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Chapter 2: Stakeholder Relationships, Social Responsibility, and Corporate Governance

Stakeholders Define Ethical Issues in Business:

In a business context, customers, investors, and shareholders, employees, suppliers, government agencies, communities, and many others who have a "stake" or claim in some aspect of a company's products, operations, markets, industry, and outcomes are known as stakeholders. Reputation is damaged from poor performance or ethical misconduct, but ethical misconduct is tougher to recover from. Those indirectly involved with an event may be influenced by other people. Some scandals can lead to boycotts and aggressive campaigns to dampen sales and earnings. New reforms to improve corporate accountability and transparency also suggest that other stakeholders can play a major role in fostering responsible decision making. Stakeholders also provide tangible and intangible resources that can be critical to a company's success. Wal-Mart, Enron, Coca-Cola, and Nike have been involved with ethical scandals recently.

Identifying Stakeholders

Primary stakeholders are those whose continued association is absolutely necessary for a firm's survival. Secondary stakeholders do not typically engage in transactions with a company and thus are not essential for it's survival. Primary stakeholders may provide more day to day concerns, but secondary stakeholders can't be ignored. There's a two- way relationship between the firm and stakeholders.

A Stakeholder Orientation

The degree to which a firm understands and addresses stakeholder demands can be referred to as stakeholder orientation. Orientation comprises three sets of activities: Organization wide generation of data about stakeholder groups, distribution of this information, and the organization's response as a

whole. Generating data begins with identifying stakeholders, then the concerns about business's conduct for each stakeholder group by getting information, and finally evaluate its impact on the issues. The communication of information is key when generating information. A stakeholder orientation is not complete unless it includes activities that address stakeholder issues. The responsiveness of the organization as a whole to stakeholder intelligence/information is critical.

Social Responsibility and the Importance of a Stakeholder Orientation

From the perspective of social responsibility, business ethics embodies standards, norms, and expectations that reflect a concern of major stakeholders. Legal and economic responsibilities are usually considered most important, but Adam Smith's form of enlightened capitalism is taking over. When companies care about stakeholders, they earn trust and can reduce costs and increase profitability.

Social Resposibility and Ethics

Social responsibility can be viewed as a contract with society, but business ethics involves carefully thought-out rules or heuristics of business conduct that guide decision making. The four levels of social responsibility are economic, legal, ethical, and philanthropic. Corporate Citizenship is used to express the extent to which businesses meet these four levels. The value of a firm's reputation is important, and one of the greatest intangible assets.

Corporate Governance Provides Formalized Responsibility to Stakeholders

The main purpose of business is to make profit, but the FSGO provides incentives for developing an ethical culture and preventing misconduct. There is a duty of care, also called a duty of diligence, to make informed and prudent decisions. The duty of loyalty means that all decisions should be made in the best interest of the corporation. Conflicts of interest occur when a superior uses their position to obtain personal gain. Most companies have developed formal systems of accountability, oversight, and control, which is known as corporate governance. This establishes fundamental systems, creates an

ethics culture, and provides mechanisms for identifying risks. Reforms in governance structures are happening all over the world.

Views of Corporate Governance

The shareholder model of corporate governance includes the goal of maximizing wealth for investors and owners. A shareholder orientation should drive a firm's decision toward serving the best interests of investors. Corporate governance mechanisms are needed to align investor and management interests. The stakeholder model of corporate governence adopts a broader view of the business. Companies must determine their primary stakeholders.

The Role of Boards of Directors

For public companies, boards of directors hold the ultimate responsibility for their firm's success or failure, as well as for the ethics of their actions. Board of directors assume legal responsibility for the firm's decisions, and shouldn't be a vehicle for personal financial gain, but provide the intangible benefit of ensuring success. Boards meet a few times a year, and monitor decisions made by executives on behalf of the company. Today, outside directors are brought in because of their expertise, competence, and diverse perspectives. One of the biggest issues board directors deal with is executive compensation. They argue whether they should be paid so much. Some say yes because they assume all the risk in the company. Some just believe that no executive is worth millions of dollars.

Implementing a Stakeholder Perspective

Although there are many different approaches, these steps have been found effective to utilize the stakeholder framework in managing responsibility and business ethics. The steps include assessing the corporate culture, idenitifying stakeholder groups, idenitfying stakeholder issues, assessing the orgainizational commitment to social responsibility, identifying resources and determining urgency, and gaining stakeholder feedback.