



THE IMPLEMENTATION OF CONNECTED REPORTING FRAMEWORK IN THE ELECTRIC UTILITY SECTOR IN THE CZECH REPUBLIC



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Abstract

Several surveys on corporate social responsibility reporting have shown that various companies around the world are currently addressing social and environmental issues in their reports. However, some companies have issued social and environmental reports for each operating division or geographic area, some for the entire corporation only, and some have included this discussion in corporate annual reports. No matter the case, it has been noticed that several companies have provided this information in an intricate way, without aligning to their corporate strategies. Unclear or insufficient targets and key sustainability performance indicators contributes to an increase in the difficulty of a real assessment of the company by all stakeholders. This situation is not different in the Czech Republic.

This study focuses in the way companies of the electric utilities sector in the Czech Republic are reporting on sustainability issues and suggests how these companies can develop an approach based on the Connected Reporting Framework set out in 2007 by the Prince of Wales Accounting for Sustainability Project. Firstly, a brief explanation on the Connected Reporting Framework is provided. Secondly, an overview on the way the companies in this sector are responding to increased stakeholder demands for information on corporate sustainability performance is given. Then, possibilities on how these companies can implement the Connected Reporting Framework are suggested.

Introduction

Since the development of the so called “Triple Bottom Line” (TBL) approach by John Elkington in 1995, a term also known as “people, planet and profits”, several companies around the world had a clearer idea of what the corporate responsibility movement consists in. A business is considered sustainable when it operates with a simultaneous concern to economic prosperity, environmental quality and social justice, the three bottom lines, which are interrelated, interdependent, and partly in conflict (Elkington, 1997, 2004).

Nowadays it can be observed that Corporate Responsibility comprises three interlinked movements in the corporate world: Corporate Social Responsibility (CSR), Corporate Sustainability (CS) and worldwide reforms on Corporate Governance (CG). The first two movements are commonly used interchangeably and there are no standard definitions or a set of criteria to differentiate them (T. & Y. Katsoulakos, 2007). However, some authors and organizations have been trying to identify the differences between these two terms.

According to Carewren Johnson, corporate social responsibility concentrates more on the non-financial societal activities that a company contributes to whereas corporate sustainability concentrates on both the impact of environmental factors on a company and the company’s impact on the environment. Carewren also referred to the article *A Strategic Approach to Climate* (2007) by Michael E. Porter and Forrest L. Reinhardt to support the idea that businesses need to look simultaneously at the impacts of company’s activities on climate and on how climate regulatory change may affect the business environment in which the company competes.

It became critical for companies to collect and analyze information on sustainability and include it in internal sustainability reports to improve managerial decision-making regarding processes and products. External stakeholders are affected by corporate strategies and actions. For this reason, information on how companies perform on sustainability is relevant for them. Various pressures have contributed for the increase in importance of social and environmental disclosures in corporate annual reports and the quantity and quality of disclosure in separate environmental or sustainability reports (Epstein, 2008).

Important research and surveys related to corporate social responsibility and sustainability reporting have been conducted since mid 1990s. Esrock and Leichty (1998) found that of the 90% of *Fortune* 500 firms that had a Web site in 1998, 82% reported on social responsibility. In 2002, a global survey of senior managers and board directors conducted by Ernst & Young reported that corporate social responsibility (CSR) had emerged as a significant business issue on many boardroom agendas and was likely to become increasingly important over the next years (Montiel, 2008).

In 2005, KPMG found in the International Survey on Corporate Responsibility Reporting that 52% of the world’s largest 250 companies published a social responsibility report in addition to their annual report. This number has increased to nearly 80% according to the second survey conducted by KPMG in 2008 (KPMG, 2008). According to this survey, the overall drivers for reporting on the TBL issues are the ethical and economic considerations, in this order. When comparing to the previous edition of the survey conducted in 2005, the ethical considerations have gained the first place from the economic considerations, jumping up from 53% to 69%, whilst the economic considerations have dropped from 74% to 68%. Other important evidences have been perceived in the significant gain of importance for other driving factors since 2005, such as: reputation or brand (increase from 27% to 55%), strengthened supplier relationship (increase from 13% to 32%), improved relationships with governmental authorities (increase from 9% to 21%), and cost savings (increase from 9% to 17%).

On the other hand, other previously key drivers have seen their importance reduced, such as: risk management or risk reduction (decreased from 47% to 35%) and access to capital or increased shareholder value (dropped from 39% to 29%). The main reason for this significant change in the importance of drivers for corporate responsibility reporting has been the occurrence of scandals in accounting, environment, governance, and human rights since 2005, which in turn contributed to a loss in business trust and a simultaneous increase in the need of enforcement of sustainable development agenda in order to maintain or increase the brand worth of companies.

