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ESSENTIALS OF MANAGEMENT

A Concise Introduction

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ESSENTIALS OF MANAGEMENT

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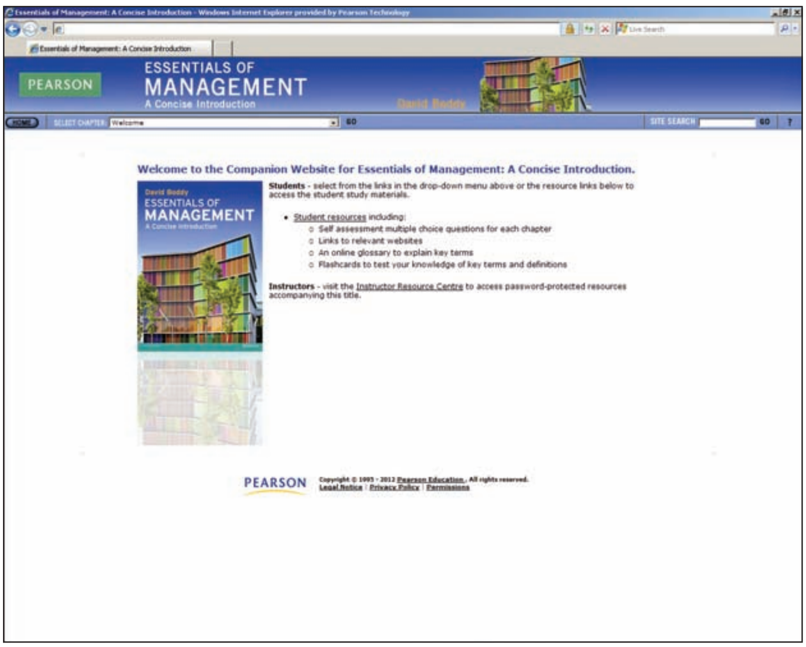

Responsible action as the corporate mission

Some companies position corporate responsibility at the heart of their business, reflecting the beliefs and values of founders and senior managers. An early example was The Body Shop which became a major retailing group by, among many other things, taking a strong ethical position on issues such as testing cosmetics on live animals. Its unique position was gradually eroded – partly by its own success. Animal testing of cosmetics (one of the firm's early campaigns) was stopped, and more people are aware of environmental issues. So a strategically valuable position became less distinctive, and L'Oréal now owns the company. Unilever (**www.unilever.com**) has a history of community involvement, and tries to continue that tradition – while stressing that 'sustainability' has to be consistent with financial requirements.

Management in practice — The co-operative www.co-operative.coop

Established in the early nineteenth century, the Co-op is now Britain's fifth largest retail chain, with a strong financial services business. It is run democratically by its members, who twice a year receive a share of the profits, based on how much they have spent in the business, and how much profit the business made in the year.

Working in line with ethical principles has always been part of the Co-op's mission and way of working – so it has been quick to take into account current concerns of corporate responsibility, such as climate change and world poverty. The company produces an annual sustainability report, outlining what the group has done throughout the business to manage it in a more sustainable way. The fund managers in its investment businesses, for example, take a distinctive approach to investing, in that they consider environmental, social and governance issues alongside financial measures.

The company website gives more information about all the group's activities supporting responsible corporate behaviour.

Source: Company website.

Responsible action to meet customer needs

Other companies, while not focused on responsibility as a mission, focus on meeting the needs of **ethical consumers** – those who take ethical issues into account when making a purchase, and try to avoid buying products from companies that damage the environment, deal with oppressive regimes, have a poor record on animal rights or pay low wages. Such consumers have supported the growth of the Fair Trade scheme, under which companies guarantee that suppliers in poor countries receive higher prices for their products than they would from market forces alone. Café Direct, Green and Black Chocolate are examples of such products.

Ethical consumers are those who take ethical issues into account in deciding what to purchase.

