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The Myth of CSR
The problem with assuming that companies can do well while also doing good is that markets don't really work that way

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REALITY CHECK

the myth of CSR

THE CORPORATE SOCIAL RESPONSIBILITY (CSR) MOVEMENT has grown in recent years from a fringe activity by a few earnest companies, like The Body Shop, and Ben & Jerry's, to a highly visible priority for traditional corporate leaders from Nike to McDonald's. Reports of good corporate behavior are now commonplace in the media, from GlaxoSmithKline's donation of antiretroviral medications to Africa, to Hewlett-Packard's corporate volunteering programs, to Starbucks' high-volume purchases of Fair Trade coffee. In fact, CSR has gained such prominence that the *Economist* devoted a special issue to denouncing it earlier this year.

Although some see CSR as simply philanthropy by a different name, it can be defined broadly as the efforts corporations make above and beyond regulation to balance the needs of stakeholders with the need to make a profit. Though traces of modern-day CSR can be found in the social auditing movement of the 1970s, it has only recently acquired enough momentum to merit an *Economist* riposte. While U.S. and European drivers for CSR have differed slightly, key events, such as the sinking of Shell's Brent Spar oil rig in the North Sea in 1996, and accusations of Nike and others' use of "sweatshop labor," triggered the first major response by big business to the uprisings against the corporate institution.

Naomi Klein's famous tome, "No Logo,"[1] gave voice to a generation that felt that big business had taken over the world, to the detriment of people and the environment, even as that generation was successfully mobilizing attacks on corporate power following the Seattle antiglobalization riots in 1999.

Rather than shrink away from the battle, corporations emerged brandishing CSR as the friendly face of capitalism, helped, in part, by the very movement that highlighted the problem of corporate power in the first place. NGOs, seeing little political will by governments to regulate corporate behavior, as free-market economics has become the dominant political mantra, realized that perhaps more momentum

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could be achieved by partnering with the enemy. By using market mechanisms via consumer power, they saw an opportunity to bring about more immediate change.

So, organizations that address social standards in supply chains, such as the Fair Label Association in the United States or the United Kingdom's Ethical Trading Initiative, have flourished. The United Nations partnered with business to launch its own Global Compact, which offered nine principles relating to human rights and the environment, and was hailed as the ethical road map for the future. And while socially responsible investment had been popular in some circles for years, eventually the mainstream investment community cottoned onto CSR: In 1999, Dow Jones created the Dow Jones Sustainability Indexes, closely followed by the FTSE4Good. All of these initiatives have been premised on the notion that companies can 'do well' and 'do good' at the same time – both saving the world and making a decent profit, too.

Some socially linked brands, such as Fair Trade coffee, are growing very rapidly in the U.S. and Europe.

The unprecedented growth of CSR may lead some to feel a sense of optimism about the power of market mechanisms to deliver social and environmental change. But markets often fail, especially when it comes to delivering public goods; therefore, we have to be concerned that CSR activities are subject to the same limitations of markets that prompted the movement in the first place.

Making Markets Work?

At face value, the market has indeed been a powerful force in bringing forward some measurable changes in corporate behavior. Most large companies now issue a voluntary social and environmental report alongside their regular annual financial report; meanwhile the amount of money being poured into socially responsible investing (SRI) funds has been growing at an exponential rate, year over year. Some socially linked brands, such as Fair Trade, are growing very quickly. Ethical consumerism in the United Kingdom was worth almost £25 billion in 2004, according to a report from the Co-operative Bank.[2]

The *Economist* article argued that the only socially responsible thing a company should do is to make money – and that adopting CSR programs was misguided, at best. But there are some strong business incentives that have either pushed or pulled companies onto the CSR bandwagon. For example, companies confronted with boycott threats, as Nike was in the 1990s, or with the threat of high-profile lawsuits, as McDonald's is over obesity concerns, may see CSR as a strategy for presenting a friendlier face to the public.

