With the release of the [Royal College of Physicians' and Surgeon-General's] reports on smoking and health, Australian medical and health organisations immediately called for government action" (Quit, 1995, introduction). Australia appeared to follow a very similar path to the rest of the Western world in terms of the legitimacy crises for tobacco companies.

It is not the intention of this paper to provide any sort of extremely detailed historical overview of the tobacco industry in Australia, only to identify some key events that would appear to be threatened the legitimacy of the organisation. However some background information about the company examined in this paper is useful to consider.

Rothmans Holding Limited (also known as Rothmans of Pall Mall), hereafter referred to as Rothmans, was incorporated in Australia in 1955. It was one of a tripartite of firms that dominated the Australian tobacco market (the other firms being W.D. and H.O. Wills, and Phillip Morris) each with about one third of the market. Its Winfield brand came to be the clear leader in the cigarette market during the 1980s and 90s (Quit, 1995, The Tobacco

Industry in Australia). In 1999 Rothmans announced a merger with W.D. and H.O. Wills, which ultimately led to the delisting of Rothmans as a company and the emergence of British American Tobacco – Australasia in 2000. This study only considers the period 1955 – 1999, the Rothmans' years.

METHOD

> Rather than engage in the further development of entirely abstract constructions of the legitimation process, I have advocated focusing on linkages to the concrete details of specific organizational situations. To this end, I have suggested that, to obtain images of legitimation processes, researchers should investigate the flow of resources from organizational constituencies as well as the pattern and content of communications (Hybels, 1995, p. 244)

The remainder of this paper examines the possibility that Rothmans undertook legitimating activities in light of the threat presented by the smoking and health debate. After an initial qualitative examination of disclosures in the annual report, examined in the context of relevant events, a more detailed quantitative analysis is undertaken in the vein suggested by Hybels (1995) above. An examination of Rothmans' annual reports provides details of 'the pattern and content of communications', while an analysis of media attention (and later government regulation and taxation) is used to 'investigate the flow of resources from organizational constituencies'.

ANNUAL REPORT ANALYSIS

The Australian annual reports of Rothmans Ltd (also known as Rothmans of Pall Mall) were gathered for the entire time that the company was listed in Australia (1955 – 1999). They were then read to identify at the sentence level instances of voluntary social or environmental disclosures using an open coding scheme. These disclosures were then sub-classified by nature, as presented in the annual report. Only four categories appeared to be present over the entire 44 years (Employees, Community, Health, and Philanthropy). The distribution of Disclosure (number of sentences) is shown in *Graph* 1 on the following page. The nature of these disclosures will be discussed in more detail in the first part of the results section that follows. Note the spike in disclosure in 1980 can be explained by the fact that this was a special 25th anniversary annual report which was much larger than usual.

Insert Graph 1 about here

MEDIA DISCLOSURE

Determination of the number of articles that were being published on Tobacco/Cigarettes in any given year would appear to be an extremely difficult endeavor. Fortunately the APIAS (Australian Public Affairs Information Service) data base provides an opportunity to overcome this problem. It started (fortuitously given the incorporation date of Rothmans in Australia) in 1955, with the aim of being "a guide to current material on Australian political, economic and social affairs" (preface to the first APAIS volume). The database indexes 'significant articles' on a huge variety of subjects (including Tobacco and Cigarettes) from a range of printed Australian sources, including but not limited to government publications, newspapers, and magazines. Although representing only a sample of Australian sources the database is taken as fairly indicative of the level of media attention given to a specific subject in a given year.

Each year the database was examined using the keywords “Tobacco”, “Rothmans”, “Cigarettes” and “Smoking”. The relevant articles listed were classified as being Industry, Health, or Anti-Smoking Related based on their title and abstract. Please see *Graph 2* on the following page. It should be noted that the range of sources sampled each year changed, so all statistical calculations are based on this information after it has been converted to a percentage of all articles, as opposed to being used in their absolute form.

Insert Graph 2 about here

STATISTICAL ANALYSIS

The question of statistical analysis deserves more attention than it perhaps has received in previous papers. Unfortunately there is not space in this paper for a full discussion of the appropriate statistical techniques to use in Corporate Social Disclosure research. This study is undertaken using exclusively non-parametric statistics. This frees the research from the underlying assumptions associated with parametric statistics, such as the data being normally distributed. Though it may appear that the use of non-parametric statistics is less sensitive to the subtleties data, the reality is the measures of variables employed in Corporate Social Disclosure research are often based on proxies, and are at such a coarse level themselves that the use of parametric statistics delivers a result that only has a veneer of precision. This paper employs Spearman’s Rho (Siegal and Castellan, 1988, p. 235) to identify correlating factors.

RESULTS AND ANALYSIS

QUALITATIVE DISCUSSION OF THE ANNUAL REPORT DISCLOSURES

Before undertaking the quantitative analysis of the annual report disclosures it is worth reviewing briefly the relevant content of the reports. This analysis is in no way intended to be comprehensive but rather to highlight interesting developments in light of legitimacy theory.

