Corporate Social Responsibility : Theory and Practice

Melkote K. Shivaswamy
Ball State University, Muncie, Indiana, USA
mshivasw@bsu.edu

Abstract

This paper focuses on the indebtedness of corporations to society that sustains them. It is their obligation to pursue goals that do not conflict with socially responsible behavior. Many cases are cited here to suggest a positive link between corporate social responsibility and financial performance. However, results of statistical studies seem inconclusive.

Whether such a link exists or not, corporations are being increasingly pressured by public opinion and by the justice system, to pursue socially responsible practices. Corporate giving as a percentage of revenues appears insubstantial. It does become noticeable when combined with gifts by top individual givers who owe their fortunes to the success of the corporations they work for. Corporate giving is only one form that social responsibility can take and progress has been made on other fronts. Corporations increasingly realize that socially and ethically responsible conduct actually helps them make more profits. It builds trust, promotes long-term relationships with stakeholders, boosts employee morale, promotes employee loyalty, and helps recruit new hires. It also enhances a company's reputation. A review of literature indicates that 'stakeholder theory' has an edge over the Friedman paradigm. Surveys indicate that the youth of today are socially and environmentally conscious and stand firmly for socially responsible corporate practices. The author concludes that if this is a trend, the future of corporate social responsibility appears secure.

Key-Words : Stakeholder; Donations; Social auditing; Moskowitz Prize; Ethically responsible conduct; Corporate citizen.

Introduction

In this competitive global economy, privatized deregulated businesses are increasingly the norm, and corporations have grown enormously in importance. Indeed, more than half of one hundred largest economies in the world are not countries but corporations. The sales of General Motors, Wal-Mart and Exxon total $508 billion, a sum that exceeds the gross domestic product of India. Internationally, corporate logos are more powerful symbols than national flags (Dobbs, 2004). Corporations are indebted to society that sustains them. It is their obligation to pursue goals that do not conflict with socially responsible behavior. Social responsibility has been defined as "a business' obligation to pursue policies, make decisions, and take actions that benefit society." It is concern for the impact of corporate actions on society as a whole (Williams, 2005).

Expectations

The owners/shareholders expect rewards through higher dividends and/or stock price. The employees expect job security, a safe working environment, support for their training and development, an environment where there is no discrimination on grounds of race, sex, and age, support and encouragement for their volunteer efforts, and respect for their privacy and individuality. The customers expect products of six sigma quality that are safe to use and priced fairly, prompt service after sales, and truth in advertising. The community expects corporations to get involved in the welfare of children, families and disadvantaged groups, to prevent pollution of air, water and earth, and to participate in clean up if they do pollute. Charitable organizations such as Red Cross and United Way expect contributions in cash and kind. In short, corporate social responsibility could take many forms and involves balancing the interests and concerns of multiple stakeholders. This paper reviews theories and practices that are related to corporate social responsibility, and also speculates on its future.

Conflicting Theories

There are two models of corporate social responsibility: (1) the shareholder and (2) the stakeholder. Milton Friedman, an exponent of the shareholder model, states "there is one and only one social responsibility of business - to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud." Donations to charitable organizations, for example, would simply mean corporations are spending other people's money. Firms run by such managers will have higher costs and eventually be driven out of the market place whereas firms that pursue the goal of maximizing shareholder wealth will attract more capital and flourish (Frank, 2004).

Andrew Carnegie, the steel magnate from Pittsburgh who is best remembered for financing public libraries, was of the view that "God wants us to do well so that we can do good." Carnegie's innovation, the Foundation, provided a model for later super-rich Americans such as Rockefeller and Ford. Julius Rosenwald, who transformed Sears, Roebuck from a failing mail order store to a successful company, believed "you have to do good to do well." He sponsored 4-H clubs and helped spread knowledge of new agricultural technology to farmers in rural America. This was good advertising and good public and customer relations for Sears and helped Sears prosper. William C. Norris of Control Data Corporation was involved in projects providing training and employment to inner-city ghetto dwellers, teaching problem learners, and rehabilitating prisoners. He saw solutions to social problems as opportunities for business success (Drucker, 1994). Merrick Dodd presented an expanded view of social responsibility in 1932. His contention was that the powers of corporate management are held in trust for the entire community ((Post, 2003). Mahatma Gandhi held similar views. Carnegie, Rosewald, Norris, Dodd and Gandhi could all be considered proponents of the stakeholders' model. The stakeholder's viewpoint has gained followers since the Great Depression when General Electric first identified shareholders, employees, customers and the general public as its stakeholders. In 1947 Johnson and Johnson acknowledged stakeholders other than shareholders and Sears, Roebuck followed suit in 1950. Until 1953 it was illegal in most states for corporations to make donations for non-business purposes. Today U.S. companies donate approximately 6 billion dollars a year to communities, causes and charities. Many states allow company Boards of Directors to consider the needs of stakeholders such as employees, creditors, suppliers, customers, and local communities, as well as those of shareholders (Williams, 2005).