Once launched, CSR initiatives may provoke changes in basic practices inside some companies. Nike is now considered by many to be the global leader when it comes to improving labor standards in developing-country factories. The company now leads the way in transparency, too. When faced with a lawsuit over accusations of sweatshop labor, Nike chose to face its critics head-on and this year published on its Web site a full list of its factories with their audited social reports. And Nike is not alone. A plethora of other brands have developed their own unique strategies to confront the activists, with varying degrees of success.

But no one could reasonably argue that these types of changes add up to a wholesale change in capitalism as we know it, nor that they are likely to do so anytime soon.

Market Failure

One problem here is that CSR as a concept simplifies some rather complex arguments and fails to acknowledge that ultimately, trade-offs must be made between the financial health of the company and ethical outcomes. And when they are made, profit undoubtedly wins over principles.

CSR strategies may work under certain conditions, but they are highly vulnerable to market failures, including such things as imperfect information, externalities, and free riders. Most

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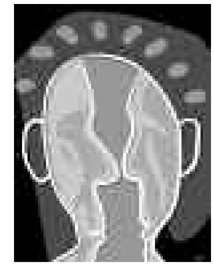


importantly, there is often a wide chasm between what's good for a company and what's good for society as a whole. The reasons for this can be captured under what I'll argue are the four key myths of CSR.

Myth #1: The market can deliver both short-term financial returns and long-term social benefits.

One assumption behind CSR is that business outcomes and social objectives can become more or less aligned. The rarely expressed reasoning behind this assumption goes back to the basic assumptions of free-market capitalism: People are rational actors who are motivated to maximize their self-interest. Since wealth, stable societies, and healthy environments are all in individuals' self-interest, individuals will ultimately invest, consume, and build companies in both profitable and socially responsible ways. In other words, the market will ultimately balance itself.

Yet, there is little if any empirical evidence that the market behaves in this way. In fact, it would be difficult to prove that incentives like protecting natural assets, ensuring an educated labor force for the future, or making voluntary contributions to local community groups actually help companies improve their bottom line. While there are pockets of success stories where business drivers can be aligned with social objectives, such as Cisco's Networking Academies, which are dedicated to developing a labor pool for the future, they only provide a patchwork approach to improving the public good.

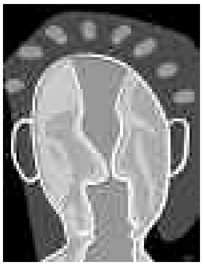
In any case, such investments are particularly unlikely to pay off in the two- to four-year time horizon that public companies, through demands of the stock market, often seem to require. As we all know, whenever a company issues a "profits warning," the markets downgrade its share price. Consequently, investments in things like the environment or social causes become a luxury and are often placed on the sacrificial chopping block when the going gets rough.

Meanwhile, we have seen an abject failure of companies to invest in things that may have a longer-term benefit, like health and safety systems. BP was fined a record $1.42 million for health and safety offenses in Alaska in 2004, for example, even as Lord John Browne, chief executive of BP, was establishing himself as a leading advocate for CSR, and the company was winning various awards for its programs.

At the same time, class-action lawsuits may be brought against Wal-Mart over accusations of poor labor practices, yet the world's largest and most successful company is rewarded by investors for driving down its costs and therefore its prices. The market, quite frankly, adores Wal-Mart. Meanwhile, a competitor outlet, Costco, which offers health insurance and

PHOTOGRAPH COURTESY OF ZEITGEIST FILMS

In the past Niketown stores drew anticorporate demonstrators, but Nike is now considered to be a leader in improving global labor standards.



CSR can hardly be expected to deliver when the stock market provides disincentives for doing so.

other benefits to its employees, is being pressured by its shareholders to cut those benefits to be more competitive with Wal-Mart.[3]

CSR can hardly be expected to deliver when the short-term demands of the stock market provide disincentives for doing so. When shareholder interests dominate the corporate machine, outcomes may become even less aligned to the public good. As Marjorie Kelly writes in her book, "The Divine Right of Capital": "It is inaccurate to speak of stockholders as investors, for more truthfully they are extractors."[4]

Myth #2: The ethical consumer will drive change.