Not all customers share these concerns, but there are enough of them to encourage some companies to meet their requirements, without necessarily adding to their costs. Hawken *et al.* (1999) provide many examples of companies finding that environmentally friendly practices are cost-neutral: by looking carefully at supply, manufacture and distribution, they work out how to make responsible practices pay. Walmart encourages suppliers to use less packaging, and in 2010 Marks & Spencer (**www.marksandspencer.com**) announced that it aims to become the world's most sustainable retailer by 2015. Many banks are re-designing offices and branches to use less energy.

Management in practice Red – Bono and Aids in Africa www.joinred.com

In 2006 Bono announced the creation of his new brand – Red – which will dedicate some of its revenue to fight Aids in Africa. The effort will include a series of joint ventures with companies like American Express, Georgio Armani and Gap to sell products under the brand (for example, go to **www.gap.com** and you will see the RED brands featured). They will be marketed first in the UK to an estimated 1.5m 'conscience consumers' who are seen as more likely to buy products associated with a social benefit. Other products available will include Converse sports shoes made with African mud-cloth, a new line of Gap vintage T-shirts and wrap-around Armani sunglasses:

> **I think doing the Red thing, doing good, will turn out to be good business for them, said Bono, who has long been associated with campaigns on African debt relief, Aids, and unfair trading rules that hurt the continent's poor. This and similar efforts are being supported by big companies worried that television advertising is losing its punch. The idea is that using good works or services will gain consumer attention – what some call 'corporate social opportunity'.**

Sources: *Financial Times*, 26 January 2006, *Independent*, 13 May 2006; U2 and RED websites.

Responsible action as part of strategy

Others follow responsible practices towards, for example, their use of resources, because it fits their business strategy. Using energy efficiently, avoiding waste and treating staff with respect are established daily practices in many companies – some of whom now present such practices as part of a responsible image. In 2009 Mars, the world's biggest confectioner, announced that its entire cocoa supply will be produced sustainably by 2020. It will achieve this by working with the Rainforest Alliance, which encourages farmers to preserve their environment. Cadbury (**www.cadbury.com**) announced that all the cocoa in Dairy Milk, Britain's biggest-selling chocolate, would be certified by Fair Trade, the organisation which works to ensure a minimum price for farmers. Both companies have substantial business reasons for their actions – they are worried about how much cocoa will be available a decade from now, as world production is falling.

Does responsible action affect performance?

The evidence is not clear. One review found a positive relationship between responsible corporate behaviour and financial performance (Orlitzky *et al.*, 2003). Ambec and Lanoie (2008) found that under pressure from stakeholders, some firms use responsible practices to increase revenue (gaining better access to markets; differentiating products; or selling pollution control technologies) and/or reduce costs (risk management; lower costs of materials, energy, capital and labour). Their examples appear to show that companies can both act responsibly and perform well economically.

Vogel (2005) is more sceptical. He found studies which showed a positive relationship between, for example, the level of emission reduction and financial performance, but the direction of causality was unclear – perhaps profitable firms could afford to invest in equipment to reduce emissions. Another possibility was that factors not included in the research affected both variables. Overall, he found an inconclusive picture of the relationship between responsibility and profitability, perhaps due to limitations in the studies:

- different measures of financial performance (one review of 95 studies found that they had 49 different accounting measures);
- different measures of corporate responsibility (95 studies used 27 different data sources); and
- questionable validity of some measures (some rankings only included the views of executives in the industry).

His overall conclusion is that the relationship between responsible behaviour and performance is unclear:

> just as firms that spend more on marketing are not necessarily more profitable than those that spend less, there is no reason to expect more responsible firms to outperform less responsible ones. (p. 33)

5.8 Managing corporate responsibility

Managers use several methods to promote responsible behaviour, including leading by example, codes of ethics, and ethical structures and reporting systems.

Leading by example

Senior managers set the tone for an organisation by their actions. If others see that they are acting in line with stated ethical principles, their credibility will rise and others are likely to follow. Leaders known to be engaging in malpractice are likely to encourage it to spread throughout the business.