In 1999, the Institute of Social and Ethical Accountability (ISEA) published the AA1000, a voluntary standard for social and ethical accounting, auditing and reporting (AccountAbility).

In the same year, Global Reporting Initiative (GRI, 1999), which is today one of the world's most prevalent standards for sustainability reporting, released an exposure draft version of its Sustainability Reporting Guidelines that gained the first full version in 2000. Subsequent reviewed versions of GRI guidelines were released in 2002 and 2006. The last version confirms the importance of stakeholders' commitments as a principle of reporting. The guidelines have been the subject of a stakeholders' consultation at the international level to take in account their perceptions, particularly concerning the sustainability performance indicators. As of January 2009, more than 1,500 organizations from 60 countries use the GRI Guidelines to produce their sustainability reports.

The guidelines and indicators created by GRI have been used as a reference source by the most prestigious sustainability indexes such as the Dow Jones Sustainability Index (DJSI) and the FTSE4Good in their analysis of candidate organizations. These indexes have been tracking the financial performance of the leading sustainability-driven companies and have given credibility and reputation among the socially responsible investorsⁱ to those listed organizations. The Socially Responsible Investment (SRI) is growing at an overwhelming pace, driven by the challenges of climate change. In the United States, the SRI encompassed an estimated \$2.71 trillion out of \$25.1 trillion in the investment marketplace according to the Social Investment Forum's 2007 Report on Socially Responsible Investing Trends. From 2005 to 2007, social investing enjoyed a growth rate of 18%, increasing from \$2.29 trillion in 2005 (Social Investment Forum, 2009). In Europe, the total SRI assets under management (AUM) have reached €2.665 trillion as of December 31, 2007 which represented as much as 17.5% of the asset management industry in Europe. This corresponded to a remarkable growth of 102% since December 31, 2005 (European Social Investment Forum, 2008).

GRI has also released specific indicators for some sectors through their sector supplements, such as the electric utilities sector. Electric utilities provide essential and vital services to society and users, which are crucial to the growth and security of economies in all countries. However, economic growth must be achieved in a sustainable manner in order to protect key resource systems, and to provide for future generations. Specifically within the electric utility industry, there are several important factors to be considered in the economic, social and environmental dimensions.

In the economic dimension, investments in new equipment and maintenance of existing infrastructure along with assets in research and development of sustainable electricity generation, transmission and distribution technologies all require significant financial resources. In the environmental dimension, electric utilities are among the largest consumers of fossil fuels in the world. Fossil fuel combustion and other modes of electricity generation can result in wide spread environmental effects, including acid rain, climate change, radioactive and other contamination, and human health issues, if not adequately addressed in the electric power generation business. In the social dimension, electric utility assets and activities are often of a large scale, potentially impacting neighboring and distant communities. Moreover, the sector employs a workforce that can be

exposed to potentially hazardous conditions such as high voltage electrical conductors and radiation at nuclear power facilities (GRI, 2009).

Rationale of the study

As shown by aforementioned surveys on corporate social responsibility, several companies around the world are currently addressing social and environmental issues in their reports. However, some companies have issued social and environmental reports for each operating division or geographic area, some for the entire corporation only, and some have included this discussion in corporate annual reports. No matter the case, it has been noticed that several companies have provided this information in an intricate way, without aligning to their corporate strategies. Unclear or insufficient targets and key sustainability performance indicators contributes to an increase in the difficulty of a real assessment of the company by all stakeholders. This situation is not different in the Czech Republic.

This study focuses in the way companies of the electric utilities sector in the Czech Republic are reporting on sustainability issues and suggests how these companies can develop an approach based on the Connected Reporting Framework set out in 2007 by the Prince of Wales Accounting for Sustainability Project. Firstly, a brief explanation on the Connected Reporting Framework is provided. Secondly, an overview on the way the companies in this sector are responding to increased stakeholder demands for information on corporate sustainability performance is given. Then, possibilities on how these companies can implement the Connected Reporting Framework are suggested.

The Connected Reporting Framework: a brief introduction

The Connected Reporting Framework is a new approach which brings a more concise, rounded and balanced picture of organization's overall performance, which reflects the organization's strategy and the way it is being addressed. It is focused on the needs of long-term investors and executive management since it attempts to identify and explain the connection between the organization's strategic objectives, the industry, market and social context within which the business operates, the associated risks and opportunities it faces, the key resources and relationships on which it depends, and the governance, reward and remuneration structures in place. Further, it should explain the connection between delivery of the business's strategy and its financial and non-financial performance (The Prince's Accounting for Sustainability Project, 2007).

