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CHAPTER 2

Stakeholder Relationships, Social Responsibility, and Corporate Governance

SUMMARY

In this chapter, first we identify stakeholders' different roles in business ethics. We examine the relationships between businesses and various stakeholder groups and examine how a stakeholder framework can help us understand organizational ethics. Then we define social responsibility and examine the relationships between having a stakeholder orientation and social responsibility. Next, we delineate how a stakeholder orientation helps to create corporate social responsibility. We then examine corporate governance as a dimension of social responsibility and its role in structuring ethics and social responsibility in business. The ethical decision making process is covered in order to provide an understanding of the importance of oversight in responding to stakeholders. Finally, we provide the steps for implementing a stakeholder perspective in creating both social responsibility and ethical decisions in business.

INSTRUCTOR NOTES FOR "AN ETHICAL DILEMMA"

Megan's dilemma is her involvement and knowledge of GAC's tracking of employees and whether to report this to higher authorities. GAC tracked one employee traveling ten miles to an area hospital every night after work and planned to reprimand the employee for using the company car for personal use. According to the company, GAC can legally place GPS devices in its company cars. Also, according to corporate policy, company cars should only be used for business activities, and any personal needs should be done with the employee's own personal car. The instructor may want to ask students their opinion on how appropriate the punishment is to the violation. The instructor could push the issue with questions such as what if this is the employee's first offense and he is otherwise a very productive worker? Could the company simply give the employee a warning?

A second case involved GAC's plans to fire another employee for sharing company secrets. Company evidence included computer activity, cell phone usage, GPS tracking, audio and video of personal conversations, dinners, and even hotel rooms. The instructor may want to ask students if GAC is within the law when obtaining this evidence. Has GAC overstepped its bounds in tracking personal conversations? Could the fired employee sue GAC for wrongful dismissal? Would it be different if the employee leaked national secrets instead of company secrets concerning an app? The company has an established ethical reputation, so one rogue employee should not tarnish that reputation if the company acts responsibly in how it handles the employee. Megan's boss brushes aside her concerns and reminds Megan how competitive the industry is and how necessary it is to make sure employees are not sharing confidential information with rivals. Megan is also reminded her job is simply to suggest appropriate action. Should Megan suggest what she really thinks? Should she 'suggest' what she knows her boss wants to hear?

LECTURE OUTLINE

I. Stakeholders Define Ethical Issues in Business
   A. Building effective relationships is considered one of the more important areas of business today. A stakeholder framework helps identify the internal stakeholders such as employees, boards of directors, and managers as well as external stakeholders such as customers, special interest groups, regulators, and others who agree, collaborate, and have confrontations on ethical issues.

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B. In a business context, customers, investors and shareholders, employees, suppliers, government agencies, communities, and others who have a "stake" or claim in some aspect of a company's products, operations, markets, industry, and outcomes are known as **stakeholders.**
   1. The survival and performance of any organization is a function of its ability to create value for all primary stakeholders. There are three approaches to stakeholder theory: normative, descriptive, and instrumental.
      a. The normative approach identifies ethical guidelines that dictate how firms ought to treat stakeholders. Principles and values provide direction.
      b. The descriptive approach focuses on the actual behavior of the firm and usually addresses how decisions and strategies are made for stakeholder relationships.
      c. The instrumental approach describes what will happen if firms behave in a particular way.
   2. The relationship between companies and their stakeholders is a two-way street. Stakeholders are influenced by business, but they also have the ability to affect businesses.
      a. Stakeholders apply their values and standards to many diverse issues—working conditions, consumer rights, environmental conservation, product safety, and proper information disclosure—that may or may not directly affect an individual stakeholder's own welfare.
      b. Stakeholders provide both tangible and intangible resources that can be critical to a firm's long-term success.
   3. When individual stakeholders share similar expectations about desirable business conduct, they may choose to organize into communities.
   4. Ethical misconduct can damage a firm's reputation, causing stakeholders to withdraw valuable resources. This gives stakeholders power over businesses.

C. Identifying Stakeholders
   1. Stakeholders can be divided into two categories.
      a. **Primary stakeholders** are those whose continued association is necessary for a firm's survival (employees, customers, investors, and stockholders, governments and communities that provide necessary infrastructure).
      b. **Secondary stakeholders** do not typically engage in transactions and are not essential for its survival (the media, trade associations, and special-interest groups).
      c. Although primary groups may present more day-to-day concerns, secondary groups cannot be ignored or given less consideration in the ethical decision-making process.
   2. The **stakeholder interaction model** indicates that there are two-way relationships between the firm and a host of stakeholders.

