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# Difference betweenCorporate Social Responsibility and Corporate Governance

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**ABSTRACT**

**Scholars and the business world have often viewed corporate social responsibility and corporate governance asparallel. But because globalization and the existence of multinational enterprises hasweakened government control, non-governmental organizations and other stakeholders arepressuring multinational enterprises for transparency, accountability and disclosure in theirglobal activities which involve social, environmental and ethical dilemmas.Stakeholders are also pressuring companies for values resonance.**

## INTRODUCTION

In the past decades the concepts corporate governance (CG) and corporate socialresponsibility (CSR) have intrigued both scholars and the business world but have mostlybeen debated independently. CG became more emphasized following the prominentcorporate financial scandals and failures in which stakeholders were heavily affectedcausing scholars to focus on agency issues and shareholder value maximization. Moreover CSR debates mostlyresulted from the need for companies to be socially, economically and environmentallyresponsible in order to achieve sustainable development.

The aftermath of the corporate scandals and collapses made the issue of responsibility to all stakeholders'shareholders inclusive become more important to corporations which have to find ways ofcreating value for the multiple stakeholders. However, withglobalization, the demands and pressures by stakeholders for transparency andaccountability have increased especially for multinational enterprises (MNEs) whose globalactivities affect a diversity of societies socially, economically and environmentally yet they have many regulations to comply with. Thus scholars and the business world are now focusing on the convergence of CG and CSR following somesimilar traits of the two concepts in terms of new governance, stakeholder issues, businessethics and regulations.

### 1. Corporate Social Responsibility

The concept of CSR has become very important for researchers and the business world.Early scholars of CSR first referred to it as 'social responsibility' (Carroll 1999).'Responsibility' for corporations has traditionally been to make money and increaseshareholder value. But besides that makingprofits, companies are responsible for their entire impact on stakeholders and the planet.Thus CSR is also a sustainable development thought that stresses the balance of threecomponents in the triple bottom line (TBL) by companies; economic wealth, social equityand environment regeneration Meeting needs likeeconomic, social, cultural and political needs "without compromising the ability of future generationsto meet their own needs" (sustainable development) means: minimizing use or waste of nonrenewableresources; sustainable use of renewable resources; keeping within the absorptivecapacity of local and global sinks for wastes (Barbier 1987).

### 1.1 CSR Definition

The concept of corporate social responsibility (CSR) has attracted a wide debate in theliterature regarding its purpose and meaning. CSR was first defined by Bowen (1953) inCarroll (1999) as "the obligations of businessmen to pursue those policies, to make those decisions, or tofollow those lines of action which are desirable in terms of the objectives and values of our society".


**Figure 1: The Pyramid of Corporate Social Responsibility,**

Source: Carroll 1991

CSR is defined as "situations where the firm goes beyond compliance and engages in 'actions that appear to further some social good, beyond the interests of the firm and that which is required by law". CSR as "the totality of the corporation's financial, social, and environmental performance in conducting its business, to create value". In a more specific way, CSR means "the social responsibility of business encompasses the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time" (Carroll 1991).

### 1.2 Other Perspectives on CSR

The awareness of the business case for CSR increased the thought of the evolution of CSRliterature and companies financial goals in that there is a shift from a focus on ethics to performance (Carroll 1991). With the old style of CSR "doing good to do good" the focuswas on social aspects while economic value as a motive to CSR was ignored; but the newworld of CSR "doing good to do well" emphasizes the need to maintain a close assessmentof the CSR initiative and company performance relationship. Thus CSR is notfor philanthropy for doing good to do good but instead more for doing well.

CSR is an important factor for profitability and should be central to the company's overallstrategy for its achievement. In fact CSR and profit were found to bepositively related in innovative firms. However, it does not necessarily mean that more responsible firms will be moreprofitable than less responsible ones (Vogel 2005). Usually established firms in largeindustries invest more in CSR and are expected to reap more also in terms of reputationand protection (McWilliams et al. 2006). Other views are that CSR is a proactive tool forvalue creation if used innovatively by companies to achieve 'smart' solutions. But Roberts (2001) sees CSR as an ethics of narcissus where companieswant to be seen as ethical when they are not (Roberts 2001). All this shows that the CSRmovement that advocates for broader corporate responsibilities for the environment, localcommunities, working conditions and ethical practices has gained impetus (Vogel 2005).

