Addressing Possible Conflicts of Ethical Management

John Briginshaw

ABSTRACT

There is increasing emphasis on corporate social responsibility (CSR) by both businesses and educational institutions. One particularly influential framework is the triple bottom line concept, which asks businesses to report not just on their economic performance, but also on their social and environmental impact. However, there may be conflict between the needs of different stakeholder groups, especially between employees and stockholders. As stewards of stockholder resources, managers should sacrifice those resources only if that sacrifice is supported by a substantial moral imperative.

Addressing Possible Conflicts of Ethical Management

The adoption or emphasizing of ethical business management practices or corporate social responsibility (CSR) is an important trend in business management and business education. Business executives appreciate these trends as a way of more closely aligning everyday practice with their moral and spiritual beliefs. Impetus for the adoption of CSR policies such as "Triple Bottom Line" has come from a variety of sources such as international and non governmental organizations, and from customer and sometimes shareholder pressure. Competitive job markets for younger employees (who tend to be more knowledgeable and sensitive to concerns about CSR) have also been a factor encouraging more attention to CSR. Business schools have increasingly become involved in promoting CSR. For example, the mission statement of Pepperdine University's Graziadio School of Business and Management affirms "a higher purpose for business practice than the exclusive pursuit of shareholder wealth"[1] and the School offers MBA courses in Leadership and Ethics, as well as the innovative student-led Values Centered Leadership Lab. UC Berkeley's Haas School launched its Center for Responsible Business in 2003 and now offers courses at the MBA and BS levels[2].

Approaches to CSR

As an example of CSR approaches, Triple bottom line[3], a concept usually credited to UK based consultant and author John Elkington, is a system where the performance of the company in serving stockholders (**economic** or profit performance) is only one of three "bottom line" performance measures – company **social** performance in its dealings with people (such as employees, customers and the broader local community) and company efforts in achieving sustainable **environmental** performance (the company bottom line with respect to planet) are also measured. For example, Starbucks CSR efforts are centered around its people – the company's six guiding principles[4] state that it seeks "embrace diversity" and to provide a "great work environment" where employees are "treated with dignity and respect". The company recognizes "that profitability is essential to our continued success," but only in the last of the six principles. British Petroleum has adopted the "Beyond Petroleum" concept, a planet-centered initiative which includes "enabling the material transition to a lower carbon future"[5]. In the US, Home Depot offers a CSR report which considers the environmental impact of its products on forests in North America and the Amazon[6].

---

[1] http://bschool.pepperdine.edu/welcome/mission/

[2] http://www.haas.berkeley.edu/responsiblebusiness/Teaching.html

[3] Savitz and Weber (2006) and http://en.wikipedia.org/wiki/Triple_Bottom_Line

[4] http://www.starbucks.com/aboutus/csrreport/csr.htm

[5] http://www.bp.com/sectiongenericarticle.do?categoryId=9028308&contentId=7019491

[6] Demos (2006)

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission. www.manaraa.com

However, some companies have been criticized as paying lip service to CSR concerns to mollify concerned stakeholders (so-called "greenwashing"), while their managements practice "business as usual" or worse. For example, commentators note that Enron issued regular reports on its CSR and had policies promoting climate change and even anti corruption[7], while engaging in widespread fraud and misrepresentation of its results and operations. The emphasis on reporting as a first stage of CSR has led to some "reviled" companies receiving high CSR ratings – corporate social responsibility consultancy Salter Baxter indentified British American Tobacco (BAT) as one of 11 CSR leaders in 2008, despite admitting that it would not accept BAT as a client[8]. Shell, the Netherlands/UK oil company sued over alleged involvement in the death of Nigerian writer and activist Ken Saro-Wiwa[9], was also noted as a CSR leader by the London based consultancy.

Can CSR Take from the Weak?

