Managing Transparency and Legitimacy in Startups

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Abstract In recent years, society and companies have faced numerous crises, which have devastated not only the economy but also the confidence of stakeholders, especially that of investors and funders. This fact has resulted in entrepreneurs fighting to raise funds for their projects, regardless of the life phase of their projects. In this sense, the scientific evidence literature indicates that reducing the asymmetry of information between a company and a funder or investor is necessary. The responsible management of companies and how they disclose non-financial information translates into an improvement in transparency, having an impact on reputation, image, legitimacy, and results and therefore on improving access to new funds and better conditions. This chapter discusses the importance of transparency as a form of engagement with stakeholders and especially with funders. The development of new technologies acts in favor of transparency in that society can obtain information from companies at the click of a button. That is why companies must maintain an attitude of resilience to changes in the environment. So, the challenge is to know how to use these variables to their advantage, that is, how appropriate use of information and transparency allows them to send positive signals to an increasingly demanding market with companies.

Keywords Transparency · Legitimacy · Entrepreneurs · Risk · Financing

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P. Sendra-Pons et al. (eds.), *New Frontiers in Entrepreneurial Fundraising*, Contributions to Finance and Accounting,
https://doi.org/10.1007/978-3-031-33994-3_9

1 Introduction

Access to financial resources and the conditions of term, cost, and enforceability are challenging for most entrepreneurs. Therefore, scientific evidence and public institutions have tried to highlight and demonstrate this financial problem, for most entrepreneurs, by implementing new instruments and mechanisms. That is why we can find numerous initiatives to face this challenge such as public aid, mutual guarantee societies, participative loans, and venture capital entities (Palacín-Sánchez and Di Pietro 2016). In the case of consolidated entrepreneurs, we find bank loans, or secondary markets, among other options, that try to mitigate, or at least soften, this challenge (Palacín-Sánchez and Di Pietro 2016).

Both founders and investors face cases where the uncertainty is so extreme that it qualifies as unknown: they decide to invest in ideas for markets that often do not exist yet, and they propose new products and services without knowing if they will work. Rather than simply being faced with decision contexts where probabilities are unknown (e.g., Knight 1921), entrepreneurial investors are faced with the kinds of "unknown unknowns" (Diebold et al. 2010), which include both uncertainty and noise due to a large amount of unsystematic risk and evolving certainty conditions around systematic risk (Knight 1921; Foss and Klein 2012). They must decide between uncertain solutions for a market and, at the same time, deal with the inherent uncertainty about the services, products, and markets themselves. This is the equivalent of "chasing an invisible moving target." Due to this problem, entrepreneurs have great difficulties in accessing financing, and this in many cases represents a major break in the development and even in the birth of new business projects (Blumberg and Letterie 2008; Krasniqi 2010; Vega et al. 2017).

That is why it seems necessary to continue investigating the process of obtaining financing for entrepreneurs, regardless of their phase, to detect new items that can help focus on the arduous task of obtaining financial resources for these business projects (Cassar 2004).

This work aims to face the reduction of uncertainty since we must be aware that, to access financing, we must provide information about the company to investors and lenders, regardless of whether it is a venture capital fund, microcredits, crowdfunding, crowdlending, or even in the more advanced levels of business projects in the stock market (Kerr and Nanda 2009; Hemer 2011; Shane 2012; Tomczak and Brem 2013; Ghosh and Guha 2014). In addition, in line with the above, there are several authors who point out that part of the problem of access to financing is of agency and information asymmetry (Denis 2004; Mahagaonkar 2009; Beck 2013). In this sense, it is very important to work to mitigate the decompensation of the information available to the parties involved (the entrepreneur and the investor), so that both parties can face the prospects with a little more security (Berger and Udell 1998; Jaworski 2012). The problem of acting in a context of information opacity translates into a manifest inability on the part of financing providers to know perfectly the quality of investment projects, which in this case are entrepreneurs or companies, so that distortion is generated in the efficient allocation of financial resources. Specifically, these asymmetries, which have been studied for decades, can manifest themselves in the well-known problems of adverse selection (Akerlof 1970; Jaworski 2012) or moral hazard that occurs when one of the intervening parties can be affected by actions taken by the other party that is not easily observed, because the information is difficult to verify (De Meza and Webb 1987).

