

# EU TAXONOMY FOR SUSTAINABLE ACTIVITIES: A SOURCE OF DECOUPLING OR A PATHWAY FOR GREENING THE CONSTRUCTION INDUSTRY?

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The European Action Plan on financing sustainable growth sets new legislative demands to meet the Paris agreement obligations and fulfil the ambition to make Europe CO<sub>2</sub> neutral by 2050. An important element in this respect is the EU taxonomy. In this paper, we ask the question how a construction organisation implements strategies in relation to the EU taxonomy and analyse the strategic responses throughout the organisation. The study builds on qualitative data from a large Danish construction company. Through an institutional theory perspective, we explore how and with what effects the regulation is received and implemented at different levels of the organisation. The preliminary results show that the taxonomy is a source of decoupling and that different levels of the organisation respond differently to the regulation with focus shifting from ensuring compliance at a strategic level to a more practice-orientated approach on the project level. In conclusion, it is argued that the taxonomy as a policy tool to greening the construction industry is still underdeveloped and immature as displayed by the observed decoupling between policy instrument and project practice.

Keywords: EU; taxonomy; institutional theory; organisational response; sustainability

## INTRODUCTION

The climate is in rapid degradation and according to Intergovernmental Panel on Climate Change (IPCC, 2022) global warming is causing irreversible threats to ecosystems, biodiversity, and human systems. This calls for radical measures and UN (2015) and the European Commission (2019, 2021) have accordingly agreed on several policy initiatives to counter the climate changes and create political pressure in the aim of e.g., minimising CO<sub>2</sub> emission globally. As the construction industry is responsible for a large part of the global pollution and use of finite resources, much attention is placed on developing solutions to the environmental problems it causes. Despite an increased focus on sustainability, the Danish construction industry has not contributed to a significant CO<sub>2</sub> reduction (Danish Climate Council, 2021). This could be a result of the various ways organisations respond to policy and regulatory pressure (Weigelt and Shittu 2016) or highlight a potential conflict in the relationship

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between political influence and organisational behaviour, as recent strategies have only led to corporate greenwashing (European Commission, 2018). To unfold these mechanisms, we focus on the attempts of a construction organisation to implement the EU taxonomy regulation and analyse the strategic responses at different levels of the organisation.

In the quest for ensuring economic growth without compromising environmental concerns, the European Commission (2018) has published an action plan for financing sustainable growth. The action plan aims at creating a more sustainable path for the European economy and suggests a series of actions that collectively should guide governments in Europe and inspire sustainable investments around the world. The actions is furthermore, answering three main development categories: (1) reorienting capital flows towards sustainable investment in order to achieve sustainable and inclusive growth, (2) managing financial risks stemming from climate change, resource depletion, environmental degradation and social issues and (3) fostering transparency and long-termism in financial and economic activity (European Commission, 2018).

The first action within the first category entails the establishment of an EU classification system for sustainable activities also referred to as the taxonomy regulation (European Parliament and the Council, 2020). Companies subject to the Non-Financial Reporting Directive (NFRD) are required to disclose information on taxonomy-eligible and taxonomy-aligned activities, defined as the proportion of a company's revenue, capital expenditures and operational expenditures. This information is intended to provide investors with insights into companies' sustainable activities, increase transparency, limit the risk of greenwashing, and provide a comparison tool for stakeholders.

Extant research has, however, demonstrated that organisations differ much in complying with regulation. A central factor is that regulation often is general in nature and developed without considering, which opportunities different companies must meet the requirements (Hillary, 2017). Moreover, it has also been documented that enforcement action often involves uncertainty, which can lead to resistance or other forms of non-compliance (Desai, 2016) that may inhibit the diffusion of regulation into practice. On this basis, we explore how an organisation integrates the legislation and discuss whether the taxonomy regulation has the intended effect on improving sustainable initiatives or constitutes a source of decoupling or resistance.