Disclosures relating to employees first appeared in 1958 as a separate section and followed a fairly standard pattern most years, generally thanking staff for their commitment, identifying that the company led the way in training, pay and conditions, and often citing good relations between the company and the unions. See *Figure 2* on the following page.

Insert Figure 2 about here

The 1963 social disclosure of a much more general nature (than just employees) appears. Interestingly this is the same financial year as the first major adverse report on smoking and health. A new section was added at the end of the annual report entitled “Helping Australia’s Progress” (pp. 20-22), within this a page was dedicated to “The Company as a Citizen” (p. 22). See *Figure 3* over page. It states that “Participation in many fields of national and civic interest continues to be a feature of activities”, and then goes on to outline the Rothmans University Endowment Fund, and other educational programs with which it was involved. There is also discussion of the company’s sponsoring of the 1962 Commonwealth Games in Perth and other support given to a range of amateur sporting associations. 1964 sees a similar section (p. 18), focusing in that year on the setting up of the Rothmans’ National Sport Foundation.

Insert Figure 3 about here

Much more interestingly, in 1964 for the first and last time there is an actual section of the Director's Report headed "Smoking and Health" (pp. 4-5). In part it says

> This is a highly scientific question and, therefore, a difficult one for the public to understand fully. The great mass of publicity has been directed against cigarette smoking, but very little publicity has been accorded to statements by many other eminent scientists and doctors who do not accept the American and British reports as conclusive… [Such dissention] is an indication of the extreme uncertainty which surrounds the accusations

This would appear to be a classic attempt at knowledge dissociation as discussed earlier in the paper.

From 1966 to 1971 the disclosures remain fairly consistent, focusing on the various specific company activities associated with sports, fine arts, education, etc. Then in 1972 (the year compulsory health warnings were introduced) there is no mention of social activities. From 1973 onwards the focus shifts to the three Rothmans' foundations (The Rothmans National Sport Foundation, The Rothmans University Endowment Fund and The Peter Stuyvesant Trust for the Development of the Arts). One significant difference is the 1980 annual report, which was presented more as a history of Rothmans' 25 years in Australia. It contained a substantial section on community service (pp. 14-15). In 1995 the last social disclosure is made, it refers to the work undertaken by the Rothmans Foundation in Australia, and states that the decision to close the foundation "was made in light of the adverse impact of anti-tobacco legislation which had severely hindered the Foundation in its work". No more disclosures of a social kind were made in the annual reports of Rothmans.

The tobacco industry in general, and Rothmans specifically, had one major threat to its legitimacy, the smoking and health issue. Except in 1964 it choose not to engage with this issue, instead focusing on community service and charitable works. This could appear to be an attempt to engage in Lindblom's (1994) third strategy, trying to get the community to accept the company's legitimacy, not in terms of the health issue, but by focusing debate to the organization's engagement in good works, therefore trying to bolster its position as a legitimate organization without having to engage in change. Ultimately this would appear to have failed, at least to the extent that the industry is now highly regulated, scrutinized and taxed, although it continues to survive. When there no longer seemed to be value in even trying to defend legitimacy the company ultimately gave up its charitable community involvement and reporting on it. This issue is now explored in more detail through quantitative means.

DISCLOSURE AND MEDIA ATTENTION

An initial analysis shows that the variable of interest (Disclosure) is not correlated with profit (a factor often examined in accounting literature as possibly being associated with Social and Environmental Disclosure (Cowen *et al.*, 1987; Hackston and Milne, 1996; Owusu-Ansah, 1998) however against expectations it is negatively correlated the number of articles (as a percentage of all articles published that year) at a $p<0.01$ (see *Table 2* on the following page).

Insert Table 2 about here

This is not easily explained and certainly provides *prima facie* evidence to reject Deegan's assertions regarding legitimacy and media theory in this industry. It is interesting to note the significant positive correlation between the company's profit (adjusted by CPI to create a 'real' profit figure) and the number of articles written about the company. As an aside this certainly would seem to support an underlying assumption of agency theory, that the 'larger' a company becomes, the more politically visible it is (see Watts and Zimmerman (1990)). Introducing lags disrupts any correlation between the variables, indicating that the company is highly reactive to events occurring at the time.

Given that the threat to legitimacy came directly from the smoking and health debate which started in 1962 (affecting the annual report from 1963 onwards) and, as discussed earlier, the company's response appears to have revolved around increased disclosure of a social nature, particularly in regards to philanthropy and corporate citizenship, a more specific set of correlations may be worth considering. The correlation between Social Disclosure (excluding that disclosure that are employee related) and articles relating to Tobacco and Health for the period after 1962 are provided in *Table 3* below:

Insert Table 3 about Here

Again social disclosure can be seen to be significantly correlated with the number of articles relating to health at less than the p=0.01 level. The concern remains that they are negatively correlated. This negative relationship between articles and disclosure contradicts expectations based on previous findings raising the question of whether Rothmans is significantly different from the average firm? Brown and Deegan (1998) suggest that Legitimacy Theory may not be appropriate where "there is a possibility that dominant players in some industries had strategically planned the timing and format of their environmental disclosures in a bid to manipulate or shape community perceptions and concerns... rather than simply reacting to changes in community concerns… Hence, assuming that a relationship between media attention and annual report environmental disclosures holds across all industries may be a simplistic assumption" (p. 33). Although this situation would seem to fairly describe Rothmans' situation, before accepting this conclusion it is worth considering whether there is an alternative factor operating that is overriding the normally expected relationship.

