

Need Corporations Be Socially Responsible – Or Not?

By Schuyler (Sky) Lance

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The opposing views:

“The enlightened corporation should try to create value for all of its constituencies. Someday businesses like Whole Foods, which adhere to a stakeholder model of deeper business purpose, will dominate the economic landscape.”

--- John Mackey, Founder and CEO of Whole Foods

“Few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible.”

--- Milton Friedman, Capitalism and Freedom, University of Chicago Press

You read it in the press:

...rapid increases in world-wide energy consumption; significant increases in CO₂/greenhouse gases causing global warming; continuing worldwide population growth especially from lesser-developed countries trying to live on 20% of the earth's resources; foreign labor abuses; growing dependency on foreign oil...

No wonder companies around the globe are grappling with the question as to whether their organizations should be doing more in the area of Corporate Social Responsibility (“CSR”).

What is CSR?

CSR refers to a company's obligation to be sensitive to needs of all of the stakeholders, broadly defined (shareholders, suppliers, employees, community, etc.). CSR is closely linked with principles of “Sustainable Development” – making decisions based not only on financial/economic factors, but also on the social and environmental consequences of a company's activities.¹ The World Business Council describes CSR as “...the continuing commitment by a business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large” – development that meets the needs of the present world without compromising the ability of future generations to meet their own needs².

CSR should not be confused with philanthropy -- making charitable donations or spending money on community projects, endowing scholarships, establishing foundations or even encouraging employees to volunteer to take part in community work. While all worthy endeavors, these alone do not define a socially responsible company. CSR is a more holistic approach to business that regards the business as being a full partner in its

community rather than seeing itself more narrowly defined as being in business solely to make profits.¹

Is there a Business Case for CSR?

Proponents say there is a strong case for voluntary CSR:

1. CSR has human resource benefits. In general, employees prefer to work for companies that earnestly employ CSR strategies. This can help in areas of employee recruitment and retention, and contributes to a positive atmosphere that can lead to higher employee morale. In fact, a 2003 Stanford University Graduate School of Business survey of MBAs from European and North American business schools found that respondents would forgo an average of \$13,700 in compensation to work at a company that had a stronger reputation than its competitors for environmental sustainability and caring about employees and stakeholders.³
2. CSR has risk management/reputation management benefits. When an organization views itself as a partner, as opposed to exploiter, of the environment, its employees, suppliers and other stakeholders, the company can avoid embarrassing issues costly to both reputation and profits. “Reputational issues can have a dramatic impact on share price and the bottom line” says Andrew Savitz, author of *Triple Bottom Line*.
3. CSR can be a source of brand differentiation. Companies such as Ben and Jerry’s ice cream carry a faithful following due in part to the company’s commitment to social goals. In fact, according to a 2002 MORI Research report, 44% (up from 24% in 1997) of respondents said that when forming a decision about buying a product or service from a particular company, it is “very important” that the company show a high degree of social responsibility.⁴
4. CSR provides a license to operate in a company’s own country as well as in foreign countries. Being viewed as a good corporate citizen, companies can also avoid undue governmental intervention.
5. CSR can divert attention from reputational issues – such as those faced by the tobacco industry. Some say an example of diversionary CSR is petroleum giant BP’s installation of wind turbines on the roofs of certain of its gas stations in the UK.

Case Study for CSR – Whole Foods: Of all the food retailers in the *Fortune 500* (including Wal-Mart), Whole Foods has the highest profits as a percentage of

sales, return on invested capital, sales per square foot, same-store sales, and growth rate. Whole Foods is currently doubling in size every three and a half years. Its sales are nearly \$5 billion, with a market capitalization over \$8 billion. The bottom line is that Whole Foods stakeholder business philosophy works and has produced tremendous value for all of its stakeholders, including its investors.⁵

What do the critics say?