The Stakeholders

Individuals or groups that have interests, rights or ownership in an organization and its activities are known as stakeholders. A short list of six stakeholders includes employees, management, owners/shareholders, suppliers, customers, and the local community (Post, 2003). Government regulators, public opinion leaders, political and other action groups (Nader Raiders, for example), and the media are other stakeholders whose actions could help or hurt a business. The World Wide Web has helped various action groups bring pressure to bear on firms that are not considered socially responsible (Hellriegel, 2002).

Opinion Surveys Favour the Stakeholder Model

Opinion surveys indicate that the majority view favours the stakeholder model. In one study, 72% of job seekers surveyed preferred to work for socially responsible companies. Another study shows that 80% of top-level managers believe it is unethical to focus just on shareholders (Williams, 2005). 88% of young people believe that corporations have an obligation to support social causes. In a survey by the research group Cone Inc., 86% of respondents said they would switch brands to companies who are socially responsible. According to a Deloitte Touche Study 72% of job seekers prefer to work for a company that supports social causes (Hempel, 2004).

The Reactive and Proactive Businesses

Firms that pursue reactive policies respond to public pressure and try to behave responsibly. By contrast, proactive firms make social responsibility a cornerstone of their strategy. Indeed, many managers in the United States increasingly recognize that the strategic interests of a business are best served when the concerns of stakeholders are properly addressed (Hellriegel, 2002). Effectively managing environmental issues, for example, could lead to a competitive advantage. Decreased operating costs and increased revenues frequently result from voluntary changes to product and process design that reduce adverse environmental impacts (Epstein, 2000).

The Social Audit

Proactive firms do social auditing to monitor implementation of socially responsible practices. A social audit is defined as "an analysis of an organization's success in carrying out programs that are socially responsible" (Wild, 2003). It identifies, monitors, and evaluates the effects that the organization has on its stakeholders and on society as a whole. Examples of such companies are Shell, Levi Strauss, AT&T, McDonald's, and Johnson and Johnson (Hellriegel, 2002).

Fostering Socially Responsible Conduct

Organizations such as Business for Social Responsibility (BSR), actively promote socially responsible conduct. Business leaders from around the world (1,000 leaders from 40 countries) meet in New York annually to share experiences, challenges and solutions relating to corporate social responsibility. The Social Investment Forum awards the Moskowitz Prize for outstanding research in the field of socially responsible investing. It is named for Milton Moscowitz, a pioneer researcher in the area of corporate social responsibility (Baue, 2004). The Ron Brown Award, instituted in 1997 recognizes corporations that show leadership in responsible social behavior. It encourages leaders to move away from the traditional utilitarian model of business and become more active in contributions to society. Early recipients include Anheuser Busch, IBM and the Bank of Boston (Hellriegel, 2002).

Some Case Studies

PETA - People for Ethical Treatment of Animals, put pressure on companies such as Procter and Gamble to take a humane approach and refrain from using animals for drug testing (Williams, 2005). Footwear companies such as Nike, Reebok, L.A. Gear, Puma and New Balance, whose contractors used child labour, were subjected to scrutiny. Chinese factories employed child labor, less than 16 years of age, paying them less than the Chinese minimum wage of $1.90 a day. The companies listened when college students refused to wear their shoes in protest. Employee layoffs at IBM and AT&T were moderated by public pressure. Employee pay and benefits affected by IBM's cash balance plan became a subject of public controversy. Sears, whose employee incentives led to unethical practices, had a market backlash. They were selling unneeded services to meet their quotas. Customers filed hundreds of complaints against this practice and the company's reputation was tarnished (Hellriegel, 2002). Tobacco companies, for years, denied that nicotine was harmful to health and, as a consequence, invited lawsuits and fines.

Enron executives sold stock before its value dropped steeply. The employees, shareholders and other stakeholders were left holding the bag. The leading figures in that case were brought to justice and are now serving prison terms. Arthur Andersen was forced out of business for shredding documents that could have incriminated Enron. Martha Stewart sold stock of Imclone Systems a day before its stock price plummeted. She had advance knowledge of FDA's rejection of the company's application for approval of a cancer drug. She was convicted and had to serve a term in prison.