Codes of practice

A code of practice is a formal statement of the company's values, setting out general principles on matters such as quality, employees or the environment. Others set out procedures for situations – such as conflicts of interest or the acceptance of gifts. Their effectiveness depends on the extent to which top management supports them with sanctions and rewards.

Corporate responsibility structures and reporting

These are the formal systems and roles that companies create to support responsible behaviour. This may include staff with direct responsibilities for developing and implementing company policies and practices, together with procedures for regular monitoring and reporting, both within the company and to external stakeholders. Most companies now include a corporate responsibility statement in their Annual Report, and may include in this an **ethical audit** profiling current practice.

Ethical audits are the practice of systematically reviewing the extent to which an organisation's actions are consistent with its stated ethical intentions.

Activity 5.2 What does 'corporate responsibility' mean?

Recall the organisation you used in Activity 5.1.

Having read the chapter, make brief notes summarising the organisation's practices in the area of corporate responsibility.

- What, if any, examples of CR issues did you identify (Refer to Table 5.2.)
- Which criteria appear to have most influence on their decisions (Refer to Section 5.4.)
- Can you identify examples of the company relating responsible actions to the wider strategy? (Refer to Section 5.7.)
- What formal practices has the company introduced to support its CR activities? (Refer to Section 5.8.)

Compare what you have found with other students on your course.

Summary

1 **Give examples of controversial, and of philanthropic, business practices**

- Negative examples include poor treatment of suppliers or staff, wasteful uses of energy and other resources during transformation, and unfair treatment of customers. Reputations are also damaged by cases of senior management fraud or high compensation to failed managers.
- In contrast there are many examples of philanthropy, in which people give to charities and other causes without expecting any specific benefit in return.

2 **Distinguish criteria that people use to justify individual and corporate actions**

- Individual
  - Moral principle – the decision is consistent with generally accepted principles.
  - Utilitarianism – the decision that benefits the greatest number of people is the right one to take.
  - Human rights – decisions that support one of several human rights (such as privacy) are right.
  - Individualism – decisions that serve the individual's self-interest are right – in the long run they will benefit society as well.
- Corporate
  - Legal responsibilities – obey the law.
  - Economic responsibilities – Friedman's view that the only function of business is to act legally in the interests of shareholders.
  - Ethical responsibilities – that business has wider responsibilities, since it depends on aspects of the society in which it operates.
  - Discretionary – actions that are entirely philanthropic.

3 **Use a model of ethical decision-making to explain behaviour**

- Figure 5.3 shows a simple model of individual and contextual factors that shape ethical or unethical behaviour.

4 **Show how stakeholders, strategies and responsible behaviour interact**

- Stakeholders' expectations and relative power will influence how managers interpret responsible behaviour, bearing in mind Vogel's point that this is only sustainable if it supports strategy. The chapter showed how this happens – when corporate responsibility is part of the mission, meets customer needs, or otherwise supports strategy.

5 **Evaluate an organisation's methods for managing corporate responsibility**

- These include leading by example, codes of practice, CR structures and reporting mechanisms.

Review questions

1 Identify two recent examples of dubious corporate behaviour (including one from the public sector) and two of philanthropic behaviour. What were their effects?

2 Describe in your own terms each of four schools of ethical theory mentioned in the chapter, and illustrate each with an example of how it has been used to justify a decision.

3 Summarise the four responsibilities which corporations may choose to meet (or not), illustrating each with an example.

4 Sketch the ethical decision-making model and use it to analyse the Pinto case – that is, to explain why managers acted as they did.
5 How can managers take account of the diverse interests of stakeholders?
6 Why is it important, in Vogel's view, to link corporate responsibility to strategy?
7 Illustrate each of the ways in which organisations do this with a current example.

Further reading

Vogel, D. (2005), *The Market for Virtue: The potential and limits of corporate social responsibility*, Brookings Institution Press, Washington, DC.

Places issues of corporate responsibility within a wider consideration of company strategy. Many current examples support the discussion.

Blowfield, M. and Murray, A. (2008), *Corporate Responsibility: A critical introduction*, Oxford University Press, Oxford.