Critics say voluntary CSR won't work because companies do not have a "conscience." Companies care little for the welfare of workers, and given the opportunity will move production to sweatshops in less regulated countries. Likewise, it is argued that they have little incentive to minimize the use of scarce resources in meeting profit objectives. Further, they care little for suppliers and look to maximize profit margins without regard to any specific supplier (e.g. shifting from a domestic supplier to a lower-cost foreign supplier). Finally, it is reasoned, companies should not have to bear the burden of the costs of their operations that will be paid by other means (e.g. the cost of cleaning pollution frequently falls on society in general – often years after the pollution occurred).

After all, the critics argue, free markets and capitalism have been at the center of economic and social development over the past 200 years in America, and improvements have occurred over that time in living conditions, health and longevity of life. These advances have only been possible because economies driven by free enterprise have progressed.¹

Free markets, critics go on to say, provide the necessary regulators of scarce resources: as a commodity (e.g. oil, steel, wood) becomes more scarce, the price of the commodity goes up, thereby curbing demand.

Profitable companies in the U.S. invest in less developed countries, which contributes to the welfare of these societies (notwithstanding these countries may have fewer protections in place for workers). Failure to invest in these countries (e.g. keeping a higher-cost domestic supplier for CSR reasons) decreases the opportunity to increase worldwide social welfare.

Unfettered market factors (supply, demand, competition), critics claim, naturally drive the need to pay well and to provide adequate working conditions that lead to an overall appropriate standard of living for the companies' workers. Otherwise they will go work somewhere else!

The critics are not completely heartless: they generally agree that because voluntary CSR does not work, governmental regulation is required to ensure companies meet minimum business requirements (regarding, for instance, environmental conduct, employee matters, and, more recently, ethical practices).

This is consistent with Milton Friedman's view that "A corporation's principal purpose is to maximize returns to its shareholders, while obeying the laws of the countries within which it works."

Case Study Against CSR - Wal-Mart: Some say Wal-Mart, the world's largest company, has achieved its famous "Everyday low prices" through ruthless cost-cutting and by dictating terms on which it operates to employees, suppliers, communities, the environment and any other stakeholder with an interest. It is providing its key stakeholders, its customers, with what they want – and it shows in the figures: Every week, approximately 140 million shoppers visit Wal-Mart; 82% of American households made at least one purchase at Wal-Mart during the year.⁶

New Business Model Emerging

Despite all the arguments, with the fast-spreading commitment to CSR, there is a fundamental new business model emerging: one that respects stakeholder and shareholder values simultaneously. In the words of General Mills Vice Chairman and CFO Jim Lawrence: "It's not social responsibility versus profitability. [Today] it's social responsibility *and* profitability."⁴

Enough debate: What are companies actually doing re: CSR?

According to a US Chamber of Commerce survey⁷ 82% of the respondents indicated "good corporate citizenship helps the bottom line." Moreover, more than half said corporate citizenship is "part of their business strategy", and in today's global interdependence, most executives said "their obligation as leaders is broader [today] than in the classic definitions of good business practice" (simply returning profit to shareholders, paying taxes, and obeying the law). Most U.S. companies say "good corporate citizenship also includes meeting ethical, environmental, and social objectives."

We see evidence that CSR is going "main stream" when leading organizations such as Thomson Financial state, "Intangibles such as good governance, strong brands, a culture

of innovation, well-managed human capital and exemplary environmental practices are what drive long-term corporate value.”⁸

Corporate America’s sudden burst of idealism can be traced to several sources, according to this month’s CFO Magazine:

1. The wave of corporate scandals that has made companies realize that they are going to be subject of the activist, consumer, and shareholder focus for a long time;
2. Thanks to the Internet, everyone has rapid access to information about that behavior. “If you had a supplier using child labor or dumping waste into a local river, that used to be pretty well hidden. Now, someone walks by with a camera and blogs about it.”⁹
3. Real concerns about resource constraints, driven by the rising costs of such crucial commodities as steel and oil, are spurring executives to action.

