Corporate Social Responsibility

Corporate social responsibility challenges businesses to attend to and interact with the firm's stakeholders while they pursue traditional economic goals. Both market and nonmarket stakeholders expect businesses to be socially responsible, and many companies have responded by making social goals a part of their overall business operations. What it means to act in socially responsible ways is not always clear, thus producing controversy about what constitutes such behavior, how extensive it should be, and what it costs to be socially responsible.

This chapter focuses on these key learning objectives:

- Understanding the basic meaning of corporate social responsibility.
- Knowing where and when the idea of social responsibility originated.
- Examining the critical arguments for and against corporate social responsibility.
- Assessing how business meets its economic and legal obligations while being socially responsible.
- Investigating how business balances its responsibilities to multiple stakeholders, including its stockholders.

Do managers have a responsibility to their stockholders? Certainly they do, because the owners of the business have invested their capital in the firm. Do managers also have a responsibility, a social responsibility, to their company's other market and nonmarket stakeholders—the people who live where the firm operates, who purchase the firm's product or service, or who work for the firm? While managers may have a clear responsibility to respond to all stakeholders, what happens when these multiple responsibilities seem to clash?

GSK Biologicals, the vaccine subsidiary of GlaxoSmithKline, bet that it could combat a global disease while still making money. In 2004, GSK introduced a new vaccine against rotavirus, a parasite that caused a deadly digestive illness. Typically, pharmaceutical companies roll out new medicines first in wealthy, industrialized countries to recoup their investment in research and development, before taking them to impoverished, developing countries. But, Jean Stephenne, president of GSK Bio, decided to take a bold, new approach, taking the drug first to Latin America, where the company committed $300 million to test the new vaccine—one of the largest and most expensive trials since the Salk vaccine for polio more than 50 years ago. This time, the target population was 60,000 low- and middle-income children living in various Latin American countries. Stephenne believed it was important to concentrate initially where the medical need was the greatest, even if there was little potential for immediate profit. If successful in Latin America, Stephenne planned to roll out the vaccine in Asia, then eventually in Europe, saving the United States, the most lucrative market, for last. "Our business model is to supply vaccines to the world, not just the U.S. and Europe," said Stephenne. The company

hoped that its rotavirus vaccine, and others under development, would attract support from charities like the Gates Foundation and government aid to poor countries.[1]

Is GSK Biologicals, under the leadership of Jean Stephenne, acting responsibly toward the firm's stockholders, or are his concerns for helping the poor and sick clouding his business judgment? Should businesses be more concerned about serving customers where the need is greatest, or focus on securing profits? Is it possible that in the long run, Stephenne's strategy will actually make more money for his company than a more conventional strategy might?

This chapter defines corporate social responsibility and discusses the advantages and drawbacks of being socially responsible. Most of all, though, it argues that stakeholders worldwide increasingly demand that corporations practice social responsibility. Whether businesses are large or small, make goods or provide services, operate at home or abroad, willingly try to be socially responsible or fight against it all the way, there is no doubt about what the public expects. Many business leaders also subscribe to the idea of social responsibility. Exhibit 3.A lists some of the organizations that support stakeholders seeking information on or examples of corporate social responsibility.

The Meaning of Corporate Social Responsibility

Corporate social responsibility (CSR) means that a corporation should be held accountable for any of its actions that affect people, their communities, and their environment. It implies that harm to people and society should be acknowledged and corrected if at all possible. It may require a company to forgo some profits if its social impacts seriously hurt some of its stakeholders or if its funds can be used to have a positive social impact.

The Many Responsibilities of Business

However, being socially responsible does not mean that a company must abandon its other missions. As discussed later in this chapter, a business has many responsibilities: economic, legal, and social. The challenge for management is the blending of these responsibilities into a comprehensive corporate strategy while not losing sight of any of its obligations. At times these responsibilities will clash; at other times they will work together to better the firm. Thus, having multiple and sometimes competing responsibilities does not mean that socially responsible firms cannot be as profitable as others less responsible; some are and some are not.

Social responsibility requires companies to balance the benefits to be gained against the costs of achieving those benefits. Many people believe that both business and society gain when firms actively strive to be socially responsible. Others are doubtful, saying that taking on social tasks weakens business's competitive strength. The arguments on both sides of this debate are presented later in this chapter.

Social Responsibility and Corporate Power

The social responsibilities of business grow directly out of two features of the modern corporation: (1) the essential function it performs for a variety of stakeholders and (2) the immense influence it has on the lives of these stakeholders. We count on corporations for job creation, much of our community well-being, the standard of living we enjoy, the tax base for essential municipal, state, and national services, and our needs for banking and financial services, insurance, transportation, communication, utilities, entertainment, and a growing proportion of health care. These positive achievements suggest that the corporate form of business is capable of performing a great amount of good for society, such as encouraging economic growth, expanding international trade, and creating new technology.

The following well-known quotation, frequently appearing in journals for business executives, challenges the readers to assume a responsible role for business in society:

> Business has become, in the last half century, the most powerful institution on the planet. The dominant institution in any society needs to take responsibility for the whole. . . . Every decision that is made, every action that is taken, must be viewed in light of that kind of responsibility.[2]

Most of the 100 largest economies in the world are global corporations. The world's largest 200 companies account for more than a quarter of the world's economic activity and have twice the economic clout of the poorest four-fifths of humanity. About one-third of world trade is simply transactions among units of the same company.

Many people are concerned about the enormous influence of business. The focused power found in the modern business corporation means that every action it takes could affect the quality of human life—for individuals, for communities, and for the entire globe. This obligation is often referred to as the *iron law of responsibility*. The **iron law of responsibility** says that in the long run, those who do not use power in ways that society considers responsible will tend to lose it.[3] With such technology as global computer networks, instantaneous commercial transactions, and exponentially increasing collection and storage of information drawing the world into a tighter and tighter global village, the entire planet has become a stakeholder of all corporations. All societies are now affected by corporate operations. As a result, social responsibility has become a worldwide expectation.

