

## WHAT IS CSR?

People build organizations to leverage their collective resources in pursuit of common goals. As organizations pursue these goals, they interact with others inside a larger context called society. Based on their purpose, organizations can be classified as for-profit, government, or nonprofit. At a minimum, *for-profits* seek to make a profit, *governments* exist to define the rules and structures of society within which all organizations must operate,<sup>1</sup> and *nonprofits* (including NGOs—nongovernmental organizations) emerge to fill the gaps when the political will or the profit motive is insufficient to address society's needs.<sup>2</sup> Aggregated across society, each of these different organization types represents a powerful mobilization of resources. In the United States alone, for example, there are more than 1.5 million “tax-exempt organizations” working to fill needs not met by either government or the private sector.<sup>3</sup>

Within society, therefore, there is a mix of these organizational forms. Each performs different roles, but each also depends on the others to provide the complete patchwork of exchange interactions (of products and services, financial and social capital, etc.) that constitute a well-functioning society. Whether labeled as corporations, companies, firms, or proprietorships, for example, for-profit businesses interact constantly with government, trade unions, suppliers, NGOs, and other groups in the communities in which they operate, in both positive and negative ways. Each of these groups, therefore, can claim to have a stake in the operations of the firm. Some benefit more, some are involved more directly, and others can be harmed by the firm's actions, but all are connected in some way to what the firm does on a day-to-day basis. Definitions of who qualifies as a firm's *stakeholder* vary (discussed in detail in Part II). For now, it is sufficient to note that it includes those individuals and groups that have a *stake* in the firm's operations.<sup>4</sup>

While stakeholders exist symbiotically with companies, the extent to which managers have paid attention to their interests fluctuates. Depending on factors such as the level of economic and social progress, the range of stakeholders whose concerns a company seeks to address has shifted—from the earliest view of the corporation as a legal entity that exists at the behest of governments in the 19th century, to a narrower focus on shareholder rights early in the 20th century, to the rise of managerialism by mid-century, and back again in the 1970s and 1980s to a distorted focus on shareholders due to the rise of agency theory.<sup>5</sup> Since then, as the expectations of business in society evolve,

firms are again adopting a broader stakeholder outlook, extending their perspective to include the communities in which they operate and social issues about which they feel passionate. As a result, managers are more likely to recognize the interdependence between the firm and each of these groups, leaving less room to ignore their separate and pressing concerns.

Just because an individual or organization meets the definition of an “interested constituent,” however, this does not compel a firm (either legally or logically) to comply with every demand that stakeholder may make. Deciding which demands to prioritize and which to ignore, however, is a challenge—even more so as social media provides individuals with the power to disseminate their grievances worldwide. If ignored long enough, affected parties may take action against the firm (such as a product boycott), or turn to government for redress, or even write a song and post it to YouTube.<sup>6</sup> Such protests can cause significant brand damage (and even revenue loss), particularly if the grievance remains unaddressed once it becomes widely known.<sup>7</sup>

In democratic societies, laws (e.g., antidiscrimination statutes), regulations (e.g., tax-exempt status for nonprofits), and judicial decisions (e.g., fiduciary responsibilities of directors)<sup>8</sup> provide a minimal framework for business that reflects a rough consensus of the governed. However, because (1) government cannot anticipate many issues, (2) the legislative process takes time, and (3) a general consensus is often slow to form, laws often lag behind social convention and technological progress. This is particularly so in areas of high complexity and rapid innovation, such as bioethics or artificial intelligence. Thus, we arrive at the discretionary area of decision making between legal sanction and societal expectation that business leaders face every day—an area of ambiguity that generates two questions from which the study of CSR springs:

1. What is the role of the for-profit firm in society?
2. Does the firm have broader social responsibilities (beyond making a profit)?

CSR, therefore, is both critical and controversial. It is *critical* because the for-profit sector is the largest and most innovative part of any free society’s economy. Companies intertwine with society in mutually beneficial ways, driving progress and affluence—creating most of the jobs, wealth, and innovations that enable society to prosper. They are the primary delivery system for food, housing, healthcare, and other necessities of life. Without modern corporations, the jobs, taxes, donations, and other resources that support governments and nonprofits would decline significantly, further diminishing general well-being. Businesses are the engines of society that propel us toward a better future, which suggests an interesting thought experiment: If you wanted to do the most social good in your career, would you enter public service (politics or nonprofits), or would you go into business? Fifty years ago, the best answer would probably have been “public service.” Today, business is the more effective vehicle for social good.

At the same time, CSR remains *controversial*. People who have thought deeply about *Why does a business exist?* or *What does profit represent?* do not agree on the answers. Do firms have obligations beyond the benefits their economic success provides? In spite of the rising importance of CSR, many still draw on the views of the Nobel Prize–winning economist Milton Friedman to argue that society benefits most when firms focus purely on financial success.<sup>9</sup> Others look to the views of business leaders who have argued for a broader perspective, such as David Packard (cofounder of Hewlett-Packard):

I think many people assume, wrongly, that a company exists simply to make money. While this is an important result of a company's existence, we have to go deeper and find the real reasons for our being. . . . A group of people get together and exist as an institution that we call a company so that they are able to accomplish something collectively that they could not accomplish separately—they make a contribution to society.<sup>10</sup>

This book navigates between these perspectives to outline a view of CSR that recognizes both its strategic value to firms and the social benefit such a perspective brings to the firm's many stakeholders. The goal is to present a comprehensive assessment of *corporate social responsibility* that, on reflection, suggests that Friedman and Packard were not as far apart as their respective proponents assume.

## A NEW DEFINITION OF CSR

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### CSR

A responsibility among firms to meet the needs of their stakeholders and a responsibility among stakeholders to hold firms to account for their actions.

The entirety of CSR can be discerned from the three words this phrase contains. CSR covers the relationship between *corporations* (or other for-profit firms) and the *societies* with which they interact, focusing on the *responsibilities* that are inherent on both sides of these ties. CSR defines society in its widest sense, and on many levels, to include all stakeholder groups that maintain an ongoing interest in the firm's operations.

