

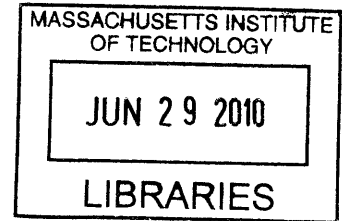
Corporate Social Responsibility (CSR): Responsibility or Innovation? An analysis of the feedback between CSR activities and the expectations placed upon corporations

by

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Submitted to the Engineering Systems Division
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ABSTRACT

This thesis uses case study and interview data to present a framework for analyzing corporate behavior in order to define corporate social responsibility (CSR). It answers the question: Can corporations tie corporate social responsibility to the profit-making mission, and, if so, how? We define CSR as the actions that exceed the expectations placed upon the corporation. We demonstrate that the level of expectations, separating social irresponsibility from responsibility, is dynamic—changing over time and by region. This level is influenced by the maximum of three forces: social norms, market forces, regulatory standards. Actions that exceed expectations, what we consider CSR, are then categorized here in three broad groups:

- 1) Philanthropic: projects dealing with social good that have little or no relation to the corporate mission.
- 2) Strategic: initiatives that align and advance social and business goals simultaneously.
- 3) Social: actions typically addressed by social entrepreneurship designed and executed predominantly to target a social need.

Finally, we validate the CSR framework and introduce areas of value-creation to be considered by corporations when making the decision to perform CSR. While CSR can be profitable and yield value, many things must be considered prior to engaging in CSR.

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Dedicated with love to Amanda, my god-daughter. Always dream big and then go one step even further.

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Chapter 1

Introduction

In an age of rising environmental concerns, financial recession, and political change, companies are increasing corporate social responsibility (CSR) activities in the face of these complex challenges. Companies are under pressure from governments, society, and markets to play a leading role in developing and undertaking society-wide solutions that address and exceed these pressures. CSR initiatives attempt to fulfill business's "contract with society"¹, by addressing environmental, social and governance issues. Executives, investors, regulators, and the public have seen CSR programs prevent or mitigate corporate scandals, enhance corporate competitiveness, and build corporate reputations, while also having profound positive social and environmental impacts. The conventional wisdom is that a company should merely meet the expectations placed upon it, and that CSR expectations are static; therefore, the same action will continue to yield the same benefit and result indefinitely. However, as companies develop a capacity to perform CSR activities and achieve sustainable benefits from performing them, CSR actions become expected and new pressure is applied on corporations to not only meet expectations but to exceed them.

This thesis uses case study methodology and interview data to present a framework for analyzing corporate behavior in order to determine those actions that should be considered CSR. We define CSR as socially-oriented actions that exceed the expectations placed upon the corporation by social norms, market competition and legal regulations. Because this level of expectations can change, what counts as CSR also changes. We examine how and why this level fluctuates over time and by region. This level of expectation is set by the maximum of three forces: social norms, market competition, and legal regulations. Actions that exceed expectations, what we consider CSR, are then categorized here in three broad groups:

¹ Discussion of the integrated social contract theory in section 1.2.1.2

1) **Philanthropic:** projects dealing with social good that have little or no relation to the corporate mission.

2) **Strategic:** initiatives that align and advance social and business goals simultaneously.

3) **Social:** actions typically addressed by social entrepreneurship designed and executed to predominantly target a social need.

Finally, we validate the CSR framework and introduce areas of value-creation to be considered by corporations when making the decision to perform CSR. While CSR can be profitable and yield value, many things must be considered prior to engaging in CSR.

1.1 Thesis Outline

This thesis challenges the conventional wisdom and answers the questions: Can corporations tie corporate social responsibility to the profit-making mission, and, if so, how? This thesis begins with a brief literature review of CSR and then develops a CSR framework based on six case studies. It later validates the framework using interview and case study data.

1. **Introduction.** Traditional and current CSR methodologies and frameworks are presented, establishing how CSR has evolved through the years, including how expectations and regulations are established and what risks are associated with engaging in CSR activities.
2. **Setting Expectations.** Chapter 2 shows how expectations are set for corporations and provides three in-depth examples which illustrate the three forces that influence expectations – social, market, and legal – and how they interact.
3. **Doing Good: Beyond Expectations.** Chapter 3 shows why, in order to be CSR, only actions performed above the level of expectation should be considered. It presents the three categories of CSR – philanthropic, strategic, and social – and examples of each.
4. **Why Perform CSR?** Chapter 4 explores the varying motives behind performing CSR and presents examples of short- and long-term benefits.
5. **Raising the Bar.** Chapter 5 illustrates how CSR can challenge business goals and create an ever increasing feedback loop that becomes a “race to the top” as competitors try to

out-do each other.

6. **Tradeoffs and Value.** Does CSR pay? Chapter 6 presents the tradeoffs that companies must consider when performing CSR activities and potential areas of value creation.
7. **Conclusion.** Chapter 7 summarizes the findings and contributions achieved as well as their implication for the future evolution of corporate social responsibility as CSR transcends from a responsibility to a potential opportunity for innovation.

1.2 Literature Review/Background

The notion of corporate social responsibility (CSR) has been open to various interpretations, reflecting the relationship of business and society at different times in history (Bichta, 2003). The study of CSR enjoys over a 50-year history: dating back to Chester Barnard's (1938) "the Functions of the Executive," J.M Clark's (1939) "Social Control of Business," Theodore Kreps' (1940) "Measurements of the Social Performance of Business," and Howard Bowen's (1953) "The Responsibility of a Businessman." These early works placed emphasis on the business leader's social conscience, rather than on the company itself. This led to the belief that CSR was determined by CEO and executive goodwill (Carroll, 1999). At the time, CSR consisted of adopting generalized philanthropic policy with little or no concern for its effect on return on investment (ROI).

While ethical analysis of CSR initially focused on the individual businessman, it has shifted over time to the organizational level (Epstein, 1987). Contemporary theories recognize and link the benefits of social responsibility to the sustainability of the corporation. Corporations, as a legal entity, can produce value from CSR activities that individuals, such as the executives, shareholders and employees do not have the capacity to gain themselves with their own money. While an individual can volunteer or donate money to a local cause, a company can transform the socio-economic conditions of a city by hiring workers, paying taxes and conducting business activities which include CSR initiatives.

Still, some argue that corporations will never be socially responsible and are simply acting "as

if” they are (Johnson, 1971). Some critics of CSR state that CSR is just a marketing tactic and that companies “act” socially responsible simply to increase sales. They believe that any social good that occurs during the course of profit-seeking actions is unintended and simply a by-product. While this might still be the case for some companies, other companies are realizing that by targeting social and economic issues, they can derive mutual value from the socially beneficial “by-product”.

1.2.1 Dominant Theories and Approaches

What “responsibilities” corporations have, if any, has been in question since CSR was introduced. Two schools of thought, each with its own frameworks and approaches, emerged throughout the literature:

- (1) Meeting objectives that produce long-term profits
- (2) Integrating social and stakeholder demands and contributing to society

While they initially seem to be mutually exclusive, there are instances of overlap in the two theories. The first focuses on maximizing profits while the second focuses on stakeholder relationships and social contributions. When companies leverage stakeholder relationships to produce value for society and the company, they satisfy both conditions. Although this might not always be the case for every corporate decision, when considering new CSR initiatives, the opportunity to satisfy social and business objectives may present itself, if companies consciously look for the opportunity.

1.2.1.1 Meeting objectives that produce long-term profits

“The only one responsibility of business toward society is the maximization of profits to the shareholders within the legal framework and the ethical customs of the country”

Milton Friedman 1970

Milton Friedman’s approach, seeking and producing long-term profits, focuses on CSR as a

means of maximizing value and profit; that is, any value created by CSR should in turn yield a higher valuation for the company, or the CSR initiative should not be done. The Milton Friedman Shareholder Theory includes maximizing the shareholder value, strategies for competitive advantage and cause-related marketing in which some value is reciprocated to the corporation as a result of its initial investment.

Milton Friedman's Shareholder Theory

On September 13, 1970, Milton Friedman wrote an article in the *New York Times* entitled: "The Social Responsibility of Business is to Increase its Profits." In the article, Friedman argues that assigning responsibility to a corporation implies treating the corporation as an individual person. If responsibilities are given to the corporation, those responsibilities must transfer to the leadership and executives which make decisions on behalf of the corporation. CEOs and corporate executives are simply the employees of the shareholders and have a binding fiduciary duty to them of maximizing shareholder profits. If they do not, the corporate leadership will be fired by either the current shareholders or the future shareholders when the stock value declines. If a CEO decides to spend corporate money on anything aside from what drives the maximum profit, it would be like imposing a tax on the income for the corporation to spend where it sees fit. Governments levy taxes because they are experts at addressing social issues. Corporations are experts in business; therefore, they should do what they do best - address business issues. If shareholders or corporate employees feel like investing in social issues, they should invest their own money, not have their charitable giving dictated by a corporate decision (Smith, 2003).

R. Edward Freeman's Stakeholder Theory

Over a decade after Friedman's *New York Times* article, R. Edward Freeman developed the stakeholder theory in his book: *Strategic Management: A Stakeholder Approach*. His theory sought to broaden the concept of strategic management beyond its traditional economic roots, by defining stakeholders as "any group or individual who is affected by or can affect the achievement of an organization's objectives." The stakeholder theory states that for any business to be successful it needs to create value for all of its stakeholders; the interests of stakeholders and the firm's are interrelated and managers and entrepreneurs must determine how to align all

of those interests in the same direction (Institute for Corporate Ethics, 2009). The purpose of stakeholder management is to devise methods to manage the myriad groups and relationships that result from corporate activity. In a sense, corporations could be said to have a responsibility to maintain a relationship with their stakeholders, which Freeman recognizes as strategic business practices.

CSR activities should not be discounted as a profit-sacrificing action. Friedman later states, management's role is "to make as much money as possible while conforming to the basic rules of society, both those embodied in the law and those embodied in ethical custom" (Friedman, 1970). By acknowledging law and ethical customs, Friedman acknowledges the existence of other business drivers aside from economic and profit, such as the influence of stakeholders on corporate decisions. If CSR activities are beneficial to corporate stakeholders, they also have the potential to yield value back to the corporation.

1.2.1.2 Integrating social demands and contributing to society

Contributing to a society in an ethically correct manner is one of the foundations of Freeman's Stakeholder Theory, which states that "managers bear a fiduciary relationship to *stakeholders*" (Freeman, 2001). Stakeholders include shareholders, employees, suppliers, governments, communities, and environments that are influenced, either directly or indirectly, by the actions of the firm (Freeman and McVea, 2001). A corporation depends on society for its existence and therefore, social demands and expectations should be integrated with business objectives. Corporate Social Performance (CSP) attempts to measure corporate actions in terms of the social value and social welfare that they produce (Wood, 1991). Within this theory of CSP, is the notion that all humans have a set of global universal rights regardless of the regulations in the country of operation, where regulations undermine the universal rights of citizens, social norms or market forces will increase the level of rights given to those citizens.

Corporations, by being entities in society, are given a sense of corporate citizenship which inherently comes with responsibilities. Hence, businesses can be viewed as having a social contract with society, referred to as the "integrative social contract theory" (Donaldson, 1994).

By being a legal entity, the corporation is granted rights and duties, and the concept of moral responsibility, as it applies to people, translates to the corporate entity (Goodpaster and Mathews, 1982).

The principles of the stakeholder theory and the social contract between corporations and society are based on a strong sense of responsibility toward supporting and improving the local community and on the consideration for the environment. Social norms are intended to support and promote these responsibilities. As companies undertake such activities, they fulfill the contract with society and the expectations placed upon them by society. In order to sustainably continue these efforts, companies must also build a capacity to continue to perform such activities in the future.

1.2.2 Other Frameworks

In 1991, Archie B Carroll developed the “Pyramid of CSR”, shown in Figure 1.1, in an attempt to visualize the responsibilities of corporations. The Pyramid of CSR consists of four corporate responsibilities: Economic, Legal, Ethical, and Sustainability. Carroll's four categories, or domains, of CSR have been utilized by numerous theorists and empirical researchers. Several business and society, and business ethics texts have incorporated Carroll's CSR domains or have depicted the CSR Pyramid. This suggests that Carroll's CSR domains and pyramid framework remains a leading paradigm of CSR in the management field (Schwartz and Carroll, 2003).



Figure 1.1 – AB Carroll's Pyramid of CSR (Carroll, 1991)

Early CSR models, such as the one illustrated by Carroll, placed economic success and profitability at the base of the pyramid - as an enabler to perform CSR. This gives the impression that CSR is a hierarchical progression. Although there is considerable value in this approach, the use of a pyramid framework to depict CSR domains may be confusing or inappropriate. Limitations in the hierarchical approach include: the interpretation that the higher in the pyramid, how much more important or difficult to achieve something might be, or thinking that Sustainability Responsibilities (top) are unrelated to Economic Responsibilities (bottom). In addition the pyramid makes no attempt at showing the interactions and complementary features of different parts of the pyramid (Schwartz and Carroll, 2003).

The pyramid structure tends to imply that companies should start at the bottom with economic responsibilities, and escalate to sustainability at the top; this is not always the case. If economic

success and legal obligations are independent of each other and economic responsibilities were addressed prior to legal responsibilities, it would allow for illegal acts and companies, such as Napster², to exist. In practice, it must be considered impossible for corporations to make a profit by committing illegal acts³. Although these actions might take place in the short-term, the fact that they are illegal makes them unsustainable in the long-term business environment.

The realization in 2003 of the limitations of the CSR pyramid, and the proposals to amend, modify, and improve the hierarchical model led to the development of the 3-domain approach in Figure 1.2 (Schwartz and Carroll 2003). The new approach converted the four tiers of the pyramid into three interrelated domains: Economic / Legal / Ethical. This interrelation of corporate responsibility from various sources is also evident throughout future theories such as, the triple bottom line⁴, as well as the CSR framework presented in this thesis.

² Napster was a peer-to-peer music and file sharing service. The service operated between June 1999 and July 2001. Its technology allowed people to easily share their MP3 files with other participants, bypassing the established market for such songs and thus leading to the music industry's accusations of massive copyright violations. The service was subsequently shut down by court order. The brand and logo have been purchased and are now being used by a legal, pay service.

³ A later analysis shows how “legality” is dependent on the governmental structure within which a corporation operates and that what is considered “legal” in a developing country might not be considered “moral” or socially acceptable in other countries where the company operates – leading to higher expectations than those held by regulation alone.

⁴ Triple bottom line accounting means expanding the traditional economic reporting framework to take into account ecological and social performance in addition to financial performance.