Key Challenges to CSR

If CEOs generally support CSR, why is it not more prevalent? There are forces in the way business is set up in America that makes it difficult for even the most CSR-desirous executives to move his or her CSR visions forward:

- CSR objectives can be difficult to define and agree upon.
- Wall Street holds companies to quarterly results; such short-term thinking often precludes companies from “investing in the future” as they would like to meet CSR goals.
- Through stock options and other mechanisms, corporate executives have strong incentives to maximize profits.
- CEOs are concerned that if they sway too far from the strictest interpretation of profit-making, they could lose their jobs.
- Boards of directors fear lawsuits if shareholder resources (the company) are perceived to be used for “the greater good.” Further, Boards have difficulty determining where expenditures on CSR fit as it relates to the board’s other duties currently under shareholder scrutiny, such as accounting oversight, performance evaluations and deferred compensation, to name a few.

Despite these hurdles, progress has been made in the area of CSR – especially in Europe -- with 45% of the top 250 companies worldwide now publishing a separate corporate report containing details of environmental and/or social performance.¹⁰ In fact, Triple Bottom Line (TBL) reporting – reporting on 1) corporate financial results, 2) corporate environmental responsibility and 3) corporate social responsibility – has even become mandatory in some countries (e.g. France).

In the U.S. companies are slowly realizing the benefits of TBL reporting, such as enhanced reputation, improved operations and management and improved risk management. As well, a company held in high regard has easier access to capital due to increased confidence from investors, and lenders. TBL can also lead to improved communications with stakeholders overall (although one would be remiss to not mention the critic's response that much of TBL reporting today is "window dressing" for marketing purposes, as is demonstrated by the fact that Enron was a producer of an annual glossy "Corporate Responsibility Annual Report" ...).

As an additional indicator of its growing importance, over the last 30 years the CSR function has moved from the VP/middle management level (individual Health, Safety and Environmental managers) to the strategic development function at the board level of many companies today.

How To Implement CSR Practices – and Stay Out of Hot Water

CSR is different for different companies. There is no universal standard, except that which makes good business sense: CSR initiatives that have benefit to the company. CSR activity generally can only be effective at achieving social or environmental outcomes to the extent it also fosters economic growth – hence the CSR slogan, "Doing well by doing good."

Some CSR initiatives show immediate financial results and are easy to justify, like focusing on new methods of production that tangibly reduce energy usage and scrap. However, many fall into the "Important, but not urgent" category, the results of which are longer-termed and harder to quantify -- such as creating reputational goodwill among customers that will lead to an indeterminable amount of repeat sales, or creating a "feel good" culture through CSR initiatives, the benefits of which (reducing employee turnover and commensurate recruiting and training costs) may not be realized for a number of years. Such longer-termed CSR initiatives need to compete as vigorously for dollars as other long-term spending alternatives, such as R&D, lobbying for tax relief or evaluating the feasibility of a long-term move of manufacturing offshore.

To implement, first determine your company's vision and values. Then you can begin to integrate CSR into the business strategy by assessing how CSR investments support your business objectives and practices. Implementation requires focusing on the individuals; just as former House Speaker Tip O'Neil was quoted as saying, "All politics is local," CSR is a global issue that must be practiced at the local level -- from the individual board members to the front-line managers and your supply chain partners. Foster an organizational ethic of education and learning, and make your employees your ambassadors. The debate regarding CSR must be both transparent and continuous.

Implementing requires forming smart partnerships -- not for PR, but to realize your CSR goals. Keep your dedication to CSR “real”; your stakeholders will know the difference.

In short, CSR requires a cultural change: it is a core company value that needs to permeate all aspects of the business.

“The debate is over” says Andrew Wilson, Director of the Corporate Environmental Strategy Project at Yale University. “The discussion now is about how to build these intangibles into the business.”⁴

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⁴ ICF Consulting report at 2003 8th Green Power Marketing Conference

⁵ John Mackey, Whole Foods CEO; October 2005, Rethinking the Social Responsibility of Business

⁶ University of Miami, “The Anti-CSR Argument”

⁷ “State of Corporate Citizenship in the US: A View from Inside”, Boston College/US Chamber of Commerce, July 2004

⁸ Presentation by John Paluszek, Senior Counsel, Ketchum at Santa Clara University Markkula Center for Applied Ethics, April, 2005

⁹ Andrew Winston, Director of the Corporate Environmental Strategy Project at Yale University

¹⁰ KPMG survey Corporate Sustainability Reporting 2002

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