

THE EMERGENCE OF CORPORATE SOCIAL RESPONSIBILITY IN MODERN BUSINESS ENVIRONMENT

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Abstract

This paper intends to provide a basic introduction to the concept of corporate social responsibility. Conventional and regular business precepts view firms as purely a commercial enterprise and there is no requirement for these firms to engage in philanthropic deeds. The concept of corporate business performance conceives that the main objective of business firms to maximise shareholders' profits. On the contrary, the notion of corporate social responsibility requires business firms to consider the broader interests of the stakeholders including customers, employees and suppliers. This paper fundamentally explores the distinction between corporate business performance and corporate social responsibility. This paper also explains some of the factors that mobilise firms to begin applying corporate social responsibility within its business framework.

1. The conventional concept of corporate business performance

Firms are traditionally only concerned with corporate business performance. Corporate business performance conventionally and literally means how well a business firm could perform in a market (Perry Newman, 1995). In other words, that means how much profit a firm is capable of earning from its targeted market. It has been asserted (Perry Newman, 1995) that:

Competitiveness requires economic performance based upon a superior, distinctive competence relative to other firms within an industry. Business-level competitive strategy . . . can be based on low costs and low prices, differentiation of products, or focus[ed] on a well-defined customer [niche]. Competitive pricing is usually based on some cost advantage in the value chain based upon superior efficiency of the business [emphasis added].

Milton Friedman (1970) argues that a corporation's main purpose is to maximise profits for its stockholders. Other moral sentiments are of little concern to corporations, which has little obligation to take them into account. According to Friedman:

It is the sole obligation of a firm to maximise its own financial gain. [Emphasis added].

Friedman's 'stockholder' approach is generally consistent with Adam Smith's 'invisible hand' theorem. Smith opined that firms' pursuit of self – interests unintentionally produces a collective good for the society (Nava Ashraf et. al, 2005). Smith clearly articulated the following:

It is not from the benevolence of the butcher, the brewer, of the baker that we expect our dinner, but from their regard to their own self-interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages (Adam Smith, 1776) [Emphasis added].

The ‘invisible hand’ concept and capitalism simply connotes that a market is freely dictated only by demand and supply of products and services. Thus, in a ‘laissez faire’ economy (or free market economy) the utilitarian objectives of private gain and benefits are of utmost importance and override other institutional and societal non-monetary related principles such as the fulfilment moral obligations. Karl Marx (1848) similarly opined that a free market economy defines no rules or principles. The society becomes an enterprise for profit making and all that is within the capitalist system is considered merely a ‘commodity’.

2.Challenging the conventional concept of corporate business performance

It has been remarked that an economy based purely on a laissez faire fundamental and stockholder approach is increasingly questioned and challenged. Consider the statement below:

We are not just cost – effective machines that can be made ever more efficient. There is another dimension that has to be recognised and that is why the message I want to leave you with today is that business is uniquely placed to take a lead and to help create that vital balance in our lives, but doing so in partnership with local communities, with government, non-governmental organizations and other representatives of the voluntary sector (Ellen Johansson and Paulina Larsson, 2000) [emphasis added]

The statement above clearly shows that corporations can no longer be self-centred. Firms cannot conduct their businesses solely on the basis of interactions between supply and demand of goods and services and disregard society’s welfare and interests. Any corporations that disregard the need to foster strategic partnerships with local communities and other stakeholders may lose its reputation (Price Waterhouse Coopers, 2002) and competitive advantage (Michael Porter and Kramer, 2002). Literatures (Jackall R, 1988) show that corporations like a natural being are constantly tempted to abuse their powers for the sole purpose of maximizing shareholders’ interests. The following paragraphs shall explain some examples of this stockholder model and the consequences following from a disregard of the welfare and interests of the society.