Comprehensive account of the topic with many examples from practice, and activities to illustrate the themes.

Weblinks

These websites have appeared in, or are relevant to, the chapter:

www.bitc.org
www.innocentdrinks.co.uk
www.acea.ch
www.unilever.com
www.co-operative.coop
www.marksandspencer.com
www.joinred.com
www.gap.com
www.cadbury.com

Visit two of the sites in the list, and navigate to the pages dealing with corporate responsibility, sustainability or corporate governance.

- What are the main concerns that they seem to be addressing?
- What information can you find about their policies?
- Compare the concerns and policies expressed on the sites.

Annotated weblinks, multiple choice questions and other useful resources can be found on www.pearsoned.co.uk/boddy

Case study The Ford Pinto

In the late 1960s, Lee Iacocca, then president of Ford, sought to improve the company's market position by having a new car, the Ford Pinto, on the market by the 1971 model year. This would be a basic vehicle selling for $2000, which meant that it had to be produced very cheaply, with a small margin between production costs and selling price.

The designers placed the petrol tank at the back of the car, six inches from a flimsy rear bumper. Bolts were placed just three inches from the tank. Other sharp metal edges surrounded the tank, and the filler pipe tended to break loose from the tank in low-speed crashes. These features could have been re-designed, but the extra expense would go against Iacocca's aim of 'a 2000 pound car for $2000'.

In testing its new design Ford found that when it was struck from behind at 20 mph the bumper would push the bolts into the tank, causing it to rupture. This posed a significant risk to those inside and contravened proposed legislation which required cars to withstand an impact at 30 mph without fuel loss. No one informed Iacocca of these findings, for fear of being fired. He was fond of saying 'safety doesn't sell'.

The car went on sale and in 1976 a magazine exposed the dangers of the Pinto petrol tank. This prompted the National Highway Traffic Safety Administration (NHTSA) to launch an investigation, which in 1977 identified 28 rear-end crashes in which petrol had leaked and caused a fire. Twenty-seven occupants had died and 24 suffered burns.

Feeling some pressure to fix the tank, Ford officials devised a polythene shield to prevent it from being punctured by the bolts, and a jacket to cushion it against impact. The engineers calculated that these improvements would cost $11 per car, and had to decide whether to recall the cars to make these repairs. They conducted a cost–benefit analysis. Using NHTSA figures for the cost to society of death or serious injury, and an estimate of the likely number of future deaths and serious injuries, Ford's calculations were:

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Benefits of altering design

Savings:	180 deaths; 180 serious injuries; 2100 vehicles
Unit cost:	$200,000 per death; $67,000 per serious injury; $700 per vehicle
Total benefit:	$49.5 million
Costs of altering the design	
Sales:	11 million cars; 1.5 million light trucks
Unit cost:	$11 per car; $11 per truck
Total cost:	$137.5 million

Since the costs of recalling and altering the cars outweighed the benefits they decided not to do so, continuing to produce the Pinto in its original form. They reasoned that the current design met federal safety standards at the time. While it did not meet proposed legislation, it was as safe as current competing models.

In 1977 the proposed fuel tank legislation was adopted and Ford decided to recall all 1971–76 Pintos to modify their fuel tanks. A month before the recall began three people in a Pinto were struck from behind in a low-speed crash and burned to death. A $120 million lawsuit followed, but Ford escaped on a technicality. Ford won the lawsuit, but its reputation suffered badly.

Court records showed that Ford's top managers knew that the Pinto was unsafe, but concluded that it was cheaper to incur the losses from lawsuits than to fix the cars. Production staff also knew of the risks, but were never given the opportunity to tell top management about it. Fords 'profit drives principle' philosophy of the time discouraged staff from drawing attention to risks. Actions were guided by the original aim for the Pinto – '2000 pounds for $2000' – and a 'safety doesn't sell' mindset. Insiders believed they were acting in line with company values. Richard Pascale (1990) noted that during the 1970s: