



CHAPTER

1

# Social Responsibility Framework

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## Corporate Activism Is in Style at Patagonia

Patagonia is more than just an outdoor clothing and gear company. Founded in 1973 by Yvon Chouinard, the company is a leader in corporate social responsibility. Patagonia has four core values that reflect its business: build the best product, cause no unnecessary harm, use business to protect nature, and do not be bound by convention. Patagonia has proven time and time again that strong ethics and environmental consciousness can pay off in the long run.

Patagonia has been fighting for what its leaders believe to be the right thing since before “corporate activism” or “conscious capitalism” had names. For example, in 1990, the company donated to Planned Parenthood while many people said they would boycott the brand and picket at its stores. Instead of appeasing the public, the company doubled down, donating an additional \$5 to Planned Parenthood for every complaint its customer service representatives received. The company’s sales were not harmed. Now more than ever before, consumers demand more action and transparency from their favorite companies, pushing more businesses to take corporate social responsibility (CSR) seriously. Patagonia, which has long been ahead of the pack, is considered a leader in CSR.

For the better part of its 50-year history, Patagonia has focused on environmental issues. For example, Chouinard helped start the 1% for the Planet movement. Participants donate 1 percent of

their sales to environmental causes. The alliance has more than 5,000 business members and is popular worldwide, demonstrating that consumers reward ethical behavior. But now, as the political environment has become increasingly volatile, Patagonia has pushed further into political activism. For example, the company donated \$1 million to fight restrictive voting laws in Georgia and stopped advertising on Facebook and Instagram to protest their spread of misinformation and hate speech. While these actions turned away many customers, the company continues to enjoy revenue of more than \$1 billion annually.

Many companies hesitate to take a stand for fear of losing valuable customers, but Patagonia has no fear. “It’s worth losing a few customers. We always gain more when we take one of these positions,” spokesperson Corley Kenna said to the *Los Angeles Times*. In reality, many of the people boycotting the brand were never Patagonia customers to begin with, so the “lost sales” do not hurt the company but rather serve as free publicity, attracting new customers that share the same values as Patagonia.

Patagonia has no plans to rein in its do-gooder mentality. Greenhouse gas emissions, renewable energy, soil health, recycling, and fair wages are just a few of the causes the apparel company is actively addressing. Customer and shareholder loyalty continue to be strong for the company due to its ethical values and actions.<sup>1</sup>

### Chapter Objectives

- Define the concept of social responsibility
- Trace the development of social responsibility
- Examine the global nature of social responsibility
- Discuss the benefits of social responsibility
- Introduce a framework for understanding social responsibility

**B**usinesses today must cope with challenging decisions related to their interface with society. Consumers and other stakeholders are increasingly emphasizing the importance of companies' reputations, which are often based on ethics and social responsibility. The meaning of the term "social responsibility" goes beyond being philanthropic or environmentally sustainable. Social responsibility includes an organization's obligation to maximize its positive impact and minimize its negative impact on society. Research has concluded that a clear majority (86 percent) of employees prefer to support or work for companies that care about the same issues they do. Social responsibility actions are often quite visible and discoverable, unlike other types of actions that companies take. In an era of intense global competition and increasing media scrutiny, consumer activism, and government regulation, all types of organizations need to become adept at fulfilling these expectations. Like Patagonia, many companies are trying, with varying results, to meet the many economic, legal, ethical, and philanthropic responsibilities they now face. Satisfying the expectations of social responsibility is a never-ending process of continuous improvement that requires leadership from high-level management, buy-in from employees, and good relationships across the community, industry, market, and government. Companies must plan, allocate, and use resources properly to satisfy the demands placed on them by investors, employees, customers, business partners, the government, the community, and others. Those who have an interest or stake in the company are referred to as "stakeholders."

In this chapter, we examine the concept of social responsibility and how it relates to today's complex business environment. First, we define social responsibility. Next, we consider the development of social responsibility, its benefits to organizations, and the changing nature of expectations in our increasingly global economy. Finally, we introduce the framework for studying social responsibility used in this text, which includes such elements as strategic management for stakeholder relations; legal, regulatory, and political issues; business ethics; corporate governance; consumer relations; employee relations; philanthropy and community relations; technology issues; sustainability issues; and global relations.

## Social Responsibility Defined

Business ethics, corporate volunteerism, philanthropic activities, going green, sustainability, corporate governance, reputation management—these are concepts that you may have heard used, or even used yourself, to describe the various rights and responsibilities of business organizations. You may have thought about what these concepts actually mean for business practice. You may also have wondered how businesses engage in these behaviors or contribute to these outcomes. In this chapter, we clarify some of the confusion that exists in the terminology that people use when they talk about expectations for business. To this end, we begin by defining social responsibility.

In most societies, businesses are granted a **license to operate** and the right to exist through a combination of social and legal institutions. Businesses are expected to provide quality goods and services, abide by laws and regulations, treat employees fairly, follow through on contracts, protect the natural environment, meet warranty obligations, and adhere to many other standards of good business conduct. Companies that continuously meet and exceed these standards are often rewarded with customer satisfaction, employee dedication, investor loyalty, strong relationships in the community, positive news and social media reports, and the time and energy to continue focusing on business-related concerns. Firms that fail to meet these responsibilities can face penalties, both formal and informal, and may have their attention diverted from core business practice. For example, Meta,

### license to operate

permission to conduct a business activity, subject to regulation by the licensing authority

Facebook's parent company, is one organization that constantly finds itself in controversy for failing to protect stakeholder interests. In one scandal, a whistleblower shared documents with the media and law enforcement that suggested the social media giant deceived the public and investors about its ability to manage hate speech and misinformation.<sup>2</sup> The goal is to prevent these negative outcomes in the future.

A large multinational corporation may be faced with protestors who voice their disdain publicly. For example, Ben & Jerry's, a subsidiary of Unilever, came under fire for halting the sale of its products in Israeli-occupied territories. In response, a pro-Israel group launched a \$500,000 billboard ad campaign criticizing the company, and the state of Arizona sold off \$93 million in Unilever bonds.<sup>3</sup> Whether the public attacks are physical or virtual, companies often spend significant resources in explaining and defending their business decisions.

Finally, a company engaged in alleged deceptive practices may face formal investigation by a government agency and spend years defending itself. In many cases, these strategies have proved unsuccessful and led to significant penalties, oversight and monitoring agreements, investor lawsuits, and new regulations for the company's entire industry. In one example, LendingClub Corporation, an online lender, paid \$18 million to settle a three-year battle with the Federal Trade Commission (FTC), which said the company deceived customers about hidden fees and the application process. According to the FTC's Bureau of Consumer Protection, business practices such as these harm both consumers and competitors that play by the rules.<sup>4</sup>

Businesses today are expected to look beyond their self-interest and recognize that they belong to a larger group, or society, that expects responsible participation. Therefore, if any group, society, or institution is to function, there must be a delicate interplay between rights (i.e., what people expect to get) and responsibilities (i.e., what people are expected to contribute) for the common good. Research indicates that the most ethical and socially responsible companies are the most profitable.<sup>5</sup> Therefore, responsible conduct and policies yield significant benefits to society, as well as to shareholders and other investors. While the media provide much coverage of misconduct and illegal activities in business, most businesses try to act in an ethical and socially responsible manner.

The term *social responsibility* came into widespread use in the business world during the 1970s. It has evolved to emphasize seven main areas: social issues, consumer protection, sustainability, corporate governance, philanthropy, legal responsibilities, and employee well-being.

We identify seven issues within social responsibility. First, social issues are linked with the idea of **common good**. The common good is associated with the development of social conditions that allow societal welfare and fulfillment to be achieved. In other words, social issues involve the ethical responsibilities a firm owes to society. Equal rights, gender roles, marketing to vulnerable populations, data protection, and internet tracking are examples of social issues common in business.

Second, **consumer protection laws** were enacted to protect vulnerable members of society. Consumer protection laws were necessary because they created formalized safeguards for unsuspecting consumers. For example, the FTC's Bureau of Consumer Protection attempts to limit prejudicial and deceitful business practices by gathering consumer complaints of deceptive conduct. From a legal perspective, the Bureau of Consumer Protection researches unlawful behavior, sues perpetrating organizations, ensures just marketplace practices, and teaches consumers and companies of their responsibilities and rights.<sup>6</sup> As a society, it is important to provide legal protection and education for consumers and businesses alike.

Third, **sustainability** is a growing area of concern in society. In the United States, the term is used more often to refer to the environmental impact on stakeholders. Green marketing practices, consumption of resources, and greenhouse gas emissions are important sustainability considerations that socially responsible businesses will have to address.

#### common good

the development of social conditions that allow for societal welfare and fulfillment to be achieved

#### consumer protection laws

regulations enacted to protect vulnerable members of society with formal safeguards for consumers

#### sustainability

a company's economic, environmental, and social impact

**corporate governance**

a company's formal system of accountability, oversight, and control

**philanthropy**

the desire to improve the welfare of others through donations of money, resources, or effort

**legal responsibility**

the most basic expectation that a company must comply with the law

**employee well-being**

the health and wellness of employees, including how workers feel about their work and their working environment

**social responsibility**

a strategic focus for fulfilling economic, legal, ethical, and philanthropic responsibilities, can also be referred to as corporate social responsibility (CSR) when adopted by a business

Fourth, **corporate governance** refers to formal systems of accountability, oversight, and control. Corporate governance continues to be an important topic in light of the number of business scandals that emerge every year. Issues in corporate governance include concerns over executive compensation, internal control mechanisms, and risk management.

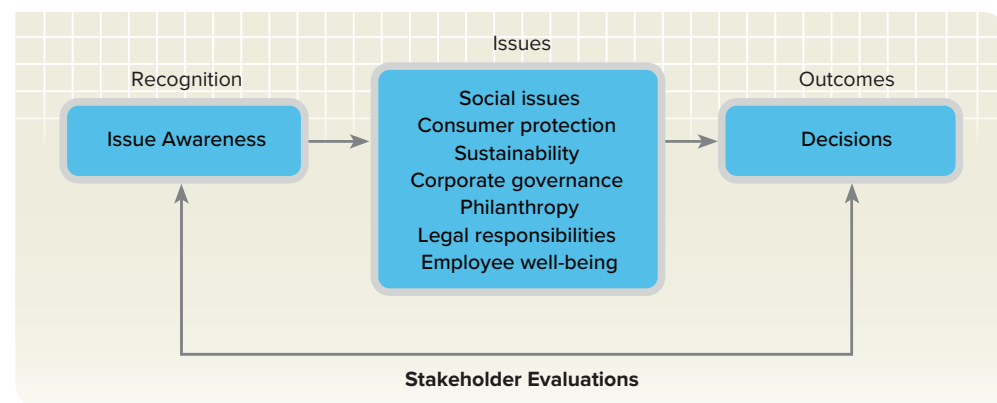
Fifth, **philanthropy** is a key element of social responsibility. Corporate philanthropy is demonstrated in many forms. For example, corporations can contribute financially through cash donations or organizational members can gift their time through volunteerism. Another way that organizations undertake philanthropic initiatives is through outside partnerships with nonprofit firms and charities. Alternatively, corporations may establish in-house philanthropic programs, thereby overseeing their own socially responsible works, when executives feel that their firms' philanthropic giving and strategic direction are aligned.<sup>7</sup>

Sixth, **legal responsibility** is a central factor of social responsibility. Legal responsibility is often thought of as the most basic expectation. Accordingly, organizations must show that they have exceeded their legal responsibilities before they can address their ethical purposes and standards. Legal responsibility is a key foundational issue that affects firms' stakeholder evaluations.<sup>8</sup>

Finally, **employee well-being** occurs when organizations create a safe, healthy, diverse, equitable, and inclusive employment environment for their workforce. Such activities include protecting employees' health and safety while creating job opportunities for development and growth. Employees thrive when their managers treat them with dignity and provide an atmosphere that emphasizes dynamic opportunities to contribute to the firm's overall mission and vision.<sup>9</sup> Taken together, social responsibility issues speak to the diverse array of corporate practices that affect firms' decision-making processes. Figure 1.1 discusses the social responsibility issues that we will be covering in this text.