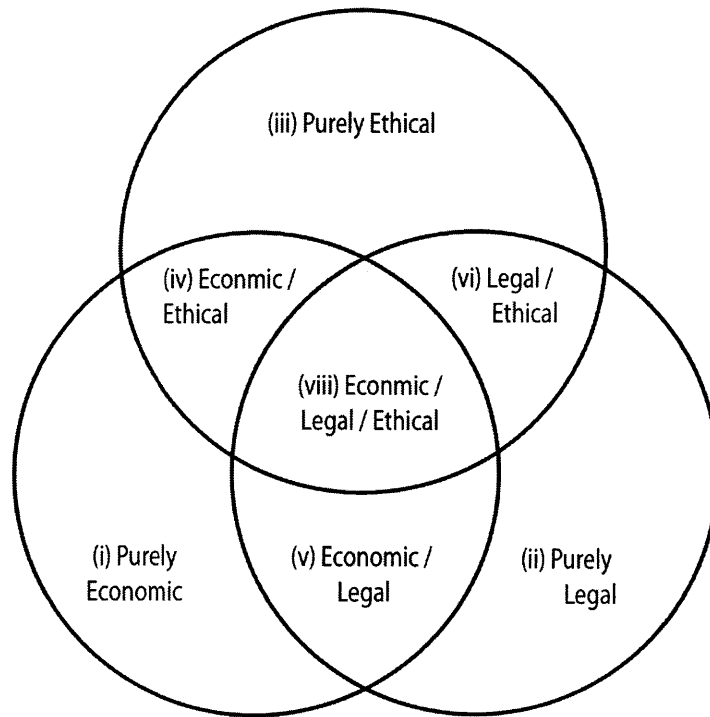


Figure 1.2 – Three-Domain Model of CSR (Schwartz and Carroll, 2003)

In 2006, Michael Porter and Mark Kramer (Porter, 2006) proposed a CSR framework, Figure 1.3, based on leveraging the interdependence of business and society. It shifted CSR from a paradigm where business was against society to a mutually beneficial model where corporations could strategically align corporate goals with social welfare. The framework categorizes three general ways for corporations to intersect with society: first, "Generic Social Issues (which we later refer to as philanthropy) where a company's operations do not significantly impact society and the issue is not material to the company's long-term competitiveness; second, "Value Chain Social Impacts" where a company's normal operations significantly impact society; and third, "Social Dimensions of Competitive Context," where social issues affect the underlying drivers of a company's competitiveness .

| Corporate Involvement in Society: A Strategic Approach | | |
|---|--|--|
| Generic Social Impact | Value Chain Social Impact | Social Dimensions of Competitive Context |
| Good Citizenship | Mitigate harm from value chain activities | Strategic philanthropy that leverages capabilities to improve salient areas of competitive context |
| Responsive CSR | Transform value chain activities to benefit society while reinforcing strategy | Strategic CSR |

Figure 1.3 – Porter and Kramer’s Strategic CSR Framework (2006)

Porter and Kramer then divide these three categories into: Responsive CSR and Strategic CSR. Responsive CSR addresses generic issues through good corporate citizenship that can add value to the corporation by mitigating harm from negative corporate impacts on society (Sam Fullerton, 1996). Responsive CSR is reactive in nature and therefore not considered CSR in this thesis’ proposed framework. Strategic CSR is more deliberate and proactive, as the name implies. Strategic CSR activities benefit society while simultaneously reinforcing the core business and also advancing strategic giving that leverages areas of competitiveness. This thesis elaborates and builds upon the notion of Strategic CSR and incorporates it in the CSR framework.

In early 2000, Bob Willard and Peter Senge integrated environmental concerns with traditional CSR issues and approaches. Environmental sustainability presents new and interesting challenges for corporations. Aside from the social pressure to be eco-friendly, there is also increased regulatory pressure. By performing CSR and in essence, self-regulation, corporations can preempt and possibly delay more stringent regulations and reduce government oversight. By

considering the environment as a stakeholder, corporations take into account the threat of limited resources and over-consumption and its affect on future business decisions.

The frameworks by Bob Willard (2005) and Peter Senge (2008) took into account the reactive and proactive nature of CSR. They acknowledged that reactive corporate decisions are carried out due to regulatory pressure or a “Public Relations Crisis”, while proactive actions can be credited to the potential for future business opportunities or CEO passion.



Figure 1.4 – Bob Willard’s (2005) adopted by Peter Senge (2008) Five Emerging Drivers and Stages to achieving sustainability

While the model, Figure 1.4, represents a 5-stage hierarchical progression, Senge recognizes that some companies emerge as level 5 while others must progress up the stages. Those companies that emerge at level 5 Purpose / Passions (which we later refer to as social enterprises) are mission-driven companies that are established for the purpose of addressing social concerns such as poverty, equity and environmental issues.

The framework alludes at an expected level of compliance which companies must meet: actions below level 3 are reactionary and above level 3 are proactive. While the CSR framework in this

thesis recognizes a proactive level, it differs in that responsive and reactive actions are explicitly not considered CSR as corporations are legally or socially obligated to perform these actions and therefore, performing these actions is expected behavior and business-as-usual.

1.3 Challenges and Risks associated with CSR

Taking responsibility for the environment and public “commons” bring about added complications for corporations. By engaging in CSR activities with shared stakeholders, such as the environment / planet, corporate actions and initiatives produce spillover benefits. Spillover benefits refer to value gained by others that did not invest in the initiative; this leads to a tragedy of the commons and free rider issues.

A tragedy of the commons infers that, while each company can save money by not investing in the environment in the short-term, the result of all other companies doing the same will degrade the industry’s ability to do business. This classic example of a tragedy of the commons, where a lack of rights exists, reduces the incentive for corporations to invest.

In economics, the free rider issue refers to a situation where some individuals in a population either consume more than their fair share of a common resource, or pay less than their fair share of the cost of a common resource. When one company pays for and performs CSR, all companies could benefit, including direct competitors; the competitors are considered free-riders. This may lead to companies deciding not to invest in activities with spillover that will yield benefits to other companies. For example, a marketing campaign for a specific brand or company is clear and direct; while a campaign to encourage recycling can have a large spillover due to the broad impact it will have beyond those that paid for the campaign.

1.4 Regulations and Expectations

The “social responsibilities” of corporations cited in the literature seem to always coincide with

public expectations and, over time, are incorporated into regulations⁵ or market standards.⁶

However, it takes an indefinite amount of time for these activities to go from being considered CSR to becoming expected. When the companies first started to perform them, the companies were not expected to do so, which is why it was considered CSR at the time. The activities then became expectations as the companies proved that they were capable of successfully performing the actions.

While regulations provide a clear and obligatory level at which corporations must operate, social norms and market forces can at times exceed the level set by regulations. This leads to social expectations or market expectations that exceed what is legally required of a company. Consequently, complying with legal requirements alone is not enough because not all public expectations are protected by laws.

In contrast to regulations, expectations are formed by many different factors: legal restrictions promulgated by a government authority, self-regulation by an industry such as, through a trade association, social norms promoted by NGOs⁷, communities or consumers, and market co-regulation through industry standards and partnerships. This thesis will focus on three forces that influence expectations – social norms, market competition and legal regulations.

⁵ Regulation is defined as "controlling human or societal behavior by rules or restrictions" (Koops, 2006).

⁶ Market standards are public expectations that are being incorporated into regulations or standards over time and give rise to the public policy approach of CSR. This approach provides sources and guidelines for companies to follow (Bichta, 2003).

⁷ A non-governmental organization (NGO) is a type of non-profit organization that works to promote human good while operating separately from any national government.

Chapter 2

Setting Expectations

Society and consumers are holding corporations to "a new and increasingly rigorous set of standards."

- Gollin Harris 2005

Companies are under pressure by society, markets, and regulators to perform disaster relief efforts, participate in charitable giving, protect the environment, offer employee health care benefits, and help solve community issues – while remaining profitable, staying in business, and complying with regulations. Meeting these expectations grants companies the license to operate⁸ (Porter, 2006). Without first meeting these expectations and thus achieving a license to operate, companies cannot begin to perform CSR initiatives.

The expectations that corporations must meet are formed by three forces: Social Norms (S), Market (M), and Legal (L). Social expectations are the moral expectations traditionally laid out by NGOs, consumers, the local community and the various stakeholders. Market expectations are primarily defined by the actions of competitors, new entrants, market standards and technological state-of-the-art. Legal obligations are forced and enforced by local and international regulatory bodies (mostly governments) which define legal and illegal corporate behavior.

Law (L), orders people to behave in certain ways; it threatens punishment if they do not obey. Laws are known ahead of time and in most cases, have consequences if violated. Social norms (S) are behavioral cues that influence expectations by threatening punishment ex post, after the fact. But unlike law, the punishments of norms are not centralized. Norms are enforced, if at all,

⁸ License to operate means that every company needs tacit or explicit permission from governments, communities, and numerous other stakeholders to do business.

by a community, not by a government. Markets (M) demonstrate influence primarily through price and competition. Undoubtedly, the market is only able to operate within the constraints of law and social norms: property and contract law govern markets and as a result, markets operate within the domain permitted by social norms (Lessig, 1998).

These three forces (S, M, L) interact and set corporate expectations, the highest of which sets the level at which corporations must operate. That is to say, expectations are defined as:

$$\text{MAX}[S,M,L] = \text{EXPECTATIONS}$$

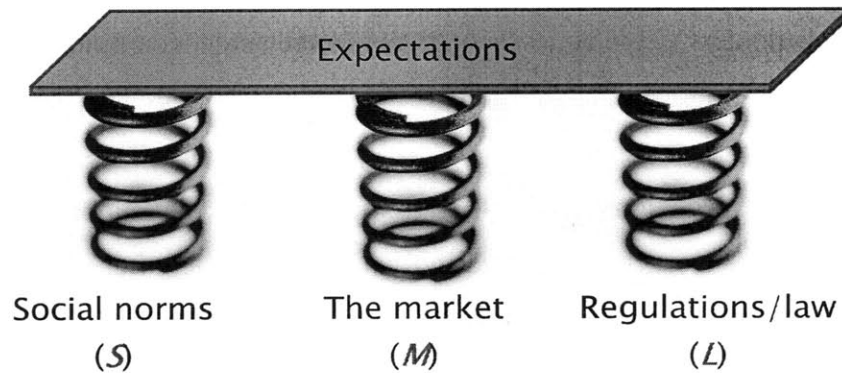


Figure 2.1 – The three forces – Social, Market and Law – that influence the expectations on corporations

The three forces (S, M, L) are the foundation on which expectations are set. The maximum of which defines the level of expectation that corporations must meet; falling short of this level is not only irresponsible, in some cases, it is illegal. Therefore, actions cannot be classified as CSR unless they meet and exceed the expectations placed on the corporation.

2.1 Social Norms

“Society has certain expectations for appropriate business behavior and outcomes.”
-DL Wood 1991

Social norms are the behavioral expectations and cues within a society or group. They are the rules that a group uses for determining appropriate and inappropriate values, beliefs, attitudes and behaviors. Social norms vary by region, culture and over time. For CSR initiatives, social norms can make the difference between praise and criticism.

In 1978, William Frederick recognized the impact of social expectation on firms when he outlined the managerial concept of corporate social responsiveness. He defined corporate social responsiveness as “the capacity of a corporation to respond to social pressures” (Frederick, 1978). Many of the theories and arguments made by Frederick were later incorporated into Freeman’s stakeholder theory, which highlights the importance of identifying and efficiently managing stakeholder expectations that influence business (Freeman and McVea 2001). It also reiterates the point that the act of a corporation responding to a crisis is expected behavior by the corporation’s stakeholders. Companies should not be rewarded or praised for responding to social norms; they are simply doing their job.

Social pressure and expectations, from NGOs, employees, media, suppliers, stockholders and other stakeholders, are categorized as social norms. For example, after recent natural disasters, the 2004 Thailand tsunami, the 2005 Hurricane Katrina, the 2009 Indonesian earthquake or the 2010 Haitian earthquake, corporations were *expected* to donate resources – time, money, services, etc. – to relief efforts, because they had done so in the past. Society expected corporations to respond for moral reasons and because corporations had established a precedent. As companies continue to expand globally, the stakeholder relationships and areas of influence also expand, and these new relationships translate into sources of pressure that must be acknowledged and managed (Muller and Whiteman, 2008).

Social norms can be established internally by a company through habits; for example, a local pizza place sponsoring a little league team year after year will create the expectation for sponsorship. Norms can also be established by the external stakeholders, such as consumers expecting quality products that are made in the USA. NGOs also apply stakeholder pressure on companies to reduce waste or cut pollution emissions; they are arguably voicing the beliefs of society. Labor unions have the ability to apply pressure from a social norm and market

perspective because of the way in which they are connected with society and across multiple companies in an industry.

A company's failure to meet social demands can result in a loss of business, consumer boycotts and negative publicity. Nike⁹ faced such consumer and NGO pressure for unacceptable labor practices¹⁰. In this case, regardless of whether the labor practices are legal (L) or competitive (M), they are nonconforming to and below the level expected by social norms (S). Nike eventually had to raise their operating standards to meet the expectations set by NGOs and consumers in the U.S., their home market, even though the factories were overseas.

2.1.1 Case Study: Meeting the bar set by Social Norms - Nike

"We believe that these are practices which the conscientious, good companies will follow in the 21st century...These moves do more than just set industry standards. They reflect who we are as a company."

- Philip H. Knight, Nike's chairman

In the 1990s, Nike's strategy involved taking advantage of global sourcing opportunities to produce lower cost products which, while financially rewarding, created significant public relations dilemmas for the company. Activists increasingly criticized labor practices at Nike's contract factories, alleging that workers were systematically subjected to adverse conditions including unjust pay practices, forced overtime, verbal and physical abuse, sexual harassment, interference with unionization, and excessive toxic chemical exposure. Nike soon came under attack as its overseas labor practices were exposed. In 1993, CBS aired a report about workers' struggles at Nike's Indonesian suppliers. In 1994, harsh criticism of the company's practices

⁹ Nike, Inc. (NYSE: NKE) is a major publicly traded sportswear and equipment supplier based in the United States. It is the world's leading supplier of athletic shoes and apparel and a major manufacturer of sports equipment. As of 2008, it employed more than 30,000 people worldwide.

¹⁰ In the early 1990s, Nike came under attack as the company's overseas labor practices were exposed. Activists increasingly criticized labor practices at Nike's contract factories, alleging workers were systematically subjected to adverse conditions including unjust pay practices, forced overtime, verbal and physical abuse, sexual harassment, interference with unionization, and excessive toxic chemical exposure.

appeared in an array of different publications: The New Republic, Rolling Stone, The New York Times, Foreign Affairs, and The Economist (Locke, 2003). Nike first denied responsibility for contract factory workers, claiming, for example, that it could not prevent Asian subcontractors from employing young children. However, as one senior manager noted, the company's denial not only failed to silence the critics, but "if anything, it raised the volume higher."

CEO Phil Knight acknowledged in a 1998 National Press Club Speech that "the Nike product has become synonymous with slave wages, forced overtime, and arbitrary abuse," which led Nike to address its labor issues in a more strategic way. Nike's hands-off approach changed as Nike formulated a Code of Conduct for its suppliers that required them to observe basic labor and environmental/health standards, despite the lack of such standards and enforcement by the factories' local governments. Nike increased the minimum age of footwear factory workers to 18 and all other workers (in apparel, equipment) to 16. It also insisted that all footwear suppliers adopt U.S. Occupational Safety and Health Administration (OSHA) standards for indoor air quality.

In 1998, Nike also consolidated corporate responsibility (CR) functions under a new Vice President position, and began studying the reasons behind its suppliers' non-compliance with its Code of Conduct. One conclusion that emerged was that Nike's internal systems encouraged the very behaviors it wanted to eliminate. For example, procurement teams' bonuses were set by price, quality, and delivery speed of orders, implicitly encouraging them to ignore suppliers' code compliance. By the late 1990s, Nike realized that CR had to be a core part of Nike's business. In fact, a quick review of some of Nike's efforts in the area of labor and environmental/health standards shows that the company is serious about doing the right thing (Locke, 2003). Today, a staff of 97 inspects several hundred factories a year, grades them on labor standards, and works with managers to improve problems. Nike also allows random factory inspections by the Fair Labor Association (Bernstein, 2004).

Regardless of market or legal forces, Nike received pressure primarily from consumers and NGOs to comply with what was considered acceptable business practices in the U.S. Although the market and regulatory standards in foreign factories were low, in Nike's case, expectations

were dominated by social norms which were much higher. This example shows the extent to which companies face pressure to meet the highest of the three forces (S,M,L).

