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**THE ROLE OF PMS IN SUPPORTING CSR STRATEGIES**

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*Abstract*

Embedding social and environmental issues into the corporate strategy as well as management control system is necessary for a strategic, comprehensive, integrated and effective implementation of sustainability principles. A well-designed Performance Management System (PMS) can help managers to formulate economic, social and environmental objectives and achieve a more comprehensive understanding of sustainability performance and its business impact on stakeholders' expectations. Hence, the purpose of this paper is to examine how the Performance Management System is used to accommodate the demands of the stakeholders and to translate the CSR strategies and programs. A qualitative case study is undertaken at the CSR Department of a state-owned oil and gas company in a developing country. This study had employed socially responsible planning and control system, supported by the performance management system framework. The data collection was conducted through semi-structured interviews with key organizational members as well as from documentary reviews. The findings revealed that the PMS's application and implementation of CSR strategies and programs were mostly influenced by the government, given that it is an influential owner of the company.

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**Keywords:** Performance management system, CSR strategies, oil and gas company, stakeholder demand.



## 1. Introduction

### 1.1. Background

Today, there is an escalating demand and pressure by stakeholders for more information regarding corporate social responsibility (CSR) activities, as well as the good relation between organizational economics and CSR performance. Hence, organizations will need to be more proactive and transparent in managing their social and environmental activities (Bartolomeo et al. 2000; Burnett & Hansen, 2008; O'Dwyer, 2002, 2005; Perego & Hartmann, 2009). The CSR activities can lead to social benefits and legitimacy for the company since they are forms of coalition involving different stakeholders' interests and concerns (Hannan & Freeman, 1984). One way of optimizing the CSR agenda is by considering and incorporating the feedbacks from the stakeholders into the managerial decision makings and management processes (Baker & Schaltegger, 2015; Petkevičienė, 2015; Maas et al., 2016). Thus, the challenge for business organizations is to have integrated and well-balanced management pertaining to the social and environmental aspects, while at the same time meeting the stakeholders' economic expectations. As such, a greater understanding of the internal processes is required through which the CSR strategies are being managed and linked to other business processes (Arjalies & Mundy, 2013).

Performance Management System (PMS) is a tool that can facilitate the management of Corporate Social Responsibility (CSR) activities. This is because it supports the internal processes in the organization including how CSR performance is being managed and linked to other business processes (Arjalies & Mundy, 2009). Ideally, the PMS would ensure the management and control of organizational performances holistically as it includes all aspects of organizational control (including controls related to the Management Control Systems) ranging from conventional to contemporary control in organizations (Ferreira & Otley, 2009, George, Siti-Nabiha, Jalaludin, & Abdalla, 2016). The PMS covers a broad range of managerial activities, including supporting strategic processes (which involves strategic formulation and strategic implementation) (Mintzberg, Ghoshal, Lampel, & Quinn, 2003; Pearce & Robinson, 2007), emergent strategies (through its learning and change facilitation role) (Mintzberg, 1978); and ongoing management activities (Ferreira & Otley, 2009). A good PMS is supported by a performance measurement system, which provides information that quantifies both the efficiency and effectiveness of the organizational actions (Neely, 2005; George et al., 2016). Overall, PMS provides the linkage between organizational objectives, strategies and internal mechanisms, hence providing directions that can support the attainment of the organizational sustainability objectives (Gond, Grubnic, Herzig, & Moon 2012; Langfield-Smith, 1997).

Prior literature on PMS mainly concentrates on the core business of the organization where CSR is normally viewed merely as a public relations exercise intended to enhance the organization's reputation and image. Nevertheless, the past ten years had witnessed various research exploring PMS and sustainability, such as the role of management control system in supporting sustainability (Maas, Schaltegger, & Crutzen, 2016; Lueg & Radlach, 2016), how management control system measures and control a company's social responsibility (Durden, 2008; Riccaboni & Leone, 2010), as well as the barriers and enablers to sustainability integration in the management control system (George et al., 2016). Other researchers, such as Klovien and Gimžauskien (2014) discussed how the PMS model (framework) should be implemented in State-owned Enterprises in Lithuania when internal and external regulators views are incorporated. Carlsson-Wall et al. (2016) investigated how the PMS deals with two different institutional

logics within a football organization. However, academic literature that specifically investigated the relationship between PMS and CSR strategies are scarce (Klovienė & Gimžauskienė, 2014) except for Arjalies and Mundy (2013), who investigated the used of management control system (MCS) to facilitate CSR strategies. They found that MCS supported the determination of the indicators for CSR and the renewal of the strategies in the organization.