These seven areas of social responsibility tend to conflict with the traditional or neoclassical view of a business's responsibility to society. The traditional view of social responsibility, articulated in the famous economist Milton Friedman's 1962 *Capitalism and Freedom*, asserts that a business has one purpose—satisfying its investors or shareholders—and that any other considerations are outside its scope.<sup>10</sup> Although this view still exists today, it has lost credibility as more and more companies have assumed a social responsibility orientation.<sup>11</sup> Companies see social responsibility as part of their overall corporate strategy and a benefit that directly increases the bottom line. We define **social responsibility** as a strategic focus for fulfilling economic, legal, ethical, and philanthropic responsibilities. Social responsibility can also be referred to as corporate social responsibility (CSR) when adopted by a business. This definition encompasses

**Figure 1.1** Major Emphases of Social Responsibility



Source: © O.C. Ferrell, 2024.

a wide range of objectives and activities, including both historical views of business and perceptions that have emerged in the last decade. Let's take a closer look at the parts of this definition.

### Social Responsibility Applies to All Types of Businesses

It is important to recognize that all types of businesses—small and large, sole proprietorships and partnerships, and large corporations—implement social responsibility initiatives to further their relationships with their customers, their employees, and their community at large. Multinational corporations, such as HP or IKEA, can have far-reaching impacts on improving education, healthcare, energy and climate change, and sustainability. But even smaller firms, such as apparel brand Bombas or meat delivery firm Butcher Box, can lead with strong ethics and values to become major players in the market. Thus, the ideas advanced in this book are equally relevant and applicable across a wide variety of businesses and nonprofits.

Nonprofit organizations are expected to be socially responsible. Relationships with stakeholders—including employees, those that are served, and the community—affect their reputation. Nonprofits are not immune from ethical misconduct. For example, the state of Florida clawed back \$5 million from the Florida Coalition Against Domestic Violence after the CEO was accused of manipulating the nonprofit's board of directors to pad her salary, giving her more than \$7.5 million over three years.<sup>12</sup> This example demonstrates that nonprofit organizations must also develop strategic plans for social responsibility. In addition, government agencies are expected to uphold the common good and act in an ethical and responsible manner.

Although the social responsibility efforts of large corporations usually receive the most attention, the activities of small businesses may have a greater impact on local communities.<sup>13</sup> Owners of small businesses often serve as community leaders, provide goods and services for customers in smaller markets that larger corporations are not interested in serving, create jobs, and donate resources to local community causes. Medium-sized businesses and their employees have similar roles and functions on both a local and a regional level. Although larger firms produce a substantial portion of the gross national output of the United States, small businesses represent more than 47 percent of U.S. employees and generate more than 32 percent of U.S. exports.<sup>14</sup> In addition to these economic outcomes, small businesses present an entrepreneurial opportunity to many people, some of whom have been shut out of the traditional labor force. Historically underrepresented groups are increasingly interested in self-employment and other forms of small business activity. It is vital that all businesses consider the relationships and expectations that our definition of social responsibility suggests.

### Social Responsibility Needs a Strategic Focus

Social responsibility is an important business concept and involves significant planning and implementation. Our definition of social responsibility requires a formal commitment, or a way of communicating the company's social responsibility philosophy. For example, the 3M Company, a multinational conglomerate with more than 60,000 products in its portfolio, established values that create a strong culture both within and outside the company (shown in Table 1.1). These values guide the way the company fulfills its responsibilities to its customers, its shareholders, its employees, the community, and the natural environment. This demonstrates the company's strategic focus on social responsibility. Other companies that embrace social responsibility

**Table 1.1** 3M's Guiding Values

- **Diversity, Equity, and Inclusion:** We are going to keep building our diversity, which will make us a much more creative and innovative company.
- **Sustainability:** We are going beyond diversity to make 3M the most inclusive enterprise we can be, not just valuing the presence of diversity but further embedding equity and inclusion into the fabric of our company to bring more voices to the table.
- **3M Code of Conduct:** We have been a leader in the space for decades and are working to expand this leadership on all fronts through our products and our operations.

Source: The 3M Company, "2021 Sustainability Report," <https://multimedia.3m.com/mws/media/20060660/2021-sustainability-report.pdf> (accessed December 17, 2021).

**mission statement**

a summary of a company's aims and values

**vision statement**

a description of a company's current and future objectives to help align decisions with their philosophy and goals

have incorporated similar elements into their strategic communications, including mission and vision statements, annual reports, and websites. A **mission statement** is a summary of a company's aims and values. For example, American Express's mission is to become essential to its customers by providing differentiated products and services to help them achieve their aspirations. A **vision statement** is a description of a company's current and future objectives to help align decisions with their philosophy and goals. American Express's vision is to provide the world's best customer experience every day.<sup>15</sup>

In addition to a company's verbal and written commitment to social responsibility, our definition requires action and results. To implement its social responsibility philosophy, the 3M Company has developed and implemented several corporate-wide strategic initiatives, including local community engagement, volunteerism, environmental initiatives, stakeholder engagement, and a commitment to diversity and inclusion. For example, through 3M's sustainability efforts, the company has reduced its greenhouse gas emissions by more than 71 percent over the last 20 years.<sup>16</sup> As this example demonstrates, effective social responsibility requires both words and action.

If any such initiative is to have strategic importance, it must be fully valued and championed by high-level management. Leaders must believe in and support the integration of stakeholder interests and economic, legal, ethical, and philanthropic responsibilities into every corporate decision. For example, company objectives for brand awareness and loyalty can be developed and measured from both a marketing and a social responsibility standpoint because researchers have documented a relationship between consumers' perceptions of a firm's social responsibility and their intentions to purchase that firm's brands. There are various ways that companies align stakeholder interests and social responsibility into business decisions. For example, engineers can integrate consumers' desires for reduced negative environmental impact into product design, and marketers can ensure that a brand's advertising campaign incorporates this product benefit. Finally, consumers' desire for an environmentally sustainable product may stimulate a stronger company interest in assuming environmental leadership in all aspects of its operations. For example, in response to consumer demand for a more sustainable denim product, Levi's introduced its Water<Less denim finishing technique more than a decade ago. Since then, the company has saved more than 4.2 billion liters of water from the finishing process, and now more than 80 percent of the company's products are made with these environmentally-friendly techniques.<sup>17</sup> Although social responsibility depends on collaboration and coordination across many parts of the business and among its constituencies, it also produces effects throughout these same groups. We discuss some of these benefits later in this chapter.

Because of the need for coordination, a large company that is committed to social responsibility often creates specific positions or departments to spearhead the various components of its program. For example, Twilio, a cloud communications company, has a dedicated CSR department with more than 30 employees that focus on social impact, community issues, grants, environmental responsibility, and more.<sup>18</sup> A smaller firm may give an executive, perhaps in human resources or the business owner, the ability to make decisions regarding community involvement, ethical standards, philanthropy, and other areas. Regardless of the formal or informal nature of the structure, this department or executive should ensure that social responsibility initiatives are aligned with the company's **corporate culture**, integrated with companywide goals and plans, fully communicated within and outside the company, and measured to determine their effectiveness and strategic impact. In sum, social responsibility must be given the same planning time, priority, and management attention that are given to any other company initiative, such as continuous improvement, cost management, investor relations, research and development, human resources, or marketing research.

**corporate culture**

shared values, attitudes, and beliefs that characterize members of an organization

## Social Responsibility Fulfills Society's Expectations

Another element of our definition of social responsibility involves society's expectations of business conduct. Many people believe that businesses should accept and abide by four types of responsibility: financial, legal, ethical, and philanthropic (see Table 1.2). To varying degrees, the four types are required, expected, and/or desired by society.<sup>19</sup>

In Stage 1, businesses have a responsibility to be financially viable so that they can provide a return on investment for their owners, create and sustain jobs for the community, and contribute goods and services to the economy. The economy is influenced by the ways that organizations relate to their shareholders, their customers, their employees, their suppliers, their competitors, their community, and even the natural environment. For example, in nations with corrupt businesses and industries, the negative effects often pervade the entire society. Transparency International, a German organization dedicated to curbing national and international corruption, conducts an annual survey on the effects of business and government corruption on a country's economic growth and prospects. The organization reports that corruption reduces economic growth, inhibits foreign investment, and often channels investment and funds into "pet projects" that may create little benefit other than high returns to the corrupt decision-makers. There are a host of practical implications for the four levels of social responsibility, business, and its effects on society.

In Stage 2, companies are required to maintain compliance with legal and regulatory requirements specifying the nature of responsible business conduct. Society enforces its expectations regarding the behavior of businesses through the legal system. If a business chooses to behave in a way that customers, special-interest groups, or other businesses perceive as irresponsible, these groups may ask their elected representatives to draft legislation to regulate the business's behavior, or they may sue the firm in a court of law in an effort to force it to "play by the rules." If a company does not abide by the law, there will be negative consequences. For example, Lee Jae Yong, the former head of Samsung, a South Korean multinational electronics company, was sentenced to more than two years in prison for a bribery and embezzlement scandal that involved the concealment of about \$7.8 million.<sup>20</sup>

Beyond financial viability and legal compliance, companies must decide what they consider to be just, fair, and right—the realm of ethics, principles, and values—in Stage 3. **Business ethics** includes the principles, values, and norms that guide individual and group behavior in the world of business. **Principles** are specific and universal boundaries for behavior that should never be violated. Principles such as fairness and honesty are determined and expected by the public, government regulators, special-interest groups, consumers, industry, and

### business ethics

the principles, values, and norms that guide individual and group behavior in the world of business

### principles

specific and universal boundaries for behavior that should never be violated

**Table 1.2** Social Responsibility Requirements

Stages	Examples
<b>Stage 1:</b> Financial Viability	Starbucks offers investors a healthy return on investment, including paying dividends.
<b>Stage 2:</b> Compliance with Legal and Regulatory Requirements	Starbucks specifies in its code of conduct that payments made to foreign government officials must be lawful according to the laws of the United States and the foreign country.
<b>Stage 3:</b> Ethics, Principles, and Values	Starbucks offers healthcare benefits to part-time employees and supports coffee growers so they get a fair price.
<b>Stage 4:</b> Philanthropic Activities	Starbucks created the Starbucks Foundation to award grants to eligible nonprofits and to give back to their communities.