DISCLOSURE AND GOVERNMENT SANCTION

Graph 3 below presents visually the relationship between disclosure, health articles and introduces a third factor 'government regulation' (see *Appendix One*, for a timetable for the introduction of each major commonwealth regulation of smoking). This clearly shows the generally downward trend in social disclosure (trend line indicated by dashed-line) and suggests a relationship with government regulation (vertical black lines).

Insert Graph 3 about here

When correlations are run using a dummy variable which increases by one each time a new major regulation is introduced there does appear to be a correlation, again negative (see *Table 4* on the following page), and this correlation would appear to be stronger than the correlation with media disclosure. This is interesting, and it would be useful at this point to remember that in the earlier discussion of strategic legitimacy theory, the media was one of a number of important stakeholder groups. The government was also mentioned as being an important group, along with the general public and the financial sector. Perhaps in this case the government is playing a much stronger influencing role.

Insert Table 4 about here

Regulation is just one of the resources related to government. Another important consideration is taxation. An analysis taking into account change in excise (as a dummy variable, increasing by 1 for each rise in excise), shows a very strong correlation with social disclosure, and again the correlation is negative (see *Table 5*).

Insert Table 5 about here

The negative correlation between Disclosure and the independent variable (in this case Government Excise) still exists however. This may not be the surprise it first appears. Consider that instead of a company defending its legitimacy (the third phase identified as part of Strategic Legitimacy Theory earlier in the paper), there is actually a fourth phase to consider, that of an organisation losing legitimacy over a period of time. This view (given previous discussion on the Tobacco Industry) would seem to be an accurate description of the situation faced by the Tobacco Industry at large, and Rothmans particularly. This fits interestingly with some ideas expressed by O'Donovan (2002, p. 350) who argues that:

> A potential problem arises if one is to test which tactics are used to maintain legitimacy. A distinction needs to be made between corporations with different levels of legitimacy to maintain. If a corporation is accepted as a good corporate citizen, acts responsibly or even in a proactive manner in regard to social issues, the public will have certain expectations in relation to the organization's social and environmental activities. The less "legitimacy" an existing organization has to begin with, the less it needs to maintain.

Based on experimental evidence, elicited through a series of vignettes, O'Donovan (2002) found that the lower the perceived legitimacy of the organisation, the less likely it was to bother providing social and environmental disclosure. "One would expect a corporation with the characteristics betrayed in this vignette [low legitimacy, e.g. weapons manufacturer] not to be too concerned about legitimacy motives in annual report disclosures… A recurring theme in arguments supporting no disclosure was that the corporation was complying with all of the current laws and regulations, therefore it did not need to do any more than that to maintain whatever "poor" reputation it already had." (O'Donovan, 2002, p. 361).

It would appear that this paper, by examining the tobacco industry, has found empirical evidence of these different disclosure strategies within a single industry which moved from relatively high legitimacy to relatively low legitimacy. This provides a potential explanation for the negative relationship between voluntary Corporate Social Disclosure and various measures of stakeholder resources (reflecting decreasing legitimacy), abutting well with legitimacy theory as characterized earlier in the paper.

FURTHER RESEARCH

The relationship between the resources provided by the range of stakeholders identified and falling legitimacy and falling disclosure levels would be interesting to explore. Other potential explanatory variables might have included cigarette consumption figures, employee salaries or share values. In relation to consumption figures, it would need to be considered whether the fact that cigarettes, containing at least one drug (nicotine) which is addictive (this statement would have been controversial in the past, but the evidence now seems irrefutable (see for example, Henningfield (1985)), would then preclude them as a good measure of legitimacy. Presumably the consumer would not be as reactive to legitimacy issues, since even if they wished to stop smoking tobacco it may be difficult. It is generally believed that cigarette companies have paid higher wages to its employees. This could be viewed as a premium that has to be paid to attract employees, particularly as the legitimacy of the industry falls relative to other industries. The impounding of legitimacy concerns into share price would also be an extremely interesting, if not technically difficult, study.

CONCLUSIONS

This paper has examined the social disclosures made by Rothmans, in the context of the tobacco industry, over almost 50 years. Its findings, both qualitative and quantitative, are significant in that they add weight to the argument that there is a legitimacy motivation, at least in part, underlying the voluntary social disclosures made by firms. The qualitative analysis strongly suggests that the voluntary social disclosures made in the annual reports of Rothmans were provided with a view to counteracting the potentially negative consequences to the firm’s legitimacy of the smoking and health debate.

Though the initial findings of the quantitative analysis were contrary to expectations based on previous empirical research, additional review in light of further theoretical development appears to still support a legitimacy explanation for this company, all be it a state of decreasing legitimacy, which has as yet received little attention in the literature. Increased focus on a resource based understanding of legitimacy may help develop the theory further and increase our understanding of firms’ social disclosure.