Similarly, the present study explores the link between the PMS and CSR strategies issue while taking into consideration the demands of stakeholders, in the context of a State-owned Enterprise. State-owned enterprises are currently facing increasing pressures in relation to their CSR management. The concerns and objectives of the stakeholders are essential aspects to consider in the effort to integrate CSR into business operations and activities of a company López-Gamero, Molina-Azorín, & Claver-Cortés, 2010). Given that organizations are now facing greater expectations from various stakeholders in the society in terms of their social and environmental contribution. The intense pressures regarding the abovementioned issues have driven them to find methods to optimize the utilization of their CSR activities (Petkevičienė, 2015). This research is focused on how PMS ensures the success of the CSR strategy while taking into consideration the stakeholders' expectations. A case study of Oil Company, a National Oil Company (NOC) is undertaken to achieve the objective of the research. The Ministry of SOEs, i.e. the owner of Oil Company, requires each SOE to make a social contribution to the country, and evaluates their performance based on the achievement of both financial and social targets.

## **1.2. Theoretical Framework**

This study utilizes both Cresti (2009), and Ferreira and Otley's (2009) frameworks. The Ferreira and Otley (2009) framework is a holistic approach for performance management system. It is an extension of Otley's (1999) five 'what' questions to ten 'what' and two 'how' questions. The questions focus on the following aspects, i.e. vision and mission, key success factors, organization structure, strategies and plans, key performance measures, target setting, performance evaluation, reward systems, information flows, systems and networks, PMS use, PMS change, and the strength and coherence. The Ferreira and Otley (2009) framework is a tool that provides powerful means to obtain an overview and appreciation of the PMS structure that is currently in use in specific organizations. Several aspects of the Ferreira and Otley's (2009) framework allow one to understand how an organization may accommodate the stakeholders' interests in their CSR practice to ensure that the strategies and plans can be effectively implemented.

In this research, the proposed PMS aspects have been simplified to five stages based on Cresti's (2009) planning and control framework. However, the external reporting aspect of the implementation of CSR programs and activities (external reporting) in the annual report is excluded from this research. The PMS of Oil Company CSR Department can be described by two components processes which are the planning and control processes. These two processes are based on Cresti's (2009) framework which provides the guidance for a strategic path of implementing CSR concerns into a business organization. The six questions adopted from Ferreira and Otley's framework (2009) are used as they are appropriate and compatible with Cresti's (2009) framework. The six questions are: (1) Vision and missions, (2) Strategies and Plans, (3) Key Performance Measures, (4) Target settings, (5) Performance Evaluation, and (6) Reward systems.

## **2. Problem Statement**

Oil Company considers itself to be environmentally and socially responsible yet it is facing various external and internal institutional pressures. They are being increasingly demanded by their stakeholders to be environmentally and socially responsible. According to Cresti (2009), a well-designed Performance Management Systems can help managers to formulate economic, social and environmental objectives and to achieve a more comprehensive understanding of sustainability performance and its business impact in relation to the stakeholders' expectations. The collaboration of the social and environmental issues into corporate strategy and the management control system is necessary for a strategic, comprehensive, integrated and effective implementation of the sustainability principles.

## **3. Research Questions**

How does Oil Company design and use PMS to accommodate the needs of its main stakeholders, as well as translating its CSR strategies?

## **4. Purpose of the Study**

The purpose of this study is to provide some understanding of how PMS is used to manage and monitor the CSR strategies in the SOE context. Specifically, the study examines the utilization of PMS in assisting the company to prioritize its key stakeholders' interests, given the power that the stakeholders have on the company. The current study identifies the problems and issues associated with PMS employment. By combining Cresti's (2009) and Ferreira and Otley's (2009) PMS frameworks in exploring the issues, the study mentioned above, it could extend the existing PMS literature. As the case study concerns the implementation of PMS by the CSR Department of an oil and gas company, in a developing country, the findings of this case study may be of value to companies of similar nature. This is particularly relevant when dealing with issues related to the implementation of CSR programs, the coordination of various subsidiaries, and the role of PMS in supporting CSR strategies as demanded by the stakeholders.