**values**

enduring beliefs and ideals that are socially enforced

**norms**

standards of behavioral expectations that guide, control, and regulate ethical conduct

**code of ethics**

a written collection of the rules, principles, values, and expectations of employee behavior

**philanthropic activities**

efforts made by a company to improve human welfare and goodwill

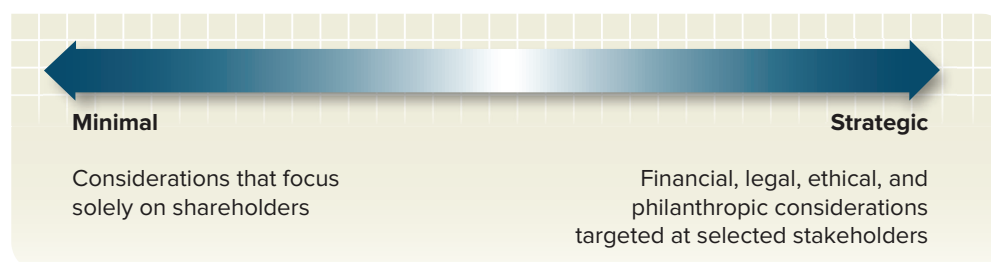
individual organizations. The most basic of these principles have been codified into laws and regulations to require that companies conduct themselves in ways that conform to society's expectations. Ethical issues exist in most managerial decisions. A firm needs to create an ethical culture with values and norms that meet the expectations of stakeholders. **Values** are enduring beliefs and ideals that are socially enforced. For example, AT&T, a U.S. telecommunications company, lives by these values: live true, think big, pursue excellence, inspire imagination, be there, stand for equality, embrace freedom, and make a difference.<sup>21</sup> **Norms** are standards of behavioral expectations. Norms guide, control, and regulate ethical conduct. Examples of ethical norms would be treating employees fairly and providing consumers with truthful information.

Many firms and industries have chosen to go beyond these basic laws in an effort to act responsibly. The Direct Selling Association (DSA), for example, has established a code of ethics that applies to all individual and company members of the association. A **code of ethics**, also called a code of conduct, is a written collection of the rules, principles, values, and expectations of employee behavior. Because direct selling involves personal contact with consumers, there are many ethical issues that can arise. For this reason, the DSA code directs the association's members to go beyond legal standards of conduct in areas such as product representation, appropriate ways of contacting consumers, and warranties and guarantees. In addition, the DSA actively works with government agencies and consumer groups to ensure that ethical standards are pervasive in the direct selling industry. Also, the DSA partners with the Better Business Bureau (BBB) National Programs to monitor the entire direct selling industry to discover misconduct and support ethical conduct. Violations of the DSA code of ethics and potential legal issues are addressed, and if the firm does not engage in corrective action, the issue can be forwarded to a regulatory agency. This form of self-regulation can be highly effective, protecting consumers and supporting fair competition.

In Stage 4 are **philanthropic activities**, which promote human welfare and goodwill. By making philanthropic donations of money, time, and other resources, companies can contribute to their communities and society and improve the quality of life. For example, the Home Depot Foundation has invested more than \$400 million over the last decade to veteran causes and has spent more than \$50 million training and certifying separating military personnel, high school students, and undeserved youths to become skilled tradespeople.<sup>22</sup>

When these dimensions of social responsibility were first introduced, many people assumed that there was a natural progression from financial viability to philanthropic activities, meaning that a firm had to be financially viable before it could properly consider the other three elements. Today, social responsibility is viewed in a more holistic fashion, with all four dimensions seen as related and integrated, and this is the view that we will use in this book.<sup>23</sup> In fact, companies demonstrate varying degrees of social responsibility at different points in time. Figure 1.2 depicts the social responsibility continuum. Companies' fulfillment of

**Figure 1.2** Social Responsibility Continuum



their responsibilities can range from a minimal to a strategic focus that results in a **stakeholder orientation**. Firms that focus only on shareholders and the bottom line operate from a legal or compliance perspective.<sup>24</sup> The opioid epidemic started, in part, because of the pharmaceutical industry's profit-driven focus. While the opioid epidemic sparked national debate, it was uncovered that the pharmaceutical industry incentivized doctors to prescribe opioids and downplayed the long-term patient risks to the public. The pharmaceutical industry's profit-maximization strategy, which resulted in high investor returns, led to unintended consumer deaths.<sup>25</sup>

**Resource-advantage theory** stresses that a firm's resources provide competitive advantage. Promoting social trust and social responsibility develops the foundation for economic growth in a firm as well as a society. Customers are often motivated to enhance organizations that exhibit socially responsible behavior. Klean Kanteen, for example, has a positive reputation for being socially responsible. The employee-owned stainless steel water bottle company focuses on the areas of plastic pollution, consumer safety, land and water conservation, and environmental stewardship.<sup>26</sup> Thus, a company's socially responsible behavior can become a resource advantage.

Strategic social responsibility is realized when a company has integrated a range of expectations, desires, and constituencies into its strategic direction and planning processes. In this case, an organization considers social responsibility an essential component of its vision, mission, values, and practices. Seventh Generation, a popular mission-driven cleaning products company, wants to "transform the world into a healthy, sustainable, and equitable place for the next seven generations." Social responsibility is woven into the fabric of the company which uses recycled materials, embraces ingredient transparency, and engages in advocacy.<sup>27</sup> Executives with this philosophy often maintain that customers will be lost, employees will become dissatisfied, and other detrimental effects will occur if a firm abandons its strategic responsibilities.

In this book, we will give many examples of firms that are at different places along this continuum to show how the pursuit of social responsibility is never ending.

## Social Responsibility Requires a Stakeholder Orientation

The final element of our definition involves those to whom an organization is responsible, including customers, employees, investors and shareholders, suppliers, governments, communities, and many others. These constituents have a stake in, or a claim on, some aspect of a company's products, industry, markets, and outcomes and are thus known as **stakeholders**. We explore the roles and expectations of stakeholders in Chapter 2. Companies that consider the diverse perspectives of these constituents in their daily operations and strategic planning are said to have a stakeholder orientation, meaning that they are focused on stakeholders' concerns. Adopting this orientation is part of the social responsibility philosophy, which implies that business is fundamentally connected to other parts of society and must take responsibility for its effects in those areas.

R. E. Freeman, a developer of stakeholder theory, maintains that business and society are "interpenetrating systems," in that each affects and is affected by the other.<sup>28</sup> For the common good to be achieved, cross-institutional and cross-organizational interactions must move society toward shared partnerships. Research suggests interorganizational networks can be an important element of a successful corporate strategy that creates shared value. By definition, **interorganizational networks** are a set of organizations that are associated through shared or mutual affiliations and interests. For example, interorganizational networks include strategic business alliances, supply chains, human and

### stakeholder orientation

the aim to benefit all parties affected by the success or failure of an organization

### resource-advantage theory

a theory stating that the value of a resource is viewed relative to its potential to create competitive differentiation or customer value

### stakeholders

constituents who have an interest or stake in a company's products, industry, markets, and outcomes

### interorganizational networks

a set of organizations that are associated through shared or mutual affiliations and interests

health services consortia, public-private partnerships, and others. Identifying businesses that are committed to similar environmental and societal issues and that promote a shared operating environment can help create not only financial success, but also socially responsible actions.<sup>29</sup> Overall, companies may affect their communities and beyond through partnering with other organizations with similar value systems.<sup>30</sup>

## Development of Social Responsibility

In 1959, Harvard economist Edward Mason asserted that business corporations are “the most important economic institutions.”<sup>31</sup> His declaration implied that companies probably affect the community and society in social terms as much as (or perhaps more than) in monetary, or financial, terms. Employment and the benefits associated with a living wage are necessary to develop a sustainable economy. The opportunity for individuals and businesses to attain economic success is necessary to create a society that can address social issues. Today, some question our economic system, but without economic resources, little progress can be made in developing society. Social responsibility has always been a part of our economic system. The history of American capitalism relates to the economic, technological, political, and social development of the country. In the early and mid-nineteenth century, most people lived in rural communities and were largely reliant on trade surpluses and commodity exchanges for substance. In 1850s, for instance, approximately 20 million of the 23 million Americans in the population lived in rural areas where few businesses had more than 300 employees. As industrialization advanced, rail systems and new technology provided an opportunity for manufacturing and retail institutions to develop. Finally, by the twentieth century, businesses were developed and their impact on society was much greater.

Although some firms have more of a social impact than others, companies influence many aspects of our lives, from the workplace to the natural environment. This influence has led many people to conclude that companies’ actions should be designed to benefit employees, customers, business partners, and the community as well as shareholders. Social responsibility has become a benchmark for companies today.<sup>32</sup> However, these expectations have changed over time. For example, the first corporations in the United States were granted charters by various state governments because they were needed to serve an important function in society, such as transportation, insurance, water, or banking services. In addition to serving as a license to operate, these charters specified the internal structure of these firms, allowing their actions to be more closely monitored.<sup>33</sup> During this period, corporate charters were often granted for a limited period of time because many people, including legislators, feared the power that corporations could potentially wield. It was not until the mid-1800s and early 1900s that profit and responsibility to stockholders became major corporate goals.<sup>34</sup>

## Historical Review of Social Responsibility

After World War II, as many large U.S. firms came to dominate the global economy, their actions inspired imitation in other nations. The definitive external characteristic of these firms was their economic dominance. Internally, they were marked by the virtually unlimited autonomy afforded to their top managers. This total discretion meant that these firms’ top managers had the luxury of not having to answer for some of their actions.<sup>35</sup> In the current business mindset, such total autonomy would be viewed as a hindrance to social responsibility because there is no effective system of checks and balances. In a later chapter, we elaborate on

*corporate governance*, the process of control and accountability in organizations that is necessary for social responsibility.

In the 1950s, the 130 or so largest companies in the United States provided more than half of the country's manufacturing output. The top 500 firms accounted for almost two-thirds of the country's nonagricultural economic activity.<sup>36</sup> U.S. productivity and technological advancements dramatically outpaced those of global competitors, such as Japan and Western Europe. For example, the level of production in the United States was twice as high as that in Europe and quadruple that in Japan. The level of research and development carried out by U.S. corporations was also well ahead of overseas firms. For these reasons, the United States was perceived as setting a global standard for other nations to emulate.

During the 1950s and 1960s, these companies provided benefits that are often overlooked. Their contributions to charities, the arts, culture, and other community activities were beneficial to the industry or to society rather than simply to the companies' own profitability. For example, the lack of competition meant that companies had the profits to invest in higher-quality products for consumer and industrial use. Although the government passed laws that required companies to take actions to protect the natural environment, make products safer, and promote equity and diversity in the workplace, many companies voluntarily adopted responsible practices rather than constantly fighting government regulations and taxes. These corporations once provided many of the services that are now provided by the government in the United States. For example, during this period, the U.S. government spent less than the government of any other industrialized nation on such things as pensions and health benefits, as these were provided by companies rather than by the government.<sup>37</sup> In the 1960s and 1970s, however, the business landscape changed.

Economic turmoil during the 1970s and 1980s changed the role of corporations. Venerable firms that had dominated the economy in the 1950s and 1960s became less important as a result of bankruptcies, takeovers, mergers, or other threats, including high energy prices and an influx of foreign competitors. The stability experienced by the U.S. firms of midcentury dissolved. During the 1960s and 1970s, the Fortune 500 had a relatively low turnover of about 4 percent. By 1990, however, one-third of the companies in the Fortune 500 of 1980 had disappeared, primarily as a result of takeovers and bankruptcies. The threats and instability led companies to protect themselves from business cycles by becoming more focused on their **core competencies** and reducing their product diversity. To combat takeovers, many companies adopted flatter organizational hierarchies. Flatter organizations meant workforce reduction but also entailed increasing empowerment of lower-level employees.