2.2 Market Demands

As a foundational element for building expectations, market forces have two facets. The first facet is the pressure to **offer more**, such as employee benefits, to help attract better talent. By looking at competitors, companies can develop a competitive market-based salary and benefits package to attract employees. Companies are expected to be competitive; therefore, the second facet is that of **reducing costs** in order to remain competitive in the market. An example of this would be for companies to reduce waste or energy consumption. Although these two might seem contradictory, the final goal of both is to find the optimal allocation of resources to keep the corporation competitive.

Market demands encompass the notion of individuals and firms competing for a greater share of a market to sell or buy goods under certain terms, conditions and standards. The nature and degree of competition hinge on five forces: the threat of new entrants, the bargaining power of customers, the bargaining power of suppliers, the threat of substitute products or services, and the “jockeying” among current contestants. These five forces act together to define the expectations on the corporation from a market perspective (Porter, 1979). In a highly competitive market, many times, a greater emphasis is placed on market expectations than on social norms - as was the case with Nike prior to the 1990s.

Market demand was described by Adam Smith in *The Wealth of Nations* (1776) and by subsequent economists as: “the allocating of productive resources to their most highly-valued uses” in order to encourage efficiency and competition. In this definition, allocating a resource to its “most highly-valued use” is expected of the company, but performing CSR is not – even though, a CSR initiative can eventually lead to a new and more “highly-valued use”. For example, if a company had a best-selling product with high margins in the market, that product would be considered high-value and resources should be dedicated to manufacturing and selling that product prior to selling any others. This differs from CSR activities which exceed market

demands and might entail creating a new product that could potentially yield higher value than the best-selling product but currently has no demand or use in the market. The market does not expect such a product and therefore, performing CSR activities comes with both risks and potential rewards.

2.2.1 Case Study: Market pressure to meet the bar - Seventh Generation and Clorox

Seventh Generation, founded in 1988, is a company committed to becoming “the world's most trusted brand for authentic, safe, and environmentally responsible products for a healthy home” (Seventh Generation). For over 20 years, Seventh Generation has been at the forefront of a cultural change in consumer behavior and business ethics. Until 2000, Seventh Generation operated in a relatively small market with little competition - selling to natural and organic specialty stores and boutiques. Its primary competition came from relatively small companies such as, San Francisco-based, Method Products.

In 2008, Clorox, a major cleaning products manufacturer since 1928 launched a new product line – Green Works. When The Clorox Company launched Green Works, they had a goal to take natural cleaning mainstream, making it more accessible and affordable without compromising cleaning performance, and it did just that - Green Works soon became the #1 brand in natural cleaning products after acquiring 42% of the market (Clorox Press Release 2009). This led to Clorox placing pressure on Seventh Generation to reduce prices.

Prior to Clorox Green Works entering the market, Seventh Generation had the ability to set a premium price by appealing to consumers through its altruism and environmental awareness - the social norms (S) domain. Seventh Generations now has to compete on price (M) with much larger multi-national competitors that are capable of producing similar products at a lower cost. In this case, Seventh Generation created a social expectation for providing “green” and eco-friendly products, and in turn, its competitors produced “green” and eco-friendly products and applied market pressure in return.

2.3 Law

The business corporation “is obligated to the same extent as a natural person to act within the boundaries set by the law”. i.e. to obey the law.

Epstein 1987

Laws and regulations are the reason why we no longer see the advertisements of the Marlboro Man¹¹ smoking and are constantly reminded to “drink responsibly”. Law is a system of rules and policies enforced through a set of institutions that shapes politics, economics and society, while serving as a primary social mediator of relations between people and legal entities. Law is exemplified by regulations, standards, and expectations that companies are obliged to follow. While obeying the law is an absolute, it is only as absolute as it can be enforced. Just as the other forces (S and M) set expectations that must later be enforced, compliance with regulations must be enforced. Corporate compliance is “based on the moral norm of obedience to law” (Epstein, 1987). Because of the sometimes lax enforcement of the law, there are instances when companies have profited by performing illegal acts. However, we must assume that the law cannot be broken and that although possibly delayed, it will be enforced. Corporations should not determine whether or not to obey a given legal rule on the basis of “rational” economic cost-benefit analysis (i.e. does it “pay” in financial terms to violate law?) (Rawls, 1971).

In general, corporations are founded within a legal system and may operate throughout various countries and regions, each with its own rules and regulations. A company incorporates within the country and state in which it will pay taxes and abide by the regulatory structure. In most cases, regulations support social and market forces. Companies must meet minimum wage regulations and are expected to do so. They also have the ability to exceed minimum wage to attract better employees. While paying minimum wage is an obligation, exceeding that amount is a CSR act, assuming that the market or social norms do not already expect that higher rate.

Although the norm is to obey the law, there are few instances when legal obligations and social

¹¹ The Marlboro Man is a figure used in tobacco advertising campaigns for Marlboro cigarettes.

pressure could interfere. In 2010, Google stated that it would no longer censor search results on its Chinese service. Google acknowledged that the decision "may well mean" the closure of Google.cn and its offices in China. By taking this stance, Google performed civil disobedience. While censoring search results in the U.S. is immoral and unethical, in China it is mandated by the Chinese Government. Aside from censoring search results, the Communist Party also blocks a number of swear words and sexual phrases that it believes to be "vulgar" or "harmful." Google initially agreed to censor "sensitive material" – such as details of human rights groups and references to the pro-democracy protests in Tiananmen Square in 1989 – when it launched Google.cn but has since changed its mind. In this case, meeting U.S. social norms of information transparency and freedom violates Chinese regulatory standards which could cause Google to lose its license to operate in China.

2.3.1 Case Study: Meeting legal obligations – Boeing and Sarbanes Oxley

“[Sarbanes Oxley is] the most far reaching reforms of American business practices since the time of Franklin D. Roosevelt.”

- President G.W. Bush

The Sarbanes–Oxley Act of 2002, commonly called Sarbox or SOX, is a United States federal law enacted on July 30, 2002, as a reaction to a number of major corporate and accounting scandals including those affecting Enron, Tyco International, Adelphia, Peregrine Systems and WorldCom. Those corporate accounting scandals caused millions of investors, consumers, and most organizations to lose their life savings and investment portfolios.

Sarbanes-Oxley was enacted to “protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes.” (Sarbanes-Oxley Act of 2002, section I). It requires corporate compliance with higher accounting standards, improved standards in corporate reporting and greater financial transparency. It does not apply to privately held companies. SOX mandates a set of internal procedures designed to ensure accurate financial disclosures.

One company that struggled with regulatory compliance was Boeing. In the two years after the SOX regulation passed, the time which companies were given to adjust and adapt to the new regulation, The Boeing Co. failed both internal and external audits to prove that it could properly protect its computer systems against manipulation, theft and fraud. The failings forced Boeing to scramble at the end of each year to assure that its financial information had not been affected. One employee described the first two years as "pure hell" for the information technology staff (Lathrop, 2007).

Companies have been monitoring their computer systems for years - but under Sarbanes-Oxley, it was the first time that all public companies¹² were required by law to do so as a part of a company's "internal control over financial reporting."

That control requirement, often nicknamed "404 compliance" after its corresponding part of the law, has been the most controversial and expensive aspect of Sarbanes-Oxley. Federal rules are now under review because many executives have bristled at the soaring costs of information technology compliance. The continuing effort to fix the problem has cost millions of dollars. Boeing has had a full-time staff of dozens and, at times, up to 65 consultants charging from \$115 to \$500 per hour, engaged in testing the systems that affect financial reporting to prove it can lock its computer doors (Lathrop, 2007).

When companies such as Enron, Tyco International, Adelphia, Peregrine Systems and WorldCom committed fraud, it was evident that self-monitoring and social norms did not provide enough accountability. Corporate violation of the law, led to an increase in regulatory standards. Social uproar and a re-examination of the lax accounting laws during the accounting scandals also influenced the regulatory measures to significantly increase.

As the regulations became more stringent, expectations rose, which companies had to comply with. Publicly held companies, that prior to SOX met legal requirements, found themselves in

¹² A public company or publicly traded company is a company that has permission to offer its registered securities (stock, bonds, etc.) for sale to the general public, typically through a stock exchange.

non-compliance after SOX's passage. Companies that did not want to comply with the new regulation faced two options: physically move elsewhere¹³, where they would be operating at an acceptable level of expectation, or go from being a publicly held company to a privately held¹⁴ company because the regulation would not apply.

2.4 Developing Expectations in Developing Countries

While social norms, markets and regulations are universally present in all societies, expectations are spatially and regionally dependent. The three forces (S,M,L) interact and the absence of one force in a particular region can allow for another to set expectations. In the absence of regulatory standards, market and social forces set expectations. The opposite can also be true, such as with minimum wage laws where social welfare depends on the minimum regulatory standards in the absence of high market or social demands.

The shipping industry is known for registering their vessels in countries that they can take advantage of lax regulatory standards. Registering in the U.S. would require that they meet higher and more costly standards than registering at Liberia, for instance, where most ships are registered. While this might not be the most socially optimal case, the companies register their ships where expectations are the lowest and rely on the fact that social groups in the U.S. have not targeted them strongly.

Outsourcing of labor has tried to take advantage of the same benefits with much less success. While regulatory standards are lower in developing countries, social norms in the U.S. set expectations for how "fairly" employees should be treated - regardless of the laws in developing countries. In this case, companies focusing solely on the established legal limit could cause them to overlook the social norms of what is "fair" and expected of them

¹³ When the regulation passed, companies had to meet the new standard or face fines. Some companies moved overseas to London, where the Financial Services Authority regulates the financial sector less stringently.

¹⁴ A privately held company or close corporation is a business company owned either by non-governmental organizations or by a relatively small number of holders who do not trade the stock publicly on the stock market. Other terms for a privately held company are unquoted company and unlisted company.

Both industries utilize a similar strategy with varying levels of success. The market and legal demands in both cases are similar. The difference between the two is the level of attention given by social norms. Where the apparel and retail companies have been scrutinized severely for their outsourcing, technology companies and the shipping industry has enjoyed less media attention. While many reasons for this might exist, the most important is that expectations and the three forces (S,M,L) fluctuate, depending on a region or an industry.

2.5 Clarity of Expectation

One obstacle when dealing with the social, market, and regulatory / legal forces is the lack of a bright line¹⁵ to determine the precise level expected. The level of certainty and the ability to define each force fades from social norm to regulations, as shown in Figure 2.2. Also, the fact that the three forces are interrelated in setting expectations demonstrates the importance of determining expectations as opposed to focusing on each individual force.

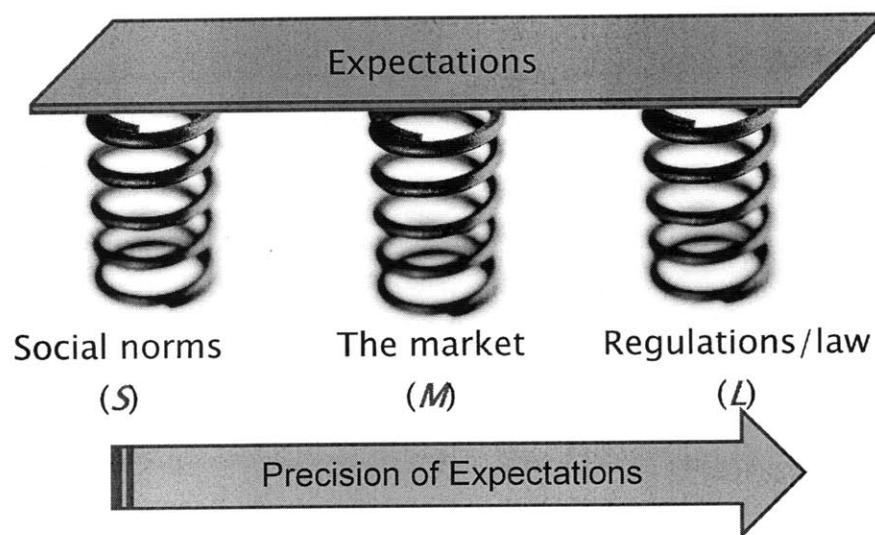


Figure 2.2 – Precision of Expectations

¹⁵ A bright-line rule (or bright-line test) is a clearly defined rule or standard, generally used in law, composed of objective factors, which leaves little or no room for varying interpretation.

Regulations are the easiest to determine, followed by market expectations and social norms, being the most abstract. Legal obligations are very precise and clear, as are the consequences for disobedience. Market trends and competitors' goals are not as clear as regulation, but available after some due diligence. Market expectations can be less clear than laws due to trade secrets and the market's competitive nature. Market expectations can also be relatively open in the case of cooperative standards or collaboration among industry partners. Social norms rarely have a clear or universal platform on which to be gauged. Determining social norms is the most difficult and abstract. In some cases, social norms are not known and understood until they are violated. Working with NGOs and being involved in the community can help mitigate some of the risk but norms can change often and with little, if any, warning.

2.6 Going from meeting expectations to CSR

Once expectations from S,M,L have been met, companies can voluntarily decide to perform CSR activities. Their actions and initiative will fall within three categories: social, strategic, and philanthropic; each with varying levels of alignment with the corporate mission and core business.

While CSR activities may indicate some corporate moral values or motivations, it does not define the entire company. CSR initiatives should be analyzed as independent activities and only as one piece of the corporation's overall impact.

Chapter 3

Doing Good: Beyond Expectations

“CSR is going above the lowest common denominator...”

-Henry Mintzberg 1983

Henry Mintzberg (1983) stated that CSR superseded the limits to the legalistic approaches and describes the lack of CSR as allowing corporate behavior to “drop to the lowest common denominator” (Mintzberg, 1983). Later, Donald Siegel (2007) stated that corporate social responsibility occurs when firms engage in activity that appears to advance a social agenda beyond that which is required by law (Siegel and Vitaliano, 2007). Legal obligations, market forces and social norms establish the level at which a company is expected to operate; going above that level of expectations is CSR.

Unfortunately, the term Corporate Social Responsibility has become a catch-all phrase for actions such as, efficiency or waste reduction, which companies have been expected to achieve all along. Those examples identify what companies should do to stay in business and are not CSR; they are expected as discussed in Chapter 2. In order to be considered socially responsible, companies need to go beyond those expectations and, in some cases, expose themselves to the risk¹⁶ associated with unprecedented, new initiatives. CSR actions can be categorized into three categories: philanthropy, strategic and social.. Philanthropic CSR is done out of benevolence for a charitable cause with little to no alignment with the corporation’s core mission. Strategic CSR advances business and social goals simultaneously, maximizing profit and social benefit. It has been coined “profit maximizing” CSR throughout the literature (Baron, 2001) (McWilliams and Siegel, 2000). Finally, social CSR is an initiative which is designed and executed for the purpose

¹⁶ Regardless of the motives and possible benefits, engaging in CSR initially adds a level of risk, such as a physical cost or potential social disapproval. The degree of risk and reward varies by company, industry and initiative.

of addressing a social need. While some actions clearly fall into one category or another, the majority fall within the general spectrum of CSR.