D. A Stakeholder Orientation
   1. The degree to which a firm understands and addresses stakeholder demands can be expressed as a **stakeholder orientation**. A stakeholder orientation involves "activities and processes within a system of social institutions that facilitate and maintain value through exchange relationships with multiple stakeholders."
   2. A stakeholder orientation comprises three sets of activities.
      a. The organization-wide generation of data about stakeholder groups and assessment of the firm's effects on these groups.
      b. The distribution of this information throughout the firm.
      c. The organization's responsiveness as a whole to this intelligence.
   3. Given the variety of employees involved in the generation of information about stakeholders, it is essential the information gathered be circulated throughout the firm.
   4. A stakeholder orientation is not complete unless it includes activities that address stakeholder issues.
   5. Responsiveness processes may involve the participation of the concerned stakeholder groups. A stakeholder orientation can be viewed as a continuum as firms adopt the concept to varying degrees.

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II. Social Responsibility and Ethics
  A. The concepts of ethics and social responsibility are often used interchangeably, although each has a distinct meaning.
    1. Social responsibility is an organization's obligation to maximize its positive impact on stakeholders and minimize negative impacts. It can be viewed as a contract with society
    2. Business ethics involves carefully thought-out rules or heuristics of business conduct that guide decision making.
  B. There are four levels of social responsibility—economic, legal, ethical, and philanthropic—and they can be viewed as steps.
  C. The term **corporate citizenship** is often used to express the extent to which businesses strategically meet the economic, legal, ethical, and philanthropic responsibilities placed on them by their various stakeholders.
    1. Corporate citizenship has four interrelated dimensions:
      a. Strong sustained economic performance
      b. Rigorous compliance
      c. Ethical actions beyond what the law requires
      d. Voluntary contributions that advance the reputation and stakeholder commitment of the organization.
  D. **Reputation** is one of an organization's greatest intangible assets with tangible value. The value of a positive reputation is difficult to quantify, but it is very important.

III. Issues in Social Responsibility
  A. Social responsibility rests on a stakeholder orientation.
    1. Companies are looking at broader issues that consider the long-term welfare of society; each stakeholder is given due consideration.
  B. Long-term relationships with stakeholders develop trust, loyalty and the performance necessary to maintain profitability.
  C. Issues generally associated with social responsibility can be separated into four general categories: social issues, consumer protection, sustainability and corporate governance.
    1. Social issues are associated with the common good and deal with concerns that affect large segments of society and the welfare of our entire society.
      a. There is a need to reflect on issues indirectly related to business, such as jobs lost through outsourcing, health issues, and gun rights when developing strategies in certain cases.
      b. Issues that more directly relate to business include obesity, smoking, and exploiting valuable or impoverished populations, as well as a number of other issues
      c. Another major social issue involves internet tracking and privacy and may soon become a consumer protection issue as the government is considering passing legislation limiting the types of tracking companies can perform over the Internet without users' permission.
    2. Consumer protection often occurs in the form of laws passed to protect consumers from unfair and deceptive business practices; these issues usually have an immediate impact on the consumer after a purchase.
      a. Major areas of concern include advertising, disclosure, financial practices, and product safety
      b. Because consumers are less knowledgeable, it is the responsibility of companies to take precautions preventing consumers from being harmed by their products.
      c. Deceptive advertising has been a hot topic in the consumer protection area, and some advertising practices skirt the line between ethical and questionable behavior.
        i. For example, native advertising blends digital advertisements or company promotions with content on the website where it is featured. This may be construed as deceptive if consumers cannot tell the difference between the ad and the content.

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   d. Companies must be knowledgeable about consumer protection laws and recognize whether their practices could be construed as deceptive or unfair.
3. Sustainability is defined as the potential for the long-term well-being of the natural environment and businesses can no longer ignore the environment as a stakeholder.
   a. Because sustainability is a major ethical issue, we will cover this topic in more detail in chapter 12.
4. **Corporate governance** involves the development of formal systems of accountability, oversight and control. Strong corporate governance mechanisms help remove the possibility for employees to make unethical decisions.
   a. Research has shown that corporate governance has a positive relationship with social responsibility and we discuss corporate governance in more detail later in this chapter.

