

1. CORPORATE SOCIAL RESPONSIBILITY

INTRODUCTION: DEFINING CORPORATE SOCIAL RESPONSIBILITY

Outside of the microfinance sector, social performance is most often associated with corporate social responsibility (CSR), a term that is used interchangeably with corporate responsibility, corporate citizenship, social enterprise, sustainability, sustainable development, or corporate ethics. Generally, CSR refers to a company's obligation to be accountable to all of its stakeholders in all its operations and activities. It encompasses a multidimensional and global set of issues with strategic implications for business and policymakers, such as health, safety, diversity, gender equity, human resource policies, human rights, supply chain, the environment, and sustainable development.

In this sense, CSR is synonymous today with the **triple bottom line**. The triple bottom line reflects an integrated understanding of business performance in which social, environmental, and economic bottom lines are interdependent. The aim of a triple bottom line approach is to ensure business performance that is socially responsible, environmentally sound, and economically viable.

CSR is concerned not only with what companies do with profits but also how they make them. CSR goes beyond philanthropy and legal/regulatory compliance to address the manner in which companies manage their economic, social, and environmental impact as well as stakeholder relationships in all key spheres of influence. The modern advent of CSR both reflects and drives society's changing mores with regards to the social roles businesses are expected to play. Companies are now facing new demands to engage in public-private partnerships. Shareholders and stakeholders—including employees, consumers, suppliers, local communities, policymakers, the environment, and society at large—also require companies to be both transparent and accountable for their social performance. (Following on the heels of the massive corporate scandals and frauds during the early 2000s, for example, CSR advocates coined a new acronym, ESG—environmental, social, and governance—to represent the popular demand for greater social transparency.)

Three important considerations will help place CSR into the appropriate context. First, it is not a new concept, the hype currently surrounding it notwithstanding. Second, there is a clear distinction between CSR stemming from a desire to do good (the normative case for CSR) and CSR stemming from enlightened self-interest (the business case for CSR). A business's motivation for doing CSR will reflect different combinations of these motivations. Third, while there is general consensus that CSR is concerned with the societal obligations of business, there is substantial uncertainty about the nature and scope of these obligations.

PROACTIVE AND HARM AVOIDANCE APPROACHES TO CSR

There are two basic approaches to CSR: harm avoidance and a proactive approach. Harm avoidance aims to minimize any negative economic impact, bad labor conditions, corruption, human rights abuses, and environmental degradations. It calls for **compliance** with internationally accepted norms, guidelines, and standards and **control** of social and environmental risks, liabilities, and any negative impact.

The proactive approach to CSR aims to do good in terms of creating new value for business and stakeholders. It is achieved through activities, such as strategic philanthropy and community investment, which harness a company's core competencies, products, and services in improving society.

Ethical trade and fair trade, both of which incorporate approaches to managing the supply chain, are two prominent examples of the positive approach to CSR. Ethical trade refers to practices throughout the supply chain that promote adherence to core labor and environmental standards and human rights. In this context, a number of large corporations are developing strategies and codes of conduct related to ethical trade and supply chain management. Leaders in the field, such as members of the [Ethical Trading Initiative](#), encourage independent monitors to visit their suppliers, identify conditions that do not meet the code, and then plan improvements in collaboration with suppliers.

Fair trade is a niche market for specially labeled products meeting international standards established by [Fairtrade Labelling Organizations International](#). Fair trade standards aim to give disadvantaged producers in developing countries better trading terms and guarantee them a minimum price above that offered by mainstream markets. Fair trade arrangements also offer a premium to producers to be used for community development projects. To date, only a limited range of products (including coffee, tea, chocolate, and bananas) carry the fair trade label, and the size of the fair trade market remains small.