It is interesting to note at this stage that while the study has been limited to a single company, social disclosure by the United Kingdom based tobacco company British American Tobacco (BAT) shown below in *Graph 4* shows an extremely similar disclosure pattern as found in this study. Though not examined in any detail, cursory analysis of the history of the UK legislative environment for tobacco shows a very similar evolution to that in Australia. This would seem to provide preliminary evidence that the findings of this study may apply more broadly, at least in the tobacco industry.

Insert Graph 4 about here

Some interesting research questions are raised by this study which more broadly based studies could examine. Do the statistically significant correlations between voluntary social and environmental disclosure and measured resource flows hold across other industries? Are the relationships for less legitimacy threatened organisations positive? If so at what point does the relationship change from positive to negative? That is how illegitimate does a company have to become before its disclosure starts to reduce?

Legitimacy theory offers researchers, and the wider public, a way to critically unpack corporate disclosures. This knowledge can then be used to provide better and more useful information to inform decision making by stakeholders. In this way society is empowered to have greater control and oversight over the way resources are allocated.

> Accounting is often characterised as a service function which proliferates economic information for decision making. However, there is a danger if we allow the disseminatory role of accounting to

be too narrowly defined… . In pluralistic societies, accounting's virtue lies in a capacity to tell multitudinous economic stories about organisations to the multitudinous audiences interested in the discourse. … It is everybody else who really needs the kind of dissemination that accounting could provide (Francis, 1990, p. 11).

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Appendix 1: Highlights of some of the federal legislation with regards to smoking in past 40 years. Based on ACOSH website http://www.acosh.org/history.htm.

1972 The health warning, "Smoking is a Health Hazard" became compulsory on cigarette packets in Australia.

1975 Federal legislation banning cigarette advertising on television and radio came into effect with the Broadcasting television Act Amendment Act 1976, Section 6.

1986 Stronger health warnings were introduced on cigarette packets under the tobacco (Warning labels) regulations 1987. The Federal government prohibited smoking on all domestic aircraft flights under the Air Navigational Act 1920.

1987 Four warnings were issued on packets: "Smoking Causes Lung Cancer, Smoking Causes Heart Disease, Smoking Damages Your Lungs, Smoking Reduces Your Fitness".

1988 Amendment to the Australian Broadcasting and Television Act, extends bans on direct advertising to include all tobacco products. The Australian Public Service was converted to a smoke-free workplace.

1990 Advertising of cigarettes in magazines and newspapers also ceased due to Federal government legislation under the Smoking & Tobacco Products Advertisements (Prohibition) Act 1989. Smoking on international airlines within Australia was banned from 1 September. Cinemas, theatres and concert halls went smoke free under the WA Health Act 1911 Public Buildings Regulations sections 39 and 58. Smoking was still permitted in the foyers and bars.

1991 'The Morling Judgement' provides a precedent for courts to deal with claims concerning passive smoking. Point of Sale Advertising under the Tobacco Control Act 1990 prohibits tobacco advertising outside of shops or in view of public places, advertising larger than 1m x 1m, larger health warning signs.

1992 The Federal government announced that all tobacco sponsorship of sport and arts end by 1995/6. Stronger health warnings and content labelling information on cigarette packages have been announced to come into effect across Australia by 1993. International airline terminals went smoke free by July. Antonio Cipollone in the United States successfully sued 3 tobacco companies following his wife's death from lung cancer, as the tobacco companies have known for many years that there was a link between cigarette smoking and cancer.