IV. Social Responsibility and the Importance of a Stakeholder Orientation

A. Many businesspeople and scholars have questioned the role of ethics and social responsibility in business because legal and economic responsibilities are accepted as the most important determinants of performance.
   1. Milton Friedman said "the basic mission of business [is]…to produce goods and services at a profit, and in doing this, business [is] making its maximum contribution to society and, in fact, being socially responsible." Friedman believes the market is a better deterrent to wrongdoing than new laws and regulations.
   2. Adam Smith, one of the founders of capitalism, established expectations for motives and behaviors in his invisible hand theory. Smith distinguished justice as consisting of perfect or inalienable rights, from beneficence, consisting of imperfect rights that *should* be performed but cannot be forced.

B. Evidence suggests that caring about the well-being of stakeholders leads to increased profits. The support stakeholders have for companies they perceive to be socially responsible can also serve to enhance the firms' profitability.

V. Corporate Governance Provides Formalized Responsibility to Stakeholders

A. Today, the failure to balance stakeholder interests can result in a failure to maximize shareholders' wealth.
   1. Directors and corporate officers have a duty of care, or *duty of diligence*, to make informed and prudent decisions.
   2. Directors have a *duty of loyalty,* which means all their decisions should be in the best interests of the corporation and its stakeholders.
   3. Two major challenges for boards of directors are officer compensation and the temptation to use knowledge about investments, business ventures, and the stock market to engage in insider trading.

B. To remove the opportunity for employees to make unethical decisions, most companies have developed formal systems of accountability, oversight, and control—known as corporate governance.
   1. *Accountability* refers to how closely workplace decisions are aligned with a firm's stated strategic direction and its compliance with ethical and legal considerations.
   2. *Oversight* provides a system of checks and balances that limit employees' and managers' opportunities to deviate from policies and strategies and that prevent unethical and illegal activities.
   3. *Control* is the process of auditing and improving organizational decisions and actions.
   4. A clear delineation of accountability helps employees, customers, investors, government regulators, and other stakeholders understand why and how the organization chooses and achieves its goals.

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5. Corporate governance establishes fundamental systems and processes for preventing and detecting misconduct, for investigating and disciplining, and for recovery and continuous improvement. The development of a stakeholder orientation should interface with the corporation's governance structure.

C. Views of Corporate Governance
   1. The **shareholder model of corporate governance** is founded in classic economic precepts, including the goal of maximizing wealth for investors and owners.
      a. Focuses on developing and improving the formal system for maintaining performance accountability between top management and the firms' shareholders.
      b. A shareholder orientation should drive a firm's decisions toward serving the best interests of investors.
   2. The **stakeholder model of corporate governance** adopts a broader view of the purpose of business because it must answer to other stakeholders, including employees, suppliers, government regulators, communities, and special-interest groups.
      a. Because of limited resources, companies must determine which of their stakeholders are primary.

D. The Role of Boards of Directors
   1. For public corporations, boards of directors hold the ultimate responsibility for their firms' success or failure, as well as for the ethics of their actions. Board members have a fiduciary duty to act in the best interests of those they serve
   2. Traditionally, boards of directors rarely perform the management function. They are concerned with monitoring the decisions made by executives on behalf of the company.
   3. Compensation, both of organizational executives and board members themselves, is a difficult ethical area because board members may place self-interest above those of shareholders.
   4. Greater Demands for Accountability and Transparency
      a. Directors are chosen for their expertise, competence, and ability to bring diverse perspectives to strategic discussions.
      b. Outside directors are thought to bring more independence to the monitoring function.
      c. Many of the corporate scandals uncovered in recent years might have been prevented if each of the companies' boards of directors had been better qualified, more knowledgeable, and less biased.
      d. The concept of board members being linked to more than one company is known as **interlocking directorate**. The practice is legal unless it involves a direct competitor.
   5. **Executive Compensation**
      a. Many boards spend more time discussing compensation than they do ensuring the integrity of the firm's financial reporting systems.
      b. How executives are compensated has become a controversial topic, with many people believing no executive is worth millions of dollars in annual salary and stock options, while others argue that because executives assume so much risk, they deserve the rewards.
      c. The topic of executive compensation is important to boards because it receives much attention in the media, sparks shareholder concern, and is hotly debated in discussions of corporate governance.
      d. One area for board members to consider is the extent to which executive compensation is linked to company performance.
      e. Issues related to high compensation are excessive risk-taking, a focus on short-term financial performance, and reduced transparency at the expense of long-term growth.