Though there is a small market that is proactively rewarding ethical business, for most consumers ethics are a relative thing. In fact, most surveys show that consumers are more concerned about things like price, taste, or sell-by date than ethics.[5] Wal-Mart's success certainly is a case in point.

In the United Kingdom, ethical consumerism data show that although most consumers are concerned about environmental or social issues, with 83 percent of consumers *intending* to act ethically on a regular basis, only 18 percent of people act ethically occasionally, while fewer than 5 percent of consumers show consistent ethical and green purchasing behaviors.[6]

In the United States, since 1990, Roper ASW has tracked consumer environmental attitudes and propensity to buy environmentally oriented products, and it categorizes consumers into five "shades of green": True-Blue Greens, Greenback Greens, Sprouts, Grousers, and Basic Browns. True-Blue Greens are the "greenest" consumers, those "most likely to walk their environmental talk," and represent about 9 percent of the population. The least environmentally involved are the "Basic Browns," who believe "individual actions (such as buying green products or recycling) can't make a difference" and represent about 33 percent of the population.[7]

Joel Makower, co-author of "The Green Consumer Guide," has traced data on ethical consumerism since the early 1990s, and says that, in spite of the overhyped claims, there has been little variation in the behavior of ethical consumers over the years, as evidenced by the Roper ASW data. "The truth is, the gap between green consciousness and green consumerism is huge," he states.[8]

Take, for example, the growth of gas-guzzling sport-utility vehicles. Even with the steep rise in fuel prices, consumers are still having a love affair with them, as sales rose by almost 8 percent in 2004. These data show that threats of climate change, which may affect future generations more than our own, are hardly an incentive for consumers to alter their behavior.[9]

Myth #3: There will be a competitive "race to the top" over ethics amongst businesses.

A further myth of CSR is that competitive pressure amongst companies will actually lead to more companies competing over ethics, as highlighted by an increasing number of awards schemes for good companies, like the Business Ethics Awards,

Charming Psychopaths

Joel Bakan is an internationally renowned legal scholar and professor in the faculty of law at the University of British Columbia. His book, "The Corporation: The Pathological Pursuit of Profit and Power," and accompanying documentary, "The Corporation," explore the corporation's legal status as a "person" by asking, "What kind of person is this?" He spoke to SSIR *about these projects and his opinion of corporate social responsibility:*

Corporations are not talked about as institutions. They're talked about as your friend, your neighbor, as doing good things for you. A lot of money has been spent on generating an image of the corporation as fundamentally benevolent and as capable of actually caring about others.

Yet legally, that is not what the institution of the corporation was created to do. It was created to be a phenomenally effective vehicle for building large pools of capital to finance enterprise. It does this by putting the interests of the shareholders above all other interests – a corporation is required by law to sacrifice all other interests to the interests of shareholders. And that makes the corporation quite an unbenevolent institution, if you're not a shareholder.

What's fascinating to me as a lawyer is that we as a society have granted this institution legal personhood. A corporation can enter contracts, it can own property, it has human rights. No other nonhuman entity has these privileges. And so in the book and film I asked, "What kind of person is the corporation?"

One of the first things you learn in corporate law is that the fundamental obligation of the corporation is to serve itself. So basically the kind of person a corporation is is a profoundly self-serving person. And as you learn in any introductory psychology class, that is the definition of a psychopath.

I'm not saying the people who work for corporations are psychopaths.

or *Fortune*'s annual "Best Companies to Work For" competitions.