1994 Billboard advertising of tobacco products is made illegal under the Tobacco Control Act 1990.

Figures

Figure 1: Layers of Legitimacy Theory

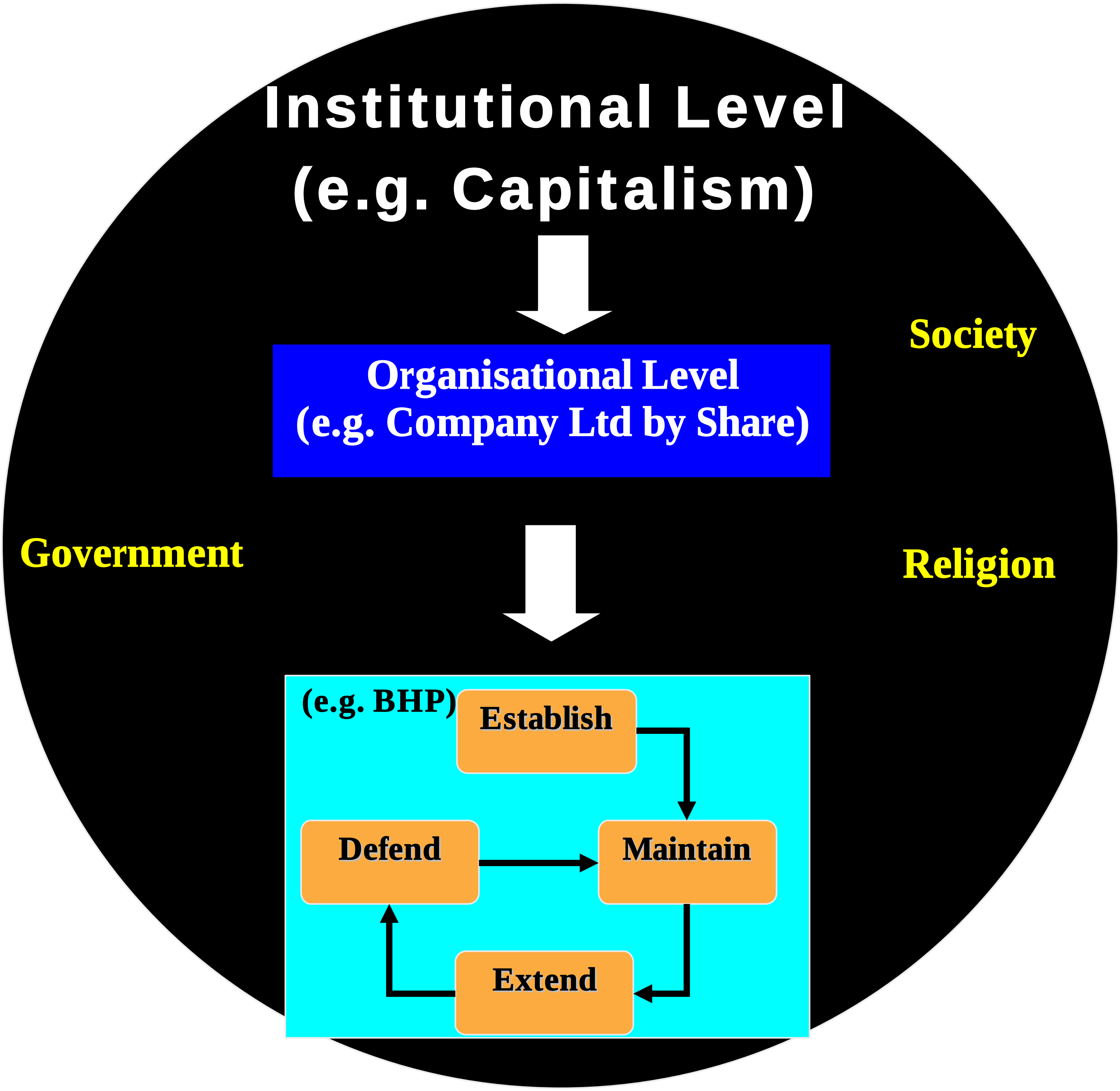
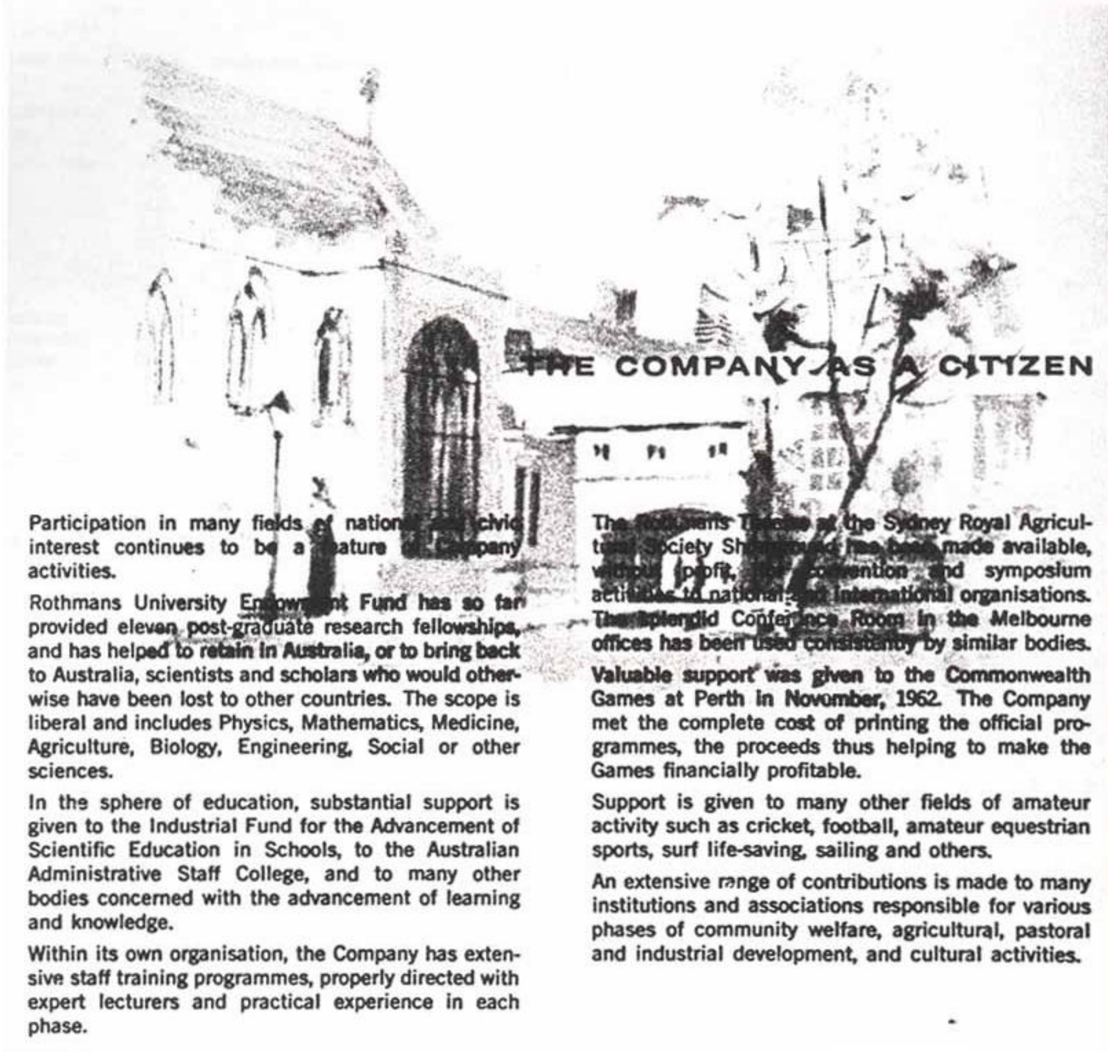


Figure 2: Transcription of Employee Related Disclosure in 1958 Annual Report

Staff:	Being a new Company, a great deal of time has been devoted to training staff, and everything possible has been done to provide model condition for all employees. The enthusiastic team-work in every section of the organization has been outstanding and warrants special mention.

Figure 3: Copy of page 22 of 1963 Annual Report



THE COMPANY AS A CITIZEN

Participation in many fields of national and civic interest continues to be a feature of Company activities.

Rothmans University Endowment Fund has so far provided eleven post-graduate research fellowships, and has helped to retain in Australia, or to bring back to Australia, scientists and scholars who would otherwise have been lost to other countries. The scope is liberal and includes Physics, Mathematics, Medicine, Agriculture, Biology, Engineering, Social or other sciences.

In the sphere of education, substantial support is given to the Industrial Fund for the Advancement of Scientific Education in Schools, to the Australian Administrative Staff College, and to many other bodies concerned with the advancement of learning and knowledge.

Within its own organisation, the Company has extensive staff training programmes, properly directed with expert lecturers and practical experience in each phase.

The [illegible] at the Sydney Royal Agricultural Society Sh[illegible] has been made available, [illegible] profit, [illegible] convention and symposium activities to national and international organisations. The splendid Conference Room in the Melbourne offices has been used consistently by similar bodies.

Valuable support was given to the Commonwealth Games at Perth in Novomber, 1962. The Company met the complete cost of printing the official programmes, the proceeds thus helping to make the Games financially profitable.

Support is given to many other fields of amateur activity such as cricket, football, amateur equestrian sports, surf life-saving, sailing and others.

An extensive range of contributions is made to many institutions and associations responsible for various phases of community welfare, agricultural, pastoral and industrial development, and cultural activities.

Tables

Table 1: Critical Organisational Stakeholder

STAKEHOLDER	RESOURCES CONTROLLED
The state	Contracts, grants, legislation, regulation, tax (Note that the last three of these could be either a 'negative' or 'positive' depending on the implementation)
The public	Patronage (as customer), support (as community interest), labour
The financial community	Investment
The media	Few 'direct resources' however can substantially influence the decisions of two (if not three) previous groups

Table 2: All Disclosure and Articles - Correlations for Rothmans (1956 – 1999)

			Disclosure	I-Profit	%articles
SPEARMAN'S RHO	Disclosure (All Social and Environmental Disclosure in Annual Report)	Correlation Coefficient			
		Sig. (2-tailed)			
		N			
	I-Profit (Accounting Profit Indexed by CPI)	Correlation Coefficient	.019		
		Sig. (2-tailed)	.900		
		N	44		
	%articles (percentage of articles relating to Tobacco)	Correlation Coefficient	-.399(**)	.530(**)	
		Sig. (2-tailed)	.007	.000	
		N	44	44	

** Correlation is significant at the 0.01 level (2-tailed).

Table 3: Specific Social Disclosures and Health Related Articles Correlations for Rothmans (1963 – 1999)

			SocDisc	Health Art	I-Profit
SPEARMAN'S RHO	SocDisc (Social (less Employee Related) Disclosure)	Correlation Coefficient			
		Sig. (2-tailed)			
		N			
	Health Art (percentage of articles relating to Health and Tobacco)	Correlation Coefficient	-.458(**)		
		Sig. (2-tailed)	.004		
		N	37		
	I-Profit (Accounting Profit Indexed by CPI)	Correlation Coefficient	-.349(*)	.760(**)	
		Sig. (2-tailed)	.034	.000	
		N	37	37	

** Correlation is significant at the 0.01 level (2-tailed).
* Correlation is significant at the 0.05 level (2-tailed).

Table 4: Specific Social Disclosure and Government Regulation Correlations for Rothmans (1963 – 1999)

			SocDisc	Health Art	Restriction
SPEARMAN'S RHO	SocDisc (Social (less Employee Related) Disclosure)	Correlation Coefficient			
		Sig. (2-tailed)			
		N			
	Health Art (percentage of articles relating to Health and Tobacco)	Correlation Coefficient	-.458(**)		
		Sig. (2-tailed)	.004		
		N	37		
	Restriction (Dummy Variable for each new major regulation)	Correlation Coefficient	-.521(**)	.784(**)	
		Sig. (2-tailed)	.001	.000	
		N	37	37	