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VI. Implementing a Stakeholder Perspective
- A. An organization that develops effective corporate governance and understands the importance of business ethics and social responsibility in achieving success should develop processes for managing these important concerns.
- B. Although there are many different approaches, there are some steps to follow that are effective in utilizing the stakeholder framework in managing responsibility and business ethics.
  1. Step 1: Assessing the Corporate Culture
     - a. To enhance organizational fit, a social responsibility program must align with the corporate culture of the organization.
     - b. The purpose of this step is to identify the organizational mission, values, and norms that are likely to have implications for social responsibility.
  2. Step 2: Identifying Stakeholder Groups
     - a. In managing this stage, it is important to recognize stakeholder needs, wants, and desires.
     - b. Stakeholders have some level of power over a business because they are in the position to withhold, or at least threaten to withhold, organizational resources.
  3. Step 3: Identifying Stakeholder Issues
     - a. This step involves understanding the nature of the main issues of concern to primary stakeholders.
  4. Step 4: Assessing Organizational Commitment to Social Responsibility
     - a. Step 4 brings the previous three steps together to arrive at an understanding of social responsibility that specifically matches the organization of interest.
  5. Step 5: Identifying Resources and Determining Urgency
     - a. The prioritization of stakeholders and issues, along with the assessment of past performance, provides guidance for allocating resources.
     - b. Two main criteria should be considered:
       - i. the level of financial and organizational investments required by different actions.
       - ii. the urgency when prioritizing social responsibility challenges.
  6. Step 6: Gaining Stakeholder Feedback
     - a. Stakeholder feedback can be generated through a variety of means.
       - i. Satisfaction or reputation surveys
       - ii. Assessment of stakeholder-generated media (blogs, websites, podcasts, and newsletters)
       - iii. Formal research using focus groups, observation, and surveys

VII. Contributions of a Stakeholder Perspective
- A. Balancing stakeholder interests requires good judgment because broader societal interests can create conflicts.
- B. This chapter provides a good overview of the issues, conflicts, and opportunities of understanding more about stakeholder relationships. The stakeholder framework helps recognize issues, identify stakeholders, and examine the role of boards of directors and managers in promoting ethics and social responsibility.

DEBATE ISSUE: TAKE A STAND

Have your students split into two teams. One team will argue for the first point, and the other will argue for the opposing view. The purpose is to get students to realize that there are no easy answers to many of these issues. This particular issue deals with whether a socially irresponsible product—in this case, a product that promotes adultery—should be sold if it is legal. Students on the first team could argue that as long as the product is legal and allows for freedom of choice, there should be no barriers to selling it. Students on the

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other team could argue that the product causes emotional harm to people. Since it is a detriment to society, it should be banned. The instructor might also want to bring up the hacking attack that ended up revealing the real names of customers because Ashley Madison refused to shut down. It would be interesting for students who believe Ashley Madison is morally wrong to discuss whether the hackers were also wrong in what they did.

"RESOLVING ETHICAL BUSINESS CHALLENGES" NOTES

In this case, Demarco has to balance various stakeholder interests in his daily job while his employer is asking him to exploit a vulnerable population. Xeon Natural Resources Incorporated hired Demarco right out of college due to his heritage and strong language skills. Xeon plans to mine niobium in a Brazilian rainforest and Demarco's job, along with a small group of other employees, is to explain to the local indigenous tribes how Xeon wants to strip mine their government issued land. The reader learns how manufacturers use niobium and how much ($5 billion over 20 years) Xeon plans to make in profits.

Demarco soon learns his assigned indigenous tribe is one of the few left unaltered by western culture, but that will soon change once Xeon begins strip mining. His boss agrees their culture will change forever but urges him to think instead of the increase in the standard of living for the tribe. Demarco still feels uneasy and believes the tribal elders are being steamrolled and do not understand the impact this mining will have on their community. His boss says she too is worried about the interests of the various stakeholders, but the time to move is now and the company is depending on these mining rights.

Instructors may ask students to name the various stakeholders and describe their interest in the project. Which stakeholder has the largest interest in the project? This depends on which stakeholder the students assign the greatest priority.

Demarco's co-workers fear their jobs are in jeopardy. Now the tribal elders have raised concerns and have called for meetings to obtain feedback from tribal members. While Xeon tries to mine using environmentally friendly methods, there really is no such thing when it pertains to strip mining. Demarco is meeting with tribal elders to discuss their concerns. He understands that some groups of stakeholders will suffer negative effects no matter how the issue is decided. Demarco is not sure what he will tell the tribal elders when they meet.