How Corporate Social Responsibility Began

In the United States, the idea of corporate social responsibility appeared around the start of the 20th century. Corporations at that time came under attack for being too big, too powerful, and guilty of antisocial and anticompetitive practices. Critics tried to curb corporate power through antitrust laws, banking regulations, and consumer-protection laws.

Faced with this social protest, a few farsighted business executives advised corporations to use their power and influence voluntarily for broad social purposes rather than for profits alone. Some of the wealthiest business leaders—steelmaker Andrew Carnegie is a good example—became great philanthropists who gave much of their wealth to educational and charitable institutions. Others, like automaker Henry Ford, developed paternalistic programs to support the recreational and health needs of their employees. (A recent example is Warren Buffet, when in 2006, he gave the bulk of his $44 billion fortune to the Bill and Melinda Gates Foundation and four other philanthropies.) These business leaders believed that business had a responsibility to society that went beyond or worked with their efforts to make profits.[4]

As a result of these early ideas about business's expanded role in society, two broad principles emerged; they are described in Figure 3.1 and in the following sections of this chapter. These principles shaped business thinking about social responsibility during the 20th century and are the foundation stones for the modern idea of corporate social responsibility.

The Charity Principle

The **charity principle**, the idea that the wealthiest members of society should be charitable toward those less fortunate, is a very ancient notion. When Andrew Carnegie and other wealthy business leaders endowed public libraries, supported settlement houses for the poor, gave money to educational institutions, and contributed funds to many other community organizations, they were continuing this long tradition of being "my brother's keeper."

> Andrew Carnegie and John D. Rockefeller are usually credited with pioneering the path of the great modern philanthropists. For some years, the world's newspapers kept score on the giving. *The London Times* reported that in 1903 Carnegie had given away $21 million, Rockefeller $10 million. In 1913, *The New York Herald* ran a final box score: Carnegie, $332 million;

Rockefeller, $175 million. All this was before the income tax and other tax provisions had generated external incentives to giving. The feeling of duty to the public good arose from inner sources.[5]

This kind of private aid to the needy members of society was especially important in the early decades of the last century. At that time, there was no Social Security, Medicare, unemployment pay, or United Way. There were few organizations capable of counseling troubled families, sheltering women and children who were victims of physical abuse, aiding alcoholics, treating the mentally ill or the disabled, or taking care of the destitute. When wealthy industrialists reached out to help others such as these, they were accepting some measure of responsibility for improving the conditions of life in their communities. In doing so, their actions helped counteract critics who claimed that business - leaders were uncaring and interested only in profits.

Before long, when it was recognized that many community needs outpaced the riches of even the wealthiest persons and families, or beginning in about the 1920s, much of the charitable load was taken on by business firms themselves rather than by the owners alone. Business leaders often gave vigorous support to this form of corporate charity, urging all firms and their employees to unite their efforts to extend aid to the poor and the needy. Businesses built houses, churches, schools, and libraries, provided medical and legal services, and gave to charity.

For some of today's business firms, corporate social responsibility means participating in community affairs by making similar kinds of charitable contributions. The Giving USA Foundation reported that total U.S. charitable contributions (including disaster relief) in 2005 reached $260 billion, an all-time record.[6] Although many corporations today make generous contributions, as will be further discussed in Chapter 17, most observers nowadays believe that corporate social responsibility encompasses much more than just charity.

The Stewardship Principle

Many of today's corporate executives see themselves as stewards, or trustees, who act in the general public's interest. Although their companies are privately owned and they try to make profits for the stockholders, business leaders who follow the **stewardship principle** believe they have an obligation to see that everyone—particularly those in need or at risk—benefits from their firms' actions. According to this view, corporate managers have been placed in a position of public trust. They control vast resources whose use can affect people in fundamental ways. Because they exercise this kind of crucial influence, they incur a responsibility to use those resources in ways that are good not just for the stockholders alone but for society generally. In this way, they have become stewards, or trustees, for society, as well as for the natural environment. As such, they are expected to act with a special degree of responsibility in making business decisions.[7]

This kind of thinking eventually produced the modern theory of stakeholder management, which was described in the opening chapter of this book. According to this theory, corporate managers need to interact skillfully with all groups that have a stake in what the corporation does. If they do not do so, their firms will not be fully accepted by the public as legitimate.

HP Brazil, a subsidiary of Hewlett-Packard, developed the Digital Garage project where the firm collaborated with local Brazilian foundations and youth clubs to provide young Brazilians from less privileged backgrounds the tools to develop self-esteem, creativity, sociability, entrepreneurship,

leadership, citizenship, teamwork, and IT skills. HP Brazil management recognized their stewardship responsibility to serve as volunteer mentors and tutors for the local youths and to empower young people with skills to enable them to participate in the growing technological society.[8]

The Corporate Social Responsibility Debate

There are strong arguments on both sides of the debate about business's social responsibilities. When a person is exposed to arguments on both sides of the debate, she or he is in a better position to judge business actions in the social environment and to make more balanced business judgments.

Arguments for Corporate Social Responsibility

Who favors corporate social responsibility? Many business executives believe it is a good idea. A global survey of business executives conducted by McKinsey in 2005 found that 84 percent agreed large corporations should "generate high returns to investors but balance [this] with contributions to the broader public good," as shown in Figure 3.2.

Many social groups that seek to preserve the environment, protect consumers, safeguard the safety and health of employees, prevent job discrimination, oppose invasions of privacy through Internet use, and maintain a strong return on their investment stress the importance of social responsibility by businesses. Government officials also ensure corporate compliance with laws and regulations that protect the general public from abusive business practices. In other words, both the supporters and the critics of business have reasons for wanting businesses to act in socially responsible ways. The major arguments used are listed in Figure 3.3.