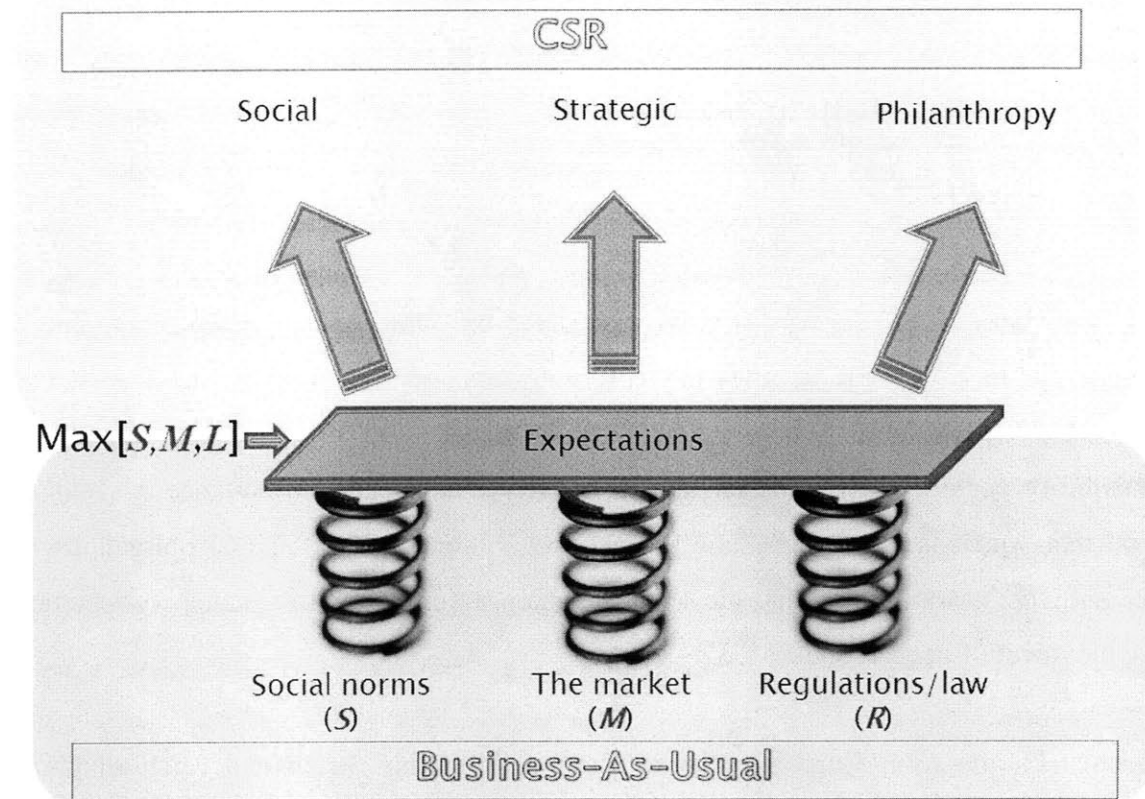


Figure 3.1 – Exceeding Expectations leads companies to operate within the spectrum of CSR. CSR activities and initiatives can be categorized as social, strategic or philanthropic.

3.1 Philanthropy

Philanthropy is one of the oldest forms of CSR. Companies have been making charitable contributions, starting foundations and supporting worthy causes since the beginning of business. Whether it is for marketing reasons, CEO altruism, tax deductions or a desire to give back to the community, companies have a long-standing history of this type of contribution. Over the years, this type of donation has earned the title: “checkbook philanthropy” which refers to giving small amounts to various nonprofits in response to specific requests (Pinckney, 2008).

Philanthropy can be used to react to an immediate event or sudden demand, such as a natural

disaster. Philanthropic contributions are usually monetary or resource allocations without strict measures or benchmarks to assess the returns. Philanthropic contributions often times consist of cash donations given to aid local civic causes or provide general operating support to universities and national charities in the hope of generating goodwill among employees, customers, and the local community. Corporations contribute to all kinds of nonprofit groups, from education and the arts to human services and the environment. Rather than being tied to well-thought-out social or business objectives, the philanthropic contributions often reflect personal beliefs and values. Indeed, one of the most popular approaches – employee matching grants – explicitly leaves the choice of charity up to the individual worker (Kramer, 2002). Companies also approach philanthropy by setting up employee volunteer groups that donate their time.

Another alternative for corporations is to spin-off a corporate foundation. This isolates the corporation from making philanthropy decisions. In this case, the foundation receives most of its funding from the corporation, and the distribution of funds to the social cause is administered by the foundation. While the foundation itself is a social enterprise, funding the foundation from the corporate perspective is considered philanthropy. The UPS (United Parcel Service) Foundation is responsible for facilitating community involvement on a local, national, and global level. Since launching its global philanthropy program in 2004, The UPS Foundation has invested nearly \$47 million in global philanthropy and more than 1.2 million employee volunteer hours. The investments of the foundation leverage UPS's funding, skills and ability while advancing social goals outside their core business.

Altruistic corporate philanthropy is what Milton Friedman adamantly opposed. With altruism, corporations do not gain any greater benefit than would the employees of the company itself (Lantos, 2001). Friedman argues that the money should either be given to employees for them to donate voluntarily or be invested back into the company to yield monetary returns for the shareholders to invest themselves. Many companies categorize their actions as philanthropic because of an intangible return on investment (ROI). However, when intangible benefits are reciprocated to the corporation due to corporate philanthropy it can have a return on investment.

Thus, philanthropy will overlap with strategic CSR¹⁷ when consumer good-will or brand marketing begins to yield value for the corporation. Furthermore, this type of value cannot be generated by an individual's donation alone because it is company-wide branding and loyalty.

3.1.1 Case Study: Philanthropy and the African Health Initiative - ExxonMobil

"Despite the more difficult economic environment it is important that business takes a long term view with its community investments."

- Rex W. Tillerson CEO ExxonMobil

In 2000, ExxonMobil launched the African Health Initiative. It began donating mosquito bed nets to areas of Africa to protect children from malaria. The ExxonMobil Corporation is an American oil and gas corporation. It is the world's largest publicly traded company when measured by either revenue or market capitalization.

Since launching the Africa Health Initiative, ExxonMobil has invested approximately \$40 million¹⁸ to support efforts to fight malaria. Malaria is a disease that is preventable, treatable and curable, yet every year there are at least 300 million acute cases of malaria globally, resulting in more than a million deaths. ExxonMobil is actively supporting a wide range of efforts to combat this major health and development issue. *Roll Back Malaria*¹⁹ reports that significant gains are being made in the fight against malaria; unprecedented levels of bed nets are being distributed and new drugs are being developed.

In 2007, ExxonMobil awarded \$12.4 million in grants to support awareness of and access to malaria treatment and prevention options, to promote strategies to build health care capacity at the community level, to fund research and development of new drugs and vaccines, and to

¹⁷ Strategic CSR is described in greater detail in section 3.2

¹⁸ Profits in the year 2000 alone were \$7.9 billion

¹⁹ Roll Back Malaria is a global partnership comprised of 500 partners.

improve international advocacy initiatives. ExxonMobil has donated more than \$121 million to organizations working in and benefiting Africa that are engaged in important community and social development projects.

Due to its philanthropic nature, there are little if any direct relations between the Africa Health Initiative and profits to ExxonMobil. Any profits that might arise will revolve around corporate branding, employee pride, marketing and brand recognition associated with the positive perception of the company for their philanthropic work. By performing philanthropy in Africa, a place where ExxonMobil happens to do business, they get some benefit from having malaria-free employees; but, by giving bed nets to the entire population, it is predominantly philanthropic giving.

3.2 Strategic

Strategic giving is when corporations use their social investments to improve their competitive context by aligning social and economic goal to improve the company's long-term business prospects. By aligning philanthropy and strategy, corporations not only give money, they donate distinct capabilities that can result in greater social good, even as it strengthens the company's competitive edge (Kramer, 2002).

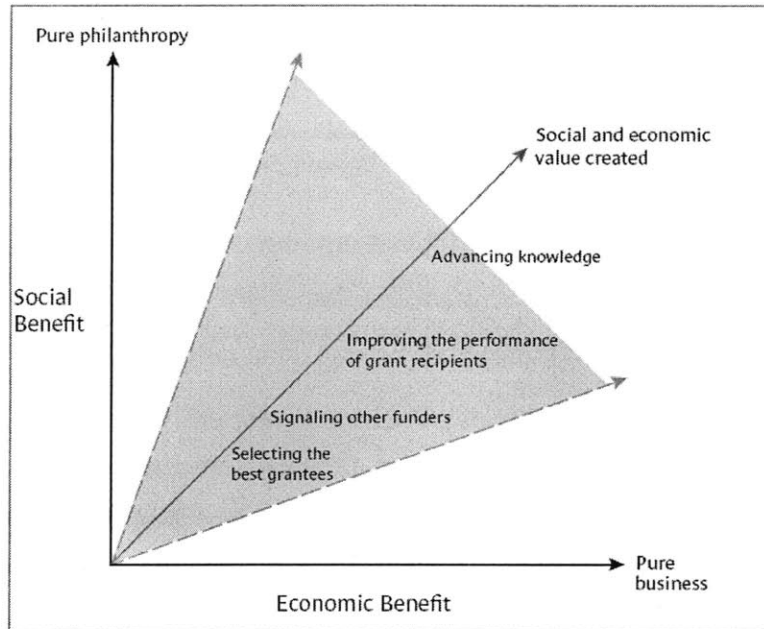


Figure 3.1 – Porter and Kramer’s Maximizing Strategic Philanthropy’s Value (2002)

By taking a strategic approach, as shown in Figure 3.1, companies can devote resources to social needs and choose those that will have the highest potential for strengthening their competitive advantage. By planning CSR as part of a company’s overall plan, organizations can ensure that profit and shareholder value don’t overshadow the need to behave ethically. Making CSR a part of corporate strategy, as GE²⁰ did when they launched the EcoMagination initiative²¹, is a way of making CSR economically and socially sustainable. With EcoMagination, GE developed socially beneficial products, such as compact fluorescent light bulbs, wind turbines and energy efficient appliances, which increased sales and benefited the company's bottom line.

Strategic CSR can be viewed as an opportunity rather than a cost because of the points of intersection between a company and society (Porter, 2006). Identifying points of intersection allow the company to work out a value proposition that is unique for its customers. Product refills, for example, are not only a way of reducing packaging material, weight, logistics cost and

²⁰ General Electric Company, or GE (NYSE: GE), is an American multinational conglomerate corporation incorporated in the State of New York. In 2009, Forbes ranked GE as the world's largest company. The company has 323,000 employees around the world.

²¹ Discussed in detail in Section 3.2.1

carbon footprint, they are also a way to maintain customers and increase margins. By giving existing and previous customers a discount on future products, through product refills, they build customer loyalty while reducing costs. In the cosmetics market, where packaging and presentation is crucial and there are no expectations to reduce packaging, taking such as step is CSR.

The Toyota Prius is another example of the overlap between business and social needs. The Prius offers less emissions, happy customers, cleaner roads and unpolluted air. Despite Toyota's efforts with the Prius, CSR is initiative specific not company specific; in 2010 Toyota came under heavy scrutiny for what some describe as a lack of responsibility for consumer safety (Linebaugh, Mitchell, & Shirouzu, 2010). Toyota had to recall numerous vehicles and halt production due to an unintended acceleration problem. A problem that some believe the company has known and done nothing about until the publicity of an accident caused by unintended acceleration in California which killed an off-duty police officer and 3 other car occupants. Toyota has profited greatly by using its innovation and manufacturing techniques developed in Japan. However, when entering the U.S market, they failed to evaluate and meet the social and regulatory expectations in the U.S. In the case of the unintended acceleration, the management of the situation was done from Japan to Japanese expectations rather than U.S expectations which to some extent led to damage of the company's reputation²².

3.2.1 Case study: GE's The EcoMagination Strategy

General Electric (GE) is a multinational American technology and services conglomerate. In 2005, the EcoMagination initiative attempted to position GE as a "green" company. EcoMagination is a business strategy to help meet and exceed customers' demand for more energy-efficient, less emissive products and to drive growth for GE that will greatly reward investors. EcoMagination was strategic CSR which benefited society through environmentally beneficial products while benefiting the company's bottom line. The initiative boosted revenue on such products from \$6.2 billion in 2004, before the initiative began, to \$10.1 billion in 2005,

²² As of the writing of this thesis, the full extent of the damage to Toyota's reputation was not known.

over halfway to the goal of \$20 billion by 2010. In 2008, sales revenue had reached \$17 billion and the target was revised to \$25 billion by 2010 (GE, 2008). EcoMagination put into practice GE's belief that financial and environmental performance can be integrated to accelerate profitable growth for the company, while taking on some of the world's biggest challenges.

GE established itself as one of the biggest players in the wind power industry and smart grid technology. It is also developing new environment-friendly products such as hybrid locomotives, desalination and water reuse solutions, and photovoltaic cells. The company has also set goals for its subsidiaries to lower their greenhouse gas emissions. In 2005, the same year in which EcoMagination was launched; Fortune Magazine listed GE as first in its "Global Most Admired Companies" list and first overall in the 2006 "America's Most Admired Companies" list.

3.3 Social

Social initiatives and social enterprises succeed because they have found a way to internalize and gain value from the social benefit that other companies consider externalities²³ and by-products. The social domain of CSR applies entrepreneurial principles to organize, create, and manage a venture or initiative specifically designed to address social change. Whereas business typically measures performance in terms of profit and ROI, social initiatives are assessed in terms of the impact they have on society while still operating with cost constraints. Social initiatives primarily work through nonprofits and citizen groups, but may also work in the private and governmental sectors. For the initiatives in the social category, social priorities are central to the business's existence; as opposed to strategic initiative where existing business goals are aligned with social issues.

Social enterprises are created to address social issues, be it health, environment, fair-trade, or micro-finance and, in some cases, social enterprises generate a profit. The social category

²³ Externalities are a phenomenon that arises when an individual or firm performs an action but does not bear all the costs (negative externality) or receive all the benefits (positive externality).

consists of subcategories: for profit social enterprises, such as Grameen Bank and Better Place²⁴; Non-profits Organizations, such as Habitat for Humanity²⁵; and NGOs, such as Oxfam International²⁶, The Red Cross²⁷ and World Food Program²⁸.

News media companies also fall into the for-profit social enterprise category because they perform a social good and make a profit. In the U.S, they provide information and allow society to exercise their first amendment right to freedom of speech and freedom of the press. The newspaper industry relies on readership, advertisement sales, and subscriptions for revenue; none-the-less, they also serve a unique social role within communities. Newspapers inform, educate, enlighten and entertain while providing news and information that people need in order to make intelligent, informed decisions, both in their daily lives and as they participate in the democratic process. While not all newspapers serve the same ideals or social benefits (i.e. tabloids), they fundamentally allow for the expression of U.S. rights. The growing popularity of online media, RSS feeds, social media and blogging has shown that society expects a news outlet. The CSR role that media companies fill cannot be filled by any one blogger or Facebook²⁹ Friend; the information comes with a sense of validity, trustworthiness and legitimacy which online social media can lack.

²⁴ Better Place is a venture-backed company based in Palo Alto, California that aims to reduce global dependency on petroleum through the creation of a market-based transportation infrastructure that supports electric vehicles.

²⁵ Habitat For Humanity International (HFHI), generally referred to as Habitat for Humanity or simply Habitat, is devoted to building "simple, decent, and affordable" housing. Homes are built using volunteer labor and are sold at no profit.

²⁶ Oxfam International is a confederation of 14 organizations working with over 3,000 partners in around 100 countries to find lasting solutions to poverty and injustice.

²⁷ The International Red Cross and Red Crescent Movement is an international humanitarian movement with approximately 97 million volunteers worldwide which was started to protect human life and health, to ensure respect for the human being, and to prevent and alleviate human suffering.

²⁸ The World Food Program (WFP) is the food aid branch of the United Nations, and the world's largest humanitarian organization addressing hunger worldwide. WFP provides food, on average, to 90 million people per year, 58 million of whom are children.

²⁹ Facebook is a social networking website founded in September 2006 that offers features such as, friends networking with others and posting on a "Wall" or "commenting" on pictures.