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CASE 2

Starbucks Mission: Social Responsibility and Brand Strength

CASE NOTES FOR INSTRUCTORS:

Students will likely have strong opinions regarding Starbucks. Many may be committed patrons who view Starbucks as a socially responsible company committed to green practices and free-trade coffee. Others might dislike Starbucks because it is a large chain that pushes out smaller local competitors. Another possible reason students may be opposed to Starbucks are its prices, which are higher than many of its competitors. Starbucks seems to be able to justify its higher prices because the company sells more than just coffee—it sells an experience. Starbucks patrons can order specialty drinks and hang out in what founder Howard Schultz envisioned to be the "third place" to be after home and work. Love it or hate it, Starbucks has been very successful at branding.

Starbucks has had a profound influence on the U.S. coffee market. Before Starbucks came onto the scene, people perceived coffee as an uninteresting product largely consumed by older people in the United States. It did not have the "cool" factor or the cache that it does today. Starbucks entry in the market largely changed how Americans consumed coffee—and what they thought about coffee shops. It all started in the cold, gray climate of Seattle—the perfect setting for launching an appealing, warm, international beverage. Starbucks emphasized quality while service and location became a critical issue.

In spite of its popularity, Starbucks faltered during the most recent recession, when many customers cut back on discretionary purchases. This prompted the return of founder Howard Schultz as CEO. Schultz implemented a restructuring process at Starbucks and closed hundreds of stores. He sought a return to the value that initially made Starbucks a great company: quality. Today Starbucks is once again thriving and expanding internationally.

No matter what one thinks of Starbucks, it is more involved in social causes and the care of its workers than many comparable chains. Starbucks is committed to employee well-being, as one can see in its employee health care system. Howard Schultz made employee health care a priority after watching his father struggle with injuries because he had no access to employee health care or worker's compensation.

The company also has a history of giving to charities that affect its primary stakeholders. As part of its commitment to ethics and sustainability, the company launched its Shared Planet website, which communicates to interested stakeholders all of the company's ethics and sustainability initiatives. The company is a large purchaser of Fair Trade Certified coffee and has partnered with Conservation International since 1998 to promote sustainable agricultural practices.

In spite of its professed commitment to caring for workers and for social causes, such a large company always will be subject to criticism. From complaints that Starbucks pushes smaller competitors out of markets, to criticisms that some of its coffee drinks are excessively fatty and caloric, Starbucks is facing many challenges. For instance, disposable cups pose a problem as the company strives to become more eco-friendly. In light of some of its weaknesses, instructors may ask students whether they feel that Starbucks deserves its image as a socially responsible brand.

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QUESTIONS AND DISCUSSION

1. *Why do you think Starbucks has been so concerned with social responsibility in its overall corporate strategy?*

   It should be obvious from examining the history of Starbucks that Schultz, the founder, was concerned with social responsibility from the very beginning. Because he made it an original core value of the company, it has remained a deeply ingrained part of the Starbucks culture. Starbucks also recognizes the benefits of customers perceiving Starbucks as a socially responsible company. Employees who receive health care are likely more satisfied because they feel that the company truly cares for them in a time when many organizations are scaling back on employee benefits. Consumers may be inclined to like Starbucks because of its many community and environmental initiatives. Thus, social responsibility for Starbucks is translating into good business.

2. *Is Starbucks unique in being able to provide a high level of benefits to its employees?*

   Students should understand that, while Starbucks does provide very good benefits to most of its workers, this is not exactly unique. While lauding Starbucks is fine, it is true that many comparable sized chains do not treat their workers as well as Starbucks. For instance, many chains do not provide any benefits to part-time workers. However, other companies also have a mission of providing for their workers. Some examples students may cite are Green Mountain Coffee, Wegmans, Whole Foods, Timberland, and the Gap.

3. *Do you think that Starbucks has grown rapidly because of its ethical and socially responsible activities or because it provides products and an environment that customers want?*