Stakeholder groups range from clearly defined customers, employees, suppliers, creditors, and regulating authorities to other, more amorphous constituents, such as the media and local communities. For the firm, tradeoffs must be made among these competing interests. Issues of legitimacy and accountability exist, such as when a nonprofit claims expertise in an area, even when it is unclear exactly how many people support its vision. Ultimately, therefore, each firm must identify those stakeholders that constitute its operating environment and then prioritize their level of importance. Increasingly, firms need to incorporate the concerns of those key stakeholder groups within their strategic outlook or risk losing societal legitimacy. CSR provides a framework that helps firms embrace these decisions and adjust the internal strategic planning process to increase the long-term viability of the organization.

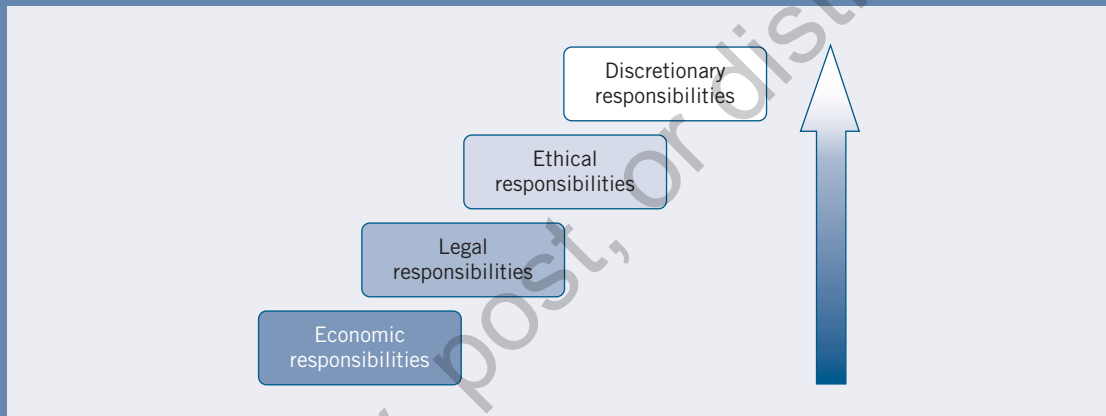
This framework is broad, however, and definitions regarding the mix of interests and obligations have varied considerably over time.<sup>11</sup> In 1979, for example, Archie Carroll defined CSR in the following way: “The social responsibility of business encompasses the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time.”<sup>12</sup>

# THE CORPORATE SOCIAL RESPONSIBILITY HIERARCHY

Archie Carroll was one of the first academics to make a distinction between different kinds of organizational responsibilities. He referred to this

distinction as a firm's "pyramid of corporate social responsibility" (Figure 1.1).<sup>13</sup>

**Figure 1.1 The Corporate Social Responsibility Hierarchy**



Source: Archie B. Carroll, "The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders," *Business Horizons*, July–August 1991, p. 42.

- Fundamentally, a firm's *economic responsibility* is to produce an acceptable return for investors.
  - An essential component of pursuing economic gain within a law-based society, however, is a *legal responsibility* to act within the framework of laws and regulations drawn up by the government and judiciary.
  - Taken one step further, a firm has an *ethical responsibility* to do no harm to its stakeholders and within its operating environment.
  - Finally, firms have a *discretionary responsibility*, which represents more proactive, strategic behaviors that benefit themselves or society, or both.
- As a firm progresses toward the top of Carroll's pyramid, its responsibilities become more discretionary in nature. In Carroll's vision, a *socially responsible* firm encompasses all four responsibilities within its culture, values, and day-to-day operations.

While useful, however, this typology is not rigid.<sup>14</sup> One of the central arguments of this book is that what was ethical or even discretionary in Carroll's model is becoming increasingly necessary due to the shifting expectations placed on firms. Yesterday's ethical responsibilities can quickly become today's economic and legal necessities. In order to achieve its fundamental economic goals today, therefore, a firm must incorporate a stakeholder perspective within its strategic outlook. As societal expectations of the firm rise, the penalties imposed for perceived behavior lapses will become prohibitive.

Definitions, therefore, can and do evolve. It seems that, in terms of CSR, the variance is considerable, with at least five dimensions identified: environmental, social, economic, stakeholder, and "voluntariness."<sup>15</sup> And, of course, there is variance not only within countries over time, but also across countries and cultures.

## CSR DEFINITIONS ACROSS CULTURES

*European Union (EU):* "Corporate social responsibility (CSR) refers to companies taking responsibility for their impact on society. The European Commission believes that CSR is important for the sustainability, competitiveness, and innovation of EU enterprises and the EU economy. It brings benefits for risk management, cost savings, access to capital, customer relationships, and human resource management."<sup>16</sup>

*Association of Southeast Asian Nations (ASEAN):* The Mission of the ASEAN CSR Network is to "promote and enable responsible business conduct in ASEAN to achieve sustainable, equitable and inclusive social, environmental and economic development."<sup>17</sup>

*United Nations (UN):* "CSR is presented as a management concept and a process that integrates social and environmental concerns in business operations, and a company's interactions with the full range of its stakeholders."<sup>18</sup>

While these definitions may seem similar on the surface, the debate around CSR is most apparent in the detail of implementation. The potential danger is that, to the extent that CSR means different things to different people (in reality), action can be ineffective or, at worst, counterproductive:

Right now we're in a free-for-all in which "CSR" means whatever a company wants it to mean: From sending employees out in matching t-shirts to paint a wall for five hours a year, to recycling, to improving supply-chain conditions, to diversity and inclusion. This makes it difficult to have a proper conversation about what [CSR] should be.<sup>19</sup>