3.3.1 Case Study: Grameen Bank: Financing the poor

Grameen Bank (GB) provides credit to “the poorest of the poor” in rural Bangladesh, without any collateral. At GB, credit is a cost effective weapon to fight poverty and serves as a catalyst in the overall development of socio-economic conditions of the poor. The bank serves those that have been kept outside the banking system due to the assumption that they are poor and hence not bankable (Grameen Bank).

Muhammad Yunus, an economics professor, believes that the poor have skills that remain under-utilized, mainly because existing institutions and policies fail to offer the support that these people require (Seelos and Mair, 2005). Professor Yunus founded Grameen Bank in 1976 as a trial to determine whether it was feasible to systematically provide credit and banking services without collateral in developing countries. After several years of testing, GB was able to achieve an astounding repayment rate of over 98% (Grameen Bank, 2007).

GB grants unsecured loans to the poor in rural Bangladesh and operates 1191 branches, serving over 3 million poor people in 43,459 villages. Where other banks provide traditional services, Grameen Bank exceeds the expectations placed on the banking sector by lending only to the poorest villagers and the landless as well as lending primarily to women, who are not only economically but also socially impoverished. The loan disbursement design is also unique. To qualify for a loan, a villager must demonstrate that her family assets are below a certain threshold. She is not required to put up collateral; instead, she must join a five-member group and a forty-member center, and attend a weekly meeting. She must also share responsibility for the loans granted to the other members of her group; it is the group, not the bank, which initially evaluates loan requests. Defaulters would spoil things for everybody, so group members must choose their partners wisely (Seelos and Mair, 2005). Once loans are repaid to the bank, these funds are recycled into the community by extending more loans. (Cochran, 2007)

As of March 2007, the institution had lent over \$6.13 billion (Grameen Bank, 2007). GB has been profitable from the outset, and has inspired a global micro-credit movement that has spread to 65 developing countries, reaching 17 million borrowers (Seelos and Mair, 2005). For

pioneering work in micro credit, Mohammed Yunus and Grameen Bank were named recipients of the 2006 Nobel Peace Prize.

Mohammed Yunus set out to tackle poverty in Bangladesh by focusing on the social issue. Although he knew the business and economic fundamentals to make GB successful, he did not try to enter the same market that existing financial institutions were operating in. The government, society and other financial institutions did not expect him to help those in poverty but Yunus founded Grameen Bank regardless and has had a tremendous impact and inspired a micro-credit movement throughout the world.

3.4 The CSR Spectrum

The boundaries between philanthropic, strategic and social CSR are obscure and fuzzy. Companies might begin donating money through philanthropy and over time develop a long-term strategy in which they can achieve sustainable business benefits. Timberland, for example³⁰, traversed the CSR spectrum as it tried to make the corporate mission align with philanthropic goals and converted their philanthropic giving into a long-term business strategy until the year 2015.

Initiatives can begin categorized as philanthropic and evolve into strategic investment once they are better understood. A systemic analysis of CSR investment can identify benefits from philanthropy which can later be used to move along the CSR spectrum towards a more strategic approach to performing CSR. The opposite can be true for social enterprises that begin to focus more on business success and profitability, and less on the social aspect of their business.

Ben and Jerry's shifted from a predominantly social enterprise approach to a strategic and philanthropic approach to CSR after it was acquired by Unilever. It was founded as a local community-supported ice cream shop in Vermont. Both founders were very involved in the community and aligned their business with the community's needs. As its popularity and value

³⁰ More information on Timberland in section 4.2

grew, it was acquired by Unilever. As a term of the acquisition, Unilever agreed to donate a minimum of \$1.1 million of pretax profits to philanthropic causes yearly. It barely exceeded the charitable expectations placed upon Ben and Jerry's and Unilever, and was significantly less than what Ben and Jerry's used to donate³¹ prior to the acquisition.

3.5 CSR regionally and culturally bound

“Obligations, social well being, legitimacy functions are time and cultural bound. Over time things that were acceptable become unacceptable and things that were overlooked become important.”

- DL Wood

Expectations and therefore, what activities constitute as CSR, vary by region. For global and multi-national companies, this complicates matters because by operating across various borders, they must consider the expectations in each region in which they operate. While these companies are accustomed to multiple regulatory environments, it is more difficult to address multiple social norms, which are diffused. Different regions have different resources and different socio-economic issues that must always be taken into account when determining expectations.

If water is scarce in one region, it is expected for corporations to reduce water usage in that region. In this context, implementing water conservation would be expected and not CSR. In areas where water is abundant, choosing to conserve water would be considered CSR. If resources are constrained, the expectation is to cut back - this is usually imposed through regulation. However, when companies decide to reduce usage without any pressure, they exceed expectations.

Companies must take the regional and cultural interpretations of their actions into consideration when performing CSR initiatives. Actions considered CSR in one region might not be perceived as CSR in another region. The advantage and benefit of performing CSR is dependent on the

³¹ Prior to the acquisition, Ben and Jerry's would donate 7.5% of profits to charity.

context in which it is performed. The success of CSR is dependent on the acceptance by society. Companies seem to choose standard universally-applicable CSR efforts such as environmental and carbon emission funds, as a way of appealing to all markets and regions. However, because those efforts are easy to perform and companies are quick to support them, they become expected behavior soon after they are performed.

Chapter 4

Why perform CSR?

As companies continue to make ever-increasing investment into CSR, they are acting on the premise that CSR is not merely the “right thing to do” but also “the smart thing to do”.

- Craig Smith 2003

4.1 The CSR Advantage

By exceeding expectations ahead of competitors, others have to react as the companies create a first-mover advantage. Performing CSR ahead of the competition reduces the learning curve and once competitors catch on, voluntarily or due to a rise in expectation, the company that initially performed CSR will have developed an advantage. Companies like Starbucks³² and Whole Foods³³ took the lead in finding preferred green suppliers of their products. They developed relationships with local farmers before their competitors and by the time market and consumer expectations began to demand organic, locally grown, fair-traded products, Starbucks and Whole Foods had the stakeholder relationships and supply chain in place to meet the expectations. While the first companies to do CSR, benefit the greatest by being ahead of the competition, they also invest the most money. They must develop a new network of relationships and create a new market. The laggards see the potential for a new type of business, merely meet current expectations, and follow in the heels of the companies before them with less benefit but also less of an investment.

In the consumer goods market and the automotive market, where similar products fight for consumer attention, product differentiation is crucial to a product’s success. Companies are

³² Starbucks Corporation (NASDAQ: SBUX) is an international coffee and coffeehouse chain based in Seattle, Washington, United States. Starbucks is the largest coffeehouse company in the world.

³³ Whole Foods Market (NASDAQ: WFMI) is an Austin, Texas-based foods grocer. As of January 2009, the company operates 279 locations in the United States, Canada, and the United Kingdom.

always looking for ways to make their products noticeable; whether it's by eco-friendly labeling, charitable contributions, or fuel efficiency. Every company wants to have an edge over their competition and CSR has demonstrated that ability.

Going above expectations with CSR permits organizations to acquire or develop an attribute or combination of attributes that allow them to outperform competitors – known as a competitive advantage. These attributes can include access to resources, such as inexpensive power, or access to highly trained and skilled human resources. The term competitive advantage is the ability gained through attributes and resources to perform at a higher level than others in the same industry or market (Christensen and Fahey 1984, Kay 1994, Porter 1980 cited by Chacarbaghi and Lynch 1999). For social enterprises, this advantage can come from meeting a social need that has never been met before. A competitive advantage from strategic CSR can come from developing and testing a product that has both a social and business need. Philanthropically, as a result of exceeding expectations, organizations can gain a competitive advantage by building a positive corporate image.

4.2 Motivation

“we can't let our critics define who we are and what we stand for”

-Lee Scott, CEO Wal-Mart

Of course, distinguishing between altruistic and economic motivations is challenging when analyzing CSR. Although firms are motivated by a combination of social and financial concerns, many cite social responsibility as the motive for actions that were actually driven by profitability. The triggers, what events occurred prior to them beginning CSR, can be determined and analyzed.

CSR can be triggered in three ways: reactive, inertial,³⁴ or proactive. Reactive, as the title

³⁴ In this context, inertial means that companies begin with a reactionary move to meet expectations and continue

implies, is simply the response by companies to catch up when they fall short of expectations. Inertial entrance into CSR is when companies react to meet expectation and once the transformation has begun in the company, it continues beyond meeting expectations to exceeding expectations. Companies are proactive, when they are currently meeting expectation and nevertheless decide to undertake CSR initiatives.

Operating below the level set by expectations presents added risk for companies (Ruggie & Kytte, 2005). Regulators, competitors, and society apply pressure causing corporations to react and meet the expectations set by the external forces. The risk is derived from not reacting and exposing the companies to possible regulatory sanction or social dissatisfaction. Companies meet and exceed the expectations of consumers, competitors and regulators to remove the risk of lawsuits and boycotts, and to remain competitive in the market. Reactive actions that meet expectations alone do not yield benefits beyond those of reducing pressure temporarily. When a company reacts to a force below the bar (S, M, L), it begins to change or modify the way it behaves and conducts business. When reacting to situations, some companies decide to stop at the level of meeting expectations and others decide to go above (Kaku, 1997) and supersede expectations.

Reacting to meet expectations requires that companies change and adjust how they do business to the new expectations. Once companies begin to transform their business, they create inertia. The inertia created from the initial move to meet expectations, allows companies to continue in the direction of social responsibility and turn a reactive move into a proactive action. Nike went from being considered one of the least socially responsible companies³⁵, to being considered one the most socially responsible because they did not stop once they met expectations; they continued beyond expectations and performed CSR.

Nike continued to push forward and set the bar for others to follow by developing tools such as the Nike Considered Index and labor auditing tools. In 2005, a Nike footwear design team released a line of more sustainable shoes which was called “Considered.” As the team’s

into the CSR realm, either deliberately or unintentionally.

³⁵ Described in section 2.1.1

developer explained it, the name came from the team “considering what was right and doing what was right.” In late 2005, Nike formed the Considered Group as a way to diffuse the Considered ethos of high-performing, aesthetically pleasing greener products. The Considered Group’s mandate was to provide the inspiration and tools to drive the Considered design philosophy deep into Nike’s product creation units and processes. The group’s objectives included helping Nike consider the impacts of choices on the entire product lifecycle from design through end of life, and understand and reduce its environmental footprint. These criteria were the foundation for the Nike Considered Index, a rating system to evaluate the environmental impact of Nike footwear.

Some companies deliberately make the move to exceed expectations without the need of a reactionary push. Timberland³⁶ was meeting expectations and still decided to do more to address social and environmental issues. The motivation to exceed expectations came from within the company, not from the three external forces (S,M,L). Timberland was proactive in performing CSR without experiencing negative publicity or other external pressure. In 2007, Timberland transitioned their CSR team from four different business units to one unified department. This led to analysis of current capabilities, priorities and strategic choices and the development of their four pillars – energy, products, workplaces and service. At Timberland, the CEO, Jeffrey Swartz, provided the vision and leadership to integrate the company’s values, which includes its social commitment, with its products and brand image. Swartz’s goal was to create a mindset within Timberland that its brand, products, and responsibility to society were mutually dependent and inseparable (O'Brien, 2001). Timberland’s move to align the company with CSR and operate at a level above and beyond what was expected of them has strategically placed them on the leading edge of the footwear industry and of CSR activities.

When coffee shops such as Starbucks and Caribou Coffee³⁷ began successfully offering shade-grown, fair trade, and organic coffee, the expectations for all other coffee vendors were driven up. While the first coffee suppliers were being proactive, they set the bar for others in the coffee

³⁶ The Timberland Company (NYSE: TBL) is a manufacturer and retailer of outdoors wear with a focus on footwear.

³⁷ Both Starbucks and Caribou began offering fair-trade coffee and formed alliances with environmental NGOs in the early 1990’s. Starbucks and Caribou are the first and second largest coffee retailer in the US, respectively.

industry. After this, current competitors and new entrants in the coffee market were pressured to meet or exceed these expectations. Companies can address social issues strategically by being proactive; this drives their business goals and social goals willfully, rather than being in a reactive and recovery position where other forces dictate their efforts.

4.3 CSR in practice

Achieving short- and long-term value depends on the initiative performed. For example, a CSR initiative related to energy efficiency, may have immediate short-term impact. Initiatives focused on employee retention or developing a future work force take much longer for the benefits to be reaped. Overall, CSR benefits include: sustainable advantage, easier hiring of the best talent, higher retention, elevated employee productivity, reduced manufacturing expense, reduced expense at commercial site, increased revenue, greater market share, and reduced regulatory risk.

4.3.1 Short-term CSR investments

Pepperidge Farm: Cookies, Crackers and Fuel Cells

"By using our ultra-clean, highly efficient fuel cells, Pepperidge Farm stands to significantly reduce power costs while lowering emissions and increasing power reliability."

- Richard Shaw, Director of Business Development

Pepperidge Farm, Incorporated, based in Norwalk, Connecticut, is a leading provider of premium quality fresh bakery products, cookies, crackers, and frozen foods. Pepperidge Farm was founded in Connecticut in 1937 by Margaret Rudkin, an entrepreneurial homemaker who began baking fresh, all-natural bread for her allergy-afflicted son. The company is now a nationwide business with 8 manufacturing facilities, almost 5,000 employees, 3,500 independent distributorships, and over \$1 billion in sales. Pepperidge Farm was acquired by Campbell Soup Company in 1961.

In 2008, Pepperidge Farm dedicated a new 1.2 megawatt fuel cell power plant, which is now the biggest power source for its 260,000 square foot manufacturing facility in Bloomfield, CT and represents the largest single commercial fuel cell power plant in the United States. The cell

operates at 47 percent electrical efficiency. When excess heat from the cell is used for bakery processes, it operates at up to 80 percent efficiency. In addition to lowering power costs for the company, the fuel cell will also drastically reduce CO2 emissions from the facility. (Pepperidge Farm, 2008)

The new fuel cells operate 24/7 and greatly improve the reliability of electricity at the site - a key issue for a plant that operates three shifts, six days a week. Additionally, excess heat from the new fuel cell is being used to support bakery processes, which helps reduce fuel needs for plant boilers. Richard Shaw, Director of Business Development for Fuel Cell Energy stated: "By using our ultra-clean, highly efficient DFC® fuel cells³⁸, Pepperidge Farm stands to significantly reduce power costs while lowering emissions and increasing power reliability."

Pepperidge Farm is strategically addressing CSR, by using technology that is socially and economically beneficial; the technology reduces emissions and reduces cost by reusing the generated heat energy, while increasing power reliability.

Molson Coors: Beer and Ethanol Production

"Bill Coors used to say that waste was a resource out of place - that thinking still drives us today to recycle, reuse and reduce our consumption of energy and materials when and where we can."
- Leo Kiely Molson Coors CEO

In 1996, Molson Coors became the nation's first major brewer to convert its waste beer into ethanol. Molson Coors Brewing Company is one of the world's largest brewers. It brews, markets and sells a portfolio of leading premium quality brands such as Coors Light, Molson Canadian, Molson Dry, Carling, Coors, and Keystone Light in North America, Europe and Asia. It operates in Canada, through Molson Canada; in the US, through the MillerCoors joint venture; and in the U.K. and Ireland, through Coors Brewers Limited.

³⁸ Pepperidge Farm's new DFC fuel cell was built by Fuel Cell Energy, Inc.

The company began recycling waste beer -- beer lost during packaging or deemed below quality standards -- and converting it to ethanol in a facility owned by Merrick & Company and operated by Coors. Today the Golden ethanol facility produces about three million gallons of ethanol per year. The production of ethanol from waste beer also helps Coors eliminate about 70 tons of VOCs (volatile organic compounds)³⁹ from its emissions annually.