In summary, the reporting framework attempts to make the connection between strategic direction, financial performance and environmental and social considerations. For achieving this goal, three key steps are required for implementation:

- 1. Connecting business strategy and sustainability:** the identification of material sustainability issuesⁱⁱ and description of how each of these impact on the organization's strategic objectives.
- 2. Key Performance Indicators (KPIs) and actions taken:** the evaluation of action taken to address each material sustainability issue and the identification of KPIs to measure performance.
- 3. The Connected Performance Report:** a balanced assessment of progress against agreed targets and towards intended outcomes.

Firstly, in the exercise of reporting according to this framework, general important aspects about the company can be highlighted, as specified in Tab. 1.

Tab. 1: General Key aspects about the organization in relation to the Connected Reporting Framework

Company profile	A brief description about the company's products or services in a manner that laypersons, as well as industry personnel, can comprehend. Information about the company's purpose and community support can add human personality to a profile. It can also be mentioned the special awards and honours a company has garnered, the donations or volunteering its employees provide the community.
Mission	The essence of the business's goals and the philosophies underlying them. It signals what the business is all about to their customers, employees, suppliers and the community.
Vision	A brief listing of the ideals and goals that the company strives to exceed. The vision statement helps motivate the employees toward a common goal while proving to investors or shareholders that the company is heading in the right direction.
Key Strategic Objectives	Broadly defined targets that an organization must achieve to make its strategy succeed. Strategic objectives are, in general, externally focused.
Sustainability context	An analysis of the environmental and social trends which have a material impact on the sector, market and regulatory context within which the business is operating, where possible in quantitative terms and supported by evidence.
Risks and Opportunities	The connection between material sustainability impacts and issues, the achievement of the company's objectives and implications for the strategies it has adopted. In this category of information, the risks and opportunities related to each strategic objective of the company have to be identified within the sustainability context.

Source: own, 2010

Subsequently, an in-depth assessment has to be undertaken concerning the sustainability of key resources (natural, human and financial) and key relationships (e. g. supplier, customer, employee, regulator, and community) upon which each strategy is dependent. In this category, the company shall highlight the key performance indicators of each strategic objective measured on annual basis and compared it against pre-defined targets and with the average performance of the sector (benchmarking).

An overview of the current situation and trends in the energy sector in the Czech Republic

The Czech Republic has one of the lowest energy import dependencies of the European Union, mainly due to its vast reserves of coal, particularly lignite, and of uranium. In fact, coal is the main domestic energy source, representing 46.20% of total primary energy supply (TPES) in 2007. The second highest share in domestic energy production is provided by two nuclear power plants. Currently, there are four nuclear power reactors in Dukovany and two in Temelín, which in 2007 jointly contributed with 14.6% of TPES and almost one third of the total domestic electricity

production. On the other hand, Czech Republic is highly dependent on the import of crude oil and natural gas, mainly from Russia. The share of energy import on the total energy consumption was roughly 40% in 2007 (Enviros, 2009).

After the major decrease in energy consumption in the 1990s caused by economic transformation, energy demand started to gradually increase after 2000 in conjunction with economic growth, illustrated by growing production, transportation loads and household consumption.

The country has one of the highest energy intensityⁱⁱⁱ levels in the European Union due to a higher share of industrial production per GDP. The relatively high energy intensity of the Czech economy and the large proportion of fossil energy sources for generating electricity negatively impact the environment in terms of higher emission levels (Czech Environmental Information Agency [CENIA], 2008).

As part of the EU common energy policy adopted in 2007 to reduce the effects of climate change, the Czech Republic also intends to increase its production and use of renewable energy in electricity, heating, cooling and transport. Such a common energy policy for the EU also contributes to growth, job creation and increase of energy security. The country has established a commitment with the EU to achieve an 8% share of electricity generated from renewable energy sources (RES) in domestic electricity generation by 2010 and achieve a share of 13% of energy made from RES per final consumption before 2020. Energy generation from RES has been increasing by approximately 10% in the Czech Republic every year; in 2007, the total share of RES was almost 5% (CENIA, 2008). Data provided by the Czech Ministry of Industry and Trade shows that hydro power plants are responsible for more than 60% of the share of RES achieved in 2007. However, the energy from biomass is expected to play an increasing role in the energy system in the country, mainly from the use of energy crops with crop rotation and good agronomic practice. The role of wind power plants, refuse incineration plants and photovoltaic systems are rather negligible in comparison with other forms of RES.