Balances Corporate Power with Responsibility

Today's business enterprise possesses much power and influence. Most people believe that responsibility must accompany power, whoever holds it. This obligation, presented earlier in this chapter, is called the *iron law of responsibility*. Businesses committed to social responsibility are aware that if they misuse the power they have, they might lose it. The antitrust cases brought against Microsoft by regulators in the United States and Europe, profiled in the discussion case at the end of Chapter 10, are examples of government efforts to reduce a company's abuses of its monopoly power in the marketplace.

Discourages Government Regulation

One of the most appealing arguments for business supporters is that voluntary social acts may head off increased government regulation. Some regulation may reduce freedom for both business and society, and freedom is a desirable public good. In the case of business, regulations tend to add economic costs and restrict flexibility in decision making. From business's point of view, freedom in decision making allows business to maintain initiative in meeting market and social forces. This view also is consistent with political philosophy that wishes to keep power as decentralized as possible in a democratic society. It is said that government is already a massive institution whose centralized power and bureaucracy threaten the balance of power in society. Therefore, if business by its own socially responsible behavior can discourage new government restrictions, it is accomplishing a public good as well as its own private good.

For example, the natural juice producer Odwalla, described in a case study later in the book, sought to improve the safety of its fresh juice drinks by pasteurizing (heat-treating) them voluntarily. The company hoped that by doing so it would avoid strict and often more costly government regulations of its production processes.

Promotes Long-Term Profits for Business

At times, social initiatives by business produce long-run business profits. A New Jersey judge [illegible][9]

A classic example of the long-term benefits of social responsibility was the Johnson & Johnson Tylenol incident. In the 1980s, several people died after they ingested Extra-Strength Tylenol capsules laced with the poison cyanide. To ensure the safety of its customers, Johnson & Johnson immediately recalled the product, an action that cost the firm millions of dollars in the short term. The company's production processes were never found defective. Customers rewarded Johnson & Johnson's responsible actions by continuing to buy its products, and in the long run the company once again became profitable.

In the opening example of this chapter, the CEO of GSK Bio believed that in the long term, its commitment to developing vaccines for underserved populations would strengthen the company's financial performance by attracting new customers, as well as support from governments and public health organizations. An empirical assessment of the question whether corporate social responsibility leads to benefits for companies' stockholders is presented later in this chapter.

Improves Business Value and Reputation

The social reputation of the firm is often viewed as an important element in establishing trust between the firm and its stakeholders. **Reputation** refers to desirable or undesirable qualities associated with an organization or its actors that may influence the organization's relationships with its stakeholders.[10] A firm's reputation is a valuable intangible asset, as it prompts repeat purchases by loyal consumers and helps to attract and retain better employees to spur productivity and enhance profitability. Employees who have the most to offer may be attracted to work for a firm that contributes to the social good of the community, or is more sensitive to the needs and safety of its consumers, or takes better care of its employees. Research has confirmed that a firm's "good deeds" or reputation increases its attractiveness to employees.[11] Thus, a company may benefit from being socially responsible by improving the quality of people it attracts as employees. In this sense, the company's social reputation is one of its intangible assets that add to the organization's wealth.

A concern for company reputation is found at the highest levels of business organizations worldwide. Sixty-five percent of CEOs surveyed in a Korn/Ferry International poll said that it was their personal responsibility to manage their company's reputation. Corporate boards are putting more pressure on CEOs to build corporate reputation. When choosing a successor, the CEOs responding to the survey overwhelmingly agreed (97 percent) that when seeking a new leader of the firm, boards place more weight than ever on a candidate's ability to protect and enhance the company's reputation.[12]

As discussed in Chapter 4, firms are often recognized for their positive reputation by various business magazines or organizations through awards programs. Recently, a "reputation index" was created to measure and hold up as a model those companies with strong social reputations. Rating Research, a British

firm, measures the critical intangible assets that constitute corporate reputation and broadly disseminates these ratings to interested parties.[13]

Corrects Social Problems Caused by Business

Many people believe business has a responsibility to compensate society for the harm it has sometimes caused. If consumers are injured due to a product defect, the manufacturer is responsible. If a business does not voluntarily recognize its responsibility, the courts will often step in to represent society and its interests. When a business pollutes the environment, the cleanup is the responsibility of that firm, as seen in the following example.

> At the insistence of the Environmental Protection Agency and thousands of concerned citizens, General Electric accepted responsibility for dredging New York's Hudson River to rid the waterway of much of the 1.3 million pounds of toxic PCBs that had been dumped there since the 1940s. Since the mid-1970s, PCBs had been linked to premature birth defects and cancer, particularly to those people who consumed contaminated fish. Although the government had stopped General Electric from continuing to dump PCBs into the river since 1975, the company had assumed no responsibility for cleaning up its mess until 2002, a project that company officials estimated would cost half a billion dollars to complete.[14]

As General Electric learned from its experience in this case, it is often much less expensive to avoid causing problems, such as chemical pollution, than to correct them afterward.

Arguments against Corporate Social Responsibility

Who opposes corporate social responsibility? The economist Milton Friedman famously stated in 1970, "There is only one responsibility of business, namely to use its resources and engage in activities designed to increase its profits."[15] Some people in the business world—such as the 16 percent of CEOs in the survey shown in Figure 3.2 who believe that the appropriate role of business is to provide the highest possible returns to shareholders while obeying all laws and regulations—clearly agree with this view. Some fear that the pursuit of social goals by business will lower firms' economic efficiency, thereby depriving society of important goods and services. Others are skeptical about trusting business with social improvements; they prefer governmental initiatives and programs. According to some of the more radical critics of the private business system, social responsibility is nothing but a clever public relations smokescreen to hide business's true intentions to make as much money as possible. See Figure 3.3 again for some of the arguments against corporate social responsibility, discussed next.