## **5. Research Methods**

The present study employs the qualitative methods via an interpretive case study (Scapens, 2004). The research questions are addressed through data collected from interviews, and supported with secondary data such as annual reports, sustainability reports, departmental and unit reports, KPI's (key performance indicators) documents, journals, magazines and the company's and ministry's websites. Semi-structured interviews were conducted with 27 employees of Oil Company and its subsidiaries. The respondents were selected from various management levels, i.e. the top management, middle management and the operational level. An interview was also conducted with the consultant who assisted the CSR Department in formulating Oil Company's CSR strategies. The interviewees were selected based on expertise in their field of work, as well as their many years of working experience in Oil Company. Given their in-depth knowledge of Oil Company, its CSR activities and PMS, the researchers were able to obtain rich information with regards to the focus of the study.

To conduct the CSR programs, Oil Company's CSR Department HQ is assisted by six refinery units, eight marketing operation regions, and 17 subsidiaries. Oil Company's CSR programs is conducted nationwide and as the coordinator of CSR programs, the CSR Department HQ has an obligation to manage and control the implementation of all the CSR programs, including ensuring that all employees would be involved in the CSR programs. In other words, the CSR activities are not the exclusive responsibility of the CSR Department HQ. For example, some of the employees from the Corporate Secretary Department were also actively involved in various CSR activities. The interview process began in August 2017 and ended in June 2018. The interviews were based on the interview guidelines prepared by the researchers to ensure that the collected data take into account all the main components of the Oil Company's PMS. The findings of the study are discussed in the following section.

## **6. Findings**

The key measurement of the success for Oil Company CSR programs and activities is the beneficiary satisfaction index. Information from the abovementioned index is used as the main, basic performance evaluation tool for Oil Company when getting feedbacks regarding the performance of the CSR Department HQ's performance. The department is mostly influenced by the government and has taken steps to ensure that all the government's regulations, especially the regulation from the Ministry of SOE as the owner of Oil Company are adhered to.

### **6.1. Identity (Vision and Mission)**

As a national energy company, Oil Company is committed to prioritize the balance between the conservation of nature, environment and society. As Oil Company strives for the welfare of human beings, nature and the environment, it focuses on sustainable business growth. In order to exist as a sustainable business entity, the company has to balance between the economic, social, and environmental concerns and these are all embedded into the company and its CSR Department HQ's vision and mission.

The initial position of a PMS in a company is its vision and mission. The vision of the company relates to an improvement in the quality of life while the mission statement pertains to the company's commitment to be socially and environmentally responsible. This will allow them to add value to all the stakeholders, support the company's growth, and to implement corporate responsibility and social awareness for sustainable community development. The CSR Department HQ's function was guided by the parent company's policies, strategies and plans for the CSR programs. The Corporate Secretary will ensure that both the CSR's and Small Medium Enterprise Partnership Program's strategies are effective and appropriate for the community, especially within the vicinity of the Oil Company's operations. This includes improving the ability of small businesses in the community so that they are stronger and independent, thus providing added value to the company and society.

### **6.2. Planning (Strategies and Plans)**

It is the Ministry of SOE that had set up the targets for all the SOEs in the country including Oil Company (both financial and non-financial targets). The targets served as a launching point for Oil

Company when setting up its five years long-term strategy and annual short-term strategy. The CSR Department HQ played a major role in supporting Oil Company to achieve its non-financial targets which included the implementation of CSR programs. The CSR Department HQ had to link the set targets to the strategic actions and activities of the company.

The Corporate Secretary and Vice President of CSR Department HQ then set the policies, strategies, and plans for the implementation of the CSR programs and activities. These became the foundations for the implementation of CSR programs and activities in all of the units and subsidiaries of the company. The vision and mission from the CSR Department HQ became the foundation on which the strategies and plans were formed. The uniformity of this CSR theme, “The Oil Company is the friend of the earth”, ensures that all the units and the subsidiaries are guided by this philosophy.

Planning is an essential part as it provides direction regarding the CSR strategies and the company’s related plans. The CSR Department HQ is tasked to define the goals and objectives that would support Oil Company’s vision in enhancing the company’s reputation and credibility through social and environmental related activities. Oil Company must follow the government’s priority agenda, which included the development of new and renewable energy and gave priority to the use of gas to increase electricity production in the country. The government is committed to implement sustainable development, in terms of low carbon economy with the target of reducing emissions by nearly 30 percent and 41 percent with international assistance by the year 2030. This emissions reduction will be conducted mainly in the energy sector, where the initiatives are mainly to increase the use of renewable energy sources to 23 percent of the national energy consumption by 2025.