** Correlation is significant at the 0.01 level (2-tailed).

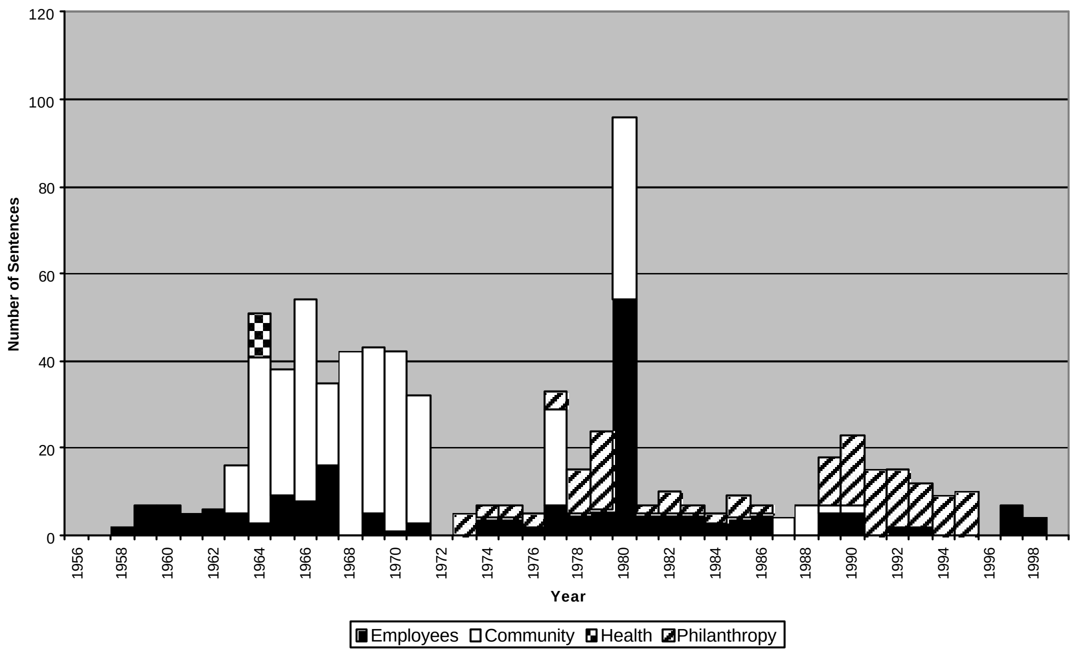
Table 5: Specific Social Disclosure and Government Excise Correlations for Rothmans (1963 – 1999)

			SocDisc	Excise
SPEARMAN'S RHO	SocDisc (Social (less Employee Related) Disclosure)	Correlation Coefficient		
		Sig. (2-tailed)		
		N		
	Excise (as a Dummy Variable)	Correlation Coefficient	-.550(**)	
		Sig. (2-tailed)	.000	
		N	37	

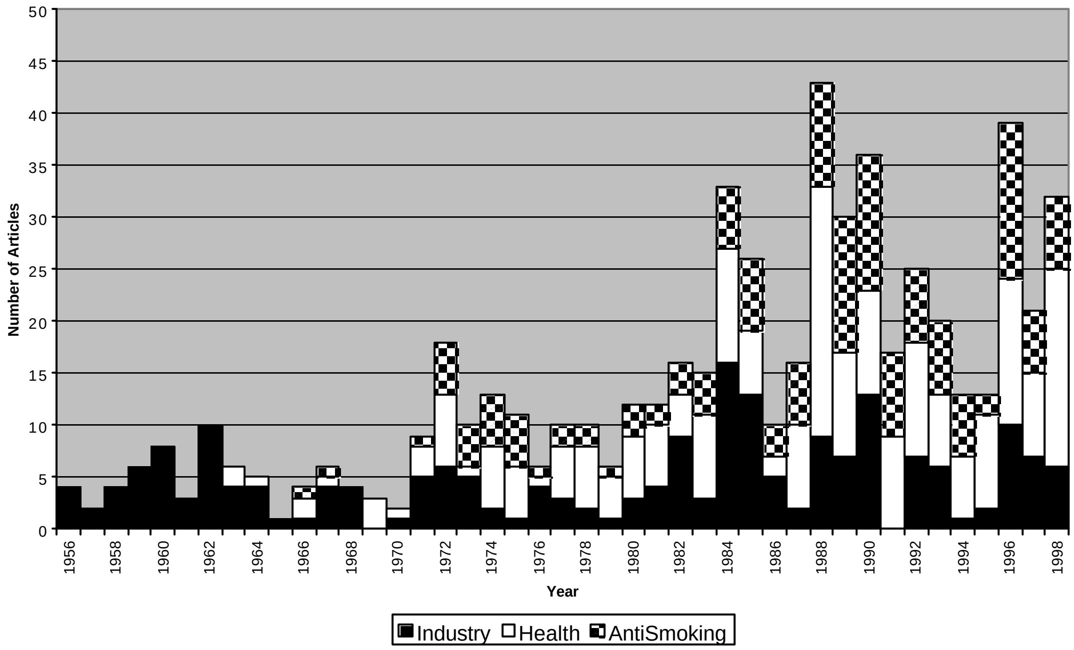
** Correlation is significant at the 0.01 level (2-tailed).