One glaring example of the stockholder approach is the scandal involved in the manufacturing of Ford Pinto in 1971 (Crowther et. al, 2004). The gasoline tank of the Ford Pinto is prone to being damaged in a rear collision, increasing the risk of a fire. This was a design defect. As a result, Ford decided that settling any claims for injuries or deaths caused by its products would be less expensive than recalling them and changing the Pinto's designs. Ford's 'calculated' move led to numerous product responsibility lawsuits against the Ford Pinto. *Grimshaw v Ford Motor Co* (1981) 119 Cal.App. 3d 757, the California Court of

Appeal for the Fourth District, concluded that Ford was responsible for compensating the two plaintiffs (one of whom was burnt to death) who were in a Ford Pinto that caught fire following a collision.

Those punitive damages amounted to \$3.5 million, and Ford were forced to pay \$2.5 million reparation. Other than legal repercussions, Ford suffered severe reputational damages and loss of customers' confidence over its products. Ford Pinto remained to be one of the worst manufactured cars of all time for five years consecutively after the Grimshaw decision.

There are many examples of corporations abusing their power. The Enron Scandal, involving Enron and Arthur Anderson in October 2001, is one of the most well-known. For the sole purpose of swaying investors, Enron and Arthur Anderson conspired to provide false accounting statements and alter auditor's reports. Its stock price was \$90 per share in the middle of 2000, but dropped to just \$0.10 per share in October 2001 once the Enron crisis was revealed. In the wake of Enron's stock price plunge, investors lost an estimated \$11 billion, which shook public faith in blue-chip businesses.

The 2008 Chinese milk scandal provides another example of abuse of corporate powers. The scandal concerned infant milk products from Sanlu Inc. that were contaminated with melamine (a substance used to produce plastics that are often illegally added as a cheap alternative to boost the concentration of protein in the milk). China reported that by the September of 2008, Chen Zhu (Health Minister of China) stated that the contaminated milk had affected more than 6,200 infants. By 23rd September, As a result of the outbreak, 54,000 people became ill, and four people died (BBC, 2004). At the end of the saga, approximately 300,000 infants were affected and a total of six infants died during the period.

The Chinese premier Mr. WenJiabao (Xinhua Net, 2008) stated that:

This incident made me feel sad...it disclosed many problems for government and company supervision of the milk sources, quality and marketing administration... The government will put more efforts into food security, taking the incident as a warning. What we are trying to do is to ensure no such event happens in future by punishing those leaders as well as enterprises responsible. None of those companies without professional ethics or social morals will be let off [emphasis added].

As a result of the scandal, Sanlu incorporation declared bankrupt due to mounting debts after the melamine incident. Andrew Ferrier (CEO of Fonterra Cooperative Group) stated that:

We were aware that Sanlu was in a very difficult situation and faced mounting debts as a result of the melamine contamination crisis...the consequence is foreseeable since Sanlu, the nation's biggest liquid-milk producer lost about 900 million yuan (\$131 million) in 2008 because of the scandal and costs disposing of adulterated product.

3.A shift from corporate business performance to corporate social responsibility

Due to the rampant abuse of corporate powers, there is now a clear and active shift in business precepts towards corporate social responsibility (hereinafter referred to as CSR) (Perry Newman, 1995). The institutional principle of CSR connotes that business corporations derive its legitimacy from the society and not solely on the need to satisfy stockholders' interests.

Wood (1991) for example clearly asserted that:

The society grants legitimacy and power to business. In the long run, those who do not use power in a manner which society considers responsible will tend to lose it [emphasis added].

A similar notion has been forwarded by Perry Newman (1995) elsewhere that the,

The key concepts of business social performance include competitiveness, responsibility, legality [,] and legitimacy. These concepts parallel the four questions outlined [below]. Economic performance requires competitiveness; ethical performance requires responsibility in seeking to do what is right; legality requires compliance with the laws and regulations that apply to the business situation; and legitimacy requires sensitivity to the political context of the situation so that the political and social support necessary for a favourable business environment can be maintained [emphasis added].