### **Organisational Responses to Regulation**

The theoretical approach to the study builds on an institutional understanding of organisational responses to regulation. Institutional theory is well-suited for this purpose due to its focus on how social, political, and cultural (i.e., institutional) factors influence the performance and operation of organisations.

Institutional theory posits that organisations conform to prescriptions of legitimate behaviour that stem from the institutional environment in which they are embedded. Early institutional literature emphasised processes of isomorphism, and the factors leading to organisations becoming increasingly uniform. Meyer and Rowan (1977) e.g., argued that formal organisational structures arise as reflections of rationalised rules in society. DiMaggio and Powell (1983) moreover described the apparent paradox that actors make their organisations increasingly similar as they try to change them in response to externally induced uncertainty and constraints. In particular, state

influence, stemming from transactions with public agencies and regulation in the form of legislation or standard setting, was considered to drive this process.

While early institutional theory assumed a somewhat causal relationship between such institutional influences and organisational responses, more recent contributions have proposed that a more heterogeneous relationship is at play. Greenwood *et al.*, (2010) have e.g., demonstrated that organisations respond differently though patterned ways to the complex institutional contexts they face. In this perspective, organisational responses are influenced by a host of specific organisational attributes, such as the organisation's position in the field, structure, identity, etc. (Greenwood *et al.*, 2011).

Such findings have highlighted that the relationship between an organisation and its institutional environment is complex, and that there exists anything but a causal link between changes at the level of the field and the organisation's operation. This is also the case when it comes to legislative and regulatory influences. Extant literature on how organisations respond to regulation has shown that organisations deploy different strategies when complying with regulatory mandates. Policy and regulatory compliance often involve uncertainty (Weigelt and Shittu, 2016), which may lead to resistance, decoupling, co-optation, symbolic action, or other forms of non-compliance (Desai, 2016). Pedersen *et al.*, (2013) moreover illustrate that non-conformance with regulatory requirements is not solely about conscious resistance, but that lack of awareness, misinterpretations and resource limitations may influence this result.

Other strands of research on organisational responses to regulation acknowledge the heterogeneous relationship between regulation and organisational impact, yet focus on the possible tensions that may arise, as organisations respond to institutional pressure and attempt to balance between conformity and operational efficiency. Here focus is directed towards issues such as understanding: (1) how a degree of institutional fit between organisational practices and regulatory demands can be maintained (Boon *et al.*, 2009), (2) how regulation is adapted to and impacts organisational practices (Ahrens and Khalifa, 2015) or (3) the strategic behaviours that organisations may enact when responding to pressure to conform with their environment (Oliver, 1991).

As this brief exposition of the literature on organisational responses regulatory pressure illustrates, there are many possible processes and ways to approach the issue at stake in this study. We use these insights in the analysis to explain how a construction company works with the taxonomy regulation and what issues arise.

## **METHOD**

The case concerns a large Danish construction company that is structured as a multi-divisional organisation consisting of a holding company (referred to as 'Holding') and five subsidiaries. In 2021, the company's annual turnover was a €940M making it one of the largest Danish construction companies. We focus on Holding and one of its subsidiaries that accounts for one third of the total turnover. In 2021, the subsidiary employed 700 persons with core activities within renovation and new-build projects for public, private, and social housing association clients. Besides production departments, the subsidiary also comprises departments within finances, human resources, IT, marketing, prequalification, and project development.

Holding defines strategies, financial structures, and overall targets for the entire company, while the subsidiaries are self-governed units that undertake different construction disciplines, such as renovation, new built and infrastructure projects. The

company strategy has a strong focus on development, collaboration, and sustainability in accordance with the national climate law and strategy for circular economy (Danish Ministry of Climate, 2020; Ministry of the Interior and Housing, 2021).