Graphs

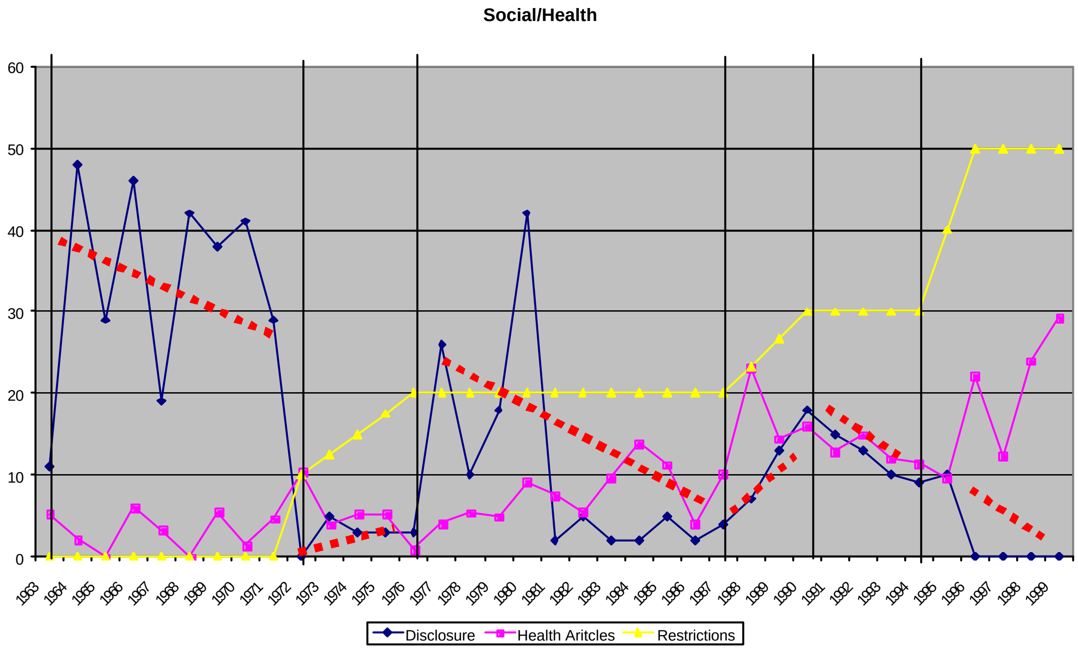
Graph 1: Number of Social and Environmental Sentences per Annual Report



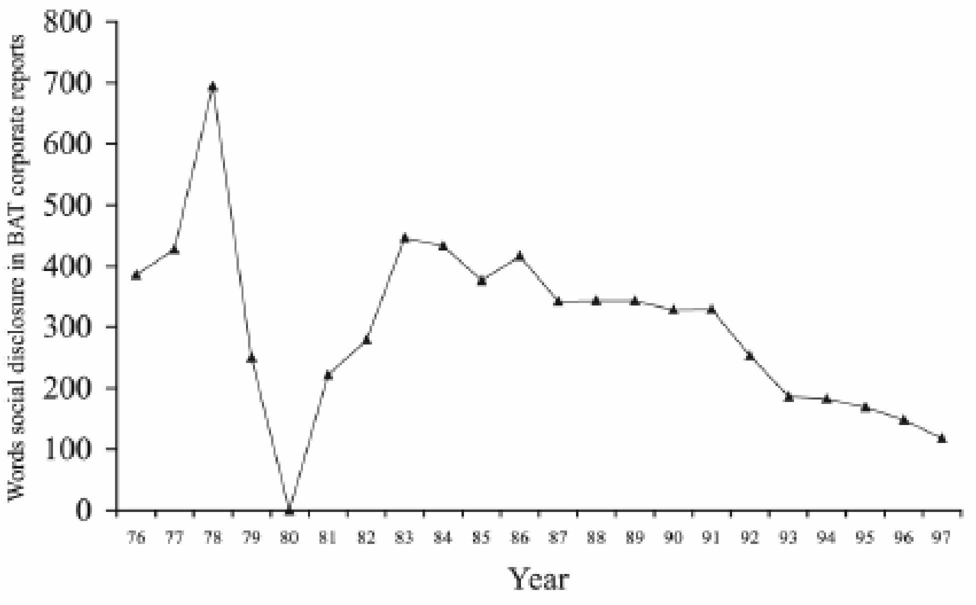
Graph 2: Number of Tobacco and Cigarette Articles in APAIS Database



Graph 3: Disclosure, Health Articles and Government Regulation



Graph 4: Words of Social Disclosure in British American Tobacco UK corporate reports 1976 - 1997 (Source: Campbell *et al.*, 2003, p. 569, figure 2)



Note: The current form of BAT resulted from a corporate reorganisation in 1975 and thus it did not report as BAT Industries plc in 1974