Coors sees a direct affect on the bottom line from this action. By converting what was once considered by-products and waste to a usable product, they not only have found a new product to sell, but also a means of reducing VOCs from their process which could give Coors an advantage if future emission regulation became more stringent.

4.3.2 Long-term CSR investments

Southwest: low-cost airfare and low absentee rates

“We follow ‘The Golden Rule,’ which means we treat each other the way we want to be treated, which is why doing the right thing by our Employees and Customers is so inherent to who we are.”

-Southwest CARES Policy

Southwest Airlines has a reputation among its customers as having a “*Fun-LUVing*” Attitude, being laid-back and extra friendly. The airline believes that the best way to succeed is to treat employees with respect and give them the latitude and encouragement they need to do their jobs better than anyone in the industry. Southwest is the largest airline in the world by number of domestic passengers carried per year. It maintains the third-largest passenger fleet of aircraft and operates approximately 3,500 flights daily (International Air Transport Association, 2008).

For Southwest, free flights for employees, profit sharing and no dress code in the office has translated into reduced tardiness, lowest employee turnover, and low absentee rate. While most of their competitors have railed for decades about the power of their employee unions,

³⁹ Volatile organic compounds (VOCs) are organic chemical compounds that have high enough vapor pressures under normal conditions to significantly vaporize and enter the atmosphere.

Southwest, with almost 90% of its employees unionized, has never had a strike and its employees are generally the highest paid in the industry. (Brancatelli 2008) Investing heavily on its current employees has translated into added productivity which allows them to have about 30 percent fewer employees per aircraft than its competitors. It has the lowest non-fuel C.A.S.M. (cost per available seat mile) of any of the major carriers.

Southwest has raised the expectations on the airline industry. They have demonstrated that it is possible to be profitable⁴⁰ while offering higher wages and better benefits. If productivity is the ultimate business objective, a company that exceeds expectations can develop a workforce that exceeds industry efficiency standards.

Cisco Systems: Networking and Educating

“The Internet and education are the two great equalizers in life, leveling the playing field for people, companies and countries worldwide.”

-John Cambers Cisco President and CEO

Cisco is an American multinational corporation that designs and sells consumer electronics, networking and communications technology and services. Headquartered in San Jose, California, USA, Cisco has more than 65,000 employees and annual revenue of \$36.11 billion as of 2009. Cisco Systems has invested in an education program, the Cisco Network Academy, to train computer network administrators.

As Internet use expanded, customers around the world encountered a chronic shortage of qualified network administrators, which became a limiting factor in Cisco's - and the entire IT industry's - continued growth. By one estimate, well over 1 million information technology jobs remained unfilled worldwide in the late 1990s. Cisco addressed this constraint through CSR by creating the Network Academy, contributing networking equipment to high schools, and getting Cisco engineers to volunteer at the schools. The program developed into a distance learning

⁴⁰ Southwest's profitability cannot solely be attributed to CSR. Southwest had a superior fuel hedging technique which allows it to pay much less for fuel than its competitors. During the 2008 fuel crisis, Southwest was paying about one dollar less per gallon than its competitors.

curriculum to train and certify secondary - and postsecondary - school students in network administration. Because the social goal of the program was tightly linked to Cisco's specialized expertise, the company was able to produce a high-quality curriculum rapidly and cost-effectively, creating far more social and economic value than if it had merely contributed cash and equipment to a worthy cause. As expectations for the program rose, and external stakeholders got involved, Cisco began to target "empowerment zones," designated by the federal government and developing countries by working with the United Nations. Cisco also organized a worldwide database of employment opportunities for academy graduates, creating a more efficient and proficient job market that benefit Cisco as well as the graduates and the regions in which they live (Porter and Kramer, 2002).

Cisco has used its unique assets and expertise, along with its worldwide presence, to create a program that no other educational institution, government agency, foundation, or corporate donor could have designed as well or expanded as rapidly. Cisco has amplified the impact by raising expectations of other corporations in its industry.

Starbucks: The Brand

"Pour Your Heart Into It. Starbucks is living proof that a company can lead with its heart and nurture its soul and still make money."

- Howard Shultz CEO Starbucks

Starbucks is an international coffee and coffeehouse chain based in Seattle, Washington that sells drip brewed coffee, espresso-based hot drinks, other hot and cold drinks, coffee beans, salads, hot and cold sandwiches and paninis, pastries, snacks, and items such as mugs and tumblers. It is the largest coffeehouse company in the world, with 16,635 stores in 49 countries, including 11,068 in the United States, nearly 1,000 in Canada and more than 800 in Japan.

Since 1971, when Starbucks opened its first store in Seattle, to its current nearly 17,000 stores around the world, Starbucks has shown a commitment to doing business responsibly and conducting themselves in ways that earn the trust and respect of their customers, partners, employees, and neighbors.

In late 2001, Starbucks announced that it would pay a premium for beans grown on environmentally and socially responsible farms which the company hopes will "create positive changes within the global coffee market and ultimately result in a fully sustainable coffee production supply chain." The sourcing guidelines are based on a flexible point system that reward performance in sustainable categories - quality, environmental impacts, social conditions and economic issues, covering issues such as energy and water conservation, pesticide use, biodiversity, and safe and fair working conditions. Qualifying suppliers were granted preferred status.

Starbucks provides cash and product donations to organizations where its partners are involved as volunteers. Examples of informal initiatives are: Earth Day clean-ups, regional AIDS walks and local literacy organizations. The company has developed a number of community building initiatives in the states with programs to improve the quality of life in neighborhoods by providing grants to local parks, violence prevention programs, cash and product donations, and economic investment in under-served communities. Across North America, Starbucks stores are addressing social causes in a variety of ways, from donating coffee to cleaning up neighborhoods. (Starbucks, 2002)

Starbucks' approach to CSR and its business strategy is strongly tied in with its reputation and brand. By building a brand around CSR, Starbucks earns a license to operate from its key stakeholders. These actions have led Starbucks to be included in the "100 Best Corporate Citizens" in Business Ethics Magazine (2000).

As for the effect on the market, Starbucks raised consumer expectations for what the coffee experience should be like. Since then, McDonalds⁴¹ and other major coffee shops have tried to provide a similar coffee experience, not as CSR but to compete with Starbucks for market share. Starbucks' CSR created an opportunity for products such as McCafe to be produced. McDonalds has branded and certified its McCafe products by the Rainforest Alliance to demonstrate its

⁴¹ McDonald's Corporation (NYSE: MCD) is one of the world's largest chain of hamburger fast food restaurants, serving nearly 47 million customers daily.

environmental sustainability.

4.4 No CSR guarantees

This CSR framework allows companies to put corporate behavior into context and determine those actions that should and should not be considered CSR, rather than predict future returns of an initiative or company. CSR is just one element of the inner workings of a corporation. All elements must be environmentally, socially, legally and economically sustainable in order for the company to derive value from the CSR initiative.

Regardless of how "responsible" a company appears today, its future success is not guaranteed. Neglect of CSR or neglect of the other business functions can take a company from being #1 to being bankrupt. Awards and recognition can only provide background information for framing current events and initiatives, not for determining whether or not companies are truly performing CSR. In order to perform CSR, expectations must first be determined and then a policy must be developed and executed to exceed those expectations. Initiatives should not be considered CSR simply because of how they are marketed.

Enron received a climate protection award from the EPA, and a corporate conscience award from the Council on Economic Priorities. Fortune named Enron "America's Most Innovative Company" for six consecutive years and it was on the Fortune's list of "100 Best Companies to Work for in America" list in 2000. Enron was at the forefront of socially responsible companies prior to the 2001 scandal⁴². The company was showered with awards and recognitions for its employee benefits and emission reduction support. At the time, Enron was one of the first to engage in "sustainable" practices by investing in wind and solar power, and lobbying for renewable mandates and carbon dioxide emission reductions.

Those particular actions and initiatives by Enron were strategic CSR. Supporting regulation that

⁴² Discussed in section 2.3

called for a reduction of carbon emissions was environmentally beneficial, but also favored Enron over its competitors; Enron was highly invested in natural gas production, transmission, and electricity generation. Those investments allowed Enron to benefit from regulations on carbon dioxide emissions because natural gas is less carbon intensive than oil and particularly, coal. Enron was also far ahead of the curve in investing in alternative energy sources. Given its business position, Enron supported the 1993 proposal for a BTU⁴³ tax, spearheaded the nation's strictest renewable energy mandate in Texas in 1999, and lobbied to regulate carbon dioxide emissions.

In 2001 Enron's CSR task force listed some of its accomplishments as:

- Secured board oversight of social/environmental performance
- Expressed support for Universal Declaration of Human Rights
- Established formal partnerships with WBCSD [World Business Council on Sustainable Development], IBLF [International Business Leaders Forum], and CI [Conservation International]
- Responding to stakeholder concerns on an ongoing basis

Enron was hailed by many, including labor unions and the workforce, as an overall great company, praised for its large long-term pensions, benefits for its workers and extremely effective management - until the exposure of corporate fraud.

Although some initiatives performed by Enron might have been socially responsible, CSR is initiative-specific and does not provide any guarantees as to the long-term success of the company. Enron was determined to affect and influence the expectations on its competitors, however, rather than drive up the expectations for social responsibility and carbon emission reduction, as its pre-scandal trajectory would indicate, it resulted in one of the largest financial

⁴³ BTU tax was another name for a carbon tax on fuel sources.

and accounting reforms – Sarbanes Oxley.

4.5 CSR Feedback

When one company performs CSR responsibly, or commits fraud irresponsibly, society, competitors, and regulators take notice and act. This creates a feedback loop⁴⁴ that in turn affects the level of expectations corporations must meet; activities go from being considered CSR to being expected. This can occur over time, as social acceptance or intolerance changes, as industries incorporate new operating standards, or as regulations are promulgated. Just as luxuries become commodities, what was once considered CSR, eventually becomes common practice. Once enough companies meet a certain level, expectations change across the industry. The bar of expectation can be raised by a company's own actions, societal actions, competitor's actions or governmental actions. As the bar increases, what was once considered CSR becomes something that a company *cannot, not do*.

⁴⁴ Feedback loop is the causal path that leads from the initial generation of the feedback signal to the subsequent modification of the event, in this case, a rise in expectations.

Chapter 5

Raising the Bar

What used to be considered "nice to do" is now "must do"

-Doing Well by Doing Good 2005. Golin Harris

Once a CSR initiative or action has gained social and market acceptance, it becomes expected. This positive feedback⁴⁵ - CSR leading to a rise in expectation - can be referred to as a *race to the top* as more and more companies try to out-do each other.

Social norms, competitors or regulatory obligations trigger corporations to engage in CSR and over time, CSR activities feed back into the social, market, and regulatory expectations from which they emerged. This rise in expectation occurs once companies demonstrate the capacity and ability to perform CSR. Mandating recycling seemed impossible when it was first being suggested and adopted. As companies engaged in recycling and demonstrated a capacity, ability, and willingness to recycle voluntarily, they laid the foundation for recycling to be incorporated into law. Once obligatory, the new regulations raised expectations above the previous level.

⁴⁵ Positive feedback, sometimes referred to as "cumulative causation", refers to situations where some effect causes more of itself. Under strong positive feedback, most systems quickly move to a limit state, where the limit is provided by external factors.

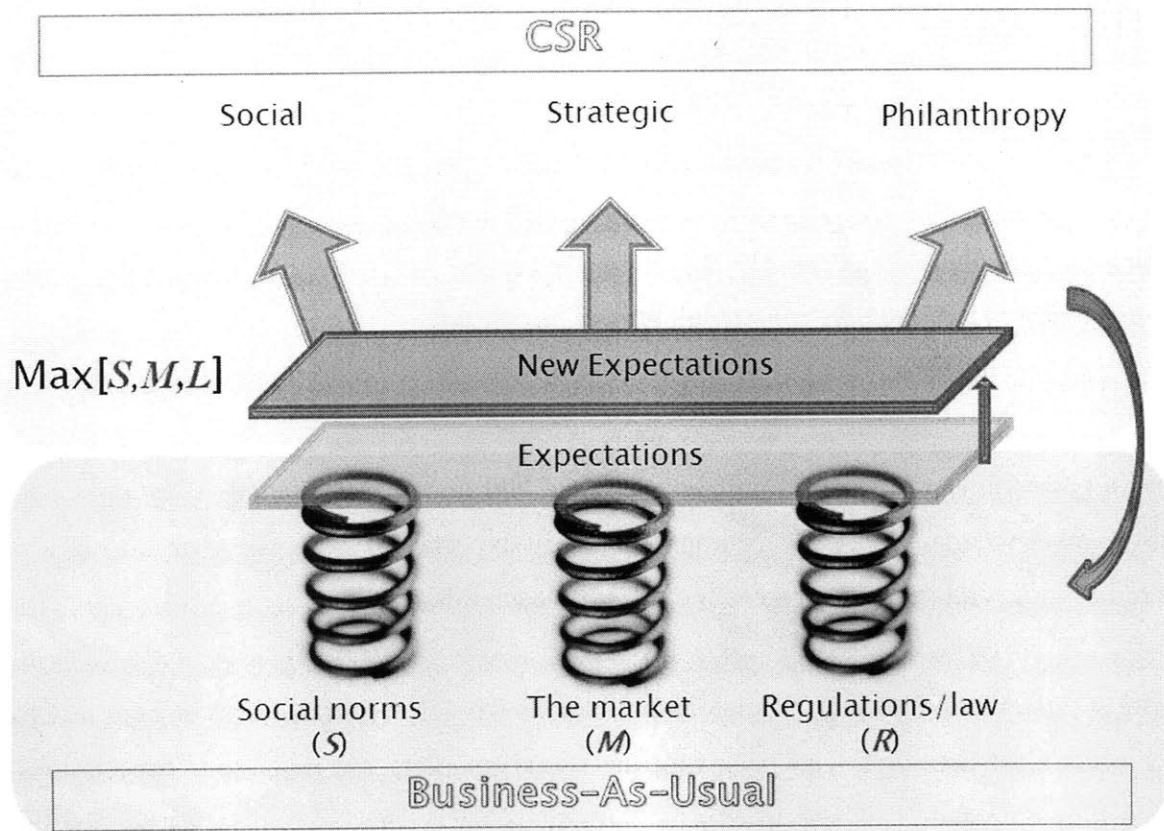


Figure 5.1 – Feedback of CSR causing a rise in expectations

5.1 Case Study: StarKist's Dolphin-Safe Tuna: A Race to the Top

The StarKist Dolphin-Safe Tuna case involves the imposition of market-access regulations on the importation and sale of certain tuna caught with methods lethal to dolphins. In brief, the dominant American tuna processors hoped to capitalize on consumer sympathy for dolphins and raise social norms and expectations to boost its market share against low-cost competitors.

Between 1975 and 1990, the US embargoed tuna imports on 23 different occasions. Mexican yellow fin tuna was banned from 1980 to 1986, in retaliation for the seizure of American tuna-boats fishing within Mexico's 200-mile coastline. On August 28, 1990, a U.S. federal judge again banned imports of Mexican tuna, this time on the grounds that Mexican tuna from the Eastern Tropical Pacific (ETP) exceeded US standards for dolphin mortality. The Eastern Tropical Pacific is the only place that dolphins school with tuna and therefore, the only place where

dolphin mortality is a concern.