Consequently, the strategic goal of the CSR Department HQ was also to support the government program to increase the use of renewable energy. The renewable energy source can be achieved by developing a green lifestyle through community engagement and sustainable development. This green lifestyle is called ‘Oil Company is the friend of the earth’, a tagline for the company’s Social and Environmental Responsibility Program that was launched by the company’s CEO in early 2011. This strategic goal focused on four pillars of strategic initiatives, all related to the sustainability of the future generation. The four pillars of this umbrella CSR programs concerned the educational, health, environment, and ecopreneurial aspects. Specific issues in each program would be translated based on local issues by each operation unit or the company’s subsidiaries.

All around the country, the Oil Company’s refinery units, regional marketing operations and the subsidiaries conduct community and socio-environmental mapping with regards to people living in the surrounding areas of their operations. These mappings were done to get insights on the socio-environmental conditions of the surrounding communities, enabling the CSR Department HQ to prepare a suitable CSR program for them. The business units submitted their proposed program planning to the CSR Department HQ. Both the business units (Refinery Units, Regional Marketing Operations and the subsidiaries) and the CSR Department HQ were assisted by a consultant.

### **6.3. Managing (Strategies and Plan)**

The philosophy from one of the CSR roadmaps for the year 2017 was to develop employee volunteerism in supporting the CSR practices in the company. The communication to the whole employees

regarding the volunteerism in CSR practice was reflected by the vision and mission of the division. Generally, the philosophy was communicated to all the employees through various networks and processes. The main goal was to ensure that the employees were aware of the vision and values of the company and behaved in alignment with the company's vision that sustainability would be part of its competitiveness. The CSR Department HQ used several networks and processes to communicate its vision and mission to its employees. Such an approach was meant to ensure efficient and continuous communication that would successfully communicate the importance of volunteerism in Oil Company.

Considering the demands of the Ministry of SOE, the CSR Department HQ, usually created the strategies via the top-down approach. This process did not involve other external stakeholders, except for the Ministry of SOE. The company's top management (CEO and board of directors) set some guidelines and directions that the divisions were required to move towards. These were then cascaded down throughout the hierarchical levels in Oil Company (e.g. to general managers and their teams).

The annual planning and the budgeting activities of the CSR Department HQ would often start in the middle of the year, and the proposal would be submitted to the Strategic Unit of the company in November. The submitted plans and the budgets of the CSR Department HQ covered a period of five years (long-term), and the short-term plans and the budgets for the next coming year or only for one year were also discussed. After all the plan was approved by the Board, the CSR Department would start working on these strategic plans. It is quite clear that the strategic priorities were set by the top management. The business plan was prepared for a five-year period and communicated firstly in the meeting involving the Board of Directors and the top managers, followed by meetings with each manager with his/her team. All the interviewees were aware of the main strategic priorities and the new activities that the organization had planned. Lower level managers and employees were given an extensive explanation about the plans related to their departments so they would become aware of their contribution in the overall organizational success, especially in the success of the CSR Department.

The external stakeholder engagement to construct the CSR strategies did not involve any external parties except for the guidance of the Ministry of SOE. Several methods were used to gather the information from each stakeholder's group, which included the interaction and participatory planning with the stakeholders to understand the common issues. The CSR Department HQ was assisted by the consultant to collect the information from the stakeholders throughout the survey using the socio-economic mapping for the communities surrounding the operation site of the company. All the information gathered would then be used in developing the programs. The CSR Department HQ only coordinate the CSR programs as the implementation of the programs were conducted by the six Refinery Units (RUs) and eight Marketing Operation Regions (MORs) and seventeen subsidiaries from all around the country, with the coordination being made by the CSR Department HQ (for the CSR corporate program). In other words, all the business units have their own CSR programs with their own budget.

#### **6.4. Measurement and Target Setting**

The CSR Division, used a wide range of key performance measures and these measures were derived from the strategic plans and objectives. Since the 2000s, State-owned Enterprise was evaluated based on their financial and non-financial targets including their social performance. The achievement of social target

became part of the SOE's performance. There is also a management contract between the Oil Company's CEO and the Minister of SOE which required the CEO to achieve all the targets proposed by the Ministry. Accordingly, the CEO from Oil Company should sign the management contract and would be evaluated based on the achievement of every component of the KPIs. The formulation of KPIs in the CSR Department started from the corporate level, based on the Management Contract from the Ministry of SOE. Then the Management Contract cascaded to the Director's level and translated into the KPIs. Then the KPI from the level of the Board of Directors (BOD) cascaded to each level of the Vice President, followed by the Manager's level and finally down to the Officer level, where the goals are regenerated annually during the meeting based on the strategic plans.