However, CSR may have even deeper problems than companies who pay lip service to the practice. If companies excessively prioritize the welfare of staff and environmental concerns, stockholders' returns may suffer, and those stockholders may be humble folk (for example, retirees) who are using their stockholders' returns to literally put food on the table. It is certainly true that ethical management is very often good business[10] and that unethical management is almost invariably bad business[11]. However, there are grey areas where the interests of employee stakeholders can conflict with those of investor stakeholders (stockholders) in a zero-sum game. In these cases a value judgment has to be made about how much of a limited pie should be allocated to each stakeholder group. This situation is complicated by the fact that the allocation decision is being made by a member of the employee stakeholder group (usually an executive officer or manager), who may have a conflict of interest as he or she may benefit if the allocation to the employee group rises.

To move away from the theoretical, let us consider the example of employee perquisites or perks – non-cash benefits to employees which enhance their experience of working for a company. These perks may also benefit the company by attracting new employees and/or enhancing the productivity of existing employees. For example, free childcare is seen by pharmaceutical company Abbott Labs as a critical "strategy to attract and retain exceptional employees." Other employers who offer childcare cite enhanced productivity and reductions in absenteeism as benefits of offering the benefit[12], arguments which, taken together, make a strong case that offering childcare has significant benefits for employee and employer alike. Looking at a more nuanced example, Cnet.com News reports that "Google has become renowned for its employee perks: massages, game rooms, gyms, laundry facilities, and free food three times a day"[13]. Within this larger range of employee benefits, it is difficult to determine which of them might be justified by employee productivity and which should be viewed as additional compensation and justified by the market value of the employees, in the same way as an appropriate cash wage would be calculated.

Any examination of the pay and benefits of management and employees (including as a component of a good corporate social responsibility policy) can be viewed as an example of what

[7] http://www.alternet.org/story/13852/building_economic_democracy

[8] Jowit (2008)

[9] Mouwad (2009). In June 2009, Shell paid an out-of-court settlement of $15.5m while denying involvement.

[10] See the empirical findings reported in Pawa and Krauz (1995), 15-16.

[11] For detailed discussion of some examples, and the consequences, see Sims (2003), especially Chapters 6-7.

[12] Shellenbarger (2009)

[13] http://news.cnet.com/8301-13577_3-10024551-36.html. In fairness, we should note that Google's founders (who determine many of the perk policies) remain substantial stockholders (and thus bear some of the cost of the perks personally), and warned potential stockholders of their perk-heavy policy at the IPO stage (see http://valleywag.gawker.com/5040986/googles-food-perks-on-the-chopping-block).

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission. www.manaraa.com

economists call the "principal-agent" problem. What the "principal-agent problem" means in layman's terms is that a company owned by one or more shareholders (the principal) and managed by one or more managers (the agent), can be the source of conflicts and problems. In the classical picture of the principal vs. agent interaction, the principal (stockholder) wishes to maximize the share price, whereas the agent (manager) wishes to minimize his or her effort and maximize his or her pay.

Clearly, this picture misrepresents how both parties behave in the real world. Does the real world stockholder wish to poison the environment to boost the share price? Of course not. Do real world employees only care about their pay and nothing else? Perhaps a proportion of employees may think this way but, in general, no. However, if stockholders are asked to provide free food to employees, they may protest (or even ask – "where's my free food?"). On the other hand, if employees see the free food in front of them (thanks to top management decision), no doubt they will take some to ensure it does not go to waste. Then the principal-agent problem is there in full force. Resources to pay for the food, allocated by the decision of top management (who themselves may benefit from the free food), come out of the stockholders' piece of the corporate "pie" with little or no likely countervailing productivity benefit. In other words, the agent (manager) may not be doing his or her best in managing the business for the principal (stockholder).

The Case of the Art Gallery

Depending on how broadly one defines the interests of the community that can benefit as a stakeholder from the company's activities, it is possible to conceive of a wide variety of examples. Many companies sponsor art galleries and other places of culture in their local communities. This certainly benefits the local community and may give employees benefits if they are allowed free or discounted entrance to the galleries. However, it is almost invariably top management who are invited to gala openings and private showings at these galleries, not the stockholders whose money has sponsored the exhibitions. If we consider a Wichita based stockholder in a New York based firm, would that stockholder not prefer to receive his or her full dividend and sponsor local galleries in Kansas with it (and perhaps even attend an opening or two), rather than see his or her money spent in New York? And is there not a strong case that it is the stockholder who should be deciding how the resources should be allocated?