For the purposes of this book, it is important to emphasize that CSR is both a means and an end. It is an integral element of the firm's strategy—the way the firm goes about

delivering its products or services to markets (*means*). It is also a way of maintaining the legitimacy of the firm's actions in the larger society by bringing stakeholder concerns to the foreground (*end*). Put another way, CSR is both a *process* and an *outcome*. At any given moment, CSR describes the process by which firms react to their stakeholders' collective set of needs. CSR is also the set of actions that are defined by what stakeholder demands require. Over time, while the process remains the same (firms should always seek to respond to the interests of their stakeholders), the actions that are required to do this will necessarily evolve in response to shifting norms, values, and societal expectations. As such, references to "CSR" in this book will sometimes be to the process and sometimes to the outcomes. The underlying principles that determine the relationship between the two, however, remain consistent. Either way, a firm's success is directly related to its ability to incorporate stakeholder concerns into its business model. CSR provides a means to do this by valuing the interdependent relationships that exist among firms and their stakeholders. The challenges associated with managing these relationships were apparent to Peter Drucker as far back as 1974:

The business enterprise is a creature of a society and an economy, and society or economy can put any business out of existence overnight. . . . The enterprise exists on sufferance and exists only as long as the society and the economy believe that it does a necessary, useful, and productive job.<sup>20</sup>

As such, CSR covers an uneven blend of different issues that rise and fall in importance from firm to firm over time. In other words, while the stakeholders stay the same, the issues that motivate them change. Whether the concern is wages, healthcare, or same-sex partner benefits, for example, a firm's employees are central to its success. A firm that consistently ignores its employees' legitimate claims is a firm that is heading for bankruptcy. CSR is a vehicle for the firm to discuss its stakeholder obligations (both internal and external) and a way of developing the means to meet these obligations, as well as a tool to identify the mutual benefits that result. Simply put, CSR encourages a firm to manage its stakeholder relations because these ties are essential to its success and, ultimately, its survival. Implementing CSR, therefore, requires the firm to acknowledge:

That markets operate successfully only when they are embedded in communities; that trust and co-operation are not antithetic to a market economy, but essential to it; that the driving force of innovation is pluralism and experiment, not greed and monopoly; that corporations acquire legitimacy only from the contribution they make to the societies in which they operate.<sup>21</sup>

CSR encompasses the range of economic, legal, ethical, and discretionary actions that affect a firm's economic performance. At a minimum, of course, firms should comply with the legal or regulatory requirements that relate to day-to-day operations. To break these regulations is to break the law, which does not constitute socially responsible behavior. But legal compliance is merely a minimum condition of CSR.<sup>22</sup> Taking these obligations as a given, the framework presented in this book focuses on the ethical

and discretionary concerns that are less precisely defined and for which there is often no clear societal consensus, but that are essential to address. Firms do this (minimizing competitive risk while maximizing potential benefit) by fully embracing CSR and incorporating it within the firm's strategic planning process.

## THE EVOLUTION OF CSR

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The call for social responsibility from businesses is not new. While specific issues may change, societies have always made demands of firms. In short, “the pursuit of profit has been ‘unloved’ since Socrates declared that ‘the more [men] think of making a fortune, the less they think of virtue.’”<sup>23</sup> As a result, ancient Chinese, Egyptian, and Sumerian writings often delineated rules for commerce to facilitate trade and ensure broader interests were considered. Ever since, public concern about the interaction between business and society has grown in proportion to the growth of economic activity.<sup>24</sup>

There has been a tradition of benevolent capitalism in the UK for over 150 years. Quakers, such as Barclays and Cadbury, as well as socialists, such as Engels and Morris, experimented with socially responsible and values-based forms of business. And Victorian philanthropy could be said to be responsible for considerable portions of the urban landscape of older town centres today.<sup>25</sup>

Evidence of social activism intended to influence firms' behavior stretches back across the centuries. Such efforts mirrored the legal and commercial development of corporations as they established themselves as the driving force of market-based societies. Periodically, society stepped in when business was deemed to be causing more harm than good: “The first large-scale consumer boycott? England in the 1790s over slave-harvested sugar.”<sup>26</sup> Although crude and lacking the efficient communication that social media enables today, it is clear that these early consumer-led protests paved the way for today's “politics of consumption.”<sup>27</sup> Protests could be effective—initially in terms of raising awareness, but soon after in terms of tangible, legislative change:

Within a few years, more than 300,000 Britons were boycotting sugar, the major product of the British West Indian slave plantations. Nearly 400,000 signed petitions to Parliament demanding an end to the slave trade. . . . In 1792, the House of Commons became the first national legislative body in the world to vote to end the slave trade.<sup>28</sup>

More recently, early academic interest in the topic of CSR in the 1950s was quickly followed by broader societal awareness that resulted in pressure on firms to respond. In particular, books such as *Silent Spring* (1962), *Unsafe at Any Speed* (1965), and *The Feminine Mystique* (1963) were “credited with being catalysts for the environmental movement, the consumer movement, and the feminist movement, respectively.”<sup>29</sup> While the extent to which these external forces influence corporate decisions will vary, it is clear

that CEOs have always faced pressure to conform to societal expectations. What is notable today is how quickly such issues emerge and diffuse. The experience of the late Ray Anderson, founder and chairman of Interface Carpets,<sup>30</sup> in relation to the environmental practices of his company, is instructive:

One day . . . it dawned on me that the way I had been running Interface is the way of the plunderer, plundering something that is not mine; something that belongs to every creature on earth. And I said to myself, . . . the day must come when this is illegal, when plundering is not allowed [and] . . . people like me will end up in jail. The largest institution on earth, the wealthiest, most powerful, the most pervasive, the most influential, is the institution of business and industry—the corporation, which also is the current present day instrument of destruction. It must change.<sup>31</sup>