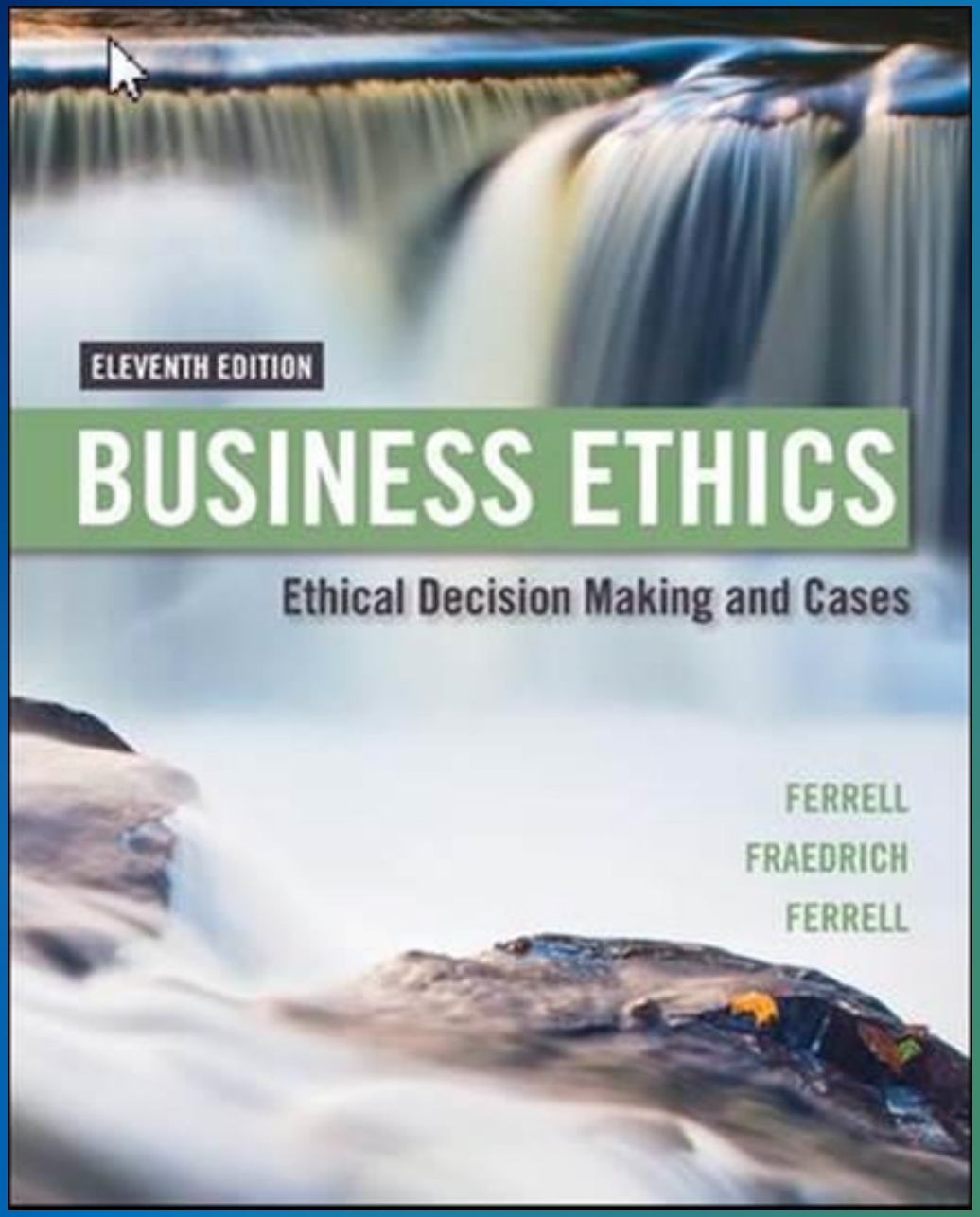
   Students' answers to this question could provoke serious debate in class. If Starbucks had a poor record in its activities, it would suffer from diminished reputation, which could lead to lower profits and reduced customer loyalty. However, many customers likely go to Starbucks, not because of its social mission, but because they like the coffee or the coffee shop atmosphere. Many customers likely began frequenting Starbucks because the locations are convenient and continue to go as long as Starbucks remains a readily available option. On the other hand, its record in responsibility has been a major selling point for consumers who care where products come from and under what conditions. These people may choose Starbucks because they offer Fair Trade coffee and organic snack products when other local coffee shops do not. Most people probably will agree that, at least to a point, Starbucks responsible activities have become a part of the total Starbucks product—a product for which many are willing to pay a premium price. In other words, both answers could be correct.

ADDITIONAL RESOURCES

- For an overview of Starbucks' Global Responsibility strategy and commitments, instructors may want to direct students to Starbucks' Global Responsibility Report, available online to download at: https://news.starbucks.com/news/starbucks-2014-global-responsibility-report.
- An extra benefit to employees that Starbucks has started offering is the chance to go back to earn a bachelor's degree at Arizona State University. The following link gives more information about the Starbucks College Achievement Plan: http://www.starbucks.com/careers/college-plan.