The operational performance indicators that needed to be adopted by the SOE included the measurement of the activities. The measurements covered all the activities that support the success of the operational strategies of the SOEs. One of the indicators from the corporate performance was the level of community development and CSR performance. The emphasis on the implementation of CSR in the SOE was based on the government's regulations that required all the companies that conduct their businesses or activities in the field and/or related to the natural resources must carry out their Corporate Social Responsibility.

KPIs play a central role in the performance management system. Therefore, depending on the position of the employee/manager "there are some KPIs that are of greater importance than others". The key performance measures are a vital part of the PMSs and they were integrated into the business plan and the strategy of the company. They were communicated to the employees using the top-down approach similar to the communication regarding the strategies and plans.

In order to achieve targets from the management contract between the CEO and the Ministry of SOE, the CSR Department HQ also set up the long-term strategy for five years and short-term strategy for every year. Performance targets were established in accordance with the objective as well as the adoptions of the strategies. The target setting in Purple Com was decided and centralized by the top management, based on criteria that have been standardized, which usually remain the same from the previous year.

The performance and reward of the CEO of the Purple Com are based on the achievement of these financial and non-financial performance. Therefore, the target of this management contract's achievement will also be linked to the reward of the employees. The CSR Department KPIs include the implementation of CSR programs, i.e., timely completion of the program and the capability to work together between the CSR Department at HQ with the CSR Operational Units. The timely completion of the CSR report for publication purpose is also a measure of performance.

## **6.5. Performance Evaluation and Reward System**

All the CSR programs were evaluated and reported to the company's headquarter. Two main areas were evaluated. First, the implementation of the programs which included the economic, educational, health, and social infrastructure aspects are evaluated. Second, the performance was evaluated by comparing the work plan and targets setting, particularly on the main programs in terms of target achievement, budget realization, targeting accuracy and stakeholder engagement. The stakeholders' level

of satisfaction was also evaluated using a survey for the beneficiaries' satisfaction. The evaluation covers the output and the impact of the program on the beneficiaries and other stakeholders

The CSR Department HQ provided appreciation and rewards to employees who had achieved their targets. This reward program was carried out in order to motivate the employees. The rewards given to the employees, individuals or groups could be in a variety of ways, in accordance to the company's policy, such as special incentives and bonuses that would be given at the end of the year. The achievement of the target would affect the bonus that would be given to the employees.

## 7. Conclusion

The process for formulating the CSR strategies is top-down, with the stakeholders' input or interest being considered. Although the strategies are set by the top management with the inclusion of all the stakeholders, delegation is given to the middle managers (the two managers from the CSR Department) to communicate these strategies to their subordinates and translate them into individual targets. This decentralization aims to mitigate conflicts, enhance accountability of the middle managers and create an atmosphere of shared commitment for the pursue of the strategies.

The alignment of the measures to evaluate the strategies is apparent; the measures are perceived as personal targets, deriving from the company's goals, plans and objectives. The managers of the CSR Department HQ set the targets and the company adopts the achievable but challenging targets. The participation of lower-level employees in choosing the specific targets is limited, but instead these employees discuss the way to achieve the targets in their meetings with their supervisors. The evaluation process is based on the individual and organizational performance and the company uses an incentive system of signing a performance contract in order to motivate the employees.

The Cresti (2009) and Ferreira and Otley's (2009) PMSs framework was able to determine at which stage of this PMS's cycle (from identity to the feedback/improvement) are the stakeholders' interests being considered. The role of external stakeholders appeared in: (a) the phase of identity, where the vision and mission, comprehensively depict its stakeholders-centric orientation as the beneficiaries of the CSR programs and activities, where they are dedicated to achieving the goal of sustainable growth by offering a high quality of life; (b) the phase of planning where the CSR Department HQ is being driven by a range of Stakeholder Relations under the Corporate Secretary, by deciding on an effective and targeted corporate CSR & SMEPP strategy for the community, particularly within the vicinity of the company's operating area, and enhancing the ability of small businesses to become resilient and independent, thus providing added value to the Company; (c) the phase of managing, it is important for the whole CSR Department HQ and the external stakeholders to participate in building up the business plan; (d) the phase of measurement, the formulation of target setting in Oil Company is indicated in its Key Performance Indicators (KPIs), based on the Management Contract from the Ministry of SOE; and (e) the phase of feedback/improvement, the stakeholders' level of satisfaction with the implementation of the CSR programs is one component which requires the evaluation of the CSR Function/Department.

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