Currently, entrepreneurs have at their disposal numerous ways to access financing, adapted to the different phases of maturity of the company, but in many cases, it faces difficulty on the part of the lender or investor to identify the most relevant entrepreneurial projects. This situation is transformed into a generalized tightening of the conditions of access to credit, which can sometimes generate an expulsion effect of the best and most solvent business projects since sometimes they are not willing to obtain financing with the required conditions (Minola and Giorgino 2008).

Bearing in mind all the above, it is necessary to know if there is any way to improve the interest of investors, in business projects, both new entrepreneurs, and those already consolidated. So, we understand that one way to answer this question is to consider as an objective of this work and analyze the importance of showing clear and transparent information about the company, in order to give the best possible image for future investors and financiers.

With this, we intend to take a step forward so that the company is better prepared to access what it wants from the existing types of external financing.

2 The Financing of Entrepreneurial Projects

In recent decades, research has been carried out on the difficulty of access to financing according to the needs, of companies, especially when they need it most, which is in its initial phases, or when they are going through a wrong time, in fact, this is one of the main factors that affect business failure (Díaz et al., 2014; Fernández-Portillo et al., 2018).

More than two decades ago authors such as Carpenter and Petersen (2002) noted in their research on this problem, which is also increased in the most innovative projects, due to the doubts generated by the return on investment associated with projects with a strong technological component (Riding et al. 2012; Hoyos-Iruarrizaga et al. 2017).

New business projects, especially those associated with new technologies, sometimes present difficulties for their commercialization, either due to a lack of maturity in their development or ignorance of the markets. In line with this, potential investors value them with a lot of risks, because they are usually associated with expensive and innovative processes, longer maturation periods, strong depreciation due to obsolescence, difficulties in communicating the milestones achieved, lack of management and marketing skills on the part of entrepreneurs, and uncertainty regarding the acceptance of the new product or service (Hoyos-Iruarrizaga and Saiz-Santos 2010; Riding et al. 2012).

In many cases, investments are based on a new and sophisticated technology or technical knowledge, which makes the investor have less information than the entrepreneur about the project to be financed, generated in most cases, by the lack of precedents in similar projects; the impossibility of carrying out an analysis of rigorous risk, which delimits access to financing; and the difficulty of recovering the investment in case of liquidation (Hoyos-Iruarrizaga et al. 2017; Minola and Giorgino 2008).

This situation means that new companies with an innovative profile cannot access bank financing due to the difficulty of demonstrating their solvency and providing guarantees, so this is not the ideal type of financing for new entrepreneurs (Freel 2007).

In this line, the business angel continuously searches for information about new entrepreneur's projects, for choosing the best project to invest in. If they do not have information, they invest in projects for intuition, with the risk added (Huang and Pearce 2015).

3 Information and Transparency: A Positive Sign for Investors

3.1 Transparency as a Vehicle for Generating Value

The concept of transparency is characterized by being of high complexity. That is why it cannot be understood as meaning that the level of transparency of the company is subject only to the rendering of its accounts or the information that it transmits to its stakeholders. Thus, Marcuello et al. (2007) identify as a transparency the company's ability to be available and capable of providing any type of information. In this line, Villanueva (2011) understands transparency as the position assumed by entities, whether public or private, to behave based on ethical standards and whose processes and results can be presented to all those who need their knowledge. This implies that the company will not be able to make distinctions between the stakeholders with which it relates. If the company were to consider that the level of transparency depends on the impact that the different stakeholders had on its activity, it could be more inclined to be more transparent with its investors, but very little with consumers or with society. Therefore, Ruiz et al. (2008) defend that the need to be transparent cannot only be identified by investors since the decisions of the company have an influence as a greater or lesser impact on all the stakeholders of the same. Therefore, transparency can be defined as the set of mechanisms whose main functions are the verification and evaluation of business actions and the analysis and communication of secure and truthful information by the different stakeholders of the company (Prado-Roman et al. 2018; Gálvez et al. (2009).