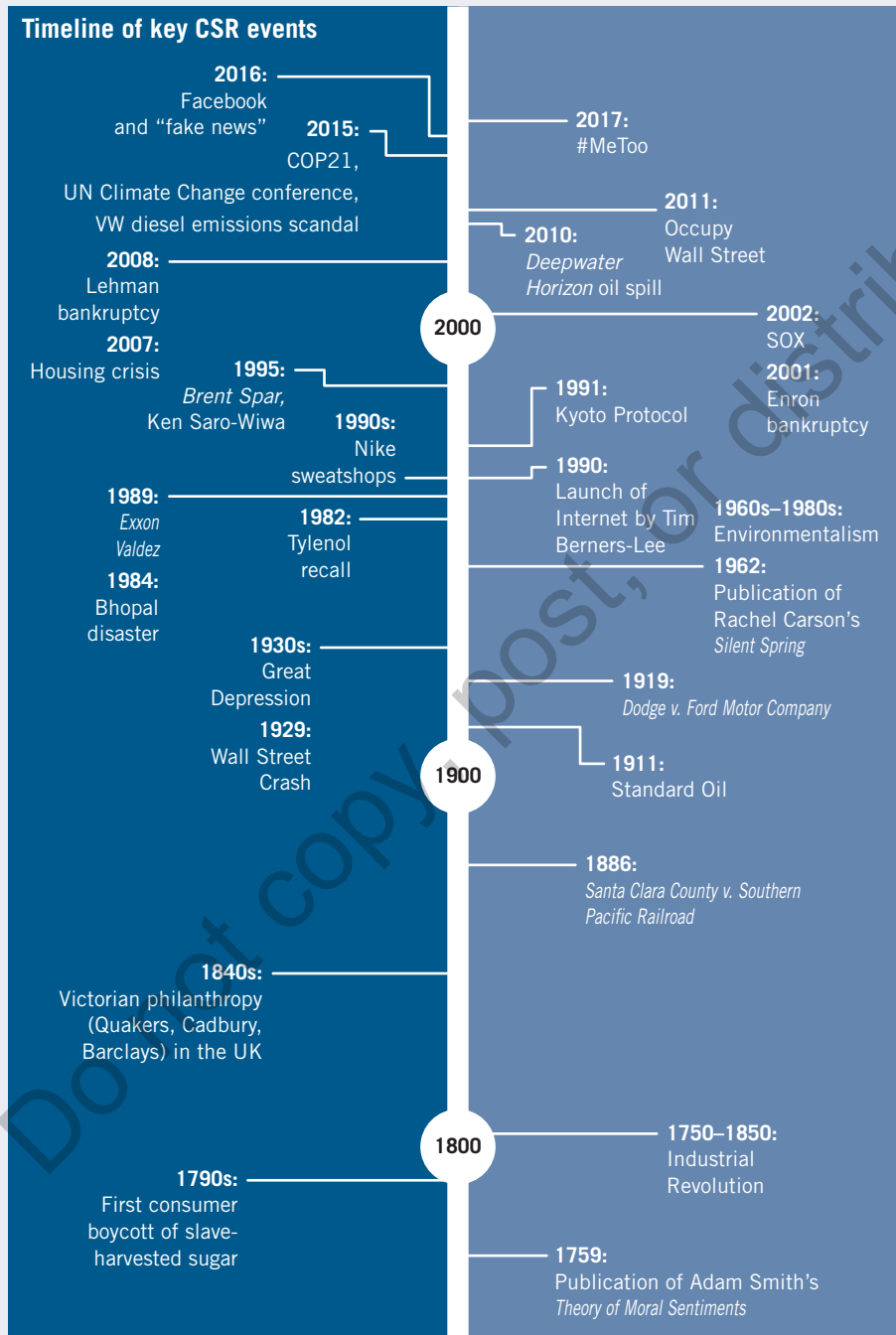
Leaders such as Anderson face a balancing act that addresses the tradeoffs among the firm's primary stakeholders, the society that enables the firm to prosper, and the environment that provides the raw materials to produce products and services of value. When elements of society view leaders and their firms as failing to act *appropriately*, activism results. That was just as true of 18th-century Britain as it is today. Current examples of social activism in response to firms' perceived lack of responsibility are in this morning's news and online social media. Whether the response is government regulation of products that are hazardous, consumer boycotts of firms that advocate overtly religious principles, or NGO-led campaigns to eradicate sweatshops abroad, societal concerns have become an increasingly relevant topic in corporate boardrooms, business school classrooms, and family living rooms. Figure 1.2 illustrates some of the key events that have defined the progress of CSR over the centuries.

This ongoing evolution ensures that meeting society's expectations is not a static target. Widespread industry practices, which were previously considered discretionary or ethical concerns, can be deemed illegal or socially unacceptable due to aggressive prosecution or novel activism. In recent years, for example, the growing criticism of investors who use high-frequency trading algorithms to gain *unfair* advantages when trading<sup>32</sup> indicates the danger of assuming that yesterday's accepted practices will continue to be acceptable. Tomorrow, it could be continued opposition to the legalization of marijuana that draws the ire of stakeholders, and beyond that, the spread of artificial intelligence. Firms operate against an ever-changing background of what is considered *socially responsible*. These ever-changing standards compound the complexity faced by corporate decision makers. Worse, these standards vary from society to society, even among cultures within a given society. Faced with a kaleidoscope of evolving expectations, the challenge for a manager is to understand what the firm's stakeholders want today and, perhaps more importantly, what they will want six months from now.

Nevertheless, the pursuit of economic gain remains a necessity. CSR does not repeal the laws of economics under which for-profit firms must operate (to society's benefit). The example of Malden Mills demonstrates that, unless a firm is economically viable, even the best of intentions will not enable stakeholders to achieve their goals.