## 2. CORPORATE GOVERNANCE

The concept of corporate governance (CG) became vital to researchers after the past decade of financial scandals that led to the collapse and failures of some prominent companies for example Enron, Barings Banks and China Aviation Oil. However, these failures were not the mastermind of CG codes, the 1960's and 1980's witnessed many scandals which echoed the need for a voluntary or compulsory structure to be a guide for CG). Also the Sarbanes-Oxley Act of 2002 was formed to try and mitigate these problems, thus companies were coerced to seriously review their governance structures (Grant 2003).

The recent global financial crisis is connected to failure to practice good CG and in fact Organization for Economic Co-operation and Development (OECD) issued a report in 2009 on 'CG lessons from the financial crisis'. Although CG codes and principles have become very important to companies they cannot be one and the same worldwide. The diversity in corporate ownership structure, culture, legal and financial systems attributes to why countries and companies formulate their own governance codes and principles to fit within their business environment. According to Ryan et al. (2010), it is inevitable for governance researchers to take on new approaches both theoretically and methodologically in order to get new directions for the research on CG. Thus a few scholars are now focusing on 'new governance' for multinational enterprises (MNEs) which takes into account CSR in CG discussions and non-financial reporting. This shows that CG is constantly adjusting to the changes in the environment (Davies & Schlitzer 2008).

**2.1 Corporate Governance Definition**

Corporate governance is a fairly new phenomenon in the business world, however the theories from which it has developed emerge from diverse disciplines ranging from management, finance, economics, accounting, law and organizational behaviour (Mallin 2010). For that reason, the term 'corporate governance' does not have a single definition. According to Shleifer and Vishny (1997) "corporate governance deals with the way suppliers of finance to a corporation assure themselves of getting a return from their investment". CG is also defined as "the system by which companies are directed and controlled" (Cadbury 2000). To Ryan et al. (2010) "Corporate governance comprises the roles, responsibilities, and balance of power among executives, directors, and shareholders".

CG has been seen in a more comprehensive way by the OECD (1999) in Mallin (2010:7) where CG is defined as: "…a set of relationships between a company's board, its shareholders and other stakeholders. It also provides the structure through which the objectives of the company are set, and the means of attaining those objectives, and monitoring performance, are determined." With the above definition, CG can provide shareholders with increased confidence for a fair return on their investment while company stakeholders can be assured that the companies manage their impact on the society and environment responsibly. This is confirmed in the description "corporate governance deals with holding a balance between economic and social goals and between individual and communal goals". To sum up, CG is basically about what the business is for and in whose interests companies should be run and how (Elkington 2006).

**2.2 Theories of Corporate Governance**

There are several theories linked to corporate governance development for example Agency theory, stakeholder theory, stewardship theory, transaction cost etc, but the extent of their applicability is dependent on the development level of a particular country (Mallin 2010). The agency and stakeholder theories have mostly incited researchers (Sullivan 2000) and will also be the theories the thesis will look at.

**Agency Theory:** Berle and Means (1932) contributed a lot to the notion of CG in their description and examination of agency problems resulting from the separation of ownership and control in organizations and how shareholder value can be exploited (Gill 2008; Mallin 2010). CG has therefore often been considered to be about the principal-agent relationship where the owner of the firm is not its manager (Bouy 2005). This setting constituted the foundation of the shareholder model dominance. The Agency theory can be problematic in that, incidences of power misuse by the owner or conflict of interest by the agent can arise (Mallin 2010; Heath 2009). Therefore in order to build shareholder investment confidence the business society turned to CG to facilitate reduction of these agency problems. Moreover the focus on agency conflict resolution made the CG dialogue to acknowledge the supremacy of the shareholder primacy model, the law and economics view of economic efficiency (Gill 2008).