Transparency is an element of enormous relevance in all areas since it has been identified as a generator of both reputation (Baraibar and Luna 2012), trust

(Arredondo et al. 2014) and legitimacy (Díez et al. 2014). In order for transparency to be considered a generator of trust, the company must be able to respond to all the questions raised by any of its stakeholders about the operation of this. We must consider that the development of ICT and the accessibility to information of companies will increase the possibilities for investors to make more convenient decisions (Kliksberg 2003). This is because the concepts of transparency and information have been able to reduce the asymmetry between the company and the information related to decision-making known to the different stakeholders (García et al. 2016), and among them, we find investors and financiers.

The disclosure of both financial and non-financial information involves an exercise in self-criticism, are we transparent? Who do we want to provide information to? The first transparency exercise will be the search for the interest groups that the company has, how they define them, and how they prioritize them (Bonilla-Priego and Benítez-Hernández 2017). In this way, it shows the commitment not only that the company towards its stakeholders, in addition to transferring the company, focuses on the search for a greater benefit in the short term but also that sustainable decisions are made, and these can influence the different stakeholders of the company (López et al. 2007). In addition, a higher level of transparency will allow the company to enjoy a higher valuation, reduce financing costs, improve the return on its investments, and give investors a greater ability to focus their investment decisions on this company, as well as improve their reputation in the market (Gibbins et al. 1990; Lev 1992; Watson et al. 2002; Baraibar and Luna 2012).

By now we know that transparency is key in the strategic management of the company. According to how the company decide to manage it, it can serve as a vehicle for legitimacy, reputation, and trust with stakeholders. An example of successful transparency management can be found in companies that year after year present themselves for awards where the use of corporate social responsibility reports has transparency as its main focus. One of these awards is the Ecumenical Social Forum's award for the best report, where the level of disclosure of both financial and non-financial information is valued; those companies with a high degree of transparency are awarded year after year. On the other hand, it is also known that bad transparency management can lead to such a significant loss of trust that it can lead to a decrease in the company's legitimacy and reputation, as well as to a significant decrease in its overall stock market and economic valuation. An example of mismanagement of transparency can be found with the Volkswagen case where since 2008 it begins an environmental awareness campaign manifesting on the one hand a commitment to both the environment and society. It is in September 2015 that the scandal comes to light. The Volkswagen group revealed the use of a software that allowed the avoidance of NOx gases when certain tests were carried out on vehicles. This lack of transparency caused not only economic repercussions worldwide with a significant decline in sales, a stock market loss of more than 31% on the German stock exchange and about 52,028 million €, but a reputational loss that to this day has not yet recovered.

3.2 Corporate Social Responsibility as an Element that Enhances the Financial Attractiveness of the Company

Globalization has led to spectacular growth in the interrelationships of the agents operating in the world, with the main consequence of increasing the power of large multinationals. The role of new technologies (Prado 1995), the inclusion of ethical values in the company's strategy (Bañon et al. 2011), the need to increase the reputation and value of human capital (Lipovetsky 2006), as well as the need to disclose all the actions and measures they carry out (Escamilla-Casado et al. 2016) imply that the business paradigm changes.

CSR focuses "on the voluntary integration by the company, both in its form of governance and management, of social, environmental, economic concerns and respect for Human Rights derived from the relations that the company maintains with its direct stakeholders, as well as with any person who is affected by the development of its economic activity" (Escamilla-Casado et al. 2016:196). In short, it is about assuming a responsibility that goes beyond what is legally required and that is focused on improving the social and economic well-being of the company, as well as the environment that surrounds them.

Those who really make an evolution of CSR possible are the stakeholders that are affected by companies (Freeman, 1984). On the one hand, shareholders demand greater transparency in the actions carried out by the company with the aim of transferring confidence to the markets; on the other hand, consumers request quality, innovative products, and services with fair prices every day (Kliksberg 2006); employees who request increasingly humanized companies and are concerned about the well-being of the company's human capital (Del-Castillo-Feito et al. 2022). And finally, society is aware that for the company to succeed, CSR cannot remain on the sidelines. The role of companies to the society must be in line with the chosen economic model, considering the company as a social entity (Navarro García 2008) that is in contact with its environment. In this context, the application of CSR policies is justified by the fact that it helps to resolve conflicts and distribute the value created among the different stakeholders. Thus, socially responsible companies will obtain positive future effects that will ensure the sustainability of both the company and society (Porter and Kramer 2003); strengthen their competitive position, motivated by the greater acceptance of their image, and, therefore, minimize their reputational risk (Porter and Kramer 2003; Méndez 2005; Valderrama 2007); acquire competitive advantages (Olmedo and Martínez 2011); and help increase their legitimacy (Díez et al. 2014).