**Figure 1.2 The Evolution of CSR**



## MALDEN MILLS

Aaron Feuerstein, CEO of Malden Mills (founded in 1906, family-owned),<sup>33</sup> was an excellent employer. He operated “a unionized plant that was strike-free, a boss who saw his workers as a key to his company’s success.”<sup>34</sup> In 1995, however, a fire destroyed the firm’s main textile plant based in Lawrence, Massachusetts, an economically deprived area in the north of the state. Feuerstein then had a decision to make:

With an insurance settlement of close to \$300 million in hand, Feuerstein could have, for example, moved operations to a country with a lower wage base, or he could have retired. Instead, he rebuilt in Lawrence and continued to pay his employees while the new plant was under construction.<sup>35</sup>

His decision to keep the factory open and continue meeting his obligations to his employees when they needed him most was applauded in the media:

The national attention to Feuerstein’s act brought more than the adulation of business ethics professors—it brought increased demand for his product,

Polartec, the lightweight fleece the catalogue industry loves to sell.<sup>36</sup>

In addition to full pay, Feuerstein continued to provide all employees with full medical benefits and guaranteed them a job when the factory was ready to restart production:

“I have a responsibility to the worker, both blue-collar and white-collar,” Feuerstein later said. “I have an equal responsibility to the community. It would have been unconscionable to put 3,000 people on the streets [at Christmas] and deliver a death blow to the cities of Lawrence and Methuen. Maybe on paper our company is [now] worth less to Wall Street, but I can tell you it’s [really] worth more.”<sup>37</sup>

But the increased demand for Polartec clothing wasn’t enough to offset the debt he had built up waiting for the plant to be rebuilt: \$100 million.<sup>38</sup> This situation was compounded by an economic downturn, as well as cheaper fleece alternatives flooding the market. Malden Mills filed for bankruptcy protection in November 2001.<sup>39</sup>

The Polartec example demonstrates vividly the complexity of CSR. While an imperfect measure of a firm’s success, profit is clearly essential. If the goal is to create value, the firm needs to stay in business. Would Malden Mills have avoided bankruptcy if it had initially fired half its employees and relocated the factory elsewhere? What is the firm’s responsibility to continue delivering a valued product to its customers, and does this outweigh the firm’s duties to its employees? The answers to these questions are difficult and will change depending on the issue at hand. What is clear is that good intentions do not replace the need for an effective business model, and no firm, whatever the motivation, can or should indefinitely spend money it does not have. Which actions should be pursued depend on many factors specific to the firm, its industry, and the society in which it is based. Manufacturing offshore in a low-cost environment, for example, remains a valid strategic decision, particularly in an increasingly globalized world. This

choice is strategic because it can provide a competitive advantage for some firms (such as Apple),<sup>40</sup> even while other firms (such as Zara)<sup>41</sup> see strategic value in onshoring operations due to rising costs and a shorter, more responsive supply chain:

Offshore production is increasingly moving back to rich countries not because Chinese wages are rising, but because companies now want to be closer to their customers so that they can respond more quickly to changes in demand. And some products are so sophisticated that it helps to have the people who design them and the people who make them in the same place.<sup>42</sup>

All business decisions have both economic and social consequences. The trick to success is to manage the conflicting interests of stakeholders in order to meet their ever-evolving needs and concerns. As societies rethink the balance between economic and social progress, CSR will continue to evolve in importance and complexity. And although this complexity muddies the wealth-creating waters, an awareness of these evolving expectations holds the potential to create a competitive advantage for those firms that do it well. The previous examples indicate that the cultural context in which the concept of *social responsibility* is perceived and evaluated is crucial.

Different societies define the relationship between business and society in different ways. Expectations spring from many factors, with wealthy societies having greater resources and, perhaps, more demanding expectations that emerge from the greater options wealth brings. The reasoning is straightforward: In poor democracies, general well-being is focused on the necessities of life—food, shelter, transportation, education, medicine, social order, jobs, and so on. *Luxuries*, such as a living wage or environmental regulations, add costs that may cause them to be delayed. As societies advance, however, expectations change and *general well-being* is redefined. A corresponding shift in the acceptable level of response by firms quickly follows, as this example of air pollution and public transportation in Chile indicates.

## SANTIAGO, CHILE

In the 1980s, air pollution in downtown Santiago, Chile, was an important issue, just as it was in Los Angeles, California. The problem, however, was addressed differently due to the varying level of economic development in these two pollution-retaining basins.

While stringent laws went into effect in Los Angeles, in Chile, necessities (including low-cost transportation) got a higher priority

because of widespread poverty. After more than a decade of robust economic growth, however, Chileans used democratic processes to limit the number of cars entering Santiago and imposed increasingly stringent pollution standards. This shift in priorities reflected their changing societal needs, along with the growing wealth to afford new rules and legal actions.

Different expectations among rich and poor societies are a matter of priorities. The need for transportation, for example, evolves into a need for nonpolluting forms of transportation as society becomes more affluent. Though poor societies value clean air just as advanced ones do, there are other more pressing concerns (such as keeping costs low). As a society prospers, new expectations compel producers to make vehicles that pollute less—a shift in emphasis. In time, these expectations evolve from a discretionary option to a mandatory (legal) requirement.

In short, it is in the best interest of any organization (for-profit, nonprofit, or governmental) to anticipate, reflect, and strive to meet the changing needs of its stakeholders. In the case of a for-profit firm, the primary stakeholder groups are its employees and customers, without whose support the business fails. Other constituents, however, from suppliers to shareholders to the local community, also matter. Firms must satisfy these core constituents if they hope to remain viable over the long term. When the expectations of different stakeholders conflict, CSR enters a gray area, and management has to negotiate among competing interests. An important part of that conflict arises from different expectations, which, in turn, reflect different approaches to CSR.

## FOUNDATIONS OF CSR

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*Strategic CSR* represents an argument for a firm's economic interests, where satisfying stakeholder needs is central to retaining societal legitimacy (and achieving financial viability). Much debate (and criticism) in the CSR community, however, springs from well-intentioned parties who argue from perspectives that differ along philosophical and ideological lines. Understanding these different arguments (ethical, moral, rational, and economic), therefore, is essential to comprehend the full breadth and depth of CSR.

