

CORPORATE SOCIAL RESPONSIBILITY

An Excellent Idea... But Can It Be Implemented ?

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Corporate Social Responsibility is a very attractive idea. It invites private sector corporations to look beyond their narrow interest and become better citizens of our global society. What does this mean exactly ?

The senior management of a corporation , usually, has to deal with at least 7 groups of stakeholders : (1) the Board of Directors (2) The Shareholders (3) The Employees (4) The Suppliers (5) The Consumers (6) The Competitors and (7) Society at large. Many corporate scandals of the last few years were based on the abuse of authority by Management vis-à-vis the Board and/or shareholders. Those abuses would fall under the narrower concept of corporate governance. CSR is a much larger issue. It involves the relationship between Management + the Board + Shareholders vis-à-vis all their external stakeholders who are outsiders and have no legal say in the priorities or conduct of the corporation itself. What makes CSR a tall order is the fact that

normal corporate law and practice provides no clear mechanisms for the protection of external stakeholders. The purpose of a corporation is to make money for its owners. It is not designed to look after the public good.

Yet CSR is now extremely important because of the size and influence of multinational enterprises. Since the Second World War, the balance of power in the global system has shifted from state to non-state actors. This shift has accelerated from 1980 to 2008 where, as a result of the 1980 Reagan-Thatcher Revolution, efforts have been made to minimize and marginalize the State as an economic player. The four pillars of Reagan-Thatcher Capitalism were: (a) deregulation, (b) privatization, (c) reductions in government expenditures and (d) moving towards universal free trade. All of these tend to reduce the influence of Government on Society,

As a result, the 193 sovereign governments who are members of the

United Nations have lost considerable influence, while non-state actors, in particular multinational enterprises have become more and more powerful. Already, by the beginning of this millennium, of the 100 greatest economic units in the world, measured by spending power, 51 were businesses and only 49 governments. The Multinationals not only derive their power from their vast spending and investing potential but also by their high transnational mobility allowing them to escape regulation and taxation. These giant corporations are not only heavyweights in their country of origin but also in the countries where they have subsidiaries.

Because of the immense influence of these companies, an unimpeachable ethical behavior, by their CEOs is very desirable. Whilst there is no recognized standard for CSR, the ideal version would enjoin corporations to pursue the so-called TBL or Triple Bottom Line, according to which they would seek to (a) maximize in a harmonized fashion shareholders equity (b) protect the environment and (c) behave responsibility to society at large.

What is the Record so far?

Discussions and policy statements about CSR have started a good fifteen years and the OECD was one of the pioneers in this type of thinking. But what has been achieved in that period of time? So far the historical record of CSR is very mixed but there are three notable successes.

- The first lies in the area of standards

and norms. Private sector agreements, sometimes with the help of governments but often at the industry level, have succeeded in harmonizing norms, setting minimum standards of quality and establishing guidelines for good corporate behavior.

- The second partial success is in the environmental field. Corporations are much more environmentally friendly than, say, thirty years ago where concern about the environment was a public relations rather than a policy question. In the last few years, significant efforts have been made by corporations throughout the world, to produce greener and safer products. Of particular note have been the attempts, pioneered by the Geneva based Global Business Council on Sustainable Development to create global sector level agreements to select production methods that minimize negative environmental impacts. By voluntarily agreeing to forego harmful production methods even though they may be cheaper, the firms involved in these sector level agreements remove any competitive disadvantage that might be suffered by individual 'green' firms acting alone. All the firms adopt green production methods together. This approach has produced some positive results, in the cement industry, among others.
- The third and, possibly, the most impressive success of CSR is the growth of private philanthropy. Many millionaires and billionaires who have emerged from the boom

economies of the last two decades have created charitable foundations and, in some cases, given generously to promote the public good. Names like Bill Gates, Warren Buffett, Ted Turner, George Soros all come to mind. Their contributions have often been substantial and beneficial, especially in the Developing World.

At the other end of the spectrum is the bad news and indeed it is very bad. The 2008 Global Economic Crisis, which is likely to become an historical turning point in the history of Capitalism, has revealed gross corporate irresponsibility in the financial world and in some industrial areas. The worst offenders were the white collar criminals, either indulging in elaborate Ponzi schemes, like Bernard Madoff or the manipulation of accounting to produce fictitious results. Massive embezzlement has too often been dominating headlines.