Holding is responsible for corporate social responsibility (CSR) reporting in accordance with the NFRD (European Commission, 2014) and is thus responsible for the taxonomy reporting. In their CSR report, Holding has defined five development areas in support of environmental and social sustainability: (1) 'local and social responsibility' that aims at e.g., increasing the number of female employees, (2) 'health and learning' that aims at decreasing injury rate and prioritising internal education, (3) 'climate and environment' to reduce CO2 emissions, (4) 'circular economy' with an aim of reaching 70 percent recycling rate; and (5) 'collaboration and certifications' that aims at increasing the proportion of environmentally certified (i.e. DGNB) projects.

### Data Collection

The empirical material consists of qualitative data gathered from documents, observations, and interviews. The document analysis is based on legal documents, including the EU delegated acts of the taxonomy regulation and Holding's strategy, annual financial- and CSR reports. We also draw on 20 hours of observations at strategy meetings related to the taxonomy, and 12 interviews covering organisational responses to the taxonomy in Holding, the subsidiary and at the subsidiary's project level. All interviews were conducted on basis of a semi-structured interview guide supported by open-ended questions making the respondent talk as freely as possible. The interviews were conducted with informants from Holding as well as top managers from the subsidiary's different operational areas as shown in Table 1.

Table 1: Respondents in the study

Respondents from Holding	Respondents from the subsidiary
Head of Sustainability (2 interviews)	Head of Sustainability
Technical Sustainability Manager	Contract Manager
External Consultant on Sustainability and Finance	Chief Financial Officer
External Consultant on Sustainability	Head of IT
	Chief Marketing Officer
	Business Area Director
	Production Support Manager

### ANALYSIS

As is illustrated in Figure 1, the analysis is structured into three parts unfolding the organisational responses to the taxonomy regulation at different organisational levels. The aim of the analysis is to understand how the taxonomy regulation as policy instrument affects a construction organisation and if the intention of accelerating sustainability reaches the project level. Furthermore, we aim to illustrate that such organisations not necessarily constitute a unitary entity that responds uniformly to regulation. This is accomplished by analysing the strategic responses and engagement of compliance at different levels in the organisation. First, we describe the strategic response at the level of Holding as they have the overall strategic responsibility for the company and communicate the taxonomy demands to the subsidiaries. Second, we describe the strategic response at the subsidiary level and analyse how different departments conform and decouple the guidelines formulated by Holding. Finally, we

describe the responses at the project level within the subsidiary as they are met with new requirements for data collection.

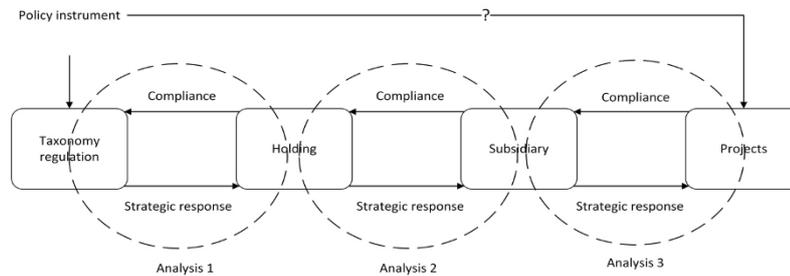


Figure 1: Levels of analysis in the study

### Holding's Response to the Taxonomy Regulation

Since 2014, Holding has published CSR reports with a strong focus on environmental and social elements, presenting their proclaimed strong engagement and responsibility towards sustainability. In Holding, the team working with sustainability sees the taxonomy regulation as an opportunity to distinguish the company from its competitors and market the company with a strong sustainable profile.

Even though the taxonomy reporting is mandatory, there has been limited government involvement in disseminating taxonomy guidelines to corporations at a national level. Consequentially, Holding's Sustainability Manager who is responsible for preparing CSR reports, and hence the taxonomy reporting, has relied on internet forums and casual dialogue with industry colleagues to gather necessary information regarding the taxonomy. The information and knowledge level in Holding is thus a result of scattered inputs and the Sustainability Manager's personal desire to understand the taxonomy regulation. As the Sustainability Manager says: "after having read sporadically about the taxonomy regulations, I realised that we need to get started on this, and we need to get started right now, and I need help". The Sustainability Manager has therefore arranged internal taxonomy working groups and established external advisory guidance. This is done to understand the scope and future relevance of the taxonomy and minimise risk by balancing the company's investment level in the aim of not under- or overperform.