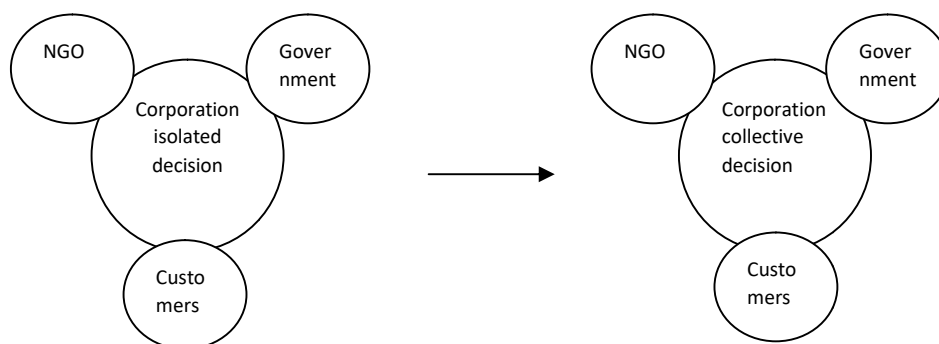
It appears that corporations no longer have the monopoly of decision making powers. Corporations cannot focus solely on their products and markets (limited to fulfilling stockholders' interests) but must also be concerned to improve the welfare and interests of the general society. Thus, organisations are increasingly required to fulfil the responsibilities of 'corporate citizenship' (Carroll, 2000). Under the advents of CSR, the decision making powers of corporations are now diluted and societal interests must be considered by organisations, and company performance is increasingly being measured by how well they meet the requirements of society.

The scope of CSR clearly requires corporations to pursue policies and actions that are in line with society's ideals and core principles (Bowen, 1953). Also, CSR requires corporations to emphasise on the interests of a broad range of stakeholders through an active interaction with all (Ramon Mullerat, 2001). Saleem Sheikh (1996) further explained the scope of CSR as where corporations either voluntarily or by virtue of statute, assume extra legal responsibilities (moral and ethical practices) whilst discharging their socio – economic obligations in society.

In brief, CSR calls for a drastic change within the strategic orientations of business corporations. Under the traditional business and corporate business performance model, corporations have absolute discretion and monopoly over decision making (solely aimed to maximise profits). Conversely, under the advents of CSR, the decision making powers of

corporations are now diluted and organisations must take into account the wider interests of the stakeholders (stakeholder analysis).

According to Freeman (1984), stakeholders are any people or groups of people that has some level of power and influence over an organisation's corporate policies. This means that the stakeholders' analysis does not only include the shareholders' interests but are also concerned with other external parties such as clients (customers), governments, non-government organisations (NGOs), suppliers as well as employees. This shift in the concentration of power is illustrated in **Diagram 1** below:



Scenario A (traditional business model)

Scenario B (CSR model)

Diagram 1: Transition and shift from isolated corporate decision making (scenario A) to collective corporate decision making (scenario B).

In **Diagram 1**, Scenario A represents a monopolistic and traditional business structure where the decision making power is centrally emphasised on the autonomy of a corporation. Therefore, business decisions are engendered without considering the needs of external stakeholders. Scenario B represents a CSR model of collective decision making where now an organisation must take into account the possible influence and interests of various external stakeholders. Therefore, CSR perceives that a firm owes moral obligations and duties to the society at large. This means that business organisations owe a duty not only to shareholders but also towards the stakeholders from a wider extra-legal perspective (referring to moral obligations). In contrast to the traditional corporate business performance model, the CSR theory envisages a multi-point responsibility between corporations and other external stakeholders (stakeholder model). An illustration of the stakeholder model is seen in

Diagram 2 below:

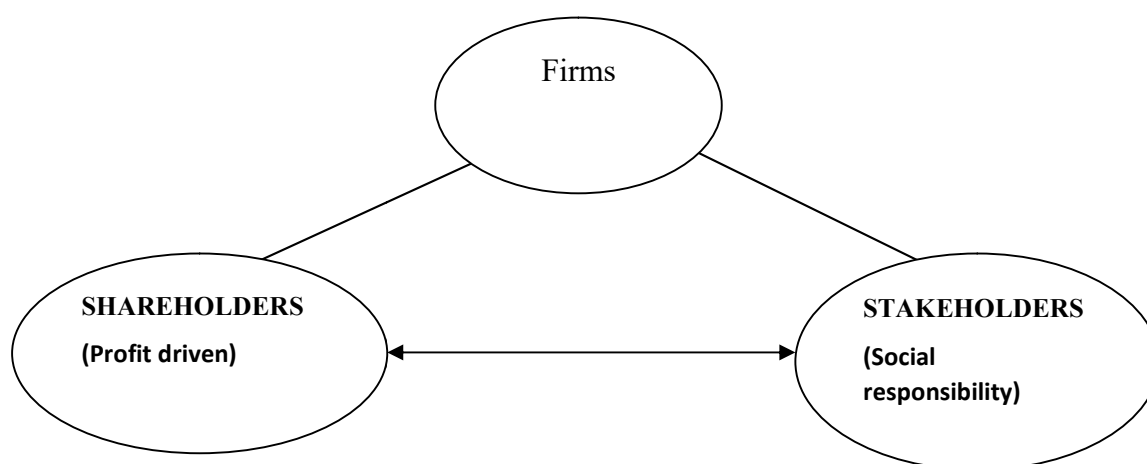


Diagram 2: Stakeholder model and multi-point responsibility

4. Factors encouraging the shift from corporate business performance to CSR

There are a few essential factors that are considered to be pivotal drivers of the shift from corporate business performance to CSR in Malaysia. The following paragraphs shall explore some of the factors in turn.

4.1 The development of legal framework

CSR was not given much emphasis a decade ago, as there were no provisions under the Companies Act 1965 requiring the implementation of CSR (ZuhairahAriff, 2008). The only hint of CSR in Malaysia during the 1990s was that Enshrined in the 1996 code, directors are expected to protect the interests of employees, creditors, and the public at large.

Part Three of the code for example specifically highlighted some limited forms of CSR. Corporate social responsibility (CSR) goals include conserving natural resources, enhancing living standards, and preventing harm to society's interests and well-being from being caused by the company's operations. Another goal is to help lower inflation.

In 2002, the Malaysian Code on Corporate Governance (MCCG 2002) (now the MCCG2021) was published. The code stipulated that the board of directors should be equipped with information that are:

Not just historical or bottom line and financial oriented but information that goes beyond assessing the quantitative performance of the enterprise and looks at other performance factors such as customer satisfaction, product and service quality ... environmental performance and so on, when dealing with any item on the agenda [emphasis added].

Publicly traded corporations must also declare in the annual reports any activities related to social responsibility that they have undertaken since 2004, as mandated by Bursa Malaysia in its Listing Requirements Malaysia (LRBM). Additional revisions to the MCCG in 2007 were spurred by the addition of Paragraph 2.17, which was drafted by the Workgroup on Quality Standards in Corporate Governance & approved by the High-Level Finance Corporate governance in 2007. To achieve the finest governance framework, the Code strives to set principles and best practises on the procedures and systems that PLCs can utilise.

Part 2 of the MCCG 2007 clearly established the best practices for public listed companies. Part 2 requires public listed companies to provide some narrative explanation in annual report the some social activities on macro social responsibility (external relation with stakeholders' interests). The public listed company may be delisted if it successively fails to provide this narrative explanation of CSR activities within its annual report.

Therefore, it is clear that there is increasing formality of legal framework (such as the LRBM and the MCCG 2007) that progressively required public companies to strive for CSR within its business activities. The legal impetus is considered to be an important justification for further research on CSR in Malaysia.

4.2 Political encouragement for CSR

Aside from legislation, the Malaysian government actively encourages companies to implement CSR. Companies who have a proven track record of CSR operations are eligible for tax deductions under Dato Seri Abdullah Badawi's (then Prime Minister for Malaysia) 2008 budget. In addition, the Prime Minister provided RM50 million in the 2008 budget to help the beginning stages of CSR implementation in enterprises from diverse industries and sectors.

There were other CSR-related initiatives initiated by the Prime Minister, including the Prime Minister's CSR Award 2007. In 2007, the Ministry for Women, Family, and Community Development introduced the CSR Award. It is the goal of the CSR Award to recognise businesses that have made substantial contributions to the well-being of their communities and society at large by implementing CSR activities to their fullest potential and effectiveness.