Beyond unlawful behavior, the banking and financial worlds have created complex investment vehicles, at the border of legality, which have transformed the World Economy into a casino. Hedge funds, derivatives, short selling, collateralization of financial assets, subprime mortgages and general, hard to discover, off balance sheet operations have generated excesses which have only been exposed when the bubbles burst. As Warren Buffett eloquently put it, *'you discover who is naked only when you empty the swimming pool, not before.'* There was very little CSR in the global financial economy of the last few years. Most observers will agree to that.

In addition the delocalization of industry to emerging countries have, in many cases created sweatshops, the exploitation of labor and the importation of defective products to the consuming world. In extreme cases, fictitious drugs has been sold in the Third World with deleterious and often lethal effects for the patients.

On balance and especially in the light of recent events following the 2008 Crisis, CSR cannot, at present be called a success story.

What can be done ?

To reach the much needed goal of true CSR, appropriate global strategies have to be put in place. There are five candidates :

(1) Voluntary Guidelines and Relying on Good Samaritans

When I was one of the governors of the OECD, in the late nineties, in my capacity as Canadian ambassador to that institution, there was much talk about voluntary guidelines. Many countries resisted the idea of imposing any kind of regulation internationally and preferred to let market forces and industry level rule-making manage the conduct of corporations.

A set of so-called voluntary guidelines were enacted, not quite the ten commandments of Moses but more, a sort of friendly advice on how ethical corporations should behave. The strategy assumed that most corporate managers were Good Samaritans and would voluntarily pursue a triple bottom line policy which would, effortlessly,

result in the promotion of the public good.

The effectiveness of that strategy, which was doubtful from the beginning, received the coup de grace, in the 2008 Financial Crisis. Like Philosopher Kings, Good Samaritans are few and far between. The Great Plato, in his idealism, argued that governance by a philosopher king, intelligent and mindful of the best interests of his people would better promote the public good, than democracy, subject to the vagaries of voters' moods. The reasoning was plausible, but Plato learned to his detriment that philosopher kings are rare, especially when the Tyrant of Syracuse, a putative student of his, threw him in jail and wanted to sell him as a slave. In the end reliance on the goodness of absolute rulers is a major gamble, too often lost.

By analogy, the search for the ethical CEO, not as the exception but as the rule has proven to be quite illusory. For every philanthropist there have been dozens of selfish managers, seeking to maximize their own gain, with little regard for the Public Good. More importantly, the very structure of a modern corporation and the reward mechanisms within it, are inimical to true CSR. As the critics of CSR have noted, Chief Executive Officers rarely receive an explicit mandate, either from their board or their shareholders to promote the public good unless it is fully compatible with private gain. Shareholders expect management to maximize their equity. If the promotion of CSR is compatible with such maximization then it can go ahead.

However if it will reduce shareholders' equity, it will be frowned upon, in spite of declarations to the contrary for public relations purposes.

For these reasons CSR based on voluntary guidelines and Good Samaritans has a very limited potential of success.

(2) Name and Shame

It has been assumed that if delinquent corporations are identified and exposed they will try to correct their behavior, if only to reduce the negative publicity and regain the public trust. Hence a Name and Shame strategy via the Internet, by civil society groups and private citizens could, conceivably, be considered by as a suitable method to achieve CSR.

The Name and Shame strategy has certainly some potential especially if it can threaten to reduce corporate profits by giving a bad name to the designated corporate entity. However, here too, the results tend to be limited. Defending against Name and Shame attacks, can become just another public relations exercise. Spin doctors can be called upon to deflect such attacks and, quite often the irresponsible social behavior of the Offending Corporation can be hidden through outsourcing to distant countries and the use of obscure subcontractors.

(3) Industry Level Governance

Some have argued that industrial associations are well suited to establish standards of good behavior and impose

them on their corporate members. After all, this is done at the national level where industry and professional associations (doctors, lawyers, accountants, sports leagues etc.) establish and enforce rules on their members.