Wrapped up in both negative and positive conceptions of CSR and the triple bottom line is the concept of sustainability, defined as *“development that meets the needs of the present without compromising the ability of future generations to meet their own needs.”* The term *sustainability* was popularized by the Brundtland Commission's 1987 report [Our Common Future](#). The definition of sustainability originally emphasized ecological sustainability, but it has been expanded to mean societal sustainability and, as used by certain companies, company sustainability as well.

CSR IN THE BUSINESS MAINSTREAM

What differentiates past and current interest in CSR is that today's calls for greater corporate social responsibility are more broadly based, more specific, and more urgent. Those calling for greater CSR include not only activists and activist organizations,¹ but also general business associations and governmental organizations.² In many cases, moreover, such calls include specific recommendations for action, such as CSR audits and stakeholder engagement.

One can point to a number of “evidences” indicating the encroachment of CSR into the business mainstream. In 1999 UN Secretary General Kofi Annan called for a new social compact between business and society. This led to the development of the [UN Global Compact](#), which consists of 10 universal principles that companies commit to uphold. By 2006 the Global Compact had nearly 3,000 signatories, including 2,500 businesses from 90 countries. Among its other activities, the Global Compact focuses the role of the financial sector on how it can integrate the Compact's Nine Principles for business performance on human rights, labor, and the environment into investment research and stock-exchange listing criteria.

In May 2006 approximately 50 institutional investors, who collectively represent nearly \$4 trillion in assets, agreed to uphold a new set of six [Principles for Responsible Investment](#).³ The Principles were de-

1. See, for example, the [World Business Council for Sustainable Development, Business for Social Responsibility, International Business Leaders Forum](#), or [World Economic Forum](#).

2. See, for example, the [Department for Business, Enterprise, and Regulatory Reform in the United Kingdom](#).

3. The six Principles are (1) we will incorporate environmental, social, and corporate governance (ESG) issues into investment analysis and decision-making processes, (2) we will be active owners and incorporate ESG issues into our ownership policies and practices, (3) we will seek appropriate disclosure on ESG issues by the entities in which we invest, (4) we will promote acceptance and implementation of the Principles within the investment industry, (5) we will work together to enhance our effectiveness in implementing the Principles, and (6) we will each report on our activities and progress toward implementing the Principles.

veloped by a group assembled by the UN Global Compact and the United Nations Environment Program consisting of 20 institutional investors from 12 countries. Initially there were 32 signatories; that number has since grown to 231, including 91 asset owners, 89 investment managers, and 51 professional service partners. The Principles are voluntary and carry no legal sanctions.

A [survey by KPMG](#) found that over one-half of the top 250 companies in the Fortune 500 issue separate sustainability reports (e.g., reports on corporate social performance), including a majority of the top 100 companies in the financial capitals of Europe, Japan, U.S., and Canada. Of companies issuing sustainability reports, 75% cited economic reasons for producing them. The database managed by [CorporateRegister.com](#) indicates that the number of corporate nonfinancial reports has grown from less than 50 in 1992 to around 2,000 today.

CRO magazine's [Best 100 Corporate Citizens](#) ranking, published annually in collaboration with KLD Research and Analytics, is regarded as the third-most influential corporate ranking behind *Fortune's* "Most Admired Companies" and "100 Best Companies to Work For" according to a *PRWeek*/Burson-Marsteller CEO Survey. The ranking scores companies on [eight social, environmental, and financial dimensions of responsibility](#).

Other examples include the [London Principles of Sustainable Finance](#), developed by the Forum for the Future in consultation with over 50 financial institutions, and the [UNEP's Finance Initiative](#). The former outlines conditions under which financial markets can best promote the financing of sustainable development, whereas the latter has brought together banks and insurance companies to promote the mainstreaming of responsible investment and banking practices. Of particular interest to investors is the Asset Management Working Group of the Finance Initiative. Its purpose is to develop the capacity of mainstream fund managers to identify and respond to social and environmental issues.