**Stakeholder Theory:** Several researchers have considered the stakeholder theory as a political matter rather than an economic theory of governance (Sullivan 2000; Freeman 1994) and others a management issue (Freeman et al. 2004). Moreover the conventional perspectives of modern economics and management theory have been criticized by stakeholder scholars (Donaldson 2002). Having two world views; shareholder view vs. stakeholder view is like having apple vs. fruit (Freeman et al. 2004). According to Mallin (2010) the stakeholder theory not only focuses on the shareholders but is composed of a broader group for example employees, shareholders, customers, suppliers, government, providers of credit, the local community, and interest groups like environmental groups. See illustration of the stakeholder group in figure 2 below

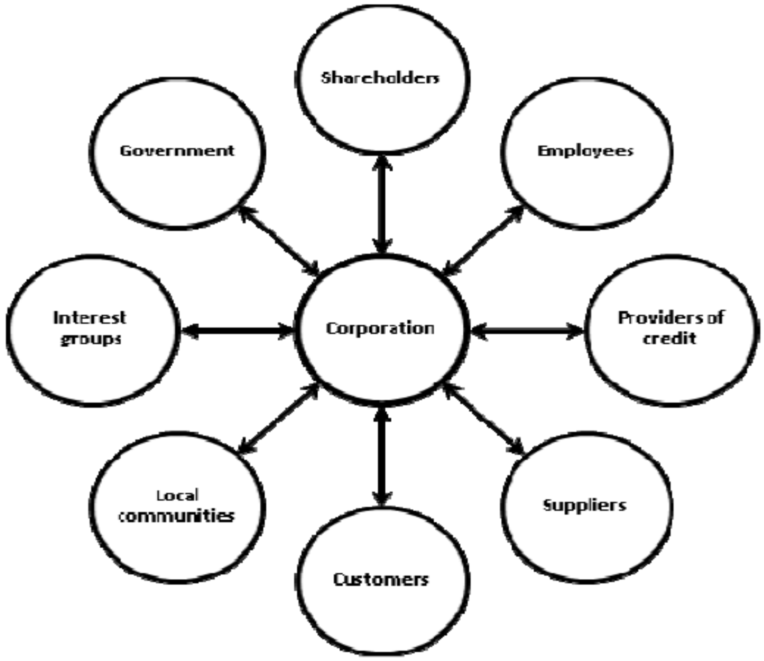


**Figure 2: The Corporation and its Stakeholders; Source: Mallin (2010:64)**

Jensen (2002) emphasized the stakeholder theory strength on value maximization and advised managers to take heed to all constituencies that affect the firm. The stakeholder theory postulates the inevitability for values in business and refutes the separation thesis of business and ethics. Thus the concept of value creation and business is closely linked to the notion of creating value for all stakeholders, basically to arrive at a win-win situation (Freeman et al. 2004). The stakeholder theory queries the firm on two grounds; 'its purpose and management's responsibility to its stakeholders' (Ibid). This necessitates ethical thinking where respect for other stakeholders is demanded and their reasoning also taken into account. The implication of the stakeholder theory is that firms could profit from engaging from some CSR activities that are vital to other stakeholders (not shareholders) who support the firm (McWilliams et al. 2006).

## 3. DIFFERENCE BETWEEN CSR AND CG

CG and CSR are two prominent independent research areas in the literature withenormous significance globally however the scholarly debate on their linkage is stillevolving. Concepts like CSR, CG, Corporate sustainability, corporate citizenship and TBLare increasingly becoming the yardstick for defining ethical business.CG that stemmed from shareholder's perspective has been emphasizing the accountabilityand transparency on the product and capital markets. On the other hand, CSR was influenced by stakeholder groups that call forgreater accountability, information and communication on the environmental demands inthe global world economy. Both CG and CSR include an ethicalelement in that with CG, ethics is explicitly communicated by company practice while withCSR ethics is seen in CSR statements and publications (Ibid).
Since there is no global standard for responsibility, no universal code of conduct (COC)and no standard system for TBL reporting, most corporationsare using the Global Reporting Initiative (GRI) guideline for preparing their social reports while others follow the UN global compact (UNGC) principles; The UNGC principles are demarcated into four sections; human rights, lab our, the environment and anti-corruption and companies are requested to adhere to theprinciples by integrating them into their core values. TheUNGC principles help entrepreneurships to promote CSR practice throughout theiractivities and act as a guide to demonstrate implementation and communicate progress totheir stakeholders (UN Global Compact 2011).

According to Enquist et al. (2008) these principles are a good beginning for CSR thinkingas they focus on public accountability, transparency, and the self-interest of companies, lab our, and civil society to initiate and share substantive action. Thus, these principlesought to be an integrated part of an entrepreneurships' mission and vision for responsible behaviour. From the ten UNGC principles, this thesis focused onprinciple 3, 5 and 10, which state that;

3) Businesses should uphold the freedom of association and the effective recognition of the rightto collective bargaining;
5) The effective abolition of child lab our;
10) Businesses should workagainst corruption in all its forms, including extortion and bribery (UN Global compact2011).