Such an approach has merit, but, nevertheless faces two major obstacles.

First, there are very few global level industrial associations capable of designing uniform rules of behavior because of cultural diversity, geographical dispersion etc. Most professional associations tend to be national and regional.

Second, even if global ethical rules of behavior are successfully agreed upon, the enforcement capability of global associations remains weak. At the national level, professional sanctions do exist (example disbarment of delinquent lawyers) backed by the coercive power of the state. But, at the global level there are few meaningful methods to force compliance and no world government to enforce them.

We are back to a variant of Name and Shame, which means that, in the final analysis, achieving CSR through industry associations is a very iffy proposition. The debacle in the banking world can only underscore this iffiness. Not only were the rules lax but their enforcement by the rating and regulatory agencies often non-existent.

(4) Recommendations by Intergovernmental Clubs

The G8, the G20, the OECD etc. are

intergovernmental clubs, with selective membership, by invitation only. All these clubs, come up with recommendations in the final communiqués, proposing ways of dealing with global problems. When the solution lies with governments then it can be assumed that the signatories will honor their commitment. Even here, this is not always the case because, when the decision-making involves a consensus, dissenting members can just opt out, and not be bound by an agreement they have not signed.

The OECD, for instance, is another club of 30 members, very active in producing recommendations and guidelines. However all OECD decisions, even the smallest ones, have to be taken by consensus (which I discovered to my dismay when I was ambassador there). This gives a de facto veto to any one member state. In addition a member may, instead of voting no, just abstain and by so doing, remain unbound by its contents. During my tenure there, opting out of unpopular agreements was frequent. As a result, the effectiveness of the sub-consensus recommendations was somewhat reduced.

Even in the cases where everyone signs, the actual record of compliance by individual signatories tend to be very varied as the G8 Research Group's monitoring of the G8 summits has shown. The average compliance record for all the members, remain low and would be even lower if individual good smarautan countries did not bring that average up, by zealous compliance. As for the G20, it is still a young 'club' and

the follow-up performance after the summit meetings, still to be tested,

In addition to the laborious decision making procedures in intergovernmental clubs and the uncertainty of compliance, it should be noted that the mandate of such clubs is to harmonize *government* behavior and not *corporate* behavior, which is left to national governments. The WTO, for instance is empowered to sanction governments. It has little direct jurisdiction on delinquent corporations. In fact, no one has such direct jurisdiction other than national governments. But the latter's authority is eroded by globalization and the foot-loose nature of corporations who can always escape regulation by moving elsewhere, at a moment's notice

(5) Enforceable Global Corporate Law

By a process of elimination the most promising strategy to bring about global CSR, is, in our view, to replicate at the international level what seemed to be working at the national level, before globalization : *enforceable corporate law*.

The most persuasive case for an international rule of law does not come from leftist extremists but from the greatest apologist of Capitalism and the founder of modern economics, Adam Smith. Although a devout advocate of free markets and the Invisible Hand, Adam Smith and many others after him, have pointed out that if Men were angels no laws would be needed. However since Men are, manifestly not

angels, laws are essential for the proper functioning of Society.

The non-angelic nature of human beings is recognized in all nation states where commercial law, the regulation of business, the protection of consumers and stakeholders is a normal part of the legal system. There are laws against usury, against false advertising, against collusion and monopolies, against price gouging etc.

If voluntary guidelines and the reliance on good corporate Samaritans were enough why would be bother with corporate law within a nation state? We would just exhort responsible behavior by corporate managers in pamphlets and websites and leave compliance to their good conscience. If they do not comply, they would be named and shamed but nothing more...

This is not how we proceed at the national level. The guidelines are not voluntary, they are binding, All corporations have to comply with a set of rules. Failure to do so will result in stiff fines, prosecution and possible jail sentences.

In fact, the United States, even in the thirty years of the Reagan-Thatcher Revolution was a highly regulated internally. As Edward Luttwack points out in his book *Turbo Capitalism*, the existence of 'greedy lawyers' (working on a contingency basis in class action suits) had had the effect of scaring corporations into abiding by the law or face huge financial settlements. The highly litigious nature of US Society has acted as a brake to corporate excesses.