Data provided by the Czech Biomass Association (Habart, 2005) estimates that in 2010 the highest quantitative potential of electricity generation from RES will be provided by forest biomass power plants, followed hydro power plants.

The production, transmission and distribution of electricity make an important contribution to the development and improvement of the quality of life of society as a whole. The Czech electric utility sector has undergone major changes since 2002 with the gradual liberalisation of the electricity market, which achieved its full implementation in 2006. Since that time, the households acquired the right of supplier choice and the activities in which competition is feasible, were no longer regulated on the open market. This was the case of electricity generation, electricity imports, and electricity trading. On the other hand, those activities with a monopoly nature continue to be subject to regulation. In this category is included electricity transport from the generating plant over the transmission and distribution systems to the final customers (MPO, 2007). Average gas and electricity prices for all customer segments in the Czech Republic are below the Europe-wide averages.

The distribution and supply of electricity in the Czech Republic is dominated by three companies (ČEZ, E.ON and Pražská energetika Group). These companies represent a market share of more than 95% of final customers' total consumption; in the case of small customers, their share is more than 99%. Besides these companies, there are about 10 independent suppliers actively operating in the retail market, which are offering electricity bought from smaller generators or imported from other countries mainly to large industrial customers. The electricity generation sector in the Czech Republic is similarly concentrated, consisting of a single generator (ČEZ) that accounts for 73% of

national production capacity, and a number of much smaller generators none of which have a share more than 3% of the total (EC, 2007).

The CSR and sustainability reporting in the Czech electric utility sector

In this study, the largest companies in the Czech Republic in electricity generation, distribution and supply were analyzed on how they are providing information about sustainable development issues and how far their reporting frameworks are from the effective and objective model proposed by the Connected Reporting Framework. The selected companies were ČEZ, Pražská energetika Group (PRE) and E.ON.

The core business activities of ČEZ are electricity production and sale and related support of power system. Other activities include production, distribution and sale of heat. The company released a separate Corporate Social Responsibility Report (CSR) in 2008 but in 2009 they provided all data on sustainability issues in specific chapters of their annual report. The annual report 2008 (released in 2009) was strongly focused on financial information and energy operations. However, it also addresses other important issues, such as human resources, although without any clear related performance indicator, nuclear safety, protection of the environment, research and development (R&D) and social responsibility. Their report is not based on the GRI guidelines. Besides financial and energy performance indicators, the report also provides indicators on other important issues in the environmental, safety and social agenda. In the environmental and safety dimension, it provides clear data on nuclear safety, production of electricity from renewable energy sources, water consumption, air emissions, waste and wastewater generated. In the social dimension, initiatives on corporate philanthropy through various donations are presented. It also gives brief information about the initiatives focused in the employees and customers dealing with the global economic crisis. Generally, the company gives more attention on the environmental indicators than on the social indicators in their reports and website. Their strategic objectives are clearly defined and a good explanation is provided on risks involved in their business operations. However, no targets are specified related to their performance indicators and no benchmark is done comparing the company performance in these indicators against the average of the sector in the Czech Republic or in the European Union (EU).

PRE Group, constituted by Pražská energetika and other companies, is focused in the electricity supply for the capital city of Prague and Rožtoky u Prahy and has become a major trader in electricity on the Czech Republic. It releases only annual reports. The strategies of the company are clearly defined and social responsibility and environmental protection are among them. Nevertheless, there are no sustainability performance indicators. The indicators are limited to financial, trading and technical scopes. Only descriptive information on environmental protection, safety and protection of health at work are provided. Moreover, the risk management of the company is mainly focused on financial and market risks.

The German group E.ON energy is present in the Czech Republic through five subsidiaries, being each specialized in a different energy business. In this study, a special focus is given to the company E.ON Energie, which is responsible for production and trading of electricity. Unlike other companies belonging to E.ON Group in other countries, the company has released no CSR or sustainability report so far but only annual reports. However, the last edition of annual report available in English dates from 2005 while the last annual report in Czech language was released in 2009. The same evidence has been found for the other companies of the group in the Czech Republic. The group in the Czech Republic addresses CSR issues, although it reports only briefly about each of them. These issues are: transparent and ethical entrepreneurial activity and positive relationships with the

investors, customers and suppliers as well as with other business partners, environmental protection, investment in work environment and community involvement. Therefore, it seems that the Czech companies of the group are mainly relying on the reputation gained by E.ON Group in other countries in the field of CSR in order to maintain its reputation in the country and remain attractive for investors. Moreover, the company does not report on a clear way their key strategic objectives and gives no references to the risks and opportunities related to their business. Finally, only financial data related to their income, cash flow, investments and assets are provided. The E.ON energy Group as a whole has clear defined strategic objectives but these objectives are not clearly endorsed by its Czech subsidiaries.