However, Holding is continuously working to strengthen their CSR profile and the added value from a potentially positive taxonomy score could benefit the company and is therefore not overlooked. As the Sustainability Manager has had the leading role in collecting taxonomy data from the subsidiaries, there has been a lot of dialogue with the entire organisation. Even though the investment level and strategic response have been debated, there is a common understanding in Holding of the relevance and opportunities in aligning projects with the taxonomy. This has resulted in a continuous knowledge seeking mentality in the sustainably team, however the challenges that the taxonomy regulation prompts are also evident in Holding. Reflecting on the role of the finance department in the taxonomy regulation, the Sustainability Manager e.g., comments: "It's a culture crash [...] now sustainability has to be calculated in financial terms [...] and they are super sceptical [...] and they have complained, they have complained a lot".

### The Subsidiary's Response to the Taxonomy Regulation

In the subsidiary the taxonomy responsibility is also centred around the Sustainability Manager, even though the reporting demands rest under a financial legislation. The

scope of the taxonomy regulation in respect of purpose and demands has been scattered throughout the organisation and elements of information have been traveling from top management to the construction projects with mixed interpretations.

In the preliminary stages of implementing the taxonomy, there has been a tug of war between financial, marketing, and environmental concerns regarding priorities and how to comply with the regulation. At the top management level, there is an insecurity about the actual impact of the taxonomy regulation, which has resulted in an indefinite strategic response and a general 'wait-and-see' attitude - albeit with important differences in different areas of the subsidiary. The marketing department has a positive attitude towards the taxonomy, as they see it as a source of new business opportunities and has consequently assumed the strategic responsibility for driving the implementation of the taxonomy, as the department has the client contact and a strong relation to the market.

The subsidiary's Sustainability Manager is affiliated with the marketing department and is in direct contact with the Sustainability Manager in Holding. The subsidiary's Sustainability Manager has been one of the first actors to take responsibility and initiate taxonomy-related work tasks relevant to the subsidiary, with a focus on collecting data from the construction projects. In collaboration with the subsidiary's IT department, he has established a new data system. The aim of the system is to make data management easier and create a platform that provides a better internal overview of sustainability data. He strongly acknowledges the importance of data and strives to make the organisation more data driven in general to improve the handling of sustainability demands in the future. Besides an interest in documentation and data collection, the Sustainability Manager also believes that the taxonomy regulation has created an opportunity for a new sustainability awareness in the subsidiary: "It helps us create a cultural change, and a wide awareness of sustainability".

The financial department exhibit a general reluctance to implementing organisational changes. The fear of doing too much work on something that could possibly lose momentum is a risk not to be overseen, as the Chief Financial Officer argues: "it is like GDPR, when it rumbled out [...] there was also a lot of things we were supposed to do [...] but that throttled down again".

As sustainability-related work activities slowly influence different departments, the added workload creates barriers that potentially could dis-align the organisation's common taxonomy acceptance and further sustainability strategy. The Chief Financial Officer thus continues: "My approach is that we should deliver what we need to deliver, but not set the bar too high and not being first movers [...] And then we must be ready if it gives us a competitive advantage [...] So, it is a bit of a balance". The combination of uncertainty regarding future market demands and the mix of economics, legal work, data handling, production, CSR strategies and sustainability in a joint legislative framing, creates uncertainty related to both the strategic response and the character and level of compliance. This uncertainty is clearly reflected in the organisation as the different departments have different perceptions of how to respond strategically and implement taxonomy standards in the organisation.