The largest tuna canner, StarKist, preempted the US regulations by four months. On April 12, 1990, one week before Earth Day (and two days before the "International Dolphin Week"), Heinz (owners of StarKist) announced a unilateral suspension of tuna purchases that were not dolphin-safe, causing the other major canners to follow suit. The U.S. Marine Mammal Protection Act (MMPA) and its embargo on ETP tuna was supported on aesthetic and moral grounds. Dolphins in the ETP were never endangered species and a National Academy of Sciences study, conducted under Congressional mandate, recommended that dolphin-setting techniques be improved through international education, monitoring, and incentives, but not stopped under the pretence that Mexican tuna posed no human health threat.

Heinz deliberately adopted a strategy of green marketing. In October 1989 (six months before its April announcement, and ten months before the US ban on Mexican tuna), J.W. Connolly, the president of Heinz-USA, wrote to top management, encouraging a dolphin-safe strategy:

“I am interested in the possibility of seizing the environmental high ground by offering the only tuna guaranteed not caught off dolphins. . . I know about the potential cost impact on the procurement of raw tuna . . . However. . . If I am right in this, and we can solve the procurement problems, we could have a very substantial volume opportunity.”

If Connolly was correct, his plan would contrast sharply with the characterization by some activists that corporate profit go against protecting the environment.

The U.S. tuna processing industry was an oligopoly. Three large companies dominated 71% of the U.S. canned tuna market in 1989: Heinz (StarKist) with a 36% market share, Van Camp (Chicken of the Sea) with 21%, and Unicord (Bumble Bee) with 14%. The parent companies of the big three tuna labels were major producers of packaged foods and had much larger sales, revenue and profits⁴⁶ compared to their competitors in the tuna-fishing industry with tiny revenues and little political or social influence. Their regulatory preferences would be swamped by those of the much larger canners.

⁴⁶ H.J. Heinz, Inc., for example, had assets of \$4.9 billion, annual net sales of \$6.6 billion, and an annual gross profit of \$2.5 billion in 1991

StarKist bought tuna from around the world. The smaller private label firms, by contrast, were more specifically invested in one area, the ETP. Smaller firms' market share depended on low-costs and narrow profit margins and the more stringent regulation caused them to rely on fishermen and canneries near the ETP to reduce transportation costs.

The U.S. Congress and courts unilaterally banned the importation or domestic sale of tuna that was caught using methods lethal to dolphin, rather than reaching a multilateral agreement on dolphin protection, or letting consumer preferences determine the demand for "dolphin-safe" tuna. The effective ban lasted for over ten years, leading to shifts in consumer demand, a retail price war, and the end of dolphin-set⁴⁷ tuna purchases by market-leader StarKist and the other two dominant firms. The regulations were met with StarKist's enthusiastic support and assistance.

The U.S. Humane Society had called for a boycott of dolphin-set tuna since 1972, nearly twenty years earlier, with little noticeable change in consumer preferences. However, when StarKist and the two other dominant firms agreed to boycott dolphin-set tuna, the change was immediate and dramatic. By supporting the ban, and regulation banning dolphin-set imports, they secured an advantage over the smaller private firms. Prior to the ban, StarKist's actions appealed to the social norms. NGOs created a "Flipper Safe" label, which a tuna canner could use only if it did not use dolphin-set tuna at all (and—incidentally—only if it paid an annual licensing fee to the "Flipper Program"). Once the regulations were in place, consumers had no choice as to which tuna they preferred because only one would be legally allowed.

Nearly a decade later, after consumer preferences had changed to support the major companies in their "dolphin-safe" campaign, the U.S. technically legalized the importation of dolphin-set tuna again. However, by 2001, even after it was legal, little, if any Mexican tuna had entered the U.S. market due to a shift in the market while the tuna was banned. In fact, to the extent that Mexican fishing practices were improved to protect dolphins, there was something of a movement toward

⁴⁷ Refers to the method of catching tuna that is lethal to dolphins and not dolphin-safe

a higher common denominator, as Mexico moved closer to U.S. “dolphin-safe” practices. (Murphy, 2002)

While the tactic of raising expectations above the level at which competitors can meet might be beneficial in the short-term, over time, if the promise of profit increases rapidly or to an extremely high level, it might become more attractive to new entrants because higher rents have to potential to have higher margins and greater profit. This gap created by over expectations could potentially leave room for a new entrant with a new, disruptive technology to out seat the incumbent⁴⁸.

5.2 Framework Analysis and Validation

The first thing to consider when determining whether an action is CSR or not, is the current level of expectation. When StarKist adopted Dolphin Safe Tuna in April 1990, social, market and regulatory forces were as follows:

Social Norms

Consumers were sympathetic to dolphins but still consuming the available tuna, which was dolphin-lethal.

Market Competition

Dolphin-safe tuna was not on the market. StarKist was the first to market and sell it. At the time, it would raise cost but the rise in cost could potentially be less for StarKist proportionally compared to its competitor’s costs. StarKist’s action to ban dolphin-lethal tuna caused its competitors to follow suit, as predicted.

⁴⁸ Disruptive innovation, a term of art coined by Clayton Christensen, describes a process by which a product or service takes root initially in simple applications at the bottom of a market and then relentlessly moves ‘up market’, eventually displacing established competitors.

Regulations / Law

Although regulation was anticipated, StarKist preempted the regulation by 4 months. Once the regulation was re-examined and was deemed overly stringent and unnecessary, StarKist continued to sell only dolphin-safe tuna.

Once the action is determined to be above expectations and therefore CSR, the category in which the action falls must be determined; it could be social, strategic, or philanthropic. Figure 5.1 illustrates how the CSR initiative was completely strategic while being partially social and less so philanthropic.

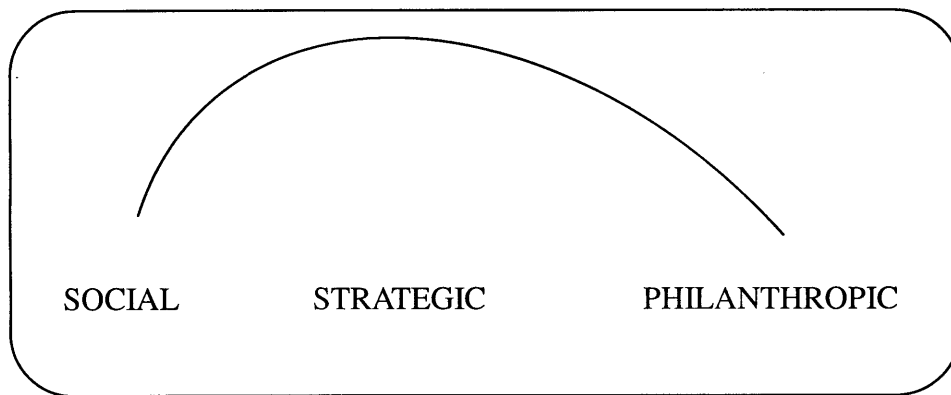


Figure 5.1: The variance of StarKist's actions across the CSR spectrum.

Social: Partially

Dolphin safety is closely related to the StarKist tuna business. However, their core business purpose is to sell tuna, not save dolphins.

Strategic: Completely

Deciding to ban dolphin lethal tuna addressed a social issue while developing StarKist's competitive advantage. StarKist had an advantage over its competitors by sourcing its tuna from multiple locations, while its competitors were primarily sourcing tuna from one market, the Eastern Tropical Pacific (ETP), the only place that dolphins school with tuna.

Philanthropic: Partially

While StarKist's actions were also philanthropic, they were primarily strategic because the issue was related to the core business. Had a technology or oil company performed the action, unrelated to their core business, it would have been considered philanthropic and not strategic.

StarKist's CSR feedback later influenced expectations socially, competitively and legally. StarKist preempted regulatory obligations and appealed to social norms and consumer's ethical judgment. This move by StarKist caused those competitors that could, to follow suit and ban dolphin-lethal tuna. While the actions did yield an advantage to StarKist for a short time, dolphin-safe tuna soon became expected. NGOs created and sold a "Flipper Safe" label. Once the market and social norms had bought into dolphin-safe tuna, there was no need for a regulatory import bans because the dominant force was not Legal (L), it was Social (S) and Market (M).

5.3 Capturing Expectations

In most cases, performing CSR will not directly affect all three forces (S, M, L), but a strong influence on any of the three will result in a rise of expectations. The maximum of the three forces sets expectations and therefore, influencing any one force to exceed expectations could secure an advantage. Having the ability to capture and influence expectations allows companies to develop and secure an advantage by performing CSR.

If the CSR influences social norms, which are fairly abstract and difficult to measure, controlling such norms and deriving an advantage would be challenging. Revlon⁴⁹ and the Body Shop⁵⁰

⁴⁹ Revlon is a multimillion dollar cosmetics company founded in the midst of the Great Depression in 1932, by Charles Revson, his brother Joseph and chemist, Charles Lachman, who contributed the "L" in the REVLON name. Revlon started with a single product — a new type of nail enamel — and expanded to offer an entire manicure line, and makeup and related products.

⁵⁰ The Body Shop International plc, known as The Body Shop, has 2,400 stores in 61 countries, and is the second largest cosmetic franchise in the world, The Body Shop carries a wide range of products for the body, face, hair and home.

were pioneers in the animal-friendly cosmetic testing techniques. In 1990, cosmetics giant Revlon became one of the first industry heavyweights to swear off all animal testing. They challenged the industry standard of testing cosmetics on animals, and by demonstrating that it was possible not to perform animal testing and still produce a high quality, safe product, they raised the expectations on the industry. Hundreds of companies have responded by switching to animal-friendly test methods. A survey by the American Medical Association found that 75 percent of Americans are against using animals in cosmetic testing. In most countries, animal testing is still legal and therefore any alternatives are done on a voluntary basis. Where animal testing is not legally banned, having animal safe products is upheld by social norms and expectations. As for Revlon and the Body Shop, most of their advantage came in the form of branding and reputation among customers.

On the other hand, affecting regulation, which is clear and precise, gives companies a distinct advantage. Companies try to secure an advantage through regulatory reform and corporate lobbying by incorporating the method, tool or technology that their company controls or has far-reaching experience with into regulation. The advantage can be viewed in two ways: an increased sales demand or the ability of exploiting their position on the learning curve.

5.3.1 Social Influence

Once a company has demonstrated the capacity and ability to perform an action or respond to a crisis, they will be expected to continue to do so and repeat it if the opportunity presents itself. By advertising their efforts in the annual report or through cause-related marketing⁵¹, they are now holding themselves to a new standard which social norms will continue to hold them to.

⁵¹ Cause-related marketing refers to a type of marketing involving the cooperative efforts of a "for profit" business and a non-profit organization for mutual benefit. The term is sometimes used more broadly and generally to refer to any type of marketing effort for social and other charitable causes, including in-house marketing efforts by non-profit organizations. Cause marketing differs from corporate giving (philanthropy) as the latter generally involves a specific donation that is tax deductible, while cause marketing is a marketing relationship generally not based on a donation.

In 2000, British Petroleum⁵² (BP) adopted the tagline “Beyond Petroleum.” However, during tough economic times, and after the retirement of Lord John Brown in 2007, many argue that BP moved from “beyond petroleum,” to “back to petroleum,” under the new leadership. BP had built a social norm around investing in alternative and renewable energy; however, soon after a change in leadership, the company cut those investments and focused again on oil production. After building an expectation, BP withdrew below what was expected of them and have faced negative consumer reaction as a result.

5.3.2 Market Influence

Once a company has performed CSR well, the next companies to follow in its footsteps are no longer first-movers. Clorox’s Green Works family of products was created, primarily, to compete with companies like Seventh Generation and take over their market-share. Seventh Generation’s initial success in the market drew the attention of other companies in the industry and led competitors to enter the “green” market. Seventh Generation raised the expectations for what cleaning products “should” be. Clorox, P&G⁵³ and Unilever have had to react to Seventh Generation’s CSR which demonstrates the shift in expectations.

5.3.3 Legal Influence

Regulatory Capture⁵⁴ is the term used when a company secures some advantage above competitors and then seeks ways to raise regulatory standards to this higher level. While the overall impact of the higher regulation might be positive, the company with the secured

⁵² British global energy company that is also the third largest global energy company and the 4th largest company in the world. As a multinational oil company, BP is the UK's largest corporation, with headquarters in St James's, City of Westminster, London.

⁵³ Procter & Gamble Co. (P&G, NYSE: PG) is a Fortune 500 American multinational corporation headquartered in Cincinnati, Ohio that manufactures a wide range of consumer goods. As of 2008, P&G is the 8th largest corporation in the world by market capitalization and 14th largest US company by profit.

⁵⁴ Regulatory Capture is an economics term used by the 1982 Nobel Memorial Prize in Economic Sciences winner, George Stigler.

advantage now has an advantage among its competitors who are being forced to react and meet the new level. Regulatory capture allows a corporation to influence and sometimes set the level of regulation that an entire industry will have to meet.

Companies use regulatory capture to influence regulation where their company has the advantage in an effort to keep others out. Regulatory capture is a way for industry to induce technology forcing in their favor. For example, if certain privately held seaports operated at a higher level of security than most, and a new regulation was passed requiring that this level was now the minimum acceptable level, these seaports would have an advantage during the time it takes competitors to match or exceed the new security standards. Regulatory capture can also make it more costly for new entrants to enter the market due to the added costs of compliance.

5.4 Other Considerations

Influencing expectations has tradeoffs and value associated with it. While advertising CSR might work in the companies' favor, it might also attract attention from regulators and competitors that could lead to a more hostile business environment. Alleviating the cost on an initiative through collaboration and partnerships might present benefits while also diluting the returns. Companies must carefully consider the options and alternatives prior to undertaking any CSR initiatives.

Chapter 6

Tradeoffs and Value

“CSR is good for the shareholders and therefore, it's good for the company.”

-Eric Schmidt, CEO Google

While the cost of a CSR program can be easily quantified, a cost-benefit analysis cannot easily quantify the benefit generated by an educated workforce in comparison to the welfare of a 10% reduction in carbon emissions. While many sustainability indexes have attempted to do this, there is little if any universal agreement on metrics and rating systems to measure social responsibility. All the metrics and measuring standards currently being used are subjective. They are based on the expectations of an industry at the point in time, that the metric was created and do not capture the dynamic nature of CSR. Instead of solely attempting to assign a cost and benefit value to CSR initiatives, they should be analyzed qualitatively and systematically, in order to more accurately determine the impact across the entire system and sources of value. Those companies in the position to exceed expectations should; those companies that cannot exceed expectations, should simply meet the expectations set by S, M and L. CSR is voluntary and therefore not an activity for all companies to perform.

Throughout the analysis and interviews, three key areas stood out as having an effect on what was considered CSR.

- 1) Whether the company was public or private
- 2) Whether the CSR was marketed or unmarketed
- 3) Whether the initiative was performed individually or in a partnership

These three areas alter the level of expectations for relatively similar companies, such as the regulations for a public company as opposed to a private company, or publicizing a CSR

initiative as opposed to performing it with no perceived desire for a reward. Partnerships can also foster a positive sense of collaboration or give a negative impression of not being fully committed to a cause. As measurement tools continue to evolve, companies must continue to analyze the tradeoffs of practicing CSR, deciding whether to keep them internal, publicize them, or share them with the industry. Companies must continuously re-evaluate the benefits, risks and tradeoffs of exceeding expectations.

6.1 Private and Public Companies

Whether the company is public or private, when considering the social impact of CSR activities, the end result is usually the same – a net benefit to society. However, the expectations and therefore what is considered CSR, does vary depending on the type of company, as shown in Figure 6.1. Public companies attract more attention and therefore are more heavily targeted by NGOs and regulators. The regulatory and social expectations on publicly traded companies are higher. From a market perspective, both private and public companies compete in the same market for the same consumers and therefore, market expectations are relatively equal for both. The advantage for the private companies is the ability to operate without as much regulatory oversight. The tradeoff is that privately held companies might have a more difficult time getting access to capital in comparison to publicly-traded companies.

| | PUBLIC | PRIVATE |
|--------------------|-------------------|------------------|
| SOCIAL NORMS | High Expectations | Low Expectations |
| MARKET COMPETITION | Same | Same |
| REGULATIONS / LAW | High Expectations | Low Expectations |

Figure 6.1: The difference in expectations for public and private companies.