Firestone's delayed recall of defective tires hurt Company's sales and profits. Merck did not withdraw Vioxx, an arthritis drug till recently even though they knew it was harmful. This invited massive lawsuits and its stock price took a deep plunge. Fortune magazine, referring to the loss of market capitalization that followed the withdrawal, calls it Merck's' own "$27 billion dollar heart attack" (Simons, 2004).

Ben and Jerry's sold more ice cream and made more profits because of its efforts to preserve the Amazon rain forests. It contributes 7.5% of its pretax earnings to charitable causes. Ben Cohen and Jerry Greenfield, the founders, believed that the company enjoyed its current position in the market place by 'brand equity' generated by its foundation work and other socially responsible actions. Manifestations of brand equity are consumer loyalty to the brand, and demand for its shares of stock. Ben and Jerry's mission is to (a) make quality products, (b) achieve economic rewards to its shareholders, and (c) meet its social mission by having a commitment to its community. All three parts are viewed by the company as working in harmony to achieve the company's goals. Being socially responsible is viewed by everyone in the company as fulfilling its mission, not a drain on its resources (Frank, 2004; Hellriegel, 2002).

Xerox offers its workers up to a year of leave to work for non-profit organizations. Nike invests in a program called PLAY (Participate in the Lives of American Youth). Many independently owned movie theaters, and leisure sports businesses offer discounts to students and senior citizens. There are also firms that sponsor events such as the Special Olympics for the disabled, and summer reading programs at the local library (Wild, 2003).

Boeing's contributions combined with those of its employees totaled nearly $60 million to support community programs in education, health and human services, civic participation and the arts. Employees and retirees also volunteered more than one million hours of their own time to serve their communities. The AT&T Cares programme provides a paid work day to employees for community services such as planting trees, clearing playgrounds, and building houses. AT&T donates money as matching gifts to programs such as the United Way, and minority and women-owned businesses. The Chiquita Environmental Charter is to protect the rain forest; to maintain clear water; to minimize the use of agrichemicals; to reduce, reuse and recycle waste; to support environmental education; and to ensure that the workforce is well trained and works safely (Wild, 2003). Tylenol chose to lose a few thousand dollars by recalling a batch of contaminated products rather than deal with millions of dollars of lawsuits. Star Kist Tuna's sales rose when it raised its price to cover the added cost of purchasing only dolphin-safe tuna from suppliers. This suggests that consumers are socially conscious and disproves the standard "free-rider" model, which suggests that buyers will not willingly pay a premium for products produced by socially responsible firms. The Body Shop sells more cosmetics because of its environmentally friendly packaging. McDonald's sells more hamburgers because of its support for the parents of seriously ill children (Frank, 2004). It's 'McRecycle USA' program has resulted in increased use of recycled materials in its operations. Since 1990, McDonald's has purchased $3 billion worth of recycled products for construction, equipment and packaging (Williams, 2005). Every December Bagel works employees choose local charities for award of financial support, promotional space, and free bagels. For the past three years, Bagel works has donated 10% or more of its profits to charities (Wild, 2003). Starbucks pays more than minimum wage and gives full health insurance coverage to those working over 20 hours per week. General Foods donates cereal to national school breakfast programs. Patagonia (Patagonia.com) pursues policies that are employee and environmentally friendly. We Are Volunteer Employees (WAVE) program is supported by FANNIE MAE and FREDDIE MAC Foundation through 10 hours of paid leave per month for employee's volunteer activities. Bill Ford the new chief of Ford Motor Company wants to push his environmentally friendly agenda ((Hellriegel, 2002). Toyota and Honda, by producing environmentally friendly cars have increased their market share and profits in the global market place. Pfizer supports Hank's Brain Trust to address the health problems of Africa. INTEL sponsors computer clubs. Avon Products has breast cancer programs in 50 countries. GE recently pledged 20 million dollars to construct hospitals in China. Hasbro, the toy maker, gives away toys to disadvantaged kids and provides grants for child health care programs (Hempel, 2004).

The International Dimension

Multinational companies are increasingly involved in causes abroad. At least 22% of their revenues come from their overseas operations and multi-nationals realize that they cannot do business abroad without being socially responsible. Developing economies increasingly demand assurance that multinationals treat customers in all geographic markets with the same respect they accord to customers in their local markets. Operating responsibly in developing countries without exploitation of local resources is considered an important aspect of business sustainability and equality. International programs now account for 16% of total U.S. corporate gifts. One quarter of 203 companies that divulged their philanthropic practices in a 2004

BusinessWeek survey had international giving programs that have grown significantly over time. Nike increased its global giving from 20% in 2000 to 39% of its overall contributions in 2004. Citigroup has increased its global giving from 20% to 30% of its total contributions during the same period. The Group has provided grants for small loans to 900,000 women in India. IBM's global giving as a percentage of total rose from 12.4% in 2000 to 30.4% in 2004 and is projected to increase to 40% in 2006 (Hempel, 2004).