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Chapter 2
Stakeholder Relationships, Social Responsibility, and Corporate Governance

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Business Ethics Ethical Decision Making and Cases 11th Edition Test Bank

Learning Objectives

- Identify stakeholders' roles in business ethics
- Define social responsibility
- Examine the relationship between stakeholder orientation and social responsibility
- Delineate a stakeholder orientation in creating corporate social responsibility

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Learning Objectives (continued)

- Explore the role of corporate governance in structuring ethics and social responsibility in business
- List the steps involved in implementing a stakeholder perspective in social responsibility and business ethics

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Relationships and Business

- Relationships are associated with both organizational success and misconduct
  - Businesses exist because of organizational relationships between employees, customers, shareholders, and the community
- Stakeholder framework identifies the internal and external stakeholders who agree, collaborate, and engage in confrontations on ethical issues
  - Allows organizations to identify, monitor, and respond to the needs and expectations of stakeholder groups

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Stakeholders

- People who have a stake or claim in some aspect of a company's operations, markets, and industry
- Approaches to stakeholder theory
  - Normative - Sets forth ethical guidelines that dictate how firms should treat stakeholders
  - Descriptive - Focuses on the actual behavior of a firm and addresses how decisions and strategies are made for stakeholder relationships
  - Instrumental - Describes what happens if a firm behaves in a particular way

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Role of Stakeholders

- Foster decision making
  - The level of social responsibility of an organization can be assessed by scrutinizing its effects on the issues of concern to its stakeholders
- Provide resources that are critical to a firm's long-term success

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Types of Stakeholders

Primary stakeholders

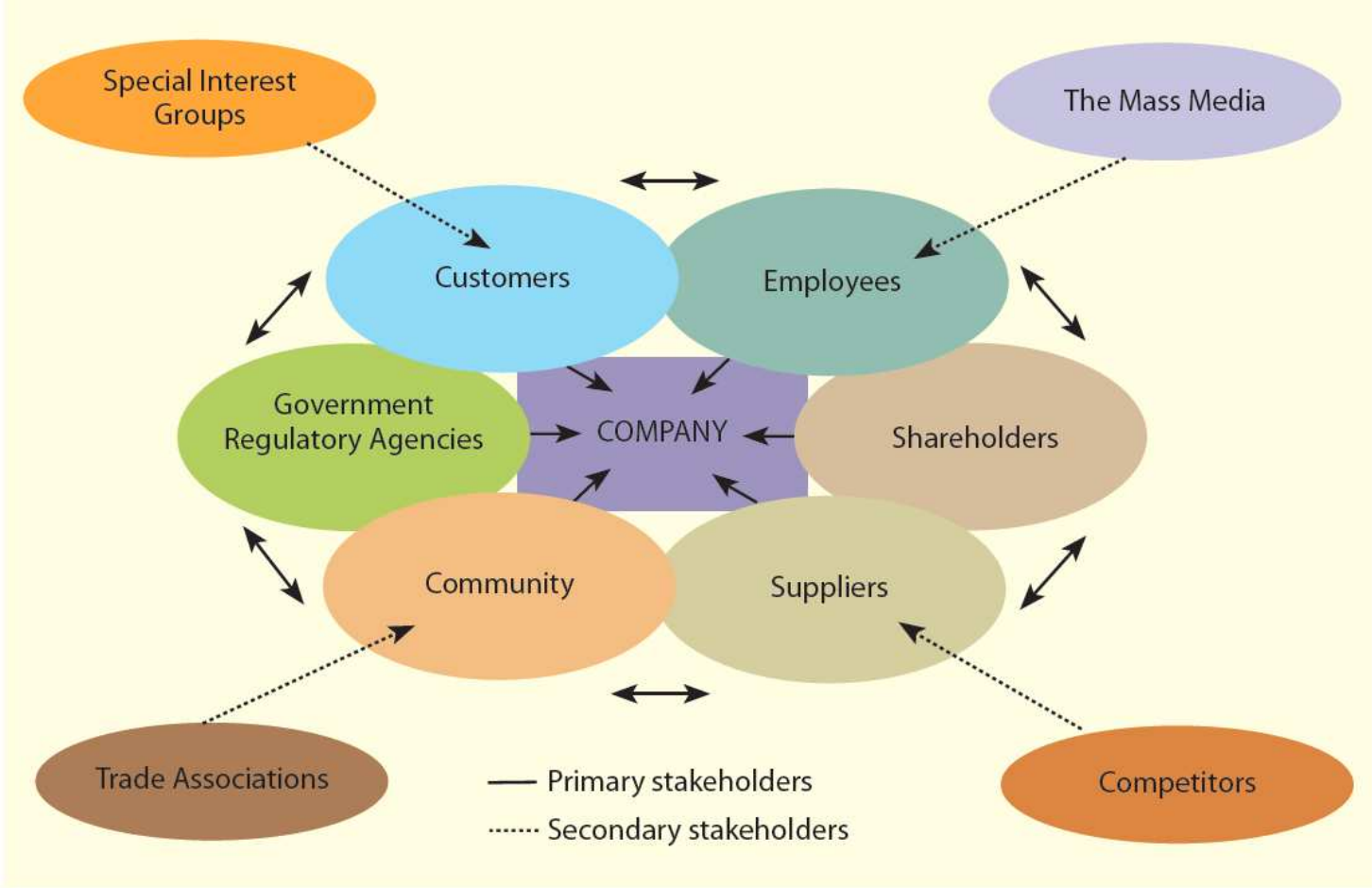
- People whose support and resources are needed for a firm's survival
- Include employees, customers, and shareholders