Tab. 2 summarizes the evidences aforementioned resulting from the analysis of these companies based on their websites, annual reports and CSR or Sustainability reports when available. Tab. 3 summarizes the analysis of the companies according to key reporting aspects that are essential themes in the Connected Reporting Framework.

Generally, the companies operating in the electric utility sector in the Czech Republic do not measure and report on social indicators within the scope of sustainability, such as: investment in workplace safety and employees' health, professional training and development, diversity of employees, customer relationship, among others. Instead, they mainly rely on social indicators related to donations for educational and cultural projects, as well as sport events. This attitude denotes a higher orientation towards philanthropy over other social issues.

In the environmental dimension, generally the companies report on electricity consumption. However, only ČEZ report on important indicators such as: water consumption, hazardous and non-hazardous waste, wastewater and emissions of air pollutants.

Other important indicators that could be addressed by local companies are: greenhouse gas (GHG) emissions intensity^{iv}, percentage of waste recycled, reused or sold, and investment in the abatement and offsetting of greenhouse gas emissions. Even those indicators that are reported by ČEZ could be presented in another way like: energy intensity as the energy consumption per direct economic value generated (in KJ/unit of CZK) or water consumption intensity (in cm³/unit of CZK).

Tab. 2: Reporting coverage on CSR and sustainability issues among the largest companies in the Czech electric utility sector

Company Name	Annual Report	CSR/Sustainability Report	Environmental and Social Coverage in the Website
ČEZ, a. s.	Yes (last 2008)	Yes (last 2007)	Environment protection only
PRE Group	Yes (last 2008)	No	Environment protection and philanthropy only
E.ON Energie, a.s.	Yes (last 2005)	No	Environmental protection and corporate responsibility

Source: Annual Reports, Sustainability Reports and websites of analyzed companies, 2010

Tab. 3: Summary of the analysis of the largest companies in the Czech electric utility sector according to key reporting aspects that are essential themes in the Connected Reporting Framework

Company Name	Strategic Objectives	Risk And Opportunities	Targets	Sustainability KPIs	Benchmark
ČEZ, a. s.	Clearly defined	Yes, but not in sustainability context	Not specified	Yes, but not in an integrated way	Not provided
PRE Group	Clearly defined	Yes, but not in sustainability context	Not specified	Not available	Not provided
E.ON Energie, a.s.	Not available	Not available	Not specified	Not available	Not provided

Source: Annual Reports, Sustainability Reports and websites of analyzed companies, 2010

Conclusions

The present study demonstrates how the largest companies in the Czech electric utility sector are still lagging in terms of reporting on sustainability issues. As a result, the implementation of the Connected Reporting Framework in these companies might become a very complicated and time-consuming task if the data necessary for reporting accordingly is not available in the internal company information system. In this case, new indicators need to be created and the corresponding amounts of resources necessary for their monitoring and control have to be allocated.

Nevertheless, major efforts in monitoring and reporting on key sustainability performance indicators might bring a fair return in terms of energy efficiency improvements, cost saving opportunities, increase of reputation and customer loyalty, talent attraction and retention, and investment attraction if the company is listed in the stock market. As previously stated, it has been evidenced by European SRI Market Study a remarkable increase of capital assets involved in SRI, which in turn clearly demonstrates a growing interest of responsible investors, particularly large institutional investors, in this area.

The Connected Reporting Framework, when well implemented, brings a clear picture of the current performance of the company against pre-defined targets and enables the investment analysts to better evaluate it in comparison with other companies in the same sector. A major progress on sustainability indicators that are commonly addressed by DJSI and FTSE4Good indexes can result in valuable investment capital attraction.

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- i Socially Responsible Investors include individuals and also institutions, such as corporations, universities, hospitals, foundations, insurance companies, public and private pension funds, non-profit organizations, and religious institutions.
- ii Material sustainability issues are those which are really important for many stakeholders, commercial success and for internal management. They demands real recognition and effort by the company and they have the potential to affect the perception of the company.
- iii Energy intensity gives an indication of the effectiveness with which energy is being used to produce added value. It is defined as the ratio of Gross Energy Consumption to Gross Domestic Product.
- iv GHG emissions per gross revenue.