Corporate and Individual Giving in Cash and Kind

On a BusinessWeek survey, which identified top corporate cash givers, Wal-Mart tops a list of ten with $176 Million (see table 1). However, none of these ten companies was included in a list of top fifteen companies ranked based on a ratio of cash gifts to revenues (see table 2). The most generous among these, Freeport McMoRan, a mining company, gave just 0.98% of revenues as cash gifts. Of the top ten corporate cash givers, only Pfizer had a place among the top fifteen givers in kind (seventh rank), on a list that presents gifts in kind as a percentage of revenues (see table 3). The most generous among the in-kind givers, HCA, gifted 3.77% of their revenues. Total cash donations made by Standard and Poor's 500-stock index companies included in the survey totals $3.26billion. By contrast, the top five individual givers alone gave $6 billion (Hempel, 2004). The top fifty individual donors, with Bill and Melinda gates at the very top have, over their life time, contributed $65 billion. By donating virtually all of their assets to charity, and doing it during their life times, many of the top fifty also provide a contrast to their fellow wealth-holders. On the average, the nation's richest 1% who own two-fifths of U.S. wealth, donate just 2% of their incomes each year vs. 6% for families in the bottom income bracket (Conlin, 2004).

Corporate Social Responsibility and Financial Performance : Statistical Studies

The Moskowitz Prize winning study by Marc Orlitzky, Frank Schmidt and Sara Rynes of Iowa finds a strong link between corporate social and financial performance. The conclusion is based on a meta-analysis of 52 studies conducted between 1972 and 1997 containing a total of 33,878 observations (Baue, 2004). The number of socially responsible mutual funds based in the United States increased from thirteen in 1991 to sixty-seven by the year 2000. This was in response to investors who are unwilling to invest in companies that are not considered socially responsible. Types of firms that are screened out by such mutual funds include those that are engaged in the production of alcohol, tobacco, weapons, and other dangerous or offensive products and services. Companies that are in the gambling industry, use animals for testing, disregard environmental safety, violate human rights, indulge in unfair labor practices, fail to promote equality of opportunity in employment, ignore community relations, and refuse to invest in the community, are also subject to screening by socially responsible mutual funds. In a study of 23 such funds, it was found that the most commonly used screen is in respect of tobacco products, followed by weapons manufacture and employment equality. How did socially responsible mutual funds perform in comparison with the more inclusive S&P 500 Index? Results of a study of ten funds for which data was available for a ten-year period were mixed (see table 4). Two funds, the Domini Social Equity and Pax World (PAXWX), judged by annualized risk-adjusted mean return, outperformed the S&P 500 Index. The other eight ranked lower (Edwards and Samant, 2003).

A Concluding Note

The cases presented do suggest a positive link between corporate social responsibility and financial performance. However results of statistical studies seem inconclusive. Whether such a link exists or not, corporations will be increasingly pressured by public opinion and by the justice system, to pursue socially responsible practices. The number of mutual funds that screen out corporations that are not socially responsible is on the rise. In the eighties, such mutual funds, for the most part, screened out companies that invested in South Africa as socially irresponsible. The number of criteria used for this determination has since multiplied.
Corporate giving as a percentage of revenues appears insubstantial. It does become noticeable when combined with gifts by top individual givers who owe their fortunes to the success of the corporations they work for. The trend appears upward particularly in an international context. Corporate giving is only one form that social responsibility can take and progress has been made on other fronts. Corporations increasingly realize that socially and ethically responsible conduct actually helps them make more profits. It builds trust, promotes long term relationships with stakeholders, boosts employee morale, promotes employee loyalty, and helps recruit new hires. It enhances a company's reputation. Besides, if things go wrong, it is easier for a company that has the reputation of being a good corporate citizen to control the damage (Hempel, 2004). They look upon socially and ethically responsible practices as good business strategy. A review of literature seems to indicate that the stakeholders' theory has an edge over the Friedman Paradigm (Post, 2003). Surveys indicate that the youth of today are socially and environmentally conscious and stand firmly for socially responsible corporate practices. If this is a trend, the future of corporate social responsibility appears secure.