Notwithstanding such high-profile examples, it is debatable whether CSR has entered the business mainstream. There remain a good many skeptics about CSR's influence and appropriateness. Meanwhile, the large majority of firms do not do CSR, and in many of those who do, CSR remains firmly embedded inside a public relations or philanthropy context and/or is at odds with positions that company actually takes on issues of social relevance.

SOCIETY'S CHANGING EXPECTATIONS FOR BUSINESS

It is undeniable that societal expectations for business are evolving. Although some may continue to argue that the sole ethical responsibility of corporations is to maximize shareholder value, this view is much rarer than it used to be. Several factors appear to be driving this process:

1. The expansion in human rights has focused attention on businesses' human rights policies and practices. Businesses are increasingly expected to be both protector and promoter of human rights.
2. The growth, reach, and influence of private business have conferred businesses with new rights and opportunities, but they have also created competitive pressures for corporate responsibility beyond traditional forms of compliance and philanthropy.
3. The failure of governments to solve many social problems has led to increased expectations of corporations to address social problems—especially those to which they may contribute—such as environmental degradation, human rights, unsafe or unsanitary working conditions, or inadequate product safety.
4. The growth in the number, sophistication, and connectivity of well-informed civil society organizations calling for increased corporate social responsibility has raised public consciousness

and turned the spotlight on corporate social behavior. The Internet and other global media have greatly expanded the outreach and influence of these civil society organizations.

5. Governments and companies are more aware that social, economic, environmental, and security challenges are too great and resources too dispersed for the public and private sectors to tackle alone, prompting action by both, collaborative and otherwise.
6. High-profile corporate ethics scandals during the early 2000s focused world and mass media attention on corporate citizenship issues and corporate governance.
7. With increased financial muscle and activism, institutional investors, together with regulators, have responded to the spate of ethics scandals and governance crises with calls for better corporate governance and accountability, transparency, and legitimacy.

This last point is a critical one. The intervention of mainstream investors in the CSR movement will do as much, or more, than anything in integrating CSR into the business mainstream. Investors' interest in CSR stems from an increased awareness of the risks and opportunities posed by a company's ethical, social, and environmental performance. Thought of by some as completely separate concepts, experience has demonstrated an overlap between the financial and social performance. The size of this overlap remains in dispute, but an emerging consensus acknowledges its existence.

TRENDS IN CSR

Increased interest in CSR has manifested itself in a number of significant ways.

Increase in 'Active Ownership' and Research by Mainstream Investors

In recent years, several large institutional investors have expressed interest in corporate governance and ethics and also in broader issues of corporate citizenship. Examples include the U.S. State and City Treasurers and Trustees, who have [issued a call](#) for greater investor attention to the risks and opportunities of global climate change; the AFL-CIO, which has launched a ["Capital Stewardship" campaign](#) to encourage more long-term, sustainable value creation; and financial institutions, such as JP Morgan, Morgan Stanley, Citigroup, UBS Warburg, and HSBC, which have all produced reports analyzing the business risks and opportunities created by issues such as global climate change, eco-efficiency, obesity, and the Millennium Development Goals.

To take another example, the [Association of British Insurers](#) has also issued disclosure guidelines on socially responsible investment (SRI), saying that "public interest in corporate social responsibility has grown to the point where it seems helpful for institutional shareholders to set out basic principles, which will guide them in seeking to engage with companies in which they invest."

Growing Influence of Socially Responsible Investment

While SRI funds constitute a small minority of global funds under management, their absolute size and relative share are growing rapidly. According to the Social Investment Forum, for example, socially screened funds in the United States grew by about 6.5% between 2001 and 2003 compared to a 4% fall in nonscreened funds. Negative screens remain popular with many investors; however, most SRI fund managers now also offer a variety of positive screens, and other social investment options, with a strong

emphasis on both financial and nonfinancial performance.⁴ SRI fund managers have also become more active in shareholder advocacy through proxy voting, dialogue with executive management, public debate, and collective initiatives with other SRI investors (see Table 1 on page 19).⁵

New Legal and Listing Requirements

In recent years, a number of countries have passed laws or established regulations or guidelines related to disclosure, corporate governance, and other areas of corporate citizenship. Examples in the United States include the [Sarbanes-Oxley Act](#) and the [SEC Mandate on Proxy Voting Guidelines](#).