### An Ethical Argument for CSR

The danger of promoting a perspective of CSR that focuses primarily on its strategic value to the firm is that the ethical and moral foundations on which much of the CSR debate rests are ignored. The advantage of making the business case for CSR is that it is more convincing to those most skeptical of broadening the firm's responsibilities and, as a result, is more likely to be implemented. In other words, the business case is expedient—it offers the greatest potential gain because it will appeal to the widest possible audience of people who need to be convinced. The danger in downplaying an ethical or moral component to CSR, however, is that doing so ignores an intellectual philosophical foundation that many believe is essential to understanding CSR.

There are three essential components encapsulated within the concept of business ethics: normative, descriptive, and practical ethics. *Normative ethics* draws on moral philosophy to categorize individual actions as either *right* or *wrong* in specific situations. *Descriptive ethics* explains why individuals make these *right* or *wrong* decisions. And *practical ethics* applies ethical principles that determine *right* and *wrong* actions to day-to-day decision making. Underpinning each of these three core components, of course, is the assumption that *right* and *wrong* can be determined. This assumption glosses over the issue of whether ethical values are relative or absolute. An ethical argument for

CSR states that, rather than being relative constructs (i.e., varying from individual to individual and culture to culture), ethical values are absolute (i.e., inalienable *rights* that are consistent across cultures and applicable to all humans). Absolute values are easily definable and, as such, exist as a standard against which behavior can be assessed.

Although many discussions around CSR assume an ethical component, the precise relationship between ethics and CSR is often unspecified. As such, the late Rushworth Kidder poses an essential question when he asks: “Can a socially responsible company be unethical?”<sup>43</sup> In constructing an answer, Kidder conceptualizes CSR as a subset of ethics:

Responsibility . . . is one of five distinct core values that define, globally, the idea of ethics. A necessary but not sufficient condition for ethics, it needs to be fleshed out by the other four values: honesty, respect, fairness, and compassion. Ethics requires all five. So can an individual or a corporation have a strong sense of responsibility without necessarily being honest? Yes. The opposite can also arise, where a deeply honest person proves to be irresponsible. These are two big, different ideas.<sup>44</sup>

An ethical argument for CSR essentially rests on one of two philosophical approaches—consequentialist reasoning or categorical reasoning.<sup>45</sup> Consequentialist (or teleological) reasoning locates ethicality in terms of the outcomes caused by an action. This stream of thought is closely aligned with utilitarianism, which was most famously advocated by the 18th-century English political philosopher Jeremy Bentham:

An action is considered ethical according to consequentialism when it promotes the good of society, or more specifically, when the action is intended to produce the greatest net benefit (or lowest net cost) to society when compared to all the other alternatives.<sup>46</sup>

In contrast, categorical (or deontological) reasoning “is defined as embodying those activities which reflect a consideration of one’s duty or obligation.”<sup>47</sup> As such, categorical reasoning represents more of a process orientation than the outcome-oriented focus of consequentialist reasoning. This perspective closely maps to Immanuel Kant’s categorical imperative, but it also includes guiding principles such as religious doctrine and core values such as trustworthiness, honesty, loyalty, accountability, and a broad sense of citizenship (i.e., acting out of a sense of responsibility to the common good).

## AN ETHICAL ARGUMENT FOR CSR

CSR is an argument based on two forms of ethical reasoning—*consequentialist* (utilitarian) and *categorical* (Kantian). Consequentialist reasoning justifies action in terms of the outcomes generated (the greatest good for the

greatest number of people), while categorical reasoning justifies action in terms of the principles by which that action is carried out (the application of core ethical principles, regardless of the outcomes).

The violation of a society's cultural heritage and ethical principles regarding issues of social justice, human rights, or environmental stewardship, for example, is unethical and socially irresponsible. This logic is the foundation of the *social contract*, which is based on societal expectations that bind firms because compliance is directly related to a social license to operate. In terms of application, therefore, the two ethical perspectives are realized in norms: "those standards . . . which have been accepted by the organization, the industry, the profession, or society as necessary for the proper functioning of business." They are institutionalized within the firm in the form of a code of conduct or code of ethics, which acts as a guide in determining whether the firm "is acting ethically according to the conventional standard."<sup>48</sup> Remaining within these implicit ethical boundaries is directly related to the firm's societal legitimacy and long-term viability.

### A Moral Argument for CSR

Although profits are necessary for any business to survive, firms are able to obtain those profits only because of the society in which they operate. All of the firm's stakeholders (even internal stakeholders, such as employees) exist primarily as members of a society. Without that social context, there is no marketplace in which firms can compete. CSR emerges from this symbiotic relationship between business and society. It is shaped by individual and societal standards of morality that define contemporary views of *right* and *wrong*.<sup>49</sup> As Howard Bowen said about managers in his famous 1953 book:

They must accept the social implications of their calling. They must recognize that ultimately business exists not for profits, for power, or for personal aggrandizement, but to serve society. . . . [The freedom and power that comes with managing a business] must be used moderately, conscientiously, and with a view to the interests of society at large.<sup>50</sup>

Given this, to what extent is a firm obliged to repay the debt it owes society for its opportunity to conduct business (and its continued success)? That is, what moral responsibilities do firms possess in return for the benefits society grants? Also, to what extent do the profits the firm generates, the jobs it provides, and the taxes it pays meet those obligations? As an academic study, CSR represents an organized approach to answering these questions. As an applied discipline, it represents the advantage to the firm of meeting its obligations as defined by evolving societal expectations.

## A MORAL ARGUMENT FOR CSR

CSR is an argument of moral reasoning that reflects the relationship between a company and the society within which it operates. It assumes that firms recognize they do not exist in a vacuum and that their ability to operate and

achieve success comes as much from societal resources (e.g., infrastructure, rule of law, educated employees) and consent (e.g., social contract, license to operate) as it does from internal factors.