3.2.1 The Effect of Disclosure of Non-financial Information

Companies must know how to interact in a global world where the demands of society will be to reward or punish for their social, environmental, and economic actions, being much more demanding as a result of the scandals experienced (Baumann 2016; Barauskaite and Streimikiene 2020). Companies must be able to harmonize and balance value creation and sustainable development (Ntanos et al. 2018). Hence, a differentiating element is the disclosure of its shares to society (Escamilla-Casado et al., 2019; Torelli 2020), especially in sectors whose social and environmental impact is greater, so that they can turn it into a competitive advantage (Escamilla-Solano et al. 2016). In this way, it allows the company to know how society reacts to the disclosure of such information (El Akremi et al. 2018). It has always been considered that transparency is a variable to consider when analyzing the disclosure of CSR information, positively valuing this commitment on the part of the company to communicate the company's actions to stakeholders (Alejos 2015). There is no doubt about the benefits generated by the disclosure of information for the company's decision-making (Piechocki 2004; Toms 2002), but just as there is no consensus on whether or not it is CSR, when we analyze the level of disclosure of company information it tends to be confused with being more or less transparent. Baraibar Diez and Luna Sotorrío (2018) reveal that there is a problem in confusing transparency with disclosure, understanding transparency as something that goes beyond disclosure. Finally, we must point out that, within the practices carried out by responsible and sustainable companies, the practice of good governance in the company is identified as essential in the establishment of an adequate level of transparency (Canales and Romero 2017).

At this point, the following question should be asked: what is the effect of disclosure of non-financial information on companies? If the voluntariness of CSR practices is already accepted, one of the challenges we face is disclosure. While the disclosure of non-financial information is becoming a common practice at a global level, Europe Directive 95/2014/EU has been a turning point in addressing how companies disclose their CSR actions (Cupertino et al. 2022), by establishing a standardization in the disclosure of non-financial information at the European level (Ştefănescu et al. 2021).

In Spain, it will be Law 11/2018, which transposes the European Directive on non-financial information and diversity, that marks the path of the disclosure of this type of practice. Although the regulations are mandatory for companies with more than 500 employees (or if for two consecutive years it has an average of 250 employees), it is interesting that all companies disclose this type of information. The objective is none other than to improve sustainability and increase the confidence of the stakeholders, and among them again, we find investors and financiers. To do this, companies should expand on the information:

- Environmental environment: analysis of current and future effects of their impact on the environment, eco-efficiency program
- Social: actions to ensure gender equality, working conditions, respect for trade union rights, health and safety at work, and relations with local communities

- The anti-corruption
- Diversity: actions related to training, professional experience, age, capacity, and gender, as well as objectives and results of equality between the presence of men and women on the Board of Directors

3.2.2 Transparency and CSR Indicators

We always consider that when it comes to addressing CSR practices, it is only done by large companies, but the reality is not so. It is necessary that the managers of companies regardless of size or, going further, future entrepreneurs become aware of the advantages of the disclosure of CSR not only as a way to make transparent the benefits that their service offers to society but as a way to obtain a competitive advantage. It is vital that the stigma that the implementation of CSR actions is an expense for the company is removed. If long-term vision is maintained, the investment in CSR will allow acquiring capacities and skills that generate competitive sources, resulting in the improvement of its reputation and image, improving relations with society and environments where it develops its activity, increasing the satisfaction of stakeholders, as well as increasing employee motivation and reinforcing the values of the company's organizational culture (Escamilla-Casado et al. 2016: 201).

When it comes to addressing which are the indicators to evaluate the degree of transparency of companies, the indicators used by the Spanish Association of Transparency Professionals (Acreditra) are interesting, distributed in three blocks: Active Advertising, Right of Access to Public Information, and Transparent Organization with a total of 149 indicators. After performing an analysis of these, standard indicators are presented that any company should consider if it wants to use transparency as a vehicle that generates value and competitive sources.