The threat of government intervention remains an important driver of the CSR agenda. Government intervention creates both risks and opportunities for business, and neither MFIs nor investors can afford to ignore them.

International Norms and Conventions

There have been a variety of international initiatives to promote or establish norms or conventions related to corporate citizenship. Examples include

- The [United Nations Convention Against Corruption](#)
- [Adoption of the Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights by the UN Sub-Commission on Promotion and Protection of Human Rights](#)
- The [ILO's World Commission on the Social Dimensions of Globalization](#)
- The [UNDP's UN Commission on the Private Sector and Development](#)
- The [Financing for Development Initiative](#)

Activist Campaigns

Social and environmental activists continue to keep corporate citizenship on the public agenda, and they are using increasingly sophisticated means to do so. NGOs such as Friends of the Earth, the World Resources Institute, Human Rights Watch, Amnesty International, Global Witness, and Oxfam are now turning their sights to the financial sector, seeing it as a key leverage point to influence corporate social and environmental behavior.

Voluntary Financial and Reporting Frameworks

The last several years have seen an increase in collective action by industry stakeholders on a variety of corporate citizenship issues in various countries and industries, including financial services:

- [Equator Principles](#): An agreement by 14 of the world's major project finance banks in conjunction with the International Finance Corporation (IFC), the Equator Principles are intended to strengthen the social and environmental criteria in project finance. The signatory banks have agreed to adhere to the IFC's rules and guidelines on sustainable development for projects over a certain size.

4. www.socialinvest.org/areas/research/trends/SRI_Trends_Report_2005.pdf

5. The [Socially Responsible Investing](#) chapter of the Social Performance Map describes broader socially responsible investment trends in depth.

- [Global Reporting Initiative \(GRI\)](#): The GRI is the most recognized global CSR framework. It uses a multistakeholder process to develop and disseminate globally applicable Sustainability Reporting Guidelines. Its guidelines are for voluntary use by organizations for reporting on the economic, environmental, and social dimensions of their activities, products, and services. In October 2006 the GRI launched [G3](#), the third version of the GRI Guidelines. The 2002 Guidelines will be in use in parallel with the G3 during a 6- to 10-month transition period, after which the G3 will fully replace the 2002 Guidelines as a global sustainability reporting framework.
- The International Organization for Standardization (ISO): The ISO has developed over 15,000 standards to date. ISO is currently in the process of developing [ISO 26000](#), a voluntary standard on social responsibility.
- [AccountAbility](#): AccountAbility has developed the AA1000 standards for sustainability reporting. AA1000 is a standard for the measuring and reporting of ethical behavior in business. It provides a framework that organizations can use to understand and improve their ethical performance, and a means for others to judge the validity of claims to be ethical.
- United Nations: The [United Nations Global Compact](#) is an initiative to encourage businesses worldwide to adopt sustainable and socially responsible policies and to report on them. The Global Compact is not a regulatory instrument, but rather a forum for discussion and a network for communication including governments; companies and labor, whose actions it seeks to influence; and civil society organizations, representing its stakeholders.
- [Association of Chartered Certified Accountants \(ACCA\)](#): The ACCA has published a Guide to Best Practice in Environmental, Social, and Sustainability Reporting. The ACCA global sustainability reporting awards have been replicated in many national-level equivalents, advancing quality reporting worldwide.
- Organization for Economic Co-Operation and Development (OECD): The [OECD Guidelines for Multinational Enterprises](#) include Section III on “Disclosure,” which encourages timely, regular, reliable, and relevant disclosure on financial and nonfinancial performance.
- [Social Accountability International \(SAI\)](#): The SAI has created SA8000, which is an auditable certification standard based on international workplace norms of International Labour Organisation (ILO) conventions, the Universal Declaration of Human Rights and the UN Convention on the Rights of the Child.