Peter Drucker expresses this sentiment—that there is no moral justification in pursuing profit alone—by suggesting that “profit for a company is like oxygen for a person. If you don’t have enough of it, you’re out of the game. But if you think your life is about breathing, you’re really missing something.”<sup>51</sup> Charles Handy similarly suggests that firms have a moral obligation to move beyond a narrow focus on profit:

The purpose of a business . . . is not to make a profit, full stop. It is to make a profit so that the business can do something more or better. That “something” becomes the real justification for the business. . . . It is a moral issue. . . . It is salutary to ask about any organization, “If it did not exist, would we invent it?” “Only if it could do something better or more useful than anyone else” would have to be the answer, and profit would be the means to that larger end.<sup>52</sup>

On one level, the moral argument for CSR reflects a give-and-take approach based on a realization of the interdependent relationship between business and society. Society makes business possible and provides what firms need to succeed, ranging from educated and healthy workers to a safe and stable physical and legal infrastructure, not to mention a vibrant consumer market for their products. Because society’s contributions make business possible, the moral argument for CSR presumes that firms have a reciprocal obligation to operate in ways that are deemed socially *responsible* and *beneficial*. And because businesses operate within a social context, society has the right to define the expectations for those organizations that operate within its boundaries:

[Free-market economists] like to portray “wealth-producing” businesses as precarious affairs that bestow their gifts independently of the society in which they trade. The opposite is the case. The intellectual, human and physical infrastructure that creates successful companies . . . is a social product . . . shaped by the character of that society’s public conversation and the capacity to build effective social institutions and processes.<sup>53</sup>

For many, a sole focus on money as the motivation for business is dispiriting—“as vital as profit is, it seems insufficient to give people the fulfillment they crave.”<sup>54</sup> It follows that money is a social good that is accompanied by a moral obligation to return to the collective a percentage of the proceeds of economic gain earned on advantages conferred by society to the firm. As Adam Smith<sup>55</sup> wrote in *The Wealth of Nations*:

The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state. The expense of government . . . is like the expense of management to the joint tenants of a great estate, who are all obligated to contribute in proportion to their respective interests in the state.<sup>56</sup>

At a deeper level, societies rest upon a cultural heritage that grows out of a confluence of religion, traditions, and norms. This heritage gives rise to a belief system that

defines the boundaries of socially acceptable behavior by participants. The moral argument for CSR claims that all members of society have a responsibility to uphold these *rules* in the interests of the common good.<sup>57</sup>

## A Rational Argument for CSR

A loss of societal legitimacy can lead to a rise in the countervailing forces of strikes (employees), activism (NGOs), boycotts (consumers), legislation (government), or bad press (media) that constrain the firm's ability to act. Violations of stakeholder expectations are material and, as such, should be avoided whenever possible, which suggests a rational argument for CSR.

Efforts to comply with stakeholder expectations are rational, regardless of ethical or moral reasoning. While compliance with ethical or moral expectations can be based on subjective values, the rational argument rests on sanction avoidance—it may be more cost-effective, for example, to address issues voluntarily. Waiting for society to impose legally mandated requirements and only then reacting allows firms to ignore their ethical and moral obligations and concentrate on generating profits in the short term; however, it also inevitably leads to strictures being imposed that not only force compliance, but often do so in ways that the firm may find neither preferable nor efficient.<sup>58</sup>

Worse, if the required actions are a complete surprise, or the firm needs time to build a competency in the relevant area, compliance can be extremely costly in terms of both immediate investment and longer-term reputational damage. By ignoring the opportunity to influence the debate in the short term through proactive behavior, a firm is more likely to find its operations and strategy constrained over the long term. One need only consider the evolution of affirmative action in the United States to see this rationale in action.

## AFFIRMATIVE ACTION

Prior to the 1960s, businesses could discriminate against employees on the basis of race, gender, religion, age, national origin, disability, sexual orientation, or any other non-merit-based criteria. Doing so was a discretionary right that was legal, if far from ethical. Social activism moved these discretionary decisions into the arena of public debate and, in time, imposed legal prohibitions. The result for many firms that were guilty of discrimination was affirmative action plans to redress imbalances among employees. Those firms that lagged quickly found themselves the test case in litigation focused on institutionalizing the new legislation. As

Robert Kennedy said during the civil rights movement to firms that were reluctant to change, “If you won’t end discriminatory practices because it’s the right thing to do; then do it because it’s good for business.”<sup>59</sup>

Similar resistance is apparent today among those firms unwilling to embrace same-sex partner benefits or gender fluidity among employees. While there may be short-term value for some in holding out, the direction in which society is moving is clear. Firms that resist normative compliance will ultimately be coerced to conform to society’s evolving standards, and could potentially pay a higher price for their resistance.



While lobbying to ensure that discrimination remains legal is theoretically an option for firms, attempts to subvert societal consensus around a particular issue represent an ethical and moral lapse that places the firm's legitimacy at risk. Instead, the rational argument advocates the benefits of avoiding the inevitable confrontation.

The rational argument for CSR is summarized by the *Iron Law of Social Responsibility*, which states: In a free society, discretionary abuse of societal responsibilities leads, eventually, to mandated reprisals.<sup>60</sup> Restated: In a democratic society, power is removed from those who abuse it. The history of social and political uprisings—from Cromwell in England, to the American and French Revolutions, to the overthrow of the shah of Iran or the Communist government of the Soviet Union—underscores the conclusion that those who abuse power or privilege sow the seeds of their own destruction. Parallels exist in the business arena. Financial scandals around the turn of this century at Enron, WorldCom, Adelphia, HealthSouth, and other icons of US business provoked discretion-limiting laws and rulings, such as the Sarbanes-Oxley Act (2002). Similarly, the most recent Financial Crisis gave rise to the Dodd-Frank Wall Street Reform and Consumer Protection Act, passed by the US Congress in 2010.