Box 1 Indicators Used by the Spanish Association of Transparency Professionals (Acreditra)

Information about the entity and governing bodies	
1	Name and basic data of the entity
2	Purpose and functions of the entity
3	Relationship with public and private entities
4	Enumeration of governing bodies
5	Nominal list of members of the governing and management bodies
6	Updated curriculum vitae of the members of the governing and management bodies
Indicators of analysis of the organization and human resources	
7	General organization chart of the entity
8	Functions of departments

9	Contact of the departments
10	List of jobs
11	Job boards
12	Staff selection processes
Indicators of analysis of the relationship with the groups of interest	
13	Opening hours
14	Website
15	Prices and number of services and fees
16	Guide to procedures and procedures and/or service catalog
17	Complaints and suggestions
Indicators for the analysis of economic-financial information and equity	
18	Full quotes
19	Annual accounts
20	Debt ratios
21	Term of payment to suppliers
22	Economic-financial ratios
23	Financial sustainability report
Indicators for analysis of the level of planning, management and evaluation	
24	Statistical data and socioeconomic indicators on their territorial or sectoral scope of action
25	General plan or program of the entity
26	General memory of the entity
27	Effectiveness and efficiency indicators
Indicators of commitment analysis and general principles of transparency and good governance	
28	Code of Good Governance or Code of Ethics
29	Transparency regulations
30	Friendly and understandable website
31	Free access to transparency information
32	Publication on the web of news of interest
33	Gender equality
34	Social responsibility actions
35	Sustainability report

Source: Own elaboration based on Acreditra (2016).

Regarding CSR indicators, it should be borne in mind that various organizations have recommended and designed indicators and indices that are taken as a reference, for example, Global Reporting Initiative (GRI), Accountability, United Nations with the 2030 Agenda. Here are some indicators that can allow assessing whether a company is socially responsible or not.

Box 2 Indicators for Social Responsibility

Social dimension	
1	Assistance and social benefits
2	Sponsorship and patronage
3	Foundation
4	Reconciliation of work and family life
5	Employment for disabled personnel
6	Continuous training
7	Equal opportunity
8	Respect for human rights
9	Occupational Health & Safety
10	Corporative volunteering
11	Customer satisfaction
12	Certificate family-responsible company
Environmental dimension	
13	ISO Certificate
14	Environmental audits
15	Innovation projects
16	Waste management
17	Eco-efficiency programs
18	CO2 reduction programs
19	Environmental training
Economic dimension	
20	Inclusion of CSR mission, values, and vision
21	Good brand management
22	Included in sustainable indexes
23	Compliance with the United Nations Global Compact
24	Cost reduction
25	Code of Ethics and Conduct
26	Relationship with suppliers
27	Information transparency
28	SDG
29	Value creation management model

Source: Escamilla-Casado et al. (2019).

4 Conclusions

To conclude this chapter, we must be aware that entrepreneurs, regardless of the phase in which their company is, may need financing and make their company attractive to investors. In this line, we have detected that the more transparent a company is in the face of its investors, and financiers, the more profitable it will be, and consequently, it is more likely that it will survive the dreaded business failure (Díaz et al., 2014; Fernández-Portillo et al., 2018; Escamilla-Casado et al., 2016; Escamilla-Solano et al., 2019).

Based on these premises, we have managed to show the most relevant indicators of the disclosure of non-financial information, which are of most interest to improve the performance of listed companies (Escamilla-Solano et al., 2019). With all this, we want to conclude that, for the entrepreneur, it can be decisive to invest in the disclosure of their information, following already defined patterns, such as those shown in this work, because they help reduce the bias of company-investor information and therefore improve confidence in the business project, on which you want to invest. As for the limitations of this work, we want to collect that this work is limited by the lack of an ad-hoc field study, which allows this study to be tested in business projects at different levels of their life cycle, in order to demonstrate that this proposal is empirically contrasted in all phases of the development of a company. For this reason, we must delve into an empirical study with companies at different stages of their life cycle. That is why, as a future line of research, we propose to carry out an empirical study with companies at different stages of their life cycle.

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