Those companies that made a major contribution to CSR in areas such as education, environmental protection and cultural and historic preservation were honoured with the awards. For example, Intel Technology SdnBhd was the winner in 2007 for the category of best CSR practices for the community and social welfare category. Intel's programme was established ten years ago focusing on the Back to School Programme supplying children with

basic education needs. The organisation also implemented the innovative Volunteer Matching Grant Programme where employees of the organisation give free tuition and participate in local schools projects.

British Petroleum (BP) Malaysia won the category of CSR for environment protection for having collaborated with the Fisheries Department and WWF to establish the Ma' Dearah Turtle Sanctuary in Terengganu. The programme is to create and increase awareness to public on the need to protect endangered species.

Perhaps the most significant political contribution to CSR is the introduction of the Silver Book Programme by the Government. The programme (directed primarily to Government Linked Companies (GLC)), contains guidelines on how CSR may be practically achieved in GLC. The programme is aimed to enhance the awareness of GLC towards the need to mitigate social costs and transform social obligations and citizenships into positive social contributions.

Guidelines 4.2 of the Silver Book Programme laid down the best practices of implementing CSR amongst GLC. Guideline 4.2 provides that GLC must align their strategies and coordinate their functions with respective ministries to ensure proper fulfilment of social obligations to the public. GLC are also required to periodically review their plans and to seek assistance (including financial allocations) from the Government to successfully implement their CSR activities.

One example of implementing the Silver Book Programme includes the Malaysian Airline System (MAS) establishment of the MAS Wings to provide air flights from rural settlements in Sabah and Sarawak to major towns in Malaysia. Another example is Telekom Malaysia's initiative since 1987 that has consistently allocated fifteen to twenty percent of its annual capital expenditure (CAPEX) on rural telephony. Since the inception of the programme in 1987, Telekom spent approximately \$4 billion despite the fact that the returns were unattractive as providing fixed telephone lines in rural areas cost approximately RM7,000 per 500 meter whereas it only costs RM2,000 in urban areas (Utusan Malaysia, 1999).

The continuous political encouragement has significant positive effects on corporate CSR activities. It has been reported (MESRA, 2006) that there was a surge in the participants and entries to the ACCA MESRA programme. The report (MESRA, 2006) showed that in 2002 there were merely 11 participants in the programme. However, in 2006 the total entries rose to 61 participants. The discussions above signified that the increasing political encouragement do have significant impact on the development of CSR. Therefore, this research is timely and aligns to the current political trend of CSR in Malaysia.

4.3 Social justification of CSR

Social issues play a large role in CSR, in addition to legal and governmental ones. As a general rule, social factors refer to CSR initiatives that aren't mandated by law or enticed by the government's pressure or other incentives.

Already, many corporations are taking proactive initiatives to boost the implementation of CSR in Malaysia as well as the Asian region. For example, the Asian Institute of Management (AIM) organised the Third Annual Asian Forum on CSR on 25th August 2004 (Utusan Malaysia, 2004). The forum addressed the importance for companies to go beyond conventional public relation methods but to craft a strategic alliance with the society.

Furthermore, there are increasing participations of CSR amongst academics that are contributing to the knowledge of the subject through appropriate research. At Nottingham University Business School's International Centre of Corporate Social Responsibility, for example, there is a focus on corporate social responsibility and Deakin University Corporate Citizenship Research Unit jointly organised a two day conference on CSR in Malaysia on 26th to 27th March 2003 (Utusan Malaysia, 2003). Professor Morris of Nottingham University stated that the conference is essential to equip private sectors on the appropriate methods and strategies than can in turn engender beneficial long-term relations with stakeholders.

Perhaps the strongest indication of societal movement on CSR is the increasing pressure by voluntary human rights groups on corporations to respect workers' rights and autonomy. More corporations including giant establishments are facing the pressure from independent human rights associations such the Amnesty International. There are increasing pressures on corporations especially against harassment of workers, corruptions, discrimination and provision of unsafe work environments (Joseph Kiarie, 2008).