Wilson (2000) lists 'Governance' as one of the seven new rules for corporate conduct. Inthis rule, the need for "the corporation to be thought of, managed and governed more as a community ofstakeholders and less as the property of owners" is emphasized. Thus ethical thinking is positionedin the heart of stakeholder theory (Donaldson 2002). Similarly, Freeman (1994) argues thatfor trust to be built in a relationship, the ethical dimension must always be considered inthe stakeholder perspective.

## 4. NEW GOVERNANCE – THE INTERACTION BETWEEN CG AND CSR

New governance is still a new concept to researchers. The increasing rate at which theprivate sector is influencing public policy and regulation is a sign of new governance (Gill2008). Moreover, democracy, deregulation, privatization and market systems are the trendworldwide (Wilson 2000). Business regulation primarily comes from increasing the numberof codes and the guidelines initiated by businesses and regulators. Moreover, newgovernance is mostly emphasized where corporate conduct is concerned because itaddresses self-regulation and meta-regulation through which CG and CSR converge (Gill2008).

### 4.1 Self-Regulation and Meta-Regulation

The concept of corporate self-regulation has attained significant consideration ininternational agencies and business entities as it now acts as a match or alternative to theofficial governmental regulation (Gill 2008). Codes of conduct normally entail stipulationsfor corporate ethics, moral guidelines, and CSR matters like human rights, labour, the environment, and sustainable development (Ibid). However, codes of conduct have notbeen spared of criticism. Concerning new governance, the basic free market beliefs of selfregulationhave been criticized on the pretext that it is complex to scrutinize the codes'possibility to create change and others have argued that codes of conduct have not exactly improved corporate behaviour globally (Ibid). Notwithstanding that, even though the codeis strongly monitored, it necessitates change in the business culture and decision making forit to have effect on the premise (ibid).

Self-regulation is also characterized by non-financial reporting (Gill 2008) for examplecorporate social reporting (see Hess 2008) which basically communicates to society acompany's CSR policies and is a medium for transparency, accountability and dialoguebetween companies and their stakeholders (Gill 2008). Similarly, Hess (2008) argues that"disclosure of material information, dialogue with stakeholders and the moral development of thecorporation" are necessary for effective corporate social reporting. For that reason,companies publish CSR or sustainability reports according to the GRI (Hess 2008; Gill2008) and others have integrated CSR and governance in their annual financial reports (Gill2008). Moreover, according to Hess (2008), the evolution of corporate social auditingshows that it "is on the verge of becoming mainstream practice with the GRI leading the way". Hencethe codes of conduct and non-financial reporting tendency show how corporate self regulation is a channel for linking CG with CSR (Gill 2008).

For self-regulation of corporate conduct to be effective there is need for externalsupervision, which brings about Meta-Regulation (Ibid). Other than regulators, met regulation is conducted through participation in the process by stakeholders. Just like self regulation, meta-regulation is also a medium for the convergence of CG and CSR to createa combined regulation (Gill 2008).

According to Gill (2008), CG is graduating from a focus on the agency problem to enablemanagers and investors to pursue stakeholder involvement. Similarly, CG has graduallyadvanced from the conventional 'profit centered model' to the social responsibility model.Emphasis on the firm's commitment to stakeholder dialogue depictsa close relation between CG and CSR and stakeholder collaborationpaves way for creating economic wealth. CG is slowly includingconcepts like "non-financial accountability, ethical codes and standards of conduct, socially driveninvestment and fiduciary duties, board diversity, stakeholder engagement, sustainability reporting, andsocially responsible business strategies" which has made it complex to differentiate between CGand CSR in the international economic scene (Gill 2008). Nowadays CG and CSR haveboth become important globally highlighting the need for accountability by companies andalso the pressure for their convergence has become vital especially in large MNEs. Indeed, it is now questionable whether social reporting guidelines beingvoluntarily applied lead corporate disclosure, dialogue with stakeholders and moraldevelopment.