Lowers Economic Efficiency and Profits

According to one argument, any time a business uses some of its resources for social purposes, it risks lowering its efficiency. For example, if a firm decides to keep an unproductive factory open because it wants to avoid the negative social effect that a plant closing would have on the local community and its workers, its overall financial performance may suffer. The firm's costs may be higher than necessary, resulting in lower profits. Stockholders may receive a lower return on their investment, making it more difficult for the firm to acquire additional capital for future growth. In the long run, the firm's efforts to be socially responsible by keeping the factory open may backfire.

Business managers and economists argue that the business of business is business. Businesses are told to concentrate on producing goods and services and selling them at the lowest competitive price. When these economic tasks are done, the most efficient firms survive. Even though corporate social responsibility is well-intended, such social activities lower business's efficiency, thereby depriving society of higher levels of economic production needed to maintain everyone's standard of living.[16]

Imposes Unequal Costs among Competitors

Another argument against social responsibility is that it imposes greater costs on more responsible companies, putting them at a competitive disadvantage. Consider the following scenario.

> A manufacturer operating in multiple countries wishes to be more socially responsible worldwide and decides to protect its employees by installing more safety equipment at its plants than local law requires. Other manufacturers in competition with this company do not take similar steps, choosing to install only as much safety equipment as required by law. As a result their costs are lower, and their profits higher. In this case, the socially responsible firm penalizes itself and even runs the risk of going out of business, especially in a highly competitive market.

This kind of problem becomes acute when viewed from a global perspective, where laws and regulations differ from one country to the next. If one nation requires higher and more costly pollution control standards, or stricter job safety rules, or more stringent premarket testing of prescription drugs than other nations, it imposes higher costs on business. This cost disadvantage means that competition cannot be equal. Foreign competitors who are the least socially responsible will actually be rewarded because they will be able to capture a bigger share of the market.

Imposes Hidden Costs Passed On to Stakeholders

Many social proposals undertaken by business do not pay their own way in an economic sense; therefore, someone must pay for them. Ultimately, society pays all costs. Some people may believe that social benefits are costless, but socially responsible businesses will try to recover all of their costs in some way. For example, if a company chooses to install expensive pollution-abatement equipment, the air may be cleaner, but ultimately someone will have to pay. Stockholders may receive lower dividends, employees may be paid less, or consumers may be charged higher prices. If the public knew that it would eventually have to pay these costs, and if it knew how high the true costs were, it might not be so insistent that companies act in socially responsible ways. The same might be true of government regulations intended to produce socially desirable business behavior. By driving up business costs, these regulations often increase prices and lower productivity, in addition to making the nation's tax bill higher.

Requires Skills Business May Lack

Businesspeople are not primarily trained to solve social problems. They may know about production, marketing, accounting, finance, information technology, and personnel work, but what do they know about inner-city issues or world poverty or violence in schools? Putting businesspeople in charge of solving social problems may lead to unnecessarily expensive and poorly conceived approaches. In a global survey on social responsibility, it was found that "only 11 percent [of the companies who have developed a CSR strategy] have made significant progress in implementing the strategy in their organization";[17] thus one might question the effectiveness and efficiency of businesspeople seeking to address social responsibility problems. Business analysts might be tempted to believe that methods that succeed in normal business operations will also be applicable to complex social issues, even though different approaches may work better in the social arena.

A related idea is that public officials who are duly elected by citizens in a democratic society should address societal issues. Business leaders are not elected by the public and therefore do not have a mandate to solve social problems. In short, businesspeople do not have the expertise or the popular support required to address what are essentially issues of public policy.

Places Responsibility on Business Rather than Individuals

The entire idea of *corporate* responsibility is misguided, according to some critics. Only *individual persons* can be responsible for their actions. People make decisions; organizations do not. An entire company cannot be held liable for its actions, only those individuals who are involved in promoting or carrying out a policy. Therefore, it is wrong to talk about the social responsibility of *business* when it is the social responsibility of *individual businesspersons* that is involved. If individual business managers want to contribute their own personal money to a social cause, let them do so; but it is wrong for them to contribute their company's funds in the name of corporate social responsibility.[18]

Together, the above arguments claim that the attempt to exercise corporate social responsibility places added burdens on both business and society without producing the intended effect of social improvement or produces it at excessive cost.

Balancing Economic, Legal, and Social Responsibilities

Any organization or manager must seek to juggle multiple responsibilities. The belief that the business of business is solely to make a profit is no longer widely held, as Figure 3.2 suggests. Rather, many business executives believe the key challenge facing their organizations today is to meet economic and social responsibilities simultaneously.

> Never was the balancing of multiple responsibilities more evident than when Jeffrey Immelt, chairman and CEO at General Electric, announced before 200 corporate officers that it would take four things to keep the company on top: execution, growth, great people, and *virtue*. Immelt appointed the company's first vice president for corporate citizenship, Bob Corcoran, to take his message globally to GE's suppliers, customers, and employees. Within a year after Immelt's announcement, GE had performed more than 3,100 labor, health, environmental and safety audits and opened up discussions with socially responsible investment funds. GE launched a global philanthropic program by providing health care to people in the poorest areas of Ghana.[19]

As shown in Figure 3.4, a business must manage its economic responsibilities to its stockholders, its legal requirements to societal laws and regulations, and its social responsibilities to various stakeholders. Although these obligations may conflict at times, a successful firm is one whose management finds ways to meet each of its critical responsibilities and develops strategies to enable these obligations to help each other.

Economic and Social Responsibilities: Enlightened Self-Interest

Being socially responsible by meeting the public's continually changing expectations requires wise leadership at the top of the corporation. Companies with the ability to recognize profound social changes and anticipate how they will affect operations have proven to be survivors. They get along better with government regulators, are more open to the needs of the company's stakeholders, and often cooperate with legislators as new laws are developed to cope with social problems.