With the advent of globalization and footloose corporations who can move to another country at a moment's notice, the effectiveness of national regulation has dropped significantly. As a result, unless a similar set of corporate rules are created at the global level with significant enforcement potential, CSR, will remain a beautiful dream and nothing more. There will be sporadic positive manifestations, here and there, an occasional headline-making philanthropic contribution but not much more. Human beings will continue to pursue their individual interests and there is no guarantee that the sum of private interests will result in the promotion of the public interest as the events of the 2008 global crisis have painfully demonstrated.

But an interesting question arises. In the absence of a world government who will make and enforce global corporate law ? At this stage, no intergovernmental institution has a clear mandate to do such a thing although many have moved into the field of making recommendations.

At first blush it would appear than an *extension of the mandate of the WTO* to allow it to create and enforce global corporate legislation may be an avenue worthy of exploration. This would

involve both the extension of its membership to near universality and a revision of its mission statement and charter. Its jurisdictional competence could also be extended beyond trade to investment and finance. This might create some duplication with the activities of the World bank and the IMF.

Institutional change of that magnitude is likely to be slow, even though the magnitude of the 2008 Global Crisis makes the unthinkable, thinkable. Who would have imagined at the end of 2007 that by the end of 2008, the Bush Administration would be nationalizing banks and coming up with huge bailout packages?

Necessity is the mother of invention and historical wild cards, such as major unforeseen event make fundamental change quite possible. Ultimately, it is our firm belief that true CSR will be attained when we have global corporate law and not before. In the meantime the other four strategies, as imperfect as they are should be continued but only until a mechanism for the global rule of law is put in place.

If we do not waste the lessons of the 2008-2009 Global Economic Crisis, this may happen earlier than expected.

FROM LA MADDALENA TO L'AQUILA

By Silvio Berlusconi,

prime minister, Italy

The clear and forthright debate among the leaders of the most industrialised countries is a valuable instrument. Global growth and development depend as never before upon the responsibility of and the willingness to co-operate among leading players on the international scene.

The events we are witnessing pose challenges and, at the same time, provide opportunities for all of us: an unprecedented financial and economic crisis, the need to stop climate change and the need to intensify the struggle against poverty in Africa. Only by working together will the international community pave the way for a stable and secure future. In this context Italy has the honour and responsibility of chairing this year's G8 summit. I believe that, even in an international environment undergoing deep changes, the clear and forthright debate among the leaders of the most industrialised countries is a valuable instrument that can provide an impulse to create a new form of global governance. I say this drawing upon the experience gained through participation in seven G8 summits, the chairing of two and, soon, of a third. In addition to the meeting of G8 leaders, there will be room for discussions with China, India, South Africa, Egypt, Mexico and Brazil. At L'Aquila we will deal with the global economic recovery, climate change, Africa's development and international political issues relating to peace and security.

On the economy, the G20 summit held in London at the beginning of April focused on the financial crisis and the adoption of measures to face the emergency. At the London Summit, Italy made a major contribution to focusing attention on the social aspects of the crisis. In addition, during the G8 summit we will work to provide citizens and enterprises with a new system of financial and economic regulation. With respect to climate change, the L'Aquila Summit will provide a great opportunity to discuss and share views before the Copenhagen negotiations at the end of 2009. For this reason an agreement was reached with US president Barack Obama to hold in L'Aquila the Major Economies Forum with the 16 countries with the highest emissions of greenhouse gases. Regarding Africa, efforts will be devoted to sustaining a global partnership for food safety and preventing the recurrence of severe crisis situations such as the one that affected several countries on the African continent last year. Access to water is another basic need awaiting action: for the first time a joint political message will be conveyed together with African countries. Among the issues on the table are health and education, which are pivotal for promoting stronger development. Finally, the G8

summit will focus on current international political issues such as the fight against terrorism, disarmament, non-proliferation of nuclear weapons and regional crises, in the belief that peace and security are values that cannot be achieved once and for all, but need to be continuously safeguarded. By dealing with these issues and promoting the involvement of emerging economies, the L'Aquila Summit will become a landmark event on the way to a more prosperous and safe world.