Thus, the 1980s and 1990s brought a new focus on profitability and economies of scale. Efficiency and productivity became the primary objectives of business. This fostered a wave of downsizing and restructuring that left some people and communities without financial security. Before 1970, large corporations employed about one of every five Americans, but by the 1990s, they employed only one in ten. The familial relationship between employee and employer disappeared, and along with it went employee loyalty and company promises of lifetime employment. Companies slashed their payrolls to reduce costs, and employees changed jobs more often. Workforce reductions and "job hopping" were almost unheard of in the 1960s but had become commonplace two decades later. These trends made temporary employment and contract work the fastest-growing forms of employment throughout the 1990s.<sup>38</sup>

Along with these changes, high-level managers were largely stripped of their former freedom. Competition intensified, and both consumers and stockholders grew more demanding. The increased competition led business managers to worry more and more about the bottom line and about protecting the company.

**core competencies**

unique advantages that differentiate a firm from its competitors

Escalating use of the internet provided unprecedented access to information about corporate decisions and conduct and fostered communication among once unconnected groups, furthering consumer awareness and shareholder activism. Consumer demands put more pressure on companies and their employees. The education and activism of stockholders had high-level management fearing for their jobs. Throughout the last two decades of the twentieth century, legislators and regulators initiated more and more regulatory requirements every year. These factors resulted in difficult trade-offs for management.

Corporate responsibilities were renewed in the 1990s. Partly as a result of business scandals and Wall Street excesses in the 1980s, many industries and companies decided to pursue and expect more responsible and respectable business practices. Many of these practices focused on creating value for stakeholders through more effective processes and decreased the narrow and sole emphasis on corporate profitability. At the same time, consumers and employees became less interested in making money for its own sake and turned toward intrinsic rewards and a more holistic approach to life and work.<sup>39</sup> This resulted in increased interest in the development of human and intellectual capital; the installation of corporate ethics programs; the development of programs to promote employee volunteerism in the community; strategic philanthropy efforts and trust in the workplace; and the initiation of a more open dialogue between companies and their stakeholders.

Despite major advances in the 1990s, the sheer number of corporate scandals at the beginning of the twenty-first century prompted a new era of social responsibility. The downfall of Enron, WorldCom, and other corporate stalwarts in the beginning of the 2000s caused regulators, former employees, investors, nongovernmental organizations (NGOs), and ordinary citizens to question the role and integrity of big business and the underlying economic system. Federal legislators passed the Sarbanes-Oxley Act to overhaul securities laws and governance structures. A new Public Company Accounting Oversight Board was implemented to regulate the accounting and auditing profession after Enron and WorldCom failed due to accounting scandals. Newspapers, business magazines, and news websites devoted entire sections to the trials and tribulations of executives, their companies and auditors, and stock analysts.

In 2007 and 2008, a housing boom in the United States collapsed, setting off a financial crisis that would later become known as the Great Recession. Homeowners could not afford to pay their mortgages. Because of the housing boom, in many cases the mortgages were higher than the houses were worth. People all across the United States began to walk away from their mortgages, leaving banks and other lenders with hundreds of thousands of houses that had decreased in value. Meanwhile, companies such as AIG were using complex financial instruments known as “derivatives” to transfer the risks of securities such as mortgages, almost as a type of insurance policy. Financial firms did not have enough of a safety net to cover so many defaults. The housing collapse created a chain reaction that led to the worst recession since the Great Depression. The government was forced to step in to bail out financial firms in order to keep the economy going and prevent the economy from collapsing further. Many established organizations went bankrupt or were acquired by other firms at a fraction of what they were originally worth. Table 1.3 describes some of the corporations and banks that collapsed in the financial crisis.

In 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act, the most sweeping legislation since Sarbanes-Oxley. Dodd-Frank is intended to protect the economy from similar financial crises in the future by creating more transparency in the financial industry. This complex law required legislators to develop hundreds of laws to increase transparency and create financial stability. The Dodd-Frank Act will be discussed in more detail in Chapter 4. The financial crisis and the collapse of many well-known institutions led to a renewed interest in business ethics and social responsibility.

**Table 1.3** Corporations and Banks Involved in the Financial Crisis

Organization	Outcome
General Motors (GM)	Declared bankruptcy and required a government bailout of \$49.5 billion to reorganize. The government sold their last shares in GM in 2013 and is estimated to have lost more than \$10 billion on its investment.
AIG	Received a government bailout of \$182 billion and was criticized for using bailout money to pay executives large bonuses. AIG repaid the last of its loans in 2013.
Bank of America	Received \$42 billion in bailout money as part of the Troubled Asset Relief Program (TARP). It paid back its loans in 2009.
Washington Mutual	Its banking subsidiaries were sold by the Federal Deposit Insurance Corporation to J. P. Morgan for \$19 billion.
Chrysler	Declared bankruptcy and required a government bailout of \$12.5 billion. By 2011, Chrysler had repaid most of the debt, and Fiat agreed to purchase the rest of the U.S. Treasury's shares in Chrysler for \$500 million.
Countrywide Financial	Acquired by Bank of America for \$4.1 billion. Bank of America inherited many of the lawsuits against Countrywide claiming it had engaged in fraudulent and discriminatory lending practices.

### Recent Developments in Social Responsibility

After the Great Recession, the economy stabilized, and the stock market recovered. Even though many banks failed during the financial crisis, today banks and other financial institutions are much larger than before. Rather than getting rid of too-big-to-fail financial institutions, they seemed to grow much larger, despite legislation. The good news is banks have proven to be much healthier and safer after the financial crisis. During the COVID-19 pandemic in 2020, which sent the economy into a brief recession and caused unemployment to soar to the highest levels since the Great Recession, banks helped keep businesses and consumers afloat through lending. As the economy recovered, banks continued to pass the Federal Reserve's stress tests, which were put into place after the financial crisis.<sup>40</sup>

Social responsibility was brought to the forefront during the COVID-19 pandemic as millions of people lost their jobs, supply chains were disrupted, and essential workers feared for their health and safety. Supply chain disruption during the pandemic was a threat to companies achieving their goals, and it severely damaged stakeholder relationships. Disruptions in the economy and supply chains, including supply shortages, resulted in inflation reaching a 30-year high, with price increases that will have a long-term impact on many consumers. This marked one of the first times the complexity of the global supply chain became apparent for many consumers. Studies suggest that sustainable procurement practices can help companies improve their supply chain resilience and reduce risk.<sup>41</sup>

When the pandemic first struck, companies such as Amazon, Apple, Google, Facebook, Microsoft, and Twitter voluntarily continued to pay contingent workers that could not work due to the outbreak.<sup>42</sup> Many companies implemented health and safety practices, donated personal protective equipment, increased corporate giving, and offered financial assistance to support employees. On the flip side, many companies were slow to respond or did not respond adequately. Companies were put under the microscope as the public looked to see how they treated stakeholders. In the face of ethical conflict, some business owners prioritized profit

### environmental, social, and governance (ESG)

A framework for evaluation of firm performance in the areas of environmental, social, and governance

over public health. The pandemic shined a light on the importance of adopting a stakeholder orientation and addressing environmental, social, and governance issues.

**Environmental, social, and governance (ESG)** Stakeholders are increasingly demanding that firms protect the environment, contribute to social causes, and engage in conduct that is responsible and ethical. This trend is causing firms to improve their ethical principles and play a more active role in society. ESG is a framework for evaluation of firm performance in the areas of environmental, social, and governance.<sup>43</sup> The ESG framework allows firms to evaluate their priorities in these three areas relative to their industry, investor priorities, peer comparisons, and the cultural and leadership priorities of the organization.

- *Environmental* refers to actions related to climate change, energy use, waste, pollution, recycling, and more.
- *Social* refers to policies and programs related to employees (human capital), equal pay, LGBTQ+ policies, and product liability, among other issues.
- *Governance* refers to corporate governance issues such as regulatory compliance, transparent accounting methods, ethical leadership, executive compensation, oversight, and accountability.<sup>44</sup>

ESG, which began as a corporate social responsibility initiative, has become mainstream. It has been widely adopted in the financial industry, leading to the rise of ESG investing and ESG bonds. ESG assets under management will exceed \$50 trillion globally within the next few years, according to *Bloomberg*.<sup>45</sup> Financial services companies such as Morningstar have developed ESG scoring tools to help guide investors. Figure 1.3 provides an example of how ESG ratings can come together. Additionally, investors can turn to mutual funds and exchange-traded funds (ETFs) created by financial services companies that bundle companies that rank highly on ESG factors. Microsoft, Accenture, Texas Instruments, and Salesforce are examples of companies with high ESG rankings. In fact, Accenture and Salesforce partnered,

**Figure 1.3** ESG Framework Example



Source: Adapted from FTSE Russel, "ESG Ratings," <https://www.ftserussell.com/data/sustainability-and-esg-data/esg-ratings> (accessed December 21, 2021).

## Ethical Responsibilities in INVESTING



### Investors Open Their Wallets to ESG

Environmentalism, social responsibility, and corporate governance are top of mind for both businesses and consumers, so much so that investors use environmental, social, and governance (ESG) factors when evaluating a company's performance. Investors consider a firm's performance in these categories relative to its industry and its peers alongside the cultural and leadership priorities of the organization. This is known as ESG investing, sometimes called socially responsible investing or sustainability investing.

Environmental factors include actions related to climate change, greenhouse gas emissions, the use of natural resources, recycling, waste, pollution, and more. For example, clothing companies that use renewable materials and sustainable manufacturing processes would rank highly on this factor. Social considerations include equal pay, LGBTQ+ policies, and product liability. Many people look for companies whose values align with their own. Governance refers to corporate governance issues such as leadership, executive compensation, oversight, and accountability.

Financial services companies, such as Robinhood, Fidelity, and Vanguard, create ESG funds, including mutual funds, index funds, and exchange-traded funds (ETFs) that allow investors to support a portfolio of socially responsible companies in a low-risk way. Since funds are created by financial experts and consist of many companies, they are less risky than buying individual stocks. Investors who

use an ESG investing strategy put their money behind companies that have a positive impact on the environment and society and lead with strong corporate governance.

Along the same lines, ESG bonds have become popular debt instruments in corporate financing as companies improve their reputation for sustainability, social responsibility, and corporate governance. For example, Apple has borrowed around \$4.7 billion in green bonds for various improvement projects, including the installation of solar panels on its plants. With green bonds, an audit report trail allows investors to make sure funds are used for their intended purpose.

Investing based on ESG factors has become incredibly popular and shows no signs of slowing down; however, several hurdles must be overcome. First, factors can be difficult to measure and quantify. Second, because of this, it is unclear if ESG ratings developed by financial services firms are truly correlated with a firm's performance on these factors. The U.S. Securities and Exchange Commission is considering requiring fund managers to disclose the criteria and data they use to apply certain labels to their investment options. Finally, many investors are still skeptical of ESG investing due to greenwashing by firms that attempt to appear more environmentally friendly than they really are. Regardless of these issues, the future for ESG investing looks green. According to *Barron's*, global investing into ESG and sustainability funds could quadruple by 2030.