Although we often have in mind a picture of "big" shareholders and downtrodden employees at the mercy of those shareholders, a quick look at our own retirement plans and at press stories of CEO "high living" may show us that this picture is an oversimplification at best. In a society where all shareholdings eventually trace back to private individuals, whether shares are directly held by private investors, or held through "institutions" such as 401K schemes or mutual funds, the donation to the art gallery may ultimately be paid for by the weak – retirees, widows, orphans and the like who rely on stocks at difficult times in their lives – to disproportionately benefit the strong – the professional managerial class which has shown such explosive growth in the recent decades.

Keeping CSR Responsible

In many ways, it may be too early to criticize CSR for "going too far" in abstracting wealth from stockholders. Many top management groups show little concern for corporate responsibility, to the disbenefit of the environment (where employees and stockholders alike reside), and to the pain of their employees (who stockholders depend on to keep the business going). Readers may remember the cavalier treatment of experienced employees by Circuit City, which showed 3400 experienced staff the door in May 2007 in a misguided cost-cutting exercise which rode roughshod over any concept of CSR, only to erode 100% of stockholder wealth by going bankrupt about 18 months later.

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission. www.manaraa.com

However, implementing triple bottom line can be complex. If performance in conserving the environment, and performance in benefiting employees and the local community is to be assessed along with financial performance – how are the performance metrics to be weighted in assessing whether the company has "done well"? A company that performs poorly in environmental terms is a problem for the community but, absent government rescue, a company repeatedly showing poor financial performance is likely to be liquidated. Secondly, how can we deal with conflicts within the stakeholder groups? For example, Wal-Mart is criticized for offering health insurance to only a proportion of its workers, and not fully funding that benefit, even though many of its employees are poor. However, higher spending on healthcare would most likely lead to higher prices at the store, which would be paid by Wal-Mart's customers, many of whom are poor.

As managers are stewards of the stockholders' resources, we would suggest that those resources be sacrificed only if that sacrifice is supported by a substantial moral imperative. And the best long term solution for ensuring that moral imperatives are respected is to require **all** companies to satisfy them by regulation at the national level. For environmental imperatives, international co-operation is needed to prevent long term damage to the planet. Early adopters of good behavior may be worthy of congratulation as opinion leaders, but they must be mindful of the need to survive financially, especially in difficult economic times.

References

Demos, Telis, "Beyond the bottom line," *Fortune* (October 30, 2006) 72.

Jowit, Julia, "Reviled firms lead responsibility list," *The Guardian* (UK) (October 28, 2008), 26.

Mouwad, Jad, "Shell to Pay $15.5 Million to Settle Nigerian Case", *The New York Times* (June 9, 2009), page B1.

Pava, Moses L. and Joshua Krausz (1995), *Corporate Responsibility and Financial Performance*, Quorum Books (Westport, CT).

Savitz, Andrew W. and Karl Weber (2006), *The Triple Bottom Line*, Jossey-Bass (San Francisco, CA).

Sims, Ronald (2003), *Ethics and Corporate Social Responsibility*, Praeger (Westport, CT).

Shellenbarger, Sue, "Work & Family Mailbox," *The Wall Street Journal* (September 2, 2009), Page B13.

John Birginshaw, *PhD, is an assistant professor of Accounting at the Graziadio School of Business and Management of Pepperdine University. He has business experience in the shipping industry and management consulting experience in the retail banking, garment, and fast-moving consumer goods sectors. He has teaching experience at London Business School and University of California, Berkeley, as well as executive training experience at Euromoney Training, London and Hong Kong. Dr. Briginshaw is the author of Internet Valuation, published by Palgrave MacMillan. He received his MBA from the London Business School and a PhD from the University of California, Berkeley.*

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission. www.manaraa.com