> What started off as a business envisioning a competitive advantage has turned into a national business alliance of social activity. In 2004, Home Depot CEO Robert Nardelli encouraged his employees to get involved in the community. More than 50,000 of the firm's 325,000 employees responded with more than 2 million hours of donated time. A year later, Nardelli

challenged a group of CEOs to get involved at the pace established by the Home Depot employees. Leaders representing Albertson's, BellSouth, Delta Air Lines and SAP America met with Nardelli and agreed to kick off "A Month of Service" in September 2005. The group created Hands-On Network, an alliance of corporate and civic leaders, to develop community service programs that deployed corporate volunteers on 2,000 projects across the country, resulting in 6.4 million volunteer hours over two years. Nardelli explained that at the core of this project was the understanding that "companies are beholden not just to stockholders, but also to suppliers, customers, employees, community members, even social activists. Things have become a lot more interdependent."[20]

The actions taken by Home Depot's CEO Nardelli are an example of a business leader being guided by **enlightened self-interest**. Nardelli recognized the long-term rewards to the company from its civic involvement in enhanced reputation, employee satisfaction, and community support. According to this view, it is in a company's self-interest in the long term to provide true value to its customers, to help its employees to grow, and to behave responsibly as a corporate citizen.[21]

Do socially responsible companies sacrifice profits by working conscientiously to promote the social good? Do they make higher profits, better-than-average profits, or lower profits than corporations that ignore or flout the public's desires for a high and responsible standard of social performance?

Scholars have explored this issue for two decades, with mixed results. In 2003, researchers at the University of Iowa conducted a methodologically rigorous review of all 52 prior studies of the relationship between corporate social responsibility and firm performance. They found that most of the time, more responsible companies also had solid financial results; the statistical association was highly to modestly positive across the range of all prior studies. The authors concluded, "corporate virtue, in the form of social responsibility and, to a lesser extent, environmental responsibility is likely to pay off."[22] In short, most of the time, socially responsibility and financial performance go together, although there may be some conditions under which this is not true.

Any social program—for example, an in-company child care center, a drug education program for employees, or the lending of company executives as advisers to community agencies—will usually impose immediate monetary costs on the participating company. These short-run costs certainly have a potential for reducing the company's profits unless the social activity is designed to make money, which is not usually the purpose of these programs. Therefore, a company may sacrifice short-run profits by undertaking social initiatives, but what is lost in the short run may be gained back over a longer period. For example, if a drug education program prevents or reduces on-the-job drug abuse, then the resulting lower employee turnover, fewer absences from work, healthier workforce, and fewer accidents and injuries may increase the firm's productivity and lower health insurance costs. In that case, the company may actually experience an increase in its long-run profits, although it had to make an expensive outlay to get the program started.

Legal Requirements versus Corporate Social Responsibility

Accompanying a firm's economic responsibility to its stockholders are its **legal obligations**. As a member of society, a firm must abide by the laws and regulations governing the society. How are a firm's legal obligations related to its social responsibilities? Laws and regulations are enacted to ensure socially responsible conduct by businesses. The standards of behavior expected by society are embodied in that society's laws. Can't businesses voluntarily decide to be socially

responsible? Of course, but legal rules set minimum standards for businesses to follow. Some firms go beyond the law; others seek to change the law to require competitors to be more socially responsible.

Laws and regulations help create a level playing field for businesses that compete against one another. By requiring all firms to meet the same social standards—for example, the safe disposal of hazardous wastes—government prevents one firm from gaining a competitive advantage over its rivals by acting irresponsibly. If a company dumped its wastes carelessly, it would risk lawsuits, fines, and possible jail terms for some of its managers and employees and unfavorable publicity for its actions.

Businesses that comply with laws and public policies are meeting a minimum level of social responsibility expected by the public. According to one leading scholar of corporate social performance, even legal compliance is barely enough to satisfy the public:

> The traditional economic and legal criteria are necessary but not sufficient conditions of corporate legitimacy. The corporation that flouts them will not survive; even the mere satisfaction of these criteria does not ensure the corporation's continued existence . . .
> Thus, social responsibility implies bringing corporate behavior up to a level where it is in congruence with currently prevailing social norms, values, and performance expectations. . . . [Social responsibility] is simply a step ahead—before the new societal expectations are codified into legal requirements.[23]

Stockholder Interests versus Other Stakeholder Interests

Top-level managers, along with a corporation's board of directors, are generally expected to produce as much value as possible for the company's owners and investors. This can be done by paying high dividends regularly and by running the company in ways that cause the stock's value to rise. Not only are high profits a positive signal to Wall Street investors that the company is being well-run—thereby increasing the stock's value—but those profits also make possible the payment of high dividends to stockholders. Low profits have the opposite effect and put great pressure on managers to improve the company's financial performance.

However, stockholders are not the only stakeholder group that management must keep in mind. The leaders of some of the world's largest organizations from Europe, Asia, and North America, organized by a group called the Caux Roundtable, recognized that all stakeholders must be considered; none can be ignored. A top manager's job is to interact with the totality of the company's stakeholders, including those groups that advocate high levels of social responsibility by business. Management's central goal is to promote the interests of the entire company, not just any single stakeholder group, and to pursue multiple company goals, not just profit goals.[24]

This broader and far more complex task tends to put more emphasis on the long-run profit picture rather than an exclusive focus on immediate returns. When this happens, dividends paid to stockholders may be less than they desire, and the value of their shares may not rise as rapidly as they would like. These are the kinds of risks faced by corporate managers who have a legal responsibility to produce high value for the company's stockholder-owners but who also must try to promote the overall interests of the entire company. Putting all of the emphasis on short-run maximum profits for stockholders can lead to policies that overlook the interests and needs of other stakeholders. Managers may also downgrade social

responsibility programs that increase short-run costs, although it is well known that the general public strongly approves of socially responsible companies.

As a response to the conflict between long- and short-term profit making, an enlightened self-interest point of view may be the most useful and practical approach. That means that incurring reasonable short-run costs to undertake socially responsible activities that benefit both the company and the general public in the long run is acceptable.