Sources: Karrie Gordon, "Get Ready for ESG Investing to Quadruple by End of Decade," *ETF Trends*, December 6, 2021, <https://www.ettrends.com/esg-channel/get-ready-for-esg-investing-to-quadruple-by-end-of-decade/> (accessed December 9, 2021); Lewis Braham, "An ESG Fund Changes the World, One Company at a Time," *Barron's*, December 8, 2021, <https://www.barrons.com/articles/esg-balanced-fund-stocks-green-bonds-51638914065> (accessed December 9, 2021); "Where Will ESG Investing Be in Five Years?" *The Wall Street Journal*, November 18, 2021, <https://www.wsj.com/articles/esg-investing-in-five-years-11637161312> (accessed December 9, 2021).

bringing together their respective technologies to help companies bring sustainability to the front of their business. The alliance allows companies to use historical and real-time ESG data to track, measure, and act on sustainability initiatives.<sup>46</sup>

## Global Nature of Social Responsibility

Although many forces have shaped the debate on social responsibility, the increasing globalization of business has made it an international concern. A common theme is criticism of the increasing power and scope of business and income differences among executives and employees. Questions of corruption, environmental protection, fair wages, safe working conditions, and the income gap between rich and poor are posed. Many critics and protesters believe that global business involves



exploitation of the working poor, destruction of the planet, and a rise in inequality.<sup>47</sup> The global pandemic put trust to the test. Business emerged ahead of NGOs, the government, and the media as the only trusted institution, according to the Edelman Trust Barometer.<sup>48</sup> In an environment where consumers distrust business, greater regulation and lower brand loyalty are the likely results. We discuss more of the relationship between social responsibility and business outcomes later in this chapter.

The globalization of business has critics who believe that the movement is detrimental because it destroys the unique cultural elements of individual countries, concentrates power within developed nations and their corporations, abuses natural resources, and takes advantage of people in developing countries. Multinational corporations are perhaps most subject to criticism because of their size and scope. Table 1.4 shows the world's largest companies, which are more powerful than many of the countries in which they do business. Because of the economic and political power that they potentially wield, the actions of large, multinational companies are under scrutiny by many stakeholders. Most allegations by antiglobalization protestors are not extreme, but the issues are still consequential. For example, the pharmaceutical industry has long been criticized for excessively high pricing, interference with clinical evaluations, some disregard for developing nations, and aggressive promotional practices. Critics have called on governments, as well as public health organizations, to influence the industry toward changing some of its practices.<sup>49</sup>

Advocates of the global economy counter these allegations by pointing to increases in overall economic growth, new jobs, new and more effective products, and other positive effects of global business. Although these differences of opinion provide fuel for debate and discussion, the global economy probably “holds much greater potential than its critics think, and much more disruption than its advocates admit. By definition, a global economy is as big as it can get. This means that the scale of both the opportunity and the consequences are at an apex.”<sup>50</sup> In responding to this powerful situation, companies around the world are increasingly implementing programs and practices that strive to achieve a balance between economic responsibilities and other social responsibilities. Nestlé, a global foods manufacturer and marketer, published the Nestlé Corporate Business Principles in 1998 and has continually revised them. These principles serve as a management tool for decision-making at Nestlé and have been translated into over 50 languages. The updated principles are consistent with the Global Compact, an accord by the United Nations that covers environmental standards, human rights, and labor conditions.<sup>51</sup> We explore the global context of social responsibility more fully throughout this book.

**Table 1.4** World's 10 Largest Companies

Rank	Company Name	Headquarters	Revenue (\$M)
1	Walmart	United States	\$523,964
2	State Grid	China	\$383,906
3	Amazon	United States	\$280,522
4	China National Petroleum	China	\$ 379,130
5	Sinopec Group	China	\$ 407,009
6	Apple	United States	\$ 260,174
7	CVS Health	United States	\$ 256,776
8	UnitedHealth Group	United States	\$ 242,155
9	Toyota Motor	Japan	\$275,288
10	Volkswagen	Germany	\$282,760

Source: “Global 500,” *Fortune*, 2021, <https://fortune.com/global500/> (accessed December 21, 2021).

In most developed countries, social responsibility involves stakeholder accountability and the financial, legal, ethical, and philanthropic dimensions discussed earlier in the chapter. However, a key question for implementing social responsibility on a global scale is: Who decides on these responsibilities? Many executives and managers face the challenge of doing business in diverse countries while attempting to maintain their employers' corporate culture and satisfy their expectations. Some companies have adopted an approach in which broad corporate standards can be adapted at a local level. For example, a corporate goal of demonstrating environmental leadership could be met in a number of different ways, depending on local conditions and needs. Sappi, a global pulp and paper company, sets the tone at the top by creating both global and regional goals that work toward the same objectives. The company releases regional sustainability reports to make data accessible and comparable.<sup>52</sup>

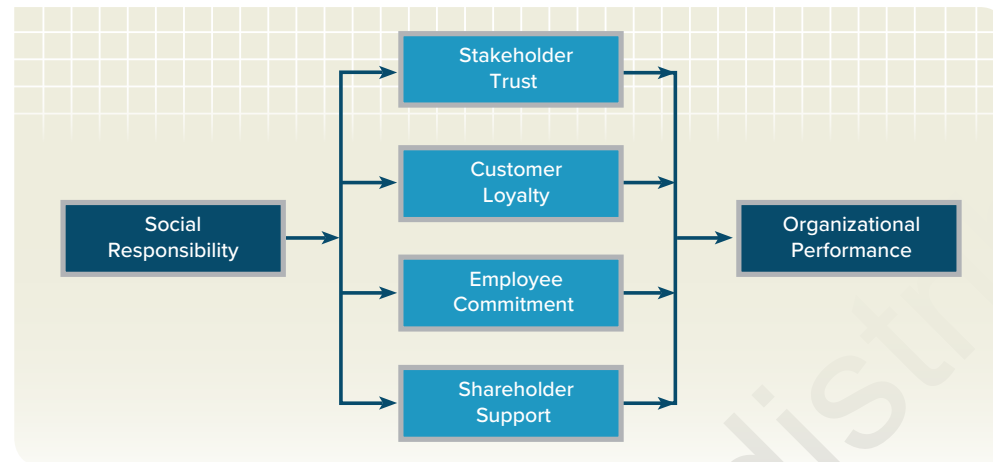
Global social responsibility also involves the confluence of government, business, trade associations, and other groups. For example, countries that belong to the Asia-Pacific Economic Cooperation (APEC) are responsible for half the world's annual production and trade volume. As APEC works to reduce trade barriers and tariffs, it has also developed meaningful projects in the areas of sustainable development, clean technologies, workplace safety, management of human resources, and the health of the marine environment. This powerful trade group has demonstrated that financial, social, and ethical concerns can be tackled simultaneously.<sup>53</sup> Like APEC, other trade groups are also exploring ways to enhance economic productivity within the context of legal, ethical, and philanthropic responsibilities.

Another trend involves business leaders becoming so-called cosmopolitan citizens by simultaneously harnessing their leadership skills, worldwide business connections, access to funds, and beliefs about human and social rights. Ben Cohen and Jerry Greenfield, the duo behind Ben & Jerry's, can often be found protesting political and social issues on Capital Hill. Dan Schulman of PayPal has stood up for transgender rights. Red Ventures CEO Ric Elias joined a pledge to give away the majority of his wealth to philanthropy.<sup>54</sup> These business leaders are acting as agents to ensure that the economic promises of globalization are met with true concern for social and environmental considerations. In many cases, such efforts supplant those historically associated with government responsibility and programs.<sup>55</sup>

In sum, progressive global businesses and executives recognize the shared bottom line that results from the partnership among businesses, communities, government, customers, and the natural environment. According to a PwC survey, 91 percent of business leaders agree that their company has a responsibility to act on ESG issues. Top issues include data security and privacy, climate change, and product safety.<sup>56</sup> Thus, our concept of social responsibility is applicable to businesses around the world, although adaptations of implementation and other details on the local level are definitely required. In companies around the world, there is also the recognition of a relationship between strategic social responsibility and benefits to society and organizational performance.

## Benefits of Social Responsibility

The importance of social responsibility initiatives in enhancing stakeholder relationships, improving performance, and creating other benefits has been debated from many perspectives.<sup>57</sup> Many business managers view such programs as costly activities that provide rewards only to society, at the expense of their company's bottom line. Another view holds that some costs of social responsibility can be recovered through improved performance. If social responsibility is strategic

**Figure 1.4** The Role of Social Responsibility in Performance

and aligned with a firm's mission and values, then improved performance can be achieved. It is hard to measure the reputation of a firm, but it is important to build trust and achieve success. Moreover, ample research evidence demonstrates that companies which implement strategic social responsibility programs are more profitable.

Some of the specific benefits include increased efficiency in daily operations, greater employee commitment, higher product quality, improved decision-making, and increased customer loyalty, as well as improved financial performance. In short, companies that establish a reputation for trust, fairness, and integrity develop a valuable resource advantage that fosters success, which then translates to greater financial performance (see Figure 1.4). This section provides evidence that resources invested in social responsibility programs reap positive outcomes for both organizations and their stakeholders.

### Trust

Trust is the glue that holds organizations together and allows them to focus on efficiency, productivity, and profits. According to Stephen R. Covey, author of *The 7 Habits of Highly Effective People*, "Trust lies at the very core of effective human interactions. Compelling trust is the highest form of human motivation. It brings out the very best in people, but it takes time and patience, and it doesn't preclude the necessity to train and develop people so their competency can rise to that level of trust." When trust is low, organizations decay and relationships deteriorate, resulting in infighting, playing politics within the organization, and general inefficiency. Employee commitment to the organization declines, product quality suffers, employee turnover skyrockets, and customers turn to more trustworthy competitors.<sup>58</sup> Any stakeholder that loses trust can create a missing link necessary for success.

In a trusting work environment, however, employees can reasonably expect to be treated with respect and consideration by both their peers and their superiors. They are also more willing to rely and act on the decisions and actions of their coworkers. Thus, trusting relationships between managers and their subordinates and among peers contribute to greater decision-making efficiency. Research by the Ethics & Compliance Initiative indicates that this trust is pivotal for supporting an ethical climate. Employees of an organization with a strong ethical culture are less likely to feel pressure to compromise ethics standards and more likely to report misconduct observed than employees in firms with a weak ethical culture.<sup>59</sup> Table 1.5 shows five indicators of trust, support, and transparency that have a

**Table 1.5** Indicators of Support, Trust, and Transparency

Employees believe that high-level management is open and honest.
Employees feel that they can openly disagree with their supervisor or raise issues of concern without fear of retaliation.
Managers talk about values frequently and make them a regular and public part of business decision-making.
Supervisors care about their employees as people.
Top managers do the right thing, even if it means that the company loses money, business, and/or clients.

Source: Ethics & Compliance Initiative, "Global Business Ethics Survey: Building Companies Where Values and Ethical Conduct Matter," <https://www.ethics.org/2018-q3-building-companies-where-values-ethical-conduct-matter/> (accessed December 21, 2021).

strong impact on whether employees will report ethical issues. As the table demonstrates, a key factor that inspires trust and transparency in organizations involves support and consistent communication from senior leadership and supervisors.

Trust is also essential for a company to maintain positive long-term relationships with customers. Volkswagen, Wells Fargo, and Boeing are just a few examples of companies that have been involved in corporate scandals. According to *The Economist*, a company loses 30 percent of its value when it loses trust. It is possible to regain trust, but it takes commitment, time, and resources to recover.<sup>60</sup> Communities and regulators that lose trust in a company can damage the firm's reputation and relationships with additional stakeholders, including shareholders, investors, and others.

### Customer Loyalty

The prevailing business philosophy about customer relationships is that a company should strive to market products that satisfy customers' needs through a coordinated effort that also allows the company to achieve its own objectives. It is well accepted that customer satisfaction is one of the most important factors for business success. Although companies must continue to develop and adapt products to keep pace with consumers' changing desires, it is also crucial to develop long-term relationships with customers. Relationships built on mutual respect and cooperation facilitate the repeat purchases that are essential for success. By focusing on customer satisfaction, a business can continually strengthen its customers' trust in the company, and as their confidence grows, this in turn increases the firm's understanding of their requirements.