Appendix

Table 1

Companies Making the Largest Cash Donations

	2003 Donations (Millions)
Wal_Mart	$176.00
Ford Motor	120.00
Altria Group	114.90
Johnson & Johnson	99.00
Exxon Mobil	97.10
JP Morgan Chase	86.00
Bank of America	85.40
Pfizer	83.30
Wells Fargo	83.00
Citi Group	81.40

Source : *BusinessWeek*, November 29, 2004, p.102.

Table 2

Companies Making the Largest Cash Donations As Percentage of Revenues

2003 Cash Donations	% of Revenue (Millions)	
Freeport-McMonRon	$21.70	0.98
Corning	29.00	0.94
Avon Products	49.30	0.72
Newmont Mining	22.80	0.71
Computer Associates	15.30	0.49
General Mills	49.30	0.47
Fifth Third Bank Corp	30.00	0.46
M&T Bank	13.70	0.46
Eli Lily & Co	51.10	0.41
Medtronic	31.00	0.4
Northern Trust	9.50	0.37
Janus Capital Group	3.30	0.34
Guidant	12.10	0.33
KeyCorp	18.60	0.33
Sallie Mae	14.10	0.32

Source : *BusinessWeek*, November 29, 2004, p.102.

Table 3

Companies Making the Largest Donations in Kind As % of Revenues

Company	2003 in-kind Donations (Millions)	% c Revenues
HCA	$821.30	3.77
Genzyme	63.00	3.68
Merck	789.00	3.51
Parametric Technology	13.70	2.04
Eli Lilly & Co	222.30	1.77
Halliburton	251.90	1.55
Pfizer	602.90	1.33
The McGraw-Hill Cos	54.90	1.14
Abbot Laboratories	200.00	1.02
Oracle	91.00	0.96
Microsoft	224.00	0.70
Johnson & Johnson	285.50	0.68
Gannett	37.10	0.55
Tribune	29.10	0.52
Kellogg	34.20	0.39

Source : *BusinessWeek*, November 29, 2004, p.102.

Table 4

10-Year Annualized Risk-Adjusted Mean Returns for Socially Responsible Mutual Funds-(1991-2000) Comparison with S&P 500 Index

Name	Risk-adjusted	
	Mean Return (%)	Rank
Domini Social Equity	18.2	1
Pax World (PAXWX)	17.93	2
S & P 500 Index	17.71	3
American Mutual (AMRMX)	16.79	4
Smith Barney Concert Social Aware B	16.79	4
Parnassus (PARNX)	14.83	6
Ariel Appreciation	13.71	7
Calvert Social Investment Balanced A	13.16	8
Calvert Social Investment Equity A	11.52	9
Rightime Social Awareness	10.71	10
New Alternatives	9.62	11

Source: Edward & Samant, p.59.

References

Baue, William, "Moscovitz Prize Study Removes Doubts over Link between Corporate Social and Financial Performance," *The Corporate Social Responsibility Newswire Service*, www.csrwire.com, October 29, 2004.

Conlin, Michelle, Lauren Gard and Jess Hempel, "The Top Givers," *BusinessWeek*, November 29, 2004, pp.87-94.

Dobbs, Lou, *Exporting America* (Warner Books, 2004).

Drucker, Peter F., *The Frontiers of Management* (Harper & Row, 1986).

Edwards, Ed, and Ajay Samant, "Investing with a Conscience: An evaluation of the Risk-Adjusted Performance of Socially Responsible Mutual Funds," *Mid-American Journal of Business*, 2003, Vol.18, No. 4, pp.51-60.

Epstein, Marc J., and Marie - Josee Roy, "Environmental Management to Improve Corporate Social Responsibility," in James M. Reeve (Ed,), *Readings and Issues in Cost Management* (South-Western, 2000), pp.171-182.

Frank, Robert H., *What Price the Moral High Ground ? — Ethical Dilemmas in Competitive Environments* (Princeton University Press, 2004).

Hellriegel, Don, Susan E. Jackson, and John W. Slocum, Jr., *Management : A Competency-Based Approach* (South-Western, 2002).

Hempel, Jess and Lauren Gard, "The Corporate Givers: U.S. Companies have discovered that Global Philanthropy can Reap Big Dividends," *BusinessWeek*, November 29, 2004, pp.100-104.

Past, Frederick R., "A Response to the Social Responsibility of Corporate Management : A Classical Critique," *Mid-American Journal of Business*, 2003, Vol.18, No.4, pp. 25-35.

Simons, John & David Stipp, "Will Merck survive Vioxx?" *Fortune*, November 1, 2004, 91-92.

Wild, John J., *Financial Accounting : Information for Decisions* (McGraw Hill, 2003).

Williams, Chuck, Management (South-Western, 2005).