Companies are naturally keen to be aligned with CSR schemes because they offer good PR. But in some cases businesses may be able to capitalize on well-intentioned efforts, say by signing the U.N. Global Compact, without necessarily having to actually change their behavior. The U.S.-based Corporate Watch has found several cases of "green washing" by companies, and has noted how various corporations use the United Nations to their public relations advantage, such as posing their CEOs for photographs with Secretary-General Kofi Annan.[10]

Meanwhile, companies fight to get a coveted place on the SRI indices such as the Dow Jones Sustainability Indexes. But all such schemes to reward good corporate behavior leave us carrying a new risk that by promoting the "race to the top" idea, we tend to reward the "best of the baddies." British American Tobacco, for example, won a UNEP/Sustainability reporting award for its annual social report in 2004.[11] Nonetheless, a skeptic might question why a tobacco company, given the massive damage its products inflict, should be rewarded for its otherwise socially responsible behavior.

While companies are vying to be seen as socially responsible to the outside world, they also become more effective at hiding socially irresponsible behavior, such as lobbying activities or tax avoidance measures. Corporate income taxes in the United States fell from 4.1 percent of GDP in 1960 to just 1.5 percent of GDP in 2001.[12] In effect, this limits governments' ability to provide public services like education. Of course, in the end, this is just the type of PR opportunity a business can capitalize on. Adopting or contributing to schools is now a common CSR initiative by leading companies, such as Cisco Systems or European supermarket chain Tesco.

A customer donates to the Salvation Army outside a Wal-Mart store. Wal-Mart voluntarily matches all donations collected at its stores.

PHOTOGRAPH BY DAVID MCNEW/GETTY IMAGES

Myth #4: In the global economy, countries will compete to have the best ethical practices.

CSR has risen in popularity with the increase in reliance on

Instead, they are people who have to live dual lives – one shaped by the mandates and requirements of the corporation, and one not. On one hand, they have to make decisions that might be very harmful or exploitative of human beings, or very bad for the environment, in order to serve their responsibility to their shareholders. But then on the other hand, they are very decent fathers, mothers, and citizens, helping to coach their kids' baseball teams and all of that. Somehow they live with that cognitive dissonance.

A useful analogy, as someone who coaches and plays hockey, is that you may be a really decent, good, kind individual when you're off the ice. But when you get on the ice you're playing by a very different set of rules, and you do things that, if you did them off the ice, could probably land you in prison for several years. The worst that happens to you when you do them on the ice is you get a penalty and sit for two minutes in the penalty box. And I figured it may be quite similar with businesspeople, that when they get into the corporation, into their roles as managers, they're playing by the set of rules that are defined by the institutional and legal demands of the corporation. And that somehow enables them to do things that, from the vantage point of their off-the-ice life, might seem quite nasty.

Corporate social responsibility lessens that on-ice/off-ice gap in the personas of corporate leaders. It lessens guilt and improves morale within the corporation. But the priority of the corporation is always going to be to create profit for its shareholders. To the extent that we embrace CSR, we're allowing the psychopath to be charming. The corporation is constituted to be profoundly self-interested, unconcerned with others, incapable of feeling guilt or remorse, criminal if it can get away with it, disdainful of social conventions – the very definition of the psychopath. Another characteristic of human psychopaths is their ability to portray themselves as benevolent and charming. That makes them all the more dangerous, because you don't see what they truly are. To some extent, corporate social responsibility plays that role.

Table 1 – Regulation or Burden?[1]

REGULATION	PREDICTION BY BUSINESS	REALITY
National minimum wage	Would result in over 1 million U.K. job losses within two years	Unemployment fell by 200,000
EEC introduction of catalytic converters	The cost of the technology would be £400 to £600 per vehicle, with a fuel consumption penalty on top	Real costs of around £30 to £50 per converter; technological innovation led to smaller, cheaper cars
U.S. Clean Air Act	Would cost the U.S. $51 to $91 billion per year and result in anywhere from 20,000 to 4 million job losses	Yearly cost of $22 billion to business, but employment in areas affected up by 22 percent; the benefits arising are between $120 and $193 billion
Montreal Protocol	Opposed by industry on economic cost grounds, but no projected figures	No impact; substitute technologies may have saved costs, according to follow-up studies

1 D. Doane, "From Red Tape to Road Signs: Redefining Regulation and Its Purpose" (London: CORE Coalition, 2004).

developing economies. It is generally assumed that market liberalization of these economies will lead to better protection of human and environmental rights, through greater integration of oppressive regimes in the global economy, and with the watchful eye of multinational corporations that are actively implementing CSR programs and policies.