The Evolving Notion of Corporate Social Responsibility

William C. Frederick, a leading scholar and a co-author of several earlier editions of this book, described in his recent book how business understanding of corporate social responsibility has evolved over the past half century. During each of the four historical periods, corporate social responsibility has had a distinct focus, set of drivers, and policy instruments, as shown in Figure 3.5. Frederick explains that the most recent phase of corporate social responsibility is corporate citizenship. The next chapter explores today's corporate citizenship practices.

As the general notion of corporate social responsibility has evolved from a sense of stewardship and charity to others to the more recent understanding of corporate citizenship, business likewise has evolved in how it reacts to and addresses the various challenges made by its stakeholders. The current test of acting as a good global corporate citizen is discussed in the next chapter.

Discussion Case: *Hurricane Katrina—Corporate Social Responsibility in Action*

On August 29, 2005, the United States experienced its most destructive and costly natural disaster ever when Hurricane Katrina, a fierce storm with winds of more than 135 miles per hour, battered the central Gulf Coast and caused unparalleled damage to coastal regions of Louisiana, Mississippi, and Alabama. Its storm surge breeched the levee system that protected New Orleans from Lake Pontchartrain and subsequently flooded significant portions of the city. Many communities along the Gulf Coast were battered, damaged and, in some cases, completely destroyed. Two months later, the official death toll stood at 1,163 and the damage was estimated to be more than $200 billion. Over 1 million people were displaced in the aftermath of this disaster.

The outpouring of charity—from cash donations to provisions of water, food and clothing—from individuals across the country and around the world was immediate. Businesses were significantly involved, demonstrating one of the greatest charitable efforts ever seen from the corporate community. While many companies have had longstanding traditions of charitable giving, particularly during economic hard times, the philanthropy provided after Hurricane Katrina emphasized a new level of giving.

Emigrant Savings Bank, a major financial lender in the region, deposited $1,000 into the account of each customer in the areas hardest hit by the storm. The *Chronicle of Philanthropy* in Washington, D.C., estimated that if the contributions continued, it was likely that cash donations by businesses to victims of Hurricane Katrina would surpass those to victims of other recent disasters, such as the September 11, 2001, terrorist attacks on New York City and

Washington, D.C., and the recent Asian tsunamis.

In addition to cash, businesses offered consumer products to those in need of these items. Georgia Pacific, a home improvement retailer, sent 65 truckloads of consumer goods—toilet paper, paper towels, paper plates, cutlery—to relief organizations, more than three times the amount it had sent the previous year during hurricane season. Wal-Mart donated $17 million in cash to relief agencies and followed up with shipping more than 100 truckloads of diapers, wipes, toothbrushes, and even beds to the Gulf Coast. Employees of pizza chain Papa John's spent a week in Biloxi, Mississippi, handing out thousands of six-inch pizza pies from a mobile trailer.

In addition to more than a million dollars in cash and equipment, General Electric provided a mobile power plant to restore capacity to a fuel transfer station in Louisiana. Amgen, a biotechnology company, donated $2.5 million worth of medical supplies, focusing on providing assistance to dialysis and cancer patients. Countless thousands of volunteers offered their assistance, including emergency service and utility crews from every state in the nation and dozens of countries.

Business became involved in helping in other ways as well. More than 14,000 casino workers in the region lost their jobs, and many their homes, in the hurricane. Their employers, four Las Vegas–based casino-operating companies—Harrah's Entertainment, MGM Mirage, Boyd Gaming, and Pinnacle Entertainment—told them they would continue to receive paychecks. Harrah's Entertainment pledged to pay workers up to 90 days after the casino was closed from the storm's damage. Although these businesses experienced devastating property damaged from Hurricane Katrina, they committed to paying their employees despite not knowing when the casinos might be in operation again.

Other businesses and their managers assumed new roles in serving their employees affected by the disaster. One day before the storm hit, Standard Company of New Orleans transferred its computer system and call center to a backup location in Boulder, Colorado. By the time New Orleans began flooding, many of the company's employees were in Dallas—a new and unfamiliar location for Standard's employees. Jefferson Gillane, a financial analyst at Standard before the storm hit, became the company's information coordinator. He found office supplies, procedures for filing insurance claims, local doctors, and schools in Dallas that were willing to enroll students from New Orleans. He also found charities that could supply clothing for employees who did not anticipate being away from home for more than a few days and had lost everything back in New Orleans. Gillane even launched a daily newsletter with information about New Orleans' sports teams.

During the nation's greatest disaster, businesses, along with many individuals and charitable organizations, found new ways to demonstrate a concern for others and to offer hope as thousands of people sought to rebuild their lives.

[1] "Vaccinating the World's Poor," *BusinessWeek*, April 26, 2004, pp. 65–69.

- Responsible Shopper (*www.responsibleshopper.org*) assists consumers by providing information on businesses' responsible and irresponsible practices, such as their environmental impacts, employee benefit programs, and financial reporting abuses.

- Social Funds (*www.socialfunds.com*) is a Web site run by SRI World Group. This site reports breaking financial news, promotes socially responsible mutual funds, and enables individuals to build an investment portfolio of socially responsible companies. Social Funds provides a free weekly e-mail newsletter, *SRI News Alert,* which includes issues beyond social investing.
- CorpWatch (*www.corpwatch.org*) is called “The Watchdog on the Web.” Information on this Web site—often unavailable on other Web sites—focuses on human rights abuses abroad, public policy, and environmental news.
- Business and Social Initiatives Database (*www.ilo.org/public/english/employment/multi/basi.htm*) is sponsored by the International Labor Organization. It compiles Internet sources on employment and labor issues, such as child labor, living wage, safe working conditions, and more.
- Capital Partnership Group (*cog.kent.edu*) is a virtual think tank of individuals who focus on issues of employee ownership. Academics and business leaders contribute to the discussions posted on this Web site, with hundreds of research papers and reports on topics such as labor-sponsored venture capital and employee governance available.
- The Green Business Letter (*www.GreenBiz.com*) emphasizes environmental business activities. Visitors to this Web site can find what companies are doing, pending environmental legislation, job listings for environmental professionals, or access to many other environmentally oriented Web sites.