### **Strategic Responses to the Taxonomy Regulation at the Project Level**

At the project level, the Production Support Manager is responsible for aligning the construction projects with the subsidiary's documentation systems - and thus the

taxonomy data from the construction projects. The Production Support Manager is in direct contact with the project managers and creates a link between the sustainability demands nested in the IT department's newly created system, and the construction projects. The Production Support Manager has been involved in several meetings to develop taxonomy standards for better and easier data collection, and he plays a key role when implementing new sustainability systems.

As the Production Support Manager acknowledges the need for data collection, he explains that in the future there is a need to hire employees who can support collection of data. As argued: "We need to get someone who has this perspective, [...] and make sure we get the right things reported, so it is actually useful in the end". Data is thus an important element, and the Production Support Manager has worked with several DGNB projects that required extensive project data. But data collection is one thing, understanding the purpose is another: "...they [craftsmen and project managers] do not need to know that once a year a huge calculation [taxonomy reporting] takes place [...] but we must obtain an understanding of why they should report data in this way".

The Production Support Manager explains that he struggles with understanding the purpose of the taxonomy regulation, and that if sustainability is important, there are several practical alternatives that could contribute more to reducing CO<sub>2</sub> than reporting for the taxonomy regulation, e.g., turning off construction lights when they are not needed. He explains that a contractor in general has only little influence on clients' design decisions and that optimising the construction processes is more useful than buying specific products: "It is crazy that we have to count and look through invoices to see how many urinals we have bought [...] we need to focus on what we can change and what makes sense".

While there is great will to promote sustainable construction at the project level, the Production Support Manager explains that the project managers should rather focus on practice-orientated elements that will create direct substantiable outcomes instead of wasting time counting toilet types: "an emission-free construction site [...] that is something I can influence". The general lack of focus on practice orientated on-site sustainability triggers frustrations for the Production Support Manager. He explains that it makes no difference for a contractor if the client chooses low flow urinals because it is only related to operation and maintenance.

The Production Support Manager also elaborates on the importance of understanding the purpose of regulation. Besides the complicated language and technical difficulties of the taxonomy, the consequences of changing documentation practices create resistance, making actors struggle with justifying the added workload. To comply with the regulatory mandate and limit the resistance, a common understanding of the taxonomy regulation is essential. As the Production Support Manager explains: "We need to get the taxonomy translated into plain language, or you never get them [the employees] interested in it". This indicates a necessity for communicating taxonomy regulation demands and describing the purpose, not only to sustainability managers and marketing departments, but throughout the entire organisation.

## **FINDINGS**

In the analysis, we have described three levels of the case organisation and how they respond and comply with the taxonomy regulation. We summarised the findings from the analysis in Table 2. On this basis we now unfold the institutional processes at play at the different levels of the organisation.

Table 2: Institutional processes in relation to the taxonomy at different levels in the company

	Holding	Subsidiary	Project level
Strategic response to institutional pressure:	Balanced response; Following the market	'Wait-and-see' attitude; Passive conformity	Decoupling from taxonomy intention
Basis of attention:	Competition; Full compliance with taxonomy regulation	Awareness; New opportunities; Counter greenwashing	Expedience; Focus on practice-oriented initiatives
Compliance responsibility:	CFO and Sustainability Manager	Sustainability Manager	Production Support Manager
Level of compliance interest:	Full compliance	Medium compliance	Low compliance
Strategic operational responsibility:	Sustainability team; CFO	Sustainability Manager	Not involved
Strategic behaviours / Practice adaptation:	Expansion of sustainability team	Implementation of new IT system	Collection of new types of data
Degree of institutional fit to regulation:	Tight regulatory-political fit	Partial social-normative fit	Low cultural-cognitive fit

In Holding, the taxonomy is seen as an additional strategic opportunity by the sustainability team to create market legitimacy for the company. This is achieved by describing a devoted taxonomy involvement in the CSR report. Furthermore, Holding closely follows the market, and the insecurity regarding the forthcoming compliance level is clearly reflected in the choice to continuously gather a high level of information. Due to uncertainties regarding the impact of the taxonomy, Holding seeks strategic support from CSR consultants and financial auditors and thus simultaneously works on understanding the scope and creating a corporate strategy that fits within the institutional environment (Boon *et al.*, 2009). This means that the corporate response transpires in an institutional political context as Holding seeks a balanced response following both market development and political obligations.