## A RATIONAL ARGUMENT FOR CSR

CSR is a rational argument that focuses on the benefits to performance of avoiding external constraints. Adopting the path of least resistance with regard to issues of concern makes common and business

sense. In today's globalized world, where firms are empowered to enact change, CSR represents a means of anticipating and reflecting societal concerns to minimize operational and financial sanctions.

The rational argument for CSR therefore underpins the idea that firms voluntarily seek to meet the needs and concerns of their stakeholders. Firms that wait until they are forced to comply may find that the costs of doing so quickly become prohibitive. In the finance industry today, for example, the global bank HSBC has announced that “nearly 25,000 of its 258,000 employees, almost 10%, work in compliance” and that “compliance was a major driver in the 5% increase in operating expenses reported.”<sup>61</sup> Eventually, corporate transgressions result in heightened oversight that forces previously discretionary and ethical issues into the legal arena.

By adopting a rational argument for CSR, firms seek to interpret evolving societal values and stakeholder expectations and act to avoid future sanctions. Sensing that the tide of public opinion in the United States was moving in favor of regulating carbon emissions, for example, firms formed groups to lobby the government for change. The group BICEP (Business for Innovative Climate and Energy Policy)<sup>62</sup> was established by five firms with proactive records—Levi Strauss, Nike, Starbucks, Sun Microsystems, and Timberland. Similarly, the NACB (National Association of Cannabis Businesses) markets itself as “the first and only self-regulatory organization in U.S. cannabis.” The organization claims that membership for a firm “tells regulators, consumers and the

industry that you go beyond state compliance and operate at the highest levels of ethics and responsibility.”<sup>63</sup> Implementing a rational perspective, these firms realize it is in their interests to engage with regulators, rather than form a barrier to progress they see as inevitable. As the CEO of Duke Energy, the late Jim Rogers, succinctly put it when addressing the role of fossil fuels in fostering climate change, “If we are not at the table, we will be on the menu.”<sup>64</sup> In other words, genuine and proactive engagement to avoid unwelcome intrusion or help shape prospective legislation is an act of rational business.

### An Economic Argument for CSR

Building on the previous three arguments for CSR is the economic argument. In addition to avoiding ethical, moral, legal, and other societal sanctions, incorporating CSR into a firm’s operations and strategic planning offers a potential point of differentiation and competitive market advantage upon which future success can be built.<sup>65</sup>

## AN ECONOMIC ARGUMENT FOR CSR

CSR is an argument of economic self-interest for business. CSR adds value because it allows firms to reflect the needs and concerns of their various stakeholder groups. By doing so, the firm is more likely to create greater value

and, as a result, retain the loyalty of those stakeholders. Simply put, CSR is a way of matching corporate operations with stakeholder values and expectations that are constantly evolving.

CSR influences all aspects of day-to-day operations. Everything a firm does causes it to interact with one or more of its stakeholder groups. As a result, companies are best served by building positive relationships with as many stakeholders as possible. Whether the firm is acting as an employer, a producer, a buyer, a supplier, or an investment, its attractiveness and success are increasingly linked to its values and culture. Concerning socially responsible investments (SRI), for example, “more than one out of every five dollars under professional management in the United States—\$8.72 trillion or more—[is] invested according to SRI strategies.”<sup>66</sup> Even for those who believe that the only purpose of a firm is to increase its shareholders’ wealth, being perceived as socially *irresponsible* risks losing access to a significant (and growing) segment of investors and their capital.

This book expounds the economic argument for CSR. It is the strongest of the four (ethical, moral, rational, and economic) arguments supporting CSR, due partly to its reliance on what we know about human psychology and economic theory. Rather than seeking to subvert patterns of exchange that have evolved over centuries, the economic argument for CSR operates at the intersection of the firm’s self-interest and the broader well-being of society. Ultimately, indeed, there is no difference between the two. If stakeholders are willing to reward the behavior they seek from firms, then it is those firms’ best interests to provide stakeholders with what they want. As long as this basic formula

holds on both sides, value will be optimized and distributed broadly across society.<sup>67</sup> Of course, what is simple to say is often difficult to put into practice. This book exists to build a framework that firms can use to address the complex process of listening to, and seeking to meet, the conflicting interests of all their stakeholders.

An important distinction that helps explain the particular value of the economic argument is between an effective *business model* and a broader, more sustainable *model for (all) business*. In other words, rather than focusing on what works in isolation, it is more effective to establish what works economy-wide. The Body Shop, for example, has implemented a successful *business model* that subscribes to a moral argument for CSR. This activist organization is able to draw on support from the small percentage of the population that is aware and sufficiently responsive to a progressive social agenda, translating this support into economic success. It is a wonderful business, but its model is not one that all businesses can emulate. Ben & Jerry's is another example, as is Patagonia. These are all great firms, but they will not introduce meaningful change across the economy or globe. For that, we need to rely on corporations that operate on a sufficiently large scale to make a difference. In contrast, an economic argument for CSR seeks to build a broad *model for business* that recognizes the limited application of moral activism and, instead, searches for a standard that can be applied across all for-profit firms. The result is an approach to business that highlights the strategic benefits to the firm of seeking to create value for its stakeholders, broadly defined.

## Strategic CSR Debate

MOTION: There are no absolute ethical or moral standards.

### QUESTIONS FOR DISCUSSION AND REVIEW

1. What is the purpose of the for-profit firm? What value does it create for society?
2. Define *corporate social responsibility*. What arguments in favor of CSR seem most important to you? Are these factors prevalent among firms today, or are they rare?
3. What are the four responsibilities of a firm outlined in Archie Carroll's *pyramid of CSR* model? Illustrate your definitions of each level with corporate examples.
4. Milton Friedman stated that "few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible."<sup>68</sup> What are two arguments in support of his assertion and two against?
5. Why does this book favor the economic argument for CSR? Why is this argument *better* than the ethical, moral, or rational arguments for CSR? Do you agree?