Source: “Web Watch: Best Resources for Corporate Social Responsibility,” *Business Ethics*, Summer 2001, pp. 16–19.

[2] David C. Korten, “Limits to the Social Responsibility of Business,” *The People-Centered Development Forum,* article 19, release date: June 1, 1996.

[3] This concept first appeared in Keith Davis and Robert Blomstrom, *Business and Its Environment* (New York: McGraw-Hill, 1966).

[4] Harold R. Bowen, *Social Responsibility of the Businessman* (New York: Harper, 1953); and Morrell Heald, *The Social Responsibility of Business: Company and Community, 1900–1960* (Cleveland: Case Western Reserve Press, 1970). For a history of how some of these business philanthropists acquired their wealth, see Matthew Josephson, *The Robber Barons: The Great American Capitalists* (New York: Harcourt Brace, 1934).

FIGURE 3.1

Foundation Principles of Corporate Social Responsibility

	Charity Principle	**Stewardship Principle**
Definition	• Business should give voluntary aid to society’s needy persons and groups	• Business, acting as a public trustee, should consider the interests of all who are affected by business decisions and policies
Type of activity	• Corporate philanthropy • Voluntary actions to promote the social good	• Acknowledging business and society interdependence • Balancing the interests and needs of many diverse groups in society
Examples	• Corporate philanthropic foundations • -Private initiatives to solve social problems • Social partnerships with needy groups	• Enlightened self-interest • Meeting legal requirements • Stakeholder approach to corporate strategic planning

[5] Michael Novak, *Business as a Calling: Work and the Examined Life* (New York: The Free Press, 1996), p. 197.

[6] Giving USA Foundation (formerly AAFRC), *Giving USA 2006* (Indianapolis, IN: 2006), pp. 14, 30.

[7] Two early statements of this stewardship-trustee view are Frank W. Abrams, “Management’s Responsibilities in a Complex World,” *Harvard Business Review*, May 1951; and Richard Eells, *The Meaning of Modern Business* (New York: Columbia University Press, 1960).

[8] “HP Wins International Corporate Conscience Award,” HP press release, *www.hp.com/hpinfo*.

FIGURE 3.2

Business Executives’ Opinion of the Role of Business in Society

Which of the following statements best describes the role that large corporations (public and private) should play in society?

84% “Generate high returns to investors but balance with contributions to the broader public good” and 16% “Focus solely on providing the highest possible returns to investors while obeying all laws and regulations.”

Source: “The McKinsey Global Survey of Business Executives: Business and Society,” *McKinsey Quarterly,* January 2006. Based on a survey of 4,238 executives (more than a quarter of CEOs or other top executives) in 116 countries, conducted in December 2005. All data weighted by GDP of constituent countries to adjust for differences in response rates from various regions. Used by permission.

FIGURE 3.3

The Pros and Cons of Corporate Social Responsibility

Arguments for Corporate Social Responsibility	Arguments against Corporate Social Responsibility
Balances corporate power with responsibility.	Lowers economic efficiency and profit.
Discourages government regulation.	Imposes unequal costs among competitors.
Promotes long-term profits for business.	Imposes hidden costs passed on to stakeholders.
Improves business value and reputation.	Requires skills business may lack.
Corrects social problems caused by business.	Places responsibility on business rather than individuals.

[9] *Barlow et al. v. A.P. Smith Manufacturing* (1951, New Jersey Supreme Court), discussed in Clarence C. Walton, *Corporate Social Responsibility* (Belmont, CA: Wadsworth, 1967), pp. 48–52.

[10] The definition of *reputation* was adapted from John F. Mahon, "Corporate Reputation: A Research Agenda Using Strategy and Stakeholder Literature," *Business & Society* 41, no. 4 (December 2002), pp. 415–45. Also see Charles Fombrun, *Reputation: Realizing Value from the Corporate Image* (Cambridge, MA: Harvard University Press, 1996) and the December 2002 special issue of *Business & Society*.

[11] Rebecca A. Luce, Alison E. Barber, and Amy J. Hillman, "Good Deeds and Misdeeds: A Mediated Model of the Effect of Corporate Social Performance on Organizational Attractiveness," *Business & Society* 40, no. 4 (2001), pp. 397–415.

[12] "CEOs Taking Greater Responsibility for Corporate Reputations," *Ethics Newsline*, Institute for Global Ethics, October 20, 2003, *www.globalethics.org*.

[13] See Fombrun, *Reputation: Realizing Value from the Corporate Image*. See also *www.reputation.org* and articles in *Corporate Reputation Review* and Rating Research LLC, *www.ratingresearch.com*.

[14] "Healing the Hudson Rover," Natural Resources Defense Council Web site at *www.nrdc.org/water/pollution/ hhudson.asp*.

[15] Milton Friedman, "The Social Responsibility of Business Is to Increase Its Profits," *New York Times Magazine,* September 13, 1970.

[16] This argument is most often attributed to Milton Friedman, ibid., pp. 33, 122–26.

[17] "Corporate Social Responsibility: Unlocking the Value," *www.ey.com/Global*.

[18] This argument, like the "lowers economic efficiency and profits" argument, often is attributed to Friedman, "Social Responsibility of Business."

[19] "Money and Morals at GE," *Fortune,* November 15, 2004, pp. 176–82.

FIGURE 3.4

The Multiple Responsibilities of Business

[20] "The Debate over Doing Good," *BusinessWeek,* August 15, 2005, pp. 76–78.

[21] Jeff Frooman, "Socially Irresponsible and Illegal Behavior and Shareholder Wealth," *Business & Society,* September 1997, pp. 221–49, argues that the negative effects on shareholder wealth when a firm acts irresponsibly support the enlightened self-interest view: act responsibly to promote shareholders' interests.