Many consumers are willing to switch to brands associated with a good cause if price and quality are equal. Consumers take for granted that they can buy high-quality products at low prices; therefore, companies need to stand out as doing something—something that demonstrates their commitment to society.<sup>61</sup> According to an *Adweek* survey, more than half of consumers would boycott a brand that did not share their social beliefs.<sup>62</sup> Another way of looking at these results is that irresponsible behavior could trigger disloyalty and refusals to buy, whereas good social responsibility initiatives could draw customers to a company's products. For example, many firms use cause-related marketing programs to donate part of a product's sales revenue to a charity that is meaningful to the product's target market.

### Employee Commitment

Employee commitment stems from employees who are empowered with training and autonomy. Adobe, an American software company, is known for its

people-centric approach. The company fosters a diverse and inclusive work environment where employees feel appreciated and excited about their work. The company considers its people (human capital) to be its greatest asset.<sup>63</sup> Evidence suggests that CSR initiatives are a good way to retain and attract employees.<sup>64</sup>

When companies fail to provide value for their employees, loyalty and commitment suffer. The COVID-19 pandemic fueled an exodus from the workforce with millions quitting their jobs. Employee loyalty declined as workers sought flexible schedules, better benefits, and career advancement.<sup>65</sup> Employees spend many of their waking hours at work; thus, an organization's commitment to goodwill and respect of its employees usually results in increased employee loyalty and support of the company's objectives. Academic research on employee commitment has highlighted the importance of communicating and implementing CSR from a values perspective, not a compliance mandate. Employee commitment is also enhanced when social responsibility principles are integrated into business processes and practices and not just viewed as window dressing or a simple add-on to corporate strategy.<sup>66</sup>

### Shareholder Support

Investors look at a corporation's bottom line for profits or the potential for increased stock prices. To be successful, relationships with stockholders and other investors must rest on dependability, trust, and commitment. But investors also look for potential cracks or flaws in a company's performance. Shareholders can even sue a company, its officers, or its directors for mismanagement, defrauding investors, or violating a fiduciary duty. A shareholder lawsuit against Pinterest alleged the company's high-level managers enabled a culture of discrimination. Pinterest settled the lawsuit and committed \$50 million to diversity, equity, and inclusion efforts.<sup>67</sup>

Many shareholders are also concerned about the reputation of companies in which they invest. Investors have even been known to avoid buying the stock of firms they view as irresponsible. For example, Nikola, an electric truck company, saw stock prices plummet when investors fled amid a securities fraud investigation. The case, which was settled with the Securities and Exchange Commission, alleged the founder defrauded investors by making false claims about its products. When executives behave irresponsibly, the firm pays the price.<sup>68</sup> Many socially responsible mutual funds and asset management firms are available to help concerned investors purchase stock in responsible companies. These investors recognize that corporate responsibility is the foundation for efficiency, productivity, and profits. In contrast, investors know that fines or negative publicity can decrease a company's stock price, customer loyalty, and long-term viability. Consequently, many chief executives spend a great deal of time communicating with investors about their firms' reputations and financial performance and trying to attract them to their stock.

The issue of drawing and retaining investors is critical for CEOs as the average time an investor holds shares is only 5.5 months, according to data from the New York Stock Exchange.<sup>69</sup> This focus on short-term gains subjects corporate managers to tremendous pressure to boost short-term earnings, often at the expense of long-term strategic plans, including those needed to fulfill strategic social responsibility goals. The resulting pressure for short-term gains deprives corporations of stable capital and forces decision-makers into a "quarterly" mentality.

Conversely, those shareholders willing to hold onto their investments for lengthy periods are more willing to sacrifice short-term gains for long-term income. Attracting these long-term investors shields companies from the volatility of the stock market and gives them flexibility and stability in long-term strategic planning. In the aftermath of the Enron scandal and other significant scandals, as

**Table 1.6** Top Corporate Scandals

Company Name	Year	Description
Enron	2001	Fraudulent financial reporting
Lehman Brothers	2008	Subprime mortgage crisis
BP	2010	<i>Deepwater Horizon</i> oil spill
Facebook	2013–2016	Privacy breach and dubious targeted ad campaigns
Valeant Pharmaceuticals	2015	Drug price inflation
Volkswagen	2015	Emissions scandal
Wells Fargo	2016	Aggressive sales goals and account fraud
Uber	2017	Culture crisis
Apple	2017	Batterygate
Kobe Steel	2017	Falsified data on product quality
Equifax	2017	Security breach
Wirecard	2020	Fraudulent accounting
Luckin Coffee	2020	Fraudulent accounting

Source: Will Hall-Smith, "Top 10 Biggest Corporate Scandals and How They Affected Share Prices," *IG*, <https://www.ig.com/no/tradingstrategies/top-10-biggest-corporate-scandals-and-how-they-affected-share-pr-181031> (accessed July 31, 2019).

listed in Table 1.6, public trust and confidence in financial audits and published financial statements were severely shaken. Gaining and retaining investors' trust and confidence are vital for sustaining a firm's financial stability, as well as the stability of entire market economies.

### The Bottom Line: Profits

Social responsibility is positively associated with return on investment, return on assets, and sales growth.<sup>70</sup> A company cannot be socially responsible and nurture and develop an ethical organizational culture continuously unless it has achieved financial performance in terms of profits. Businesses with greater resources—regardless of their staff size—have the ability to promote their social responsibility along with serving their customers, valuing their employees, and establishing trust with the public. More than 90 percent of the 250 largest U.S. companies publish an annual CSR report and spend billions on environmental and social causes every year. These annual reports are important internal- and external-facing documents that detail a company's social responsibility initiatives and their impact.<sup>71</sup> As mentioned before, the stock returns of the world's most ethical companies are often higher than that of companies listed on the S&P 500. Many studies have identified a positive relationship between social responsibility and financial performance.<sup>72</sup> Investors buying shares in a company can evaluate their ESG score. Research has found that a high ESG rating is positively related to profitability and valuation and negatively related to volatility. Firms with a high ESG rating are likely to outperform other firms.<sup>73</sup>

In summary, a company with strong efforts and results in social responsibility is generally not penalized by market forces, including the intention of consumers to purchase the firm's products. Social responsibility efforts and performance serve as a reputational lever and resource advantage that managers may use to influence and cultivate stakeholders as partners. A high-performing company may also receive endorsements from governmental officials or other influential groups, and these are more believable than company messages. A company with a strong

social responsibility orientation often becomes quite proactive in managing and changing conditions that yield economic benefits, including avoiding litigation and increased regulation. Finally, corporate social performance and corporate financial performance are positively correlated. These findings subjugate the belief that social responsibility is just a “cost factor” for business and has no real benefits to the firm.<sup>74</sup>

### National Economy

An often-asked question is whether business conduct has any bearing on a nation’s overall economic performance. Many economists have wondered why some market-based economies are productive and provide a high standard of living for their citizens, whereas other market-based economies lack the kinds of social institutions that foster productivity and economic growth. Perhaps a society’s economic problems can be explained by a lack of social responsibility. Trust stems from principles of morality and serves as an important “lubricant of the social system.”<sup>75</sup> Many descriptions of market economies fail to take into account the role of such institutions as family, education, and social systems in explaining standards of living and economic success. Perhaps some countries do a better job than others of developing economically and socially because of the social structure of their economic relationships.

Social institutions, particularly those that promote trust, are important for the economic well-being of a society.<sup>76</sup> Society has become economically successful over time “because of the underlying institutional framework persistently reinforcing incentives for organizations to engage in productive activity.”<sup>77</sup> In some developing countries, opportunities for political and economic development have been stifled by activities that promote monopolies, graft, and corruption and by restrictions on opportunities to advance individual, as well as collective, well-being. As found in Table 1.7, L. E. Harrison offers four fundamental factors that promote economic well-being: “(1) The degree of identification with others in a society—the radius of trust, or the sense of community; (2) the rigor of the ethical system; (3) the way authority is exercised within the society; and (4) attitudes about work, innovation, saving, and profit.”<sup>78</sup>

Countries with institutions based on strong trust foster a productivity-enhancing environment because they have ethical systems in place that reduce transaction costs and make competitive processes more efficient and effective. In market-based systems with a great degree of trust, such as Australia, Canada, Germany, the Netherlands, and the United Kingdom, highly successful enterprises can develop through a spirit of cooperation and ease in conducting business.<sup>79</sup>

Superior financial performance at the firm level within a society is measured as profits, earnings per share, return on investment, and capital appreciation. Businesses must achieve a certain level of financial performance to survive and reinvest in the various institutions in society that provide support. However, at

**Table 1.7** Fundamental Factors That Promote Economic Well-Being

Factor	Description
Factor 1	The degree of identification with others in a society—the radius of trust or the sense of community
Factor 2	The rigor of the ethical system
Factor 3	The way that authority is exercised within the society
Factor 4	Attitudes about work, innovation, saving, and profit

Source: Lawrence E. Harrison, *Who Prospers? How Cultural Values Shape Economic and Political Success* (New York: Basic Books, 1992).

**Table 1.8** Perceptions of Countries as Least/Most Corrupt

Least Corrupt Countries			Most Corrupt Countries		
Rank	Country	CPI Score	Rank	Country	CPI Score
1	New Zealand	88	179	Somalia	12
1	Denmark	88	179	South Sudan	12
3	Finland	85	178	Syria	14
3	Switzerland	85	176	Yemen	15
3	Singapore	85	176	Venezuela	15
3	Sweden	85	174	Sudan	16

Note: Corruption Perceptions Index (CPI) score relates to perceptions of the degree of public-sector corruption as seen by businesspeople and country analysts and ranges between 10 (highly clear) and 0 (highly corrupt).

Source: Transparency International, *Corruption Perceptions Index 2020*, <https://www.transparency.org/en/cpi/2020/index/nzl> (accessed December 22, 2021).

the institutional or societal level, a key factor distinguishing societies with high standards of living from those with lower standards of living is whether the institutions within the society are generally trustworthy. The challenge is to articulate the process by which institutions that support social responsibility can contribute to superior, firm-level financial performance.<sup>80</sup>