Of course, again, the doctrine of responsibility is to blame for all of this complication. Parent firms might avoid responsibility for human rights breaches committed by their completely or partly owned subsidiaries due to the existence of limitations on their legal liability.

The separate legal entity and limited liability principle provides potentiality for corporations to breach workers' rights. Therefore, CSR is becoming increasingly essential to mollify the calamitous effect (Otto Kahn Freund, 1944) of the limited liability and separate legal entity doctrine.

4.4 Environmental reasons for CSR implementation

Environmental factors such as the 'greenhouse effects' (global warming) are instigating more concerted efforts of implementing CSR for greater sustainable growth. For example, UN GC was officially founded in July 2000 with the primary goal of coordinating best practises among businesses in constructing a sustainable environment, and it has been active ever since (DilekCetindamar, 2007). Several protocols are included in the framework to help create a more sustainable environment. A growing number of organisations across a wide range of industries are incorporating environmental considerations into their business plans as a result of rising environmental concerns. On the other hand, in Malaysia, PetronasNasionalBerhad has taken aggressive initiatives to minimise GHG emissions (Petronas Sustainability Report, 2008).

PetronasBhd established the GHG accounting and inventorisation across the organization. The inventorisation is an effective method to monitor GHG emission to mitigate climatic

changes. PetronasBhd has begun installing Cogeneration units to clean and filter burning natural gasses. It is estimated that the units can reduce GHG emissions by 500,000 tonnes of carbon dioxide 2,000 tonnes of acid gasses annually.

Similarly, Nestle Corporation in Malaysia also focuses on the importance of preserving natural environment. It has been stated clearly that:

At Nestlé, we define sustainable development as the process of increasing the country's access to higher quality nutritious food, while contributing to long-term social and economic development, and preserving the environment for future generations (Nestle Corporate Review, 2008).

The Nestle Environmental Management System (NEMS) was established to provide a systematic framework of all its environmental strategies. For example, Nestle manufacturing plants in Petaling Jaya and Shah Alam completed conversion to use natural gases (NGV) for its operations resulting in a reduction of 6 percent of GHG emission in 2008.

Furthermore, Nestle implemented an extensive integrated waste Management (IWM) approach that increased production efficiency and source reduction. The programme includes recovery and recycling solid was disposals. Nestle was able to reduce its solid wastes by 1,500 tonnes per year in 2008. One of the most successful programme is the redesign of Nestle Yogurt Cup that has reduced the thickness of the cup by 60 percent whilst maintaining the same strength and durability (Nestle Corporate Review, 2008).

Therefore, the arguments above clearly show that the study of CSR is becoming more important in light of growing concerns on environmental sustainability. This study therefore is aligned to the developing impetus of international efforts such as the Kyoto Protocol and the Montreal Protocol that stressed on the strategic importance of organisations pursuing a sustainable business strategy.

4.5 Religious rationale for the shift to CSR

There is growing importance of CSR as the principle is also aligned to religious requirements on preserving sustainable environments. For example, the Holy Quran (Surah Al Baqarahayat 11) stresses on the need to preserve the earth for the benefit of future generations. It has been written:

Janganlahkamumembuatkerusakan di mukabumi. (You are not to destroy and damage the earth).

Another aspect of CSR in Islam can be seen from its emphasis on manufacturing quality and reliable products. It has been written (Surat Al Araf, ayat 85):

Makasempurnakanlahtakarandantimbangandanjanganlahkamukurangkanbagi manusiabarang-barangtakarandantimbangannya (Meaning that one must sell merchandises according to specifications and quality).

Therefore, CSR is growing in importance as the subject also encompasses a study of natural law and religious principles. Therefore, CSR is not restrictively a management concern but includes a wider study of religious and spiritual doctrines.

5. Conclusion

It cannot be denied that CSR is gaining momentum as the forefront of business concerns. It is no longer viable for business firms to continually embrace the conventional concept of corporate business performance but firms must begin to comprehend the increasing demands of fulfilling corporate citizenship. Therefore, the narrower view of stockholder model must now clearly give way to the wider context of stakeholder approach.

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