[22] Mark Orlitzky, Frank Schmidt, and Sara Rynes, "Corporate Social and Financial Performance: A Meta-analysis," *Organization Studies,* 2003, pp. 403–41. Other studies investigating this issue include Bernadette M. Ruf et al., "An Empirical Investigation of the Relationship between Change in Corporate Social Performance and Financial Performance: A Stakeholder Theory Perspective," *Journal of Business Ethics,* 2001, pp. 143–56; Marc Orlitzky and John D. Benjamin, "Corporate Social Performance and Firm Risk: A Meta-analytic Review," *Business & Society* 2001, pp. 369–96; and Amy J. Hillman and Gerald D. Keim, "Shareholder Value, Stakeholder Management, and Social Issues: What's the Bottom Line?" *Strategic Management Journal*, 2001, p. 135.

[23] S. Prakash Sethi, "A Conceptual Framework for Environmental Analysis of Social Issues and Evaluation of Business Response Patterns," in S. Prakash Sethi and Cecilia M. Falbe, eds., *Business and Society: Dimensions of Conflict and Cooperation* (Lexington, MA: Lexington Books, 1987), pp. 42–43.

[24] See the Caux Roundtable Web site at *www.cauxroundtable.org*.

FIGURE 3.5

Evolving Phases of Corporate Social Responsibility

Phases of Corporate Social Responsibility	CSR Drivers	CSR Policy Instruments

CSR_1 funding	**Corporate Social Stewardship**	Executive conscience	Philanthropic
1950s–1960s	Corporate philanthropy—acts of charity Managers as public trustee-stewards Balancing social pressures	Company image/reputation	Public relations
CSR_2 strategy	**Corporate Social Responsiveness**	Social unrest/protest	Stakeholder
1960s–1970s compliance	Social-impact analysis	Repeated corporate misbehavior	Regulatory
	Strategic priority for social response Organizational redesign and training	Public policy/government regulation	Social audits Public affairs
function reform	for responsiveness	Stakeholder pressures	Governance
	Stakeholder mapping and	Think-tank policy papers	Political
lobbying			
	implementation		
CSR_3	**Corporate/Business Ethics** Mission/vision/values	Religious/ethnic beliefs	
1980s–1990s	Foster an ethical corporate culture	Technology-driven value changes Human rights pressures	statements CEO leadership
ethics			
	Establish an ethical	Code of ethics	organizational
climate	Ethics committee/officer/audits		
	Recognize common	Ethics training	ethical
principles	Stakeholder negotiations		
(i) CSR_4	**Corporate/Global Citizenship** Intergovernmental 1990s–2000s compacts Global audit standards NGO dialogue Sustainability audits/reports shifts/competition	Global economic Stakeholder partnerships Integrate financial, social, and environmental performance Identify globalization impacts Sustainability of company and environment	trade/investment High-tech communication networks Geo-political Ecological
		awareness/concern	NGO
pressures			

Source: Adapted from William C. Frederick, *Corporation, Be Good! The Story of Corporate Social Responsibility* (Indianapolis, IN: Dog Ear Publishing, 2006). Used with permission.

- Corporate social responsibility means that a corporation should be held accountable for any of its actions that affect people, their communities, and their environment. Businesses must recognize their vast power and wield it to better society.
- The idea of corporate social responsibility in the United States was adopted by business leaders in the early 20th century. The central themes of social responsibility have been charity—which means giving aid to the needy—and stewardship—acting as a public trustee and considering all corporate stakeholders when making business decisions.
- Corporate social responsibility is a highly debatable notion. Some argue that its benefits include discouraging government regulation, promoting long-term profitability for the firm, and enhancing the company's reputation. Others believe that it lowers efficiency, imposes undue costs, and shifts unnecessary obligations to business.
- Socially responsible businesses should attempt to balance economic, legal, and social obligations. Following an enlightened self-interest approach, a firm may

be economically rewarded while society benefits from the firm's actions. Abiding by legal requirements can also guide businesses in serving various groups in society.

- Managers should consider all of the company's stakeholders and their interests, not only their shareholders. Management's central goal is to promote the interests of all stakeholders by pursuing multiple company goals. This broader, more complex task emphasizes the long-run objectives and performance of the firm.

Key Terms

charity principle, *48*
corporate social responsibility, *45*
enlightened self-interest, *56*
iron law of responsibility, *47*
legal obligations, *57*
reputation, *52*
stewardship principle, *49*

Internet Resources

www.csracademy.org.uk CSR Academy
www.csr-monitor.com CSR Monitor
www.csrwire.com -The Newswire of Corporate Social Responsibility
www.worldbank.org/wbi/corpgov/csr -The World Bank Group, Corporate Governance and Corporate Social Responsibility

Source: "Hurricane Katrina," *http://en.wikipedia.org/wiki/Hurricane_Katrina;* "Casino Companies Still Paying Displaced Workers' Salaries," *Casino City Times*, September 7, 2005, *www.casinocitytimes.com;* "Challenges Loom for Management in Katrina's Wake," *Pittsburgh Post-Gazette*, September 13, 2005, *www.post-gazette.com;* "Katrina: The Aftermath," *Atlanta Journal-Constitution*, September 13, 2005, *ajc.com;* "When Good Will Is Also Good Business," *The New York Times*, September 14, 2005, *www.nytimes.com/2005/09/14/business*.

Discussion Questions

1. Do the demonstrations of kindness described in this story exemplify the charity principle or the stewardship principle, or both?
2. Which arguments for corporate social responsibility support the actions of the companies profiled here, and which arguments against corporate social responsibility raise questions concerning these actions?
3. Enlightened self-interest occurs when a business recognizes the interrelationship between its company's economic interests and its social obligations. Do you think that the acts of corporate generosity described in this case represent examples of enlightened self-interest? Why or why not?
4. Is it businesses' duty to help those in extreme need, such as victims of Hurricane Katrina, or is this the job of governments and individuals? How far should a company go to assist the community, their employees, and others affected by a natural disaster?