## 5. CORPORATIONS AND THEIR STAKEHOLDERS: A GUIDE TO CORPORATE SOCIAL RESPONSIBILITY

The corporation has grown up with industrialization, modernization and now globalization. It made them possible. The corporation is the work-horse of modern civilization. Without corporations, there might not be modern civilization with high living standards, longer life-spans, and great personal comforts. And, modernization and globalization remain the world's most viable mechanisms to enable the poor nations and peoples to share in the growing global prosperity. Only the corporation has been able to combine for economic value creation, financial capital, new technologies, and human resources. Sole proprietorships and partnerships were too limited to achieve the scale of research and production that corporations could.

Corporations will continue to create much of the wealth of society and open up new possibilities for humanity. Having said that, it is still manifest that a corporation is a set of relationships among different stakeholders. Each stakeholder plays some role in the success of the corporation. Without capital and stockholders, there can be no corporate entity. Without banks and other debt investors, the corporation cannot maximize its ability to earn a return on its equity capital.

But without customers, there will be no business for the corporation to do. Without employees, the corporation will be unable to do business. Quality and cost efficient suppliers are necessary for the success of any business. And, if the community turns against a company, losing confidence in its good faith, then that corporation will lose its business legitimacy, sometimes very rapidly as we have just seen in several cases around the globe. The corporation must also have concern for the physical and social environments in which it does business and must take care not to take unfair advantage of its competitors. By aligning and attending to the needs of these stakeholders, the corporation fulfills its duty to society to promote modernization and a better life for all in a sustainable way.

## 6. CORPORATE GOVERNANCE AND STAKEHOLDER INTERESTS

But, a modern corporation is under fire from many directions. It has duties and obligations to different stakeholders when these duties and obligations often seem to conflict with one another.

How is a corporation to decide what to do?

That is the role of governance. Corporate governance is the mechanism by which the values, principles, management policies and procedures of a corporation are made manifest in the real world.

The fundamental basis of corporate governance and responsibility is the value system of the corporation:

- Itshuman resource principles – respect and dignity for all
- Itsdedication to accurate and transparent accounting and financial standards
- Itsconcern for the environment, for good business ethics and conduct, for social advancement
- Itsover-riding passion to serve customers
- Its insistence on fair treatment of suppliers – and competitors
- Its uncompromising standard to comply with government laws and regulations in all countries in which it operates
- Its desire to work with others to lead society to a better economic standard and quality of life

The managerial skill lies in accomplishing these things at the same time. In the famous business book, "Built To Last" the authors describe the ability of good corporations to sustain themselves over generations by practicing "the genius of the and", accomplishing potentially conflicting objectives at the same time. A good structure of corporate governance satisfies these needs and interests of different stakeholders in a way that provides for long-term growth in the value of the company and its contribution to society. Its reputation and good will are enhanced, it commands success in the market for its products or services, its employees are productive and loyal, its equity owners are rewarded with good dividends and a rising price for their stock, and its growth is not impeded by external forces. Corporate governance divides responsibilities for policy-making, business decisions, and implementation among a board of directors, executive management, all management, and all employees. This is the general pattern for corporations around the world, with differences in detail arising in different countries.

No matter the structure, good governance requires checks and balances and responsible oversight to insure that many factors and points of view are considered. For example, a board should have the power, and spend the time, to probe into, and give informed opinions about, the plans of management.When employees, managers, executive management, or board members, look too much to their own power, prestige or financial reward, they act less and less as good stewards for the interests of stakeholders.  To state it differently, good corporate governance aligns the interests of management, shareholders and other stakeholders. The management and board of a corporation must define the values and principles for the company. To be effective and relevant to an individual company's specific circumstances, business principles must be developed and implemented by companies themselves, not mandated by outsiders.

## CONCLUSION

From the theories, it has been seen that CG and CSR are increasingly not being regardedindependently and there is an evolution of research on their integration. This chapter hasmade head-way in highlighting some of those arguments. In summary, corporations exist because they, in a sustainable fashion, enable people to constructively practice their craft and create jobs, economic value, and wealth for the society and the enterprise.

Stakeholders – customers, employees, investors, communities, suppliers, and competitors– all have a part in the fulfillment of a corporation's responsibilities.Governance is based on the corporation's values and is the responsibility of all membersof a corporation for development, implementation and oversight.And finally, the greatest beneficiary of good corporate governance and socialresponsibility will be the people of the developing and emerging worlds, for these ideals are truly our best hope to help close the poverty gap and enable all people to share in a global prosperity.

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