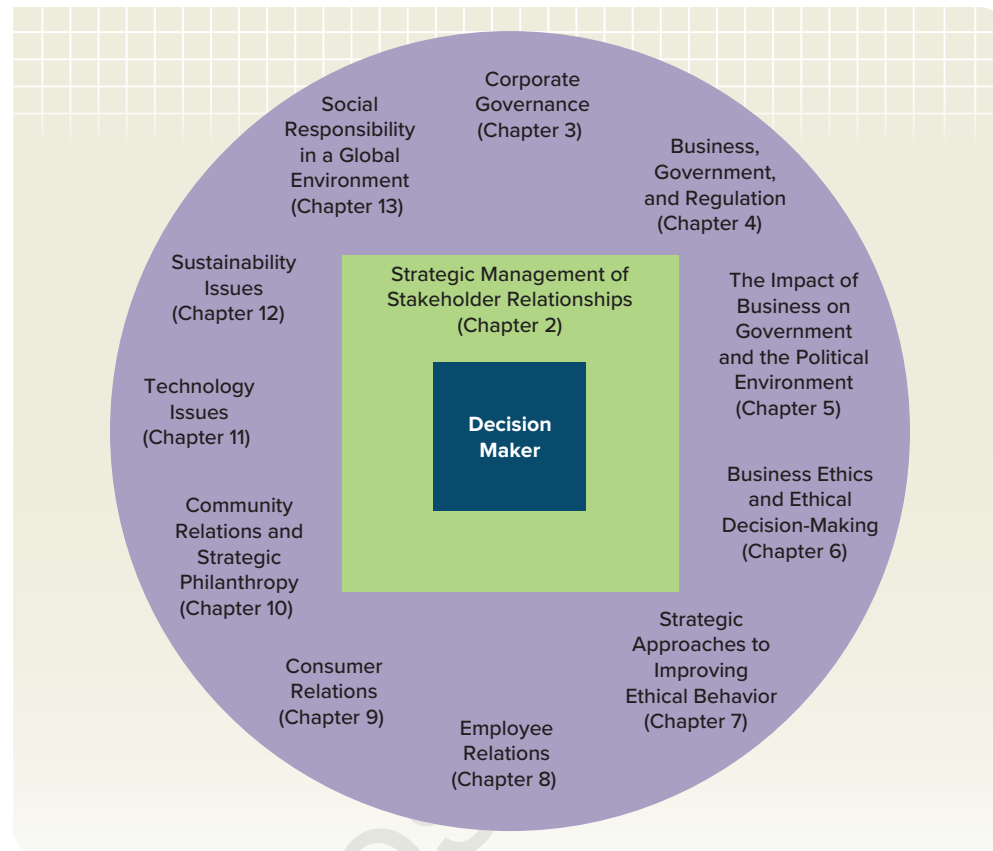
A comparison of countries that have high levels of corruption and underdeveloped social institutions with countries that have low levels of corruption reveals differences in the economic well-being of the country's citizens. Transparency International, an organization discussed earlier, publishes an annual report on global corruption that emphasizes the effects of corruption on the business and social sectors. Table 1.8 lists the countries with the most- and least-corrupt public sectors, as perceived by Transparency International. As stated several times in this chapter, conducting business in an ethical and responsible manner generates trust and leads to relationships that promote higher productivity and a positive cycle of effects.<sup>81</sup>

## Framework for Studying Social Responsibility

The framework that we have developed for this text is designed to help you understand how businesses fulfill social expectations. It begins with the social responsibility philosophy, includes the four levels of social responsibilities, involves many types of stakeholders, and ultimately results in both short- and long-term performance benefits. As discussed earlier, social responsibility must have the support of high-level management—both in words and deeds—before it can become an organizational reality. Every year the Ethisphere Institute release its “World’s Most Ethical Companies” list, recognizing businesses with an outstanding commitment to business integrity. They look at five categories to rate businesses: 1) governance, 2) leadership and reputation, 3) ethics and compliance, 4) culture of ethics, and 5) ESG. Honorees include Aflac, Dell, LinkedIn, Salesforce, and Visa, among 130 others.<sup>82</sup>

Once the social responsibility philosophy is accepted, the four aspects of CSR are defined, implemented, and refined through programs that incorporate stakeholder input and feedback. Vizient, the largest member-owned healthcare company in the United States, has earned a World’s Most Ethical Company designation from the Ethisphere Institute every year since its inception. Vizient analyzes internal data, employee surveys, external stakeholder interviews, and feedback from members, suppliers, industry associations, and community organizations to improve its CSR programs. The top priorities identified by its stakeholders are business model



**Figure 1.5** An Overview of This Book

and product stewardship, human capital, leadership and governance, environment, and social capital.<sup>83</sup> When social responsibility programs are put into action, they have both immediate and delayed outcomes.

Figure 1.5 depicts how the chapters of this book fit into our framework. This framework begins with a look at the importance of working with stakeholders to achieve social responsibility objectives. It also includes an examination of the influence on business decisions and actions of the legal, regulatory, and political environment; business ethics; and corporate governance. The remaining chapters of the book explore the responsibilities associated with specific stakeholders and issues that confront business decision-makers today, including the process of implementing a social responsibility audit.

### Strategic Management of Stakeholder Relationships

Social responsibility is grounded in effective and mutually beneficial relationships with customers, employees, investors, competitors, government, the community, and others who have a stake in the company. Increasingly, companies are recognizing that these constituents both affect and are affected by their actions. For this reason, many companies attempt to address the concerns of stakeholder groups, recognizing that failure to do so can have serious long-term consequences. There is a shift occurring from stockholder capitalism to stakeholder capitalism, meaning corporations are orienting themselves to better create long-term value for their stakeholders.<sup>84</sup> Chapter 2 examines the types of stakeholders and their attributes, how stakeholders become influential, and the processes for integrating and managing stakeholders' influence on a firm. It also examines the impact of corporate reputation and crisis situations on stakeholder relationships.

## Corporate Governance

Because both daily and strategic decisions affect a variety of stakeholders, companies must maintain a governance structure to ensure proper control of their actions and assign responsibility for those actions. In Chapter 3, we define corporate governance and discuss its role in achieving strategic social responsibility. Key governance issues addressed include the rights of shareholders, the accountability of high-level management for corporate actions, executive compensation, and strategic-level processes for ensuring that financial, legal, ethical, and philanthropic responsibilities are satisfied.

## Legal, Regulatory, and Political Issues

In Chapters 4 and 5, we explore the complex relationship between business and government. Every business must be aware of and abide by the laws and regulations that dictate acceptable business conduct. These chapters also examine how business can influence government by participating in the public policy process. A strategic approach for legal compliance is also provided.

## Business Ethics and Strategic Approaches to Improving Ethical Behavior

Because individual values are a component of organizational conduct, these findings raise concerns about the ethics of future business leaders. Chapters 6 and 7 are devoted to exploring the role of ethics in business decision-making. These chapters explore business responsibilities that go beyond the conduct that is legally prescribed. We examine the factors that influence ethical decision-making and consider how companies can apply this understanding to increase their ethical conduct. We also examine ethical leadership and how it contributes to an ethical corporate culture.

## Employee Relations

In today's business environment, most organizations want to build long-term relationships with a variety of stakeholders, but particularly with employees—the focus of Chapter 8. Employees today want flexible work schedules, fair treatment, excellent compensation and benefits, and assistance in balancing work and family obligations. Privacy has also become a major concern and a top priority for workers, especially as more and more employees go remote. Employee monitoring software that tracks employee activity and performance is increasingly common, but critics question whether the use of such software contributes to an environment of trust and commitment. Research has shown that committed and satisfied employees are more productive, serve customers better, and are less likely to leave their employers. These benefits are important to successful business performance, but organizations must be proactive in their human resources programs if they are to receive them.

## Consumer Relations

Chapter 9 explores companies' relationships with consumers or consumer relations. This constituency is part of a firm's primary stakeholder group, and there are a number of financial, legal, ethical, and philanthropic responsibilities that companies must address. This chapter, therefore, considers the obligations that companies have toward their customers, including health and safety issues, honesty in marketing, consumer rights, and related responsibilities.

## Community and Philanthropy

Chapter 10 examines community relations and strategic philanthropy, which is the synergistic use of organizational core competencies and resources to address key stakeholders' interests and to achieve both organizational and social benefits. Whereas traditional benevolent philanthropy involves donating a percentage of sales to social causes, a strategic approach aligns employees and organizational resources and expertise with the needs and concerns of stakeholders, especially the community. Strategic philanthropy involves both financial and nonfinancial contributions (employee time, goods and services, technology and equipment, and facilities) to stakeholders and reaps benefits for the community and company.

## Technology Issues

In Chapter 11, we examine the issues that arise as a result of enhanced technology in the business environment, including the effects of new technology on privacy, intellectual property, and health. We also discuss the rise of artificial intelligence and its enablers, such as big data, blockchain, drones, and robotics. The strategic direction for technology depends on government, as well as on a business's ability to plan the implementation of new technology and to assess the influence of that technology on society.

Thanks to the internet and other technological advances, we can communicate faster than ever before, find information about just about anything, and live longer, healthier lives. However, not all of the changes that occur as a result of new technologies are positive. For example, many jobs have been eliminated by robots and automation, and millions of workers require reskilling and retraining. Many experts predict, however, that AI will lead to long-term job growth, creating more jobs than it eliminates.<sup>85</sup>

## Sustainability Issues

In Chapter 12, we dedicate the entire content to issues of sustainability, including the interdependent nature of economic development, social development, and environmental impact. "Sustainability" has become a watchword in business and community circles, and this chapter explores the ways in which companies define and develop goals, implement programs, and contribute to sustainability concerns. The Dow Jones Sustainability Index (DJSI) makes an annual assessment of companies' economic, environmental, and social performance based on more than 50 general and industry-specific criteria. The DJSI includes 2,500 companies from 20 countries and is used by investors who prefer to make financial investments in companies engaged in socially responsible and sustainable practices.<sup>86</sup>

## Global Social Responsibility

Finally, for many businesses to remain competitive, they must evolve continually to reach global markets and anticipate emerging world trends. Chapter 13 delves into the complex and intriguing nature of social responsibility in a global economy. Building on key concepts discussed throughout this book, we examine the forces that make overseas business plans and activities of paramount concern to host countries, local and national governments, NGOs, and other members of society. The chapter covers a wide range of challenges and opportunities, such as outsourcing, environmental protection, living wages, labor standards, and trade restrictions.

We hope that this framework provides you with a way of understanding the range of concepts, ideas, and practices that are involved in an effective social responsibility initiative. So that you can learn more about the practices

of specific companies, a number of cases are provided at the end of the book. In addition, every chapter includes an opening vignette and other examples that shed more light on how social responsibility works in today's businesses. Every chapter also includes a real-life scenario entitled "What Would You Do?" a contemporary debate issue, and another exercise to help you apply concepts and examine your own decision-making process. As you will soon see, the concept of social responsibility is both exciting and controversial; it is in a constant state of development—just like all important business concepts and practices. A recent survey of thought leaders in the area of social responsibility found that a majority believes that social responsibility has made steady progress into conventional business thinking. Much like the social responsibility continuum introduced in this chapter, the thought leaders described several stages of commitment to CSR. These stages range from shallow, where companies are concerned about responding to complaints, to deep, where companies are founded on a business model of improving social or environmental circumstances. Many companies fall somewhere in between, with a focus on complying with new standards and surviving in a climate of increasing social responsibility expectations.<sup>87</sup> We encourage you to draw on current news events and your own experiences to understand social responsibility and the challenges and opportunities that it poses for your career, profession, role as a consumer, and leadership approach, as well as the business world.

## Summary

The term *social responsibility* came into widespread use during the last several decades, but there remains some confusion over the term's exact meaning. This text defines social responsibility as the adoption by a business of a strategic focus for fulfilling the economic, legal, ethical, and philanthropic responsibilities expected of it by its stakeholders.

All types of businesses can implement social responsibility initiatives to further their relationships with their customers, their employees, and the community at large. Although the efforts of large corporations usually receive the most attention, the actions of small businesses may have a greater impact on local communities.

The definition of social responsibility involves the extent to which a firm embraces the social responsibility philosophy and follows through with the implementation of initiatives. Seven main areas of social responsibility include social issues, consumer protection, sustainability, corporate governance, philanthropy, legal responsibilities, and employee well-being. Social responsibility must be fully valued and championed by top managers and given the same planning time, priority, and management attention as is given to any other company initiative.

Many people believe that businesses should accept and abide by four types of responsibilities: financial, legal, ethical, and philanthropic. Companies have a responsibility to be financially or economically viable so that they can provide a return on investment for their owners, create jobs for the community, and contribute goods and services to the economy. They are also expected to obey laws and regulations that specify what is responsible business conduct. "Business ethics" refers to the principles and standards that guide behavior in the world of business. Philanthropic activities promote human welfare or goodwill. These responsibilities can be viewed holistically, with all four related and integrated into a comprehensive approach. Social responsibility can also be expressed as a continuum. Because customers, employees, investors and shareholders, suppliers, governments, communities, and others have a stake in or claim on some aspect

of a company's products, operations, markets, industry, and outcomes, they are known as "stakeholders." Adopting a stakeholder orientation is part of the social responsibility philosophy.