NOTE ON CSR STRATEGY

Widespread anecdotal evidence suggests that the debate about CSR is shifting. It is less about whether to do CSR and more about how to do CSR. Although there is no boilerplate CSR strategy, the general consensus is that a firm’s CSR strategy should be unique, reflecting not only its industry characteristics but also the firm’s mission, values, core business activities, and strategic direction. Formulating CSR strategy also requires an understanding of the firm’s current social performance, which in turn requires development of appropriate metrics for measuring social performance.

Regardless of the CSR strategy, stakeholder engagement is, or should be, at the heart of CSR. CSR is about more than promoting a company’s own values and principles; it also includes an understanding of the values and principles of those who have a stake in its operations.

That said, there is often substantial uncertainty regarding a firm’s obligations to its stakeholders, and the form that this engagement should take is subject to much debate. Some see stakeholders as having a sig-

nificant input on decision making, while others see stakeholders as akin to an information resource with little influence over management. There is also the question as to whether the firm's institutional culture and management style support stakeholder engagement; there is often a large gap between the firm's style and that of its stakeholders. Then there is the issue of which stakeholders have legitimate standing in the firm's deliberations. Firms will need to consider the legitimacy, contribution, and influence of the stakeholder to determine whether engagement is appropriate and/or likely to result in a productive relationship.

In any case, stakeholder engagement is critical to the process. All firms will need to work through the process and find their own way to deal with these issues.

Despite a firm's best efforts, there is always the risk that doing CSR will backfire. Taking a public stand on CSR might, for example, draw unwanted attention to the firm, perhaps in areas in which its social performance is less than stellar. Or it may result in the firm being held to higher standards than its competitors who have not taken a stand on CSR. Negative attention might also be the result of poor implementation.

When asked to name the three to five major leadership or strategic management challenges in managing CSR and balancing stakeholder expectations, participants at a Kennedy School of Government roundtable on CSR (including representatives of business, civil society organizations, fund managers, and academics) identified the three broad themes (in decreasing order of importance): (1) integrating CSR into corporate strategy, (2) executive and board leadership, and (3) measuring and demonstrating the value of CSR.⁶ Table 1 shows a sampling of specific issues raised by respondents under each of the three themes.

6. "Leadership, Accountability and Partnership: Critical Trends and Issues in Corporate Social Responsibility."

CORPORATE SOCIAL RESPONSIBILITY

Table 1. Critical Challenges in Managing CSR and Stakeholders' Expectations

| Theme | Issues |
|--|--|
| Integrating CSR into corporate strategy | <ul style="list-style-type: none"> • Mainstreaming key issues from CSR departments to boards • Building CSR into the fabric of values, governance, and reporting • Integration across the organization • The need to break down silos • Adopting a strategic vision • Addressing social risk in the context of total risk management • Implementation that creates a CSR culture, not CSR departments • Infusing social responsibility among buyers, suppliers, customers, and competitors • Integrating CSR into corporate governance • Moving from CSR as public relations to CSR as core business strategy • CSR as a risk to be managed as opposed to one that can be electively avoided • CSR still seen as good public relations rather than inherent part of business |
| Executive and board leadership | <ul style="list-style-type: none"> • Proactive citizenship vs. reactive social responsibility • Engaging leadership outside the CSR silo • Adopting and executing a strategic vision • Leadership buy-in and commitment to instill CSR in corporate fabric • Need for senior management education • Fear of being held to higher standards for speaking up relative to laggards |
| Measuring and demonstrating the value of CSR | <ul style="list-style-type: none"> • Challenge of making the business case to investors • Lack of understanding as to what CSR means in media and investor relations • Need to do a better job communicating the public and social value of core business operations and economic impact • Convincing the board that CSR makes business sense |