For private and public companies, the level of expectation is proportional to the number of stakeholders. A public company is large in size, has a greater footprint, has more stakeholders than a

private company, more employees, more shareholders and therefore more attention. The larger the company, the more that is expected from it and the more pressure it has to perform and give back to society. Large, multi-nationals companies make the most profits and are therefore expected to give back the most.

This is not to say that a smaller firm cannot attract attention. Companies like Seventh Generation and Method are looking for attention and setting the bar high for themselves. This could potentially give them an advantage because they can set, meet and exceed social and market expectations with less stringent regulatory pressure. However, once they succeed in making social or market forces their level of expectation, any regulatory advantage they might have by not being publicly traded, will be irrelevant.

For publicly-held companies the standard measure of success, though limited, has been stock price. Privately-held companies and non-profit organizations, although not scrutinized by shareholders, must eventually answer to investors or parent organizations that provide funding. For a private company, the economic value does not need to be as tangible to the owners as do the profits of a publicly-held company. Keeping a company private allows the management to be more discretionary with their spending. In 1993, Seventh Generation went public in an effort to raise capital. After receiving pressure from shareholders, Jeffrey Hollender, the CEO and co-founder, decided that it would be in the best interest of the company if the company re-purchased all the stocks. He made the company private shortly thereafter; reducing the shareholder and regulatory pressure significantly. In some cases, mission-driven, social enterprises are at odds with their shareholders because the socially driven decision might not be the most profitable, short-term decision. However, they must make the case that there is a potential for long-term value.

Privately-held companies have the ability to set private agendas and address personal issues. Because the investment is privately held, they need not answer to numerous shareholders. Added risk taken on through CSR activities is isolated to a small number of investors, if any. Aaron Feuerstein was CEO of Malden Mills, a textile company whose plant was destroyed by a fire in 1995. Rather than moving operations to a lower-wage region after the fire, Feuerstein continued

to pay his idled workforce while the plant was being rebuilt⁵⁵. Unlike the typical CEO of a publicly held corporation, who is accountable to various shareholders, Feuerstein was free to act so generously because he only had to answer to a few family members (shareholders). Publicly-held corporations have to answer to many more stakeholders. They are subject to pressures from shareholders, citizens, employees, and political authorities. While the majority of social enterprises and mission-driven corporations are privately-held or non-profit, the Grameen Bank.⁵⁶ is an example of a publicly-held for-profit, social enterprise.

6.2 Internal versus publicized CSR

Some companies are choosing to develop the internal capacity to perform CSR and marketing it; others are keeping it as an internal mantra and divulging information only when asked. Nike began working on their Nike Considered Index⁵⁷ much earlier than it began to market it and share technology with its competitors. Walmart on the other hand, chose to develop a packaging score card⁵⁸ and distributed it by charging a fee for suppliers and other companies to access it.

There is a clear business case made for advertising and promoting high expectations. Firstly, large multi-national corporations (MNC) have an advantage over smaller regional companies in meeting higher and more costly expectations. By being a larger company, they have more resources to leverage and more access to capital that they can use in the short-term, which

⁵⁵ In November 2001, Malden Mills declared bankruptcy after the recession at the beginning of the new year left the company unable to pay creditors—related to its rebuilding and payroll commitments. Feuerstein was relieved of actual control of the company by its creditors.

⁵⁶ On July 11, 2005 the Graeme Mutual Fund One (GMFO), approved by the Securities and Exchange Commission of Bangladesh, was listed as an Initial Public Offering. One of the first mutual funds of its kind, GMFO will allow the over four million Graeme bank members, as well as non-members, to buy into Bangladesh's capital markets. The Bank and its constituents are together worth over USD 7.4 billion.

⁵⁷ The Nike Considered index was discussed previously in section 4.2

⁵⁸ Wal-Mart's packaging scorecard is a measurement tool that allows suppliers to evaluate themselves relative to other suppliers, based on specific metrics. The metrics in the scorecard evolved from a list of favorable attributes announced earlier this year, known as the "7 R's of Packaging: Remove, Reduce, Reuse, Recycle, Renew, Revenue, and Read."

smaller competitors cannot. Although this might cut into profits on the one hand, it will increase their competitive position by reducing competitors later. Secondly, by advertising high standards, large MNCs can promote their brand - increased branding equates to increased revenue.

Announcing CSR goals can provide a short-term reflection in stock price as shareholders react to the announcement. This provides a public metric to determine if the CSR goals and activities meet or exceed expectations. In publishing future goals, companies run into similar risks as when advertising CSR. While the company might look good if they meet or exceed their goals, they can also suffer from scrutiny if the long-term CSR goals and initiatives are too lax and they fall short of expectations.

Despite the benefits of marketing, building brand loyalty, and having a recognized image, there are tradeoffs and various reasons for keeping CSR actions internal, as shown in Figure 6.2. Companies might not always want to brand themselves as the market leader or be recognized as the most socially responsible company. This practice attracts attention from competitors, consumers, NGOs and regulatory bodies, which brings added scrutiny and higher expectations in the future.

| | INTERNAL and INVISIBLE | EXTERNAL and VISIBLE |
|--------------------------------|--|---|
| UNMARKETED and UNPUBLICIZED | NO ONE KNOWS – NO EXPECTATIONS RAISED | SOMEONE MIGHT FIND OUT AND ASK FOR MORE INFO |
| MARKETED and PUBLICIZED | PUBLIC KNOWLEDGE, BAR IS RAISED FOR THAT COMPANY | PUBLIC KNOWLEDGE, THE BAR IS RAISED FOR THE COMPANY AND OTHERS |

Figure 6.2: The tradeoffs associated with marketing CSR goals and initiatives.

Another common reason to keep initiatives private is that over-marketing of CSR can be perceived negatively by the public. CSR can be viewed as disingenuous – a marketing scheme - and not true goodwill. Just as a company enhances its reputation, a company can also degrade its reputation by using CSR insincerely. By not marketing CSR, the company gives the impression that it is doing it, not for recognition but, for some other altruistic reasons. Some CSR projects have an explicit “no advertising and no publicity” policy. Public skepticism of CSR derives from companies that have gone as far as to spend more money marketing a CSR campaign than the amount of money being donated; such as when Philip Morris⁵⁹ staged a PR commercial that cost more money to produce than the amount being donated through the CSR initiative.

Demonstrating a capacity to perform CSR can bring about added pressure and risk to the company. Companies risk raising standards and expectations, above what they can sustainably achieve in the long-term by advertising their ability to perform CSR. Once expectations are raised on a company, it is much more difficult to lower expectations without suffering a loss of brand value.

6.3 Partnerships: sharing costs and benefits

A new CSR trend is emerging in which companies are forming strategic partnerships and sharing their technology. In this sense, they may decide not to publicize their actions, and still gain an advantage by sharing their technology and potentially becoming the de-facto industry standard among competitors. Nike produced an adhesive with low VOC emission that reduced the toxic fumes inhaled by the shoe makers. However, because the shoe manufacturing factory was shared with other companies, the workers would still inhale the chemicals from other adhesives unless all the adhesives used in the factory were replaced. Nike then partnered with its competitors to use the adhesive in shared manufacturing facilities. In this case, the Nike technology became the standard adhesive giving Nike an advantage in the market and having little affect on social norms

⁵⁹ Philip Morris International (PMI) (NYSE: PM) is an international tobacco company, with products sold in over 160 countries. In 2007, it held a 15.6% share of the international cigarette market outside of the USA and reported revenues net of excise taxes of \$22.8 billion and operating income of \$8.9 billion. Until a spin-off in March 2008, Philip Morris International was an operating company of Altria Group.

or regulations.

Over the years, many companies have formed joint ventures and partnered with NGOs to perform CSR. One example is Coca-Cola⁶⁰ and the World Wildlife Foundation⁶¹ (WWF) that created the CSR initiatives to address broad social issues, as opposed to specific corporate needs. Corporations can associate with NGOs, government, academia, and competitors in order to address the problems, and in doing so, they create strategic alliances with which to share the costs and benefits of the work. Partnerships provide a cost-effective way for companies to perform CSR, enabling them to leverage the efforts and infrastructure of their partners.

By partnering to perform CSR, companies can focus their efforts on their business and not in being “more responsible” than their competitors; this helps to reduce the race to the top scenario which can lead to CSR reaching an unsustainably high level. Chiquita⁶² developed strategic alliances with credible environmental organizations in an effort to certify their products. These alliances provide the external competencies and credibility necessary to make the certification program successful. Chiquita’s certification program is called the *Better Banana Project* and involves a partnership with the Rainforest Alliance, a not-for-profit organization dedicated to protecting endangered ecosystems and biodiversity. The program sets rigorous environmental and social standards for banana farms including soil and water conservation, minimal use of agrichemicals, protection of the ecosystem, and fair treatment of workers (Chiquita, 2000). Rainforest Alliance brings its skills and experiences in managing integrated conservation projects as well as credibility to the effort. Chiquita is betting that the Rainforest Alliance’s stamp of

⁶⁰ The Coca-Cola Company (NYSE: KO) is a beverage company, manufacturer, distributor, and marketer of non-alcoholic beverage concentrates and syrups. The company is best known for its flagship product Coca-Cola.

⁶¹ The World Wide Fund for Nature (WWF) is an international non-governmental organization working on issues regarding the conservation, research and restoration of the environment, formerly named the World Wildlife Fund, which remains its official name in the United States and Canada. It is the world's largest independent conservation organization with over 5 million supporters worldwide, working in more than 90 countries, supporting around 1300 conservation and environmental projects around the world. It is a charity, with approximately 60% of its funding coming from voluntary donations by private individuals.

⁶² Chiquita Brands International Inc. (NYSE: CQB) is a producer and distributor of bananas and other produce, under a variety of subsidiary brand names, collectively known as Chiquita.

approval on its bananas will add value and increase demand for the certified product among the growing number of consumers concerned about the environment (Carlton, 2000).

Figure 6.3 suggests rule for partnership based on the spillover affects produced by the CSR initiative. Activities that have high spillover effects should be performed with partners as a way of involving others whom will benefit from the collaborative activities and reap the spillover benefits which cannot be contained. Although this is still prone to free-riders, not even attempting to partner and not providing an opportunity for others to collaborate offers no alleviation in cost. If the overall value derived from the action is large enough, even with the partnership, all the collaborators involved will receive enough individual benefit. In other words, where spillover is high, companies should partner to split the cost, even though they will not get the full benefit due to spillover, they will not be able to gain it regardless, so the company might as well split the cost.

| | HIGH SPILL OVER | LOW SPILL OVER |
|------------|-----------------|----------------|
| PARTNER | + | - |
| INDIVIDUAL | - | + |

Figure 6.3: Determining when to partner based on the spillover effects produced by the CSR initiative.

Where spillover is low, the company should attempt to perform CSR on its own and get the most benefit from it. Even though the CSR initiative might be more expensive, the company can benefit most from it individually. Inverse conditions cause individual investment with high spillover and partnership investment with low spillover to be yield negative results.

6.4 Social Welfare

| | LARGE SOCIAL IMPACT | SMALL SOCIAL IMPACT |
|-------------|---------------------|---------------------|
| PRIVATE | + | + |
| PUBLIC | + | + |
| MARKETED | + | + |
| UNMARKETING | + | + |
| PARTNER | + | + |
| INDIVIDUAL | + | + |

Figure 6.4: The social benefit resulting from CSR is positive in all cases.

Because of the nature of CSR, *any* positive impact on social welfare will be beneficial to society regardless of who performs it, whether CSR is advertised or not, and regardless of how it is performed. The conditions under which CSR is performed do not alter its positive impact though these conditions do affect the value and profit that is derived from CSR.

Chapter 7

Conclusion

7.1 Tomorrow's CSR

As companies continue to perform CSR, they are setting the example for others to follow by demonstrating best practices, and raising the expectations for the competition. Regardless of whether they are public or private, companies need to stay in business (be profitable), in order to be able to perform at the levels that society expects. If the expectations are set too high, companies will fall short. If companies cannot meet regulations or cannot price their products at a reasonable rate, they will eventually shut down. Being proactive with CSR initiatives allows companies to determine the direction and pace at which expectations placed upon them fluctuate and thereby, align CSR initiatives with their profit-making mission.

This thesis argues that a company's social responsibility is not merely to meet expectations but to exceed them. Companies have been meeting the expectations placed upon them for years simply by staying in business; some have even tried to market their "business-as-usual" as CSR. However, in order for their actions to be considered CSR, companies must first identify expectations and then exceed them. While this might not have been the intended definition of CSR when it was first introduced, over time, the definition of CSR has evolved from risk mitigation to deliberately seeking an advantage by exceeding expectations. Companies exceed expectations in order to gain an advantage from performing CSR. The requirement for corporations to be socially aware has given them an opportunity to create innovative CSR initiatives. Corporations that undertake social initiatives, strategic CSR, and philanthropy, exceed what is expected of them and as a result, value and benefit accrues to the company.

There are many examples of companies that have gone above expectations and have added value to their business. By aligning CSR with their corporate mission, they have found ways to add value to the company while simultaneously fulfilling their social and economic goals. There are also examples of companies that have gone out of business or not received the ROI they expected due to

CSR. There are no guarantees as to the outcome of CSR initiatives or how society will react to the actions performed. Companies position themselves to be successful, by understanding the benefits and tradeoffs associated with CSR.

As more companies perform CSR initiatives, they will have to continue to innovate and exceed expectations. Exceeding expectations to secure a competitive advantage allows companies to profit from their CSR initiatives. However, an advantage from CSR cannot be sustained indefinitely because, as companies succeed, others will notice and replicate their efforts, and expectations will rise. Regardless, failure to perform CSR at all or to meet expectations, social, market, or regulatory, could put a company at a disadvantage – indeed, in a position from which they might not recover, and which could lead to the downfall of the company.

CSR is determined by the influence of three forces – social norms, market competitions, and regulatory obligations. Focusing on only one, be it market forces as large corporations are accused of doing, or on social indicators, as do many NGOs and non-profits, might work while that force is dominant and setting expectations, but will have a much less favorable effect if expectations are being set by one of the other two forces. Focusing on the market or performing CSR because other companies are doing it is not the correct approach. Each company must determine what benefit they would like to achieve from performing CSR and approach it as they would approach innovating a new or existing product.

7.2 Future Work

This thesis spends ample time discussing how expectations can rise over time and how performing CSR can be a race to the top. It might be interesting to see how the level of expectation could be lowered due to constraints by the three forces (S,M,L) and by any other constraints that might be introduced due to the cost of performing CSR. The level of expectation is a dynamic factor and should both rise and fall.

In addition, a comparison of existing quantitative metrics, such as the Dow Jones Sustainability Index and Human Development Index, with the qualitative analysis presented here. As companies continue to create metrics and scorecards to evaluate CSR activities, the dynamic nature of CSR and the impact that it has on society's welfare is being obscured, making it inevitably problematic to quantify and rank CSR initiatives. Although many companies attempt to, there will never be universal agreement about how to place a value on social welfare or how to measure the value of human life. As social expectations, market expectations, and regulations fluctuate, so do the activities that corporations are performing. In the time it takes for metrics to be created and validated, the metrics can become obsolete. The outcome yields a subjective result based on a quantitative rubric which has advantages and disadvantages, granted that the caveats in the results are understood.

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