The influence of business has led many people to conclude that corporations should benefit their employees, their customers, their business partners, and their community as well as their shareholders. However, these responsibilities and expectations have changed over time. After World War II, many large U.S. firms dominated the global economy. Their power was largely mirrored by the autonomy of their top managers. Because of the relative lack of global competition and stockholder input during the 1950s and 1960s, there were few formal governance procedures to restrain management's actions. The stability experienced by midcentury firms dissolved in the economic turmoil of the 1970s and 1980s, leading companies to focus more on their core competencies and reduce their product diversity. The 1980s and 1990s brought a new focus on efficiency and productivity, which fostered a wave of downsizing and restructuring. Concern for corporate responsibilities was renewed in the 1990s. In the 1990s and beyond, the balance between the global market economy and an interest in social justice and cohesion best characterizes the intent and need for social responsibility. Despite major advances in the 1990s, the sheer number of corporate scandals at the beginning of the twenty-first century prompted a new era of social responsibility. The Great Recession of 2008 and the collapse of many well-known institutions led to a renewed interest in business ethics and social responsibility. Later, the COVID-19 pandemic shined a light on the importance of adopting a stakeholder orientation and addressing environmental, social, and governance issues.

Today, stakeholders are increasingly demanding that firms protect the environment, contribute to social causes, and engage in conduct that is responsible and ethical. Environmental, social, and governance (ESG) is a framework for evaluation of firm performance in the areas of environmental, social, and governance. ESG, which began as a corporate social responsibility initiative, has become mainstream.

The increasing globalization of business has made social responsibility an international concern. In most developed countries, social responsibility involves economic, legal, ethical, and philanthropic responsibilities to a variety of stakeholders. Global social responsibility also involves responsibilities to a confluence of governments, businesses, trade associations, and other groups. Progressive global businesses recognize the shared bottom line that results from the partnership among businesses, communities, governments, and other stakeholders.

The importance of social responsibility initiatives in enhancing stakeholder relationships, improving performance, and creating other benefits has been debated from many perspectives. Many business managers view such programs as costly activities that provide rewards only to society, at the expense of their bottom line. Others hold that some costs of social responsibility can be recovered through improved performance. Although it is true that some aspects of social responsibility may not accrue directly to the bottom line, we believe that organizations benefit indirectly over the long run from these activities. Moreover, ample research and anecdotal evidence demonstrate that there are many rewards for companies that implement such programs.

The process of social responsibility begins with the social responsibility philosophy, includes the four responsibilities, involves many types of stakeholders, and ultimately results in both short- and long-term performance benefits. Once the social responsibility philosophy is accepted, the four types of responsibility are defined and implemented through programs that incorporate stakeholder input and feedback.

## Responsible Business Debate



## Royal Dutch Shell Pays the Price for Going Green

**Issue:** *Should oil companies be rewarded for going green?*

Royal Dutch Shell PLC has been faster than other major oil and gas companies when it comes to reducing emissions and changing its strategic direction. The Anglo-Dutch multinational oil and gas company leads the pack on carbon emissions and environmental, social, governance (ESG) factors among big oil companies. And yet, the company's stock is undervalued, trading significantly lower than U.S. peers Exxon and Chevron, despite having strategic plans for a decarbonized future. For this reason, Third Point LLC, one of Shell's largest investors, is urging Shell to separate its legacy fossil-fuel operations from its lower-carbon renewables business to retain and attract investors.

Shell has made significant progress in recent years. The company was the first oil company to target reduced carbon emissions from customers and has done more than competitors to move away from fossil fuels. Because of these efforts, it is the closest of any of the oil giants, including Eni, BP, Total Energies, Exxon Mobile, Chevron, and ConocoPhillips, to meeting the carbon target set by the Paris Agreement, an international treaty on climate change. It's worth noting that even though Shell's ESG scores are even better than Tesla, the leader in electric vehicles, Shell has faced low market valuations, failing to attract investors that have rejected oil investments entirely. And, despite the company's progress relative to other major oil and gas companies, Shell faces a court order in the Netherlands to reduce its emissions by 45 percent by 2030.

To improve the company's stock performance, Third Point, an activist investor, says Shell should split in two, separating its "brown" fossil-fuel operations from its "green" renewables business. This strategy, Third Point argues, would be simpler for investors to understand and would focus the businesses. The brown side of the business would appeal to traditional oil investors looking for a large dividend from a declining business. The green side of the business would appeal to investors looking

for heavy investment in growth and would likely have a premium valuation. Third Point says that the current business organization satisfies no one.

ESG pressures have caused major oil companies to sell their "dirty" business. For example, Shell sold its U.S. shale-oil business to ConocoPhillips for \$9.5 billion, and BHP Group sold its oil and gas business to Woodside Petroleum for \$28 billion and a large stake in Woodside. The issue that exists with these business deals is that the dirty business simply changes ownership. Major players looking to sell may find that buyers are scarce, pushing prices down. Those willing to buy can potentially get a great return in the long run. According to Third Point, splitting Shell into two companies avoids the pitfalls of selling off dirty business and is better for both shareholders and the environment. The company believes that the brown side of Shell would have a higher cost of capital and a visibly lower valuation. This could result in less investment in production and speed up the transition to cleaner forms of energy.

Many experts, however, disagree. Some say that shareholder pressure and carbon taxes are more effective than the share price at pushing change. Additionally, critics suggest that in the long-term, separating green and brown companies will not make a significant difference when it comes to benefiting the environment. Shell has defended its business model, saying that its business is more powerful as a single unit than it would be split into two units. In fact, the company says its legacy oil and gas business is needed to fund its lower-carbon business.

#### **There Are Two Sides to Every Issue**

1. Oil companies that perform well on ESG factors should separate their fossil-fuel operations from their renewables business to receive the full benefits of going green.
2. Oil companies that perform well on ESG factors will be rewarded for going green in the long run whether they separate their fossil-fuel operations from their renewables business or not.

*Sources:* James Mackintosh, "Shell Is the Greenest Big Oil Company. Look What That Got It," *The Wall Street Journal*, October 31, 2021, <https://www.wsj.com/articles/shell-is-the-greenest-big-oil-company-look-what-that-got-it-11635698403> (accessed December 14, 2021); Justin Worland, "'Change is Coming.' Activists Just Scored Big Wins Against ExxonMobil, Chevron and Shell," *Time*, May 27, 2021, <https://time.com/6051404/exxonmobil-board-chevron-shell/> (accessed December 14, 2021); Rochelle Toplensky, "Third Point Doesn't Have the Answer for Shell," *The Wall Street Journal*, October 28, 2011, <https://www.wsj.com/articles/third-point-doesnt-have-the-answer-for-shell-11635432093> (accessed December 14, 2021).

## Key Terms

business ethics (p. 9)	interorganizational networks (p. 11)	social responsibility (p. 6)
code of ethics (p. 10)	legal responsibility (p. 6)	stakeholders (p. 11)
common good (p. 5)	license to operate (p. 4)	stakeholder orientation (p. 11)
consumer protection laws (p. 5)	mission statement (p. 8)	sustainability (p. 5)
core competencies (p. 13)	norms (p. 10)	values (p. 10)
corporate culture (p. 8)	philanthropic activities (p. 10)	vision statement (p. 8)
corporate governance (p. 6)	philanthropy (p. 6)	
employee well-being (p. 6)	principles (p. 9)	
environmental, social, and governance (ESG) (p. 16)	resource advantage theory (p. 11)	

## Discussion Questions

1. Define social responsibility. How does this view of the role of business differ from your previous perceptions? How is it consistent with your attitudes and beliefs about business?
2. If a company is named to one of the “best in social responsibility” lists, what positive effects can they potentially reap? What are the possible costs or negative outcomes that may be associated with being named to one of these lists?
3. What historical trends have affected the social responsibilities of business? How have recent scandals affected the business climate, including any changes in responsibilities and expectations?
4. What is the environmental, social, governance (ESG) framework and how is it used? Provide examples of each factor.
5. On the basis of the social responsibility model presented in this chapter, describe the philosophy, responsibilities, and stakeholders that make up a company’s approach to social responsibility. What are the short- and long-term outcomes of this effort?
6. Consider the role that various business disciplines, including marketing, finance, accounting, and human resources, play in social responsibility. What specific views and philosophies do these disciplines bring to the implementation of social responsibility?

## Experiential Exercise

Evaluate *Fortune* magazine’s annual list of the most admired companies found on the magazine’s website (fortune.com). These companies as a group have superior financial performance compared to other firms. Go to each company’s website and try to assess its management commitment to

the welfare of stakeholders. If any of the companies have experienced legal or ethical misconduct, explain how this may affect specific stakeholders. Rank the companies on the basis of the information available and your opinion on their fulfillment of social responsibility.

## Two Sides to Electronic Cigarettes: What Would You Do?



Jamie Ramos looked out her office window at the early morning sky and gazed at the small crowd below. The words and pictures on their posters were pretty tame this time, she thought. The last protest group used graphic photos to show the effects of vaping on a person’s internal organs. Their words were also hateful—so much so that employees at the Unified E-Cigarettes USA headquarters were afraid to walk in and out of the main building. Those who normally took vaping breaks on the back patio decided to skip them and eat something at the company-subsidized cafeteria instead.

By midday, Unified hired extra security to escort employees in and out of the building and to ensure that protestors followed the state guideline of staying at least 15 feet from the company’s entrance. The media picked up on the story—and the photos—and it caused quite a stir in the national press. At least this protest group seemed fairly reasonable. Late yesterday, a state court had provided a reduced judgment to the family of a teen smoker who

experienced seizures. This meant that Unified was going to owe millions less than originally expected. The length and stress of the lawsuit had taken its toll, especially on high-level management, although all employees were certainly affected. After two years of being battered in the media, learning of a huge settlement, and then continuing on with the appeals process, emotions were wearing thin under the brunt of the continued criticism.

Jamie wondered what this day would bring. As the manager of community relations, her job was to represent Unified in the community, manage the employee volunteer program, create a quarterly newsletter, serve as a liaison to the company’s philanthropic foundation, develop solid relationships, and serve on various boards related to social welfare and community needs. The company’s foundation donated nearly \$1.5 million a year to charities and causes. Over one-quarter of its employees volunteered 10 hours a month in their communities.

Jamie reported to a vice president and was pleased with the career progress that she had made since graduating from college eight years earlier. Although some of her friends wondered out loud how she could work for an e-cigarette company, Jamie was steadfast in her belief that even e-cigarette and tobacco firms could contribute something meaningful to society. She had the chance to affect some of those contributions in her community relations role.

Jamie's phone rang and she took a call from her vice president. The vice president indicated that, although the protestors seemed relatively calm this time, he was not

comfortable with their presence. Several employees had taped signs in office windows telling the protestors to "Go away." Other vice presidents had dropped by his office to discuss the protest and thought that the responsibility for handling these issues fell to his group. He went on to say that he needed Jamie's help, and the assistance of a few others, in formulating a plan to (1) deal with the protest today and (2) strengthen the strategy for communicating the company's message and goodwill in the future. Their meeting was slated to begin in one hour, so Jamie had some time to sketch out her recommendations on both issues. What would you do?