In the subsidiary, the taxonomy regulation influences processes in many operational areas. Nevertheless, taxonomy-related tasks are centred around the Sustainability Manager, who are responsible for collecting and passing on project information to Holding. As previously stated, tensions may arise when organisations try to balance conformity and operational efficiency accompanied by institutional pressure. There are various ways organisations can respond to such pressure (Oliver, 1991) and organisations are not always conforming to the expectations from the environment. In the case, we nevertheless see that there is a general understanding in the subsidiary of following the taxonomy development and creating operational systems for conforming to documentation criteria.

At the same time, the future impact of the taxonomy is indistinct and creates strategic insecurity and a 'wait-and-see' attitude. Furthermore, as Ahrens and Khalifa (2015) describe, organisational meaning-making is necessary to comply with regulation. This is substantiated in the case, as the subsidiary's Sustainability Manager seeks to legitimise the taxonomy work in the organisation as an opportunity for increased substantiality awareness and creation of cultural-cognitive changes to support nuances of the concept of sustainability.

At the project level, the organisational response to taxonomy regulation resembles a distinct type of decoupling described by Bromley and Powell (2012) as a means-ends decoupling. When data necessary for complying with the regulation is collected, internal taxonomy strategies are implemented in practice, but they also have a weak link to the organisation's practice-orientated approach to sustainability at the project level. This is highlighted in the analysis by the Production Support Manager, being

responsible for aligning project-level activities with new requirements forwarded by the department heads, who argues that the taxonomy regulation is perceived as a policy tool rather than a tool that is expedient in the projects.

This perception contributes to decreasing the experienced institutional pressure as the taxonomy regulation is framed as inexpedient in projects. Employees working at the level of the project thus collect and report taxonomy regulation data demanded by the department heads, but distance themselves from the idea that the regulation should be more suitable than other instruments to promote sustainable construction. A consequence hereof is a low level of compliance at the project level and a low degree of institutional fit.

Finally, the analysis has illustrated that the aim of a taxonomy as competitive tool to distinguish companies' sustainability efforts from each other may be at risk, being undermined and instead give rise to isomorphism (DiMaggio and Powell, 1983). The current strategic response from Holding thus rests on a "balanced" insecurity between under- and overperforming. When faced with uncertainty associated with the need for new resource investments (Weigelt and Shittu, 2016) companies may thus be inclined to aim at being in the "middle of the class" to reduce financial risk while maintaining legitimacy. This in turn may compromise the intention of the taxonomy as a pathway for greening the construction industry.

## **CONCLUSION**

The focus in the paper has been to explore how a construction company responds to new sustainable regulation. We have examined the taxonomy regulation, which represents the European Union's latest policy attempt to meet the climate obligations. We have focused on three different parts of a Danish construction organisation and analysed the strategic responses and level of compliance in relation to the taxonomy regulation. We found that the different levels of the organisation respond differently to the regulation. The basis of attention shifts from regulatory fit and high strategic response at Holding, to a more practice-orientated approach on project level, focusing on hands-on initiatives that promote operational sustainability partly regarding regulation demand as non-instrumental.

Through the analysis, we displayed some elements of isomorphic tendencies at Holding level, as the response to the taxonomy unintentionally places the company in a stream of uncertainty, which results in desires to neither under- nor overperform. We thus conclude that the taxonomy as a competitive investment tool is still underdeveloped, and immature as displayed by the observed decoupling between policy instrument and organisational practice.

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