Nonetheless, companies often fail to uphold voluntary standards of behavior in developing countries, arguing instead that they operate within the law of the countries in which they are working. In fact, competitive pressure for foreign investment among developing countries has actually led to governments limiting their insistence on stringent compliance with human rights or environmental standards, in order to attract investment. In Sri Lanka, for example, as competitive pressure from neighboring China has increased in textile manufacturing, garment manufacturers have been found to lobby their government to increase working hours.

In the end, most companies have limited power over the wider forces in developing countries that keep overall wage rates low. Nevertheless, for many people a job in a multinational factory may still be more desirable than being a doctor or a teacher, because the wages are higher and a worker's rights seem to be better protected.

What Are the Alternatives to CSR?

CSR advocates spend a considerable amount of effort developing new standards, partnership initiatives, and awards programs in an attempt to align social responsibility with a business case, yet may be failing to alter the overall landscape. Often the unintended consequences of good behavior lead to other secondary negative impacts, too. McDonald's sale of apples, meant to tackle obesity challenges, has actually led to a loss of biodiversity in apple production, as the corporation insists on uniformity and longevity in the type of apple they may buy – hardly a positive outcome for sustainability.[13]

At some point, we should be asking ourselves whether or not we've in fact been spending our efforts promoting a strategy that is more likely to lead to business as usual, rather than tackling the fundamental problems. Other strategies – from direct regulation of corporate behavior, to a more radical overhaul of the corporate institution, may be more likely to deliver the outcomes we seek.

Traditional regulatory models would impose mandatory rules on a company to ensure that it behaves in a socially responsible manner. The advantage of regulation is that it brings with it predictability, and, in many cases, innovation. Though fought stridently by business, social improvements may be more readily achieved through direct regulation than via the market alone, as some examples show in Table 1.

Other regulatory-imposed strategies have done more to alter consumer behavior than CSR efforts. Social labeling, for example, has been an extremely effective tool for changing consumer behavior in Europe. All appliances must be labeled with an energy efficiency rating, and the appliances rated as the most energy efficient now capture over 50 percent of the market. And the standards for the ratings are also continuously improving, through a combination of both research and legislation.[14]

Perhaps more profoundly, campaigners and legal scholars in Europe and the United States have started to look at the legal structure of the corporation. Currently, in Western legal systems, companies have a primary duty of care to their shareholders, and, although social actions on the part of companies are not necessarily prohibited, profit-maximizing behavior is the norm. So, companies effectively choose financial benefit over social ones.[15] (See sidebar, p. 29.) While a handful of social enterprises, like Fair Trade companies, have forged a different path, they are far from dominating the market. Yet lessons from their successes are being adopted to put forward a new institutional model for larger shareholder-owned companies.

In the United Kingdom, a coalition of 130 NGOs under the aegis of the Corporate Responsibility Coalition (CORE), has presented legislation through the Parliament that argues in favor

PARADOXICAL CONSEQUENCES OF CSR *by Naomi Abasta -Vilaplana*

As CSR spreads into the developing world, it may be inadvertently triggering new barriers to humane labor practices, according to recent reports from the field. Over the past year, evidence has emerged that at least in some cases, factory officials in charge of manufacturing consumer goods for Western markets are falsifying records in order to appear to be in compliance with the tougher labor standards demanded by their multinational corporate customers.

Such factories simultaneously face demands to enforce fair labor standards and to reach levels of productivity that could only be attained by breaking these standards. Factory managers may thus consider these ethical labor standards to be a sham in light of corporations' other message: produce at all costs.