Secondary stakeholders

- Do not engage directly in transactions with a company
- Not essential to a firm's survival
- Include the media and trade associations

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Figure 2.2 - Interactions between a Company and Its Primary and Secondary Stakeholders



Source: Adapted from Isabelle Maignan, O. C. Ferrell, and Linda Ferrell, "A Stakeholder Model for Implementing Social Responsibility in Marketing." *European Journal of Marketing* 39 (2005): 956–977. Used with permission.

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Stakeholder Orientation

- Degree to which a firm understands and addresses stakeholder demands
- Consists of the following activities:
  - Organization-wide generation of data about stakeholder groups and assessment of the firm's effects on these groups
  - Distribution of the generated data throughout the firm
  - Responsiveness of the organization as a whole to the data generated

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Figure 2.3 - Steps of Social Responsibility



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Source: Adapted from Archie B. Carroll, "The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders," *Business Horizons* (July–August 1991): 42, Fig. 3.

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Corporate Citizenship

- Degree to which businesses strategically meet the economic, legal, ethical, and philanthropic responsibilities placed on them by their stakeholders
- Dimensions
  - Strong sustained economic performance
  - Rigorous compliance
  - Ethical actions beyond what the law requires
  - Voluntary contributions that advance the **reputation** and stakeholder commitment of the organization

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Issues in Social Responsibility

Social issues

Consumer protection

Sustainability

Corporate governance

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Importance of Stakeholder Orientation in Social Responsibility

- Friedman's view - Stakeholders do not have any role in requiring businesses to demonstrate responsible and ethical behavior
- Adam Smith's view - Values that a firm should adopt to produce in a more socially responsible way correlates with the needs and concerns of the stakeholders
- Stakeholder support for companies that are socially responsible enhances a firm's profitability

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Corporate Governance and Stakeholders

- Corporate governance provides formalized responsibility to stakeholders
  - Directors and officers of corporations - Fiduciaries for the shareholders
    - Directors perform a duty of diligence and share a duty of loyalty
- Accountability - Degree to which workplace decisions align with a firm's goals and its compliance with ethical and legal considerations

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Corporate Governance and Stakeholders (continued)

- Corporate governance establishes systems and processes for:
  - Preventing and detecting misconduct
  - Investigating and disciplining
  - Recovery and continuous improvement
- The development of a stakeholder orientation should interface with the corporation's governance structure

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Models of Corporate Governance

- **Shareholder model**
  - Goal - Maximize wealth for investors and owners
  - Focuses on developing and improving the formal system for maintaining performance accountability between top management and shareholders
- **Stakeholder model**
  - Company is answerable to its stakeholders
  - Promotes stakeholder welfare along with corporate needs and interests

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Board of Directors

- Responsible for the ethics of a firm's actions
  - Have a fiduciary duty
- Assume ultimate authority for their organization's effectiveness and subsequent performance
- Governed by the amendments of the Federal Sentencing Guidelines for Organizations (FSGO)

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Demand for Accountability and Transparency

- Directors today are increasingly chosen for their expertise, competence, and ability to bring diverse perspectives to strategic discussions
  - Outside directors are hired as they do not have vested interests
  - The concept of interlocking directorate is not illegal unless it involves a direct competitor
    - **Interlocking directorate**: Board members linked to more than one company

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Executive Compensation

- Compensation paid to top executives of the company
- Ratio between the salaries of the highest-paid executives and the median employee wage should be less
  - Stakeholders support high level of compensation only when it is linked to strong company performance

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Steps to Implementing a Stakeholder Perspective



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