According to a report issued last year by Oxfam,[1] this tension leads many suppliers to keep fake records and to resort to such tactics as training and bribing workers to lie about working conditions to auditors. In the May 2005 issue of *Supply Management*, author Emma Clarke reports that there are now even software packages that are designed to help factory managers in China keep double books.

As Oxfam found, "[Suppliers] have to make compromises somewhere, and the factory managers know that so long as they do not indulge in gross abuses of human rights such as using child labor or forced labor, fulfilling the order according to the requirements of time, cost, and quality is the greater priority." And so unless the internal purchasing practices of large corporations are reassessed, excessive working hours, forced overtime, and harassment of workers who attempt to form unions may continue to be the norm.

1 Oxfam GB, Clean Clothes Campaign, and Global Unions, "Play Fair at the Olympics," March 2004.

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of an approach to U.K. company law that would see company directors having multiple duties of care – both to their shareholders and to other stakeholders, including communities, employees, and the environment. Under their proposals, companies would be required to consider, act, mitigate, and report on any negative impacts on other stakeholders.[16]

Across the pond, Corporation 20/20, an initiative of Business Ethics and the Tellus Institute, has proposed a new set of principles that enshrines social responsibility from the founding of a company, rather than as a nice-to-have disposable add-on. The principles have been the work of a diverse group including legal scholars, activists, business, labor, and journalism, and while still at the discussion phase, such principles could ultimately be enacted into law, stimulating the types of companies that might be better able to respond to things like poverty or climate change or biodiversity. Values such as equity and democracy, mainstays of the social enterprise sector, take precedence over pure profit making, and while the company would continue to be a profit-making entity in the private realm, it would not be able to do so at a cost to society.

Of course, we are a long way from having any of these ideas adopted on a large scale, certainly not when the CSR movement is winning the public relations game with both governments and the public, lulling us into a false sense of security. There is room for markets to bring about some change through CSR, but the market alone is unlikely to bring with it the progressive outcomes its proponents would hope for. While the *Economist* argument was half correct – that CSR can be little more than a public relations device – it fails to recognize that it is the institution of the corporation itself that may be at the heart of the problem. CSR, in the end, is a placebo, leaving us with immense and mounting challenges in globalization for the foreseeable future. □

CORPORATION 20/20 DRAFT PRINCIPLES[1]

1. The purpose of the corporation is to harness private interests in service of the public interest.
2. Corporations shall accrue fair profits for shareholders, but not at the expense of the legitimate interests of other stakeholders.
3. Corporations shall operate sustainably, helping to meet the needs of the present generation without compromising the ability of future generations to meet theirs.
4. Corporations shall distribute their wealth equitably among those who contribute to its creation.
5. Corporations shall be governed in a manner that is participatory, transparent, and accountable.

1 See www.corporation2020.org

1 N. Klein, *No Logo: Taking Aim at the Branding Bullies* (United Kingdom: HarperCollins, 2001).
2 Co-operative Bank, 2004 Ethical Purchasing Index, http://www.co-operativebank.co.uk/servlet/Satellite?cid=1077610044424&pagename=CoopBank%2FPage%2FtplPageStandard&c=Page.
3 A. Zimmerman, "Costco's Dilemma: Be Kind to Its Workers, or Wall Street," *Wall Street Journal*, March 26, 2004.
4 M. Kelly, *The Divine Right of Capital: Dethroning the Corporate Aristocracy* (San Francisco: Berrett-Koehler, 2003).
5 U.K. Institute of Grocery Distributors, 2003.
6 "Who Are the Ethical Consumers?" Co-operative Bank, 2000.
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14 Ethical Purchasing Index, 2004.
15 E. Elhauge, "Sacrificing Corporate Profits in the Public Interest," *New York University Law Review* 80, 2005.
16 See www.corporate-responsibility.org.