Chapter 3

Strategic analysis: Ethics and Corporate Social Responsibility

Chapter learning objectives:

Lead	Component	Indicative syllabus content
A.1 Evaluate the influence of key external factors on an organisation's strategy.	(c) Discuss the drivers of external demands for environmental sustainability and corporate social responsibility and the organisation's response.	• External demands for sustainability and responsible business practices and ways to respond to these.
A.2 Evaluate ethical issues arising from the organisation's interaction with its environment.	(a) Evaluate ethical issues and their resolution within a range of organisational contexts.	• Business ethics and the CIMA Code of Ethics for Professional Accountants (Parts A and B) in the context of the implementation of strategic plans.

1. External Demands for Responsible Business Practices

> **Corporate social responsibility (CSR):** a firm's obligation to maximise its positive impacts upon stakeholders while minimising its negative effects.

- CSR covers an organisation's economic, ethical, legal and charitable responsibilities towards its stakeholders.
- As different individuals have differing views regarding corporate social responsibility, managers will need to manage their strategies to fulfil their responsibilities towards both society and the shareholders.

Arguments for CSR	Arguments against CSR
• ***Improved reputation and brand name:*** a more socially responsible organisation will have a better reputation and attract more customers. CSR could be a basis for differentiation for a business. • ***Greater access to human resources:*** non-discrimination and better working conditions will attract more and higher quality staff. • ***Cost savings*** – Better environmental practices could help avoid the fines and taxes imposed on polluting businesses. – Improving the efficiency of resources can lead to lower costs, thus improving competitive advantage. – Sponsorships and charitable donations are tax-deductible. • ***Greater trading opportunities:*** the more socially responsible a business is, the easier it will be to gain support from the societies and nations in which it wishes to invest. • ***Funding:*** good CSR is likely to attract more finance from ethical investors. • ***Sustainable business:*** a socially responsible business will have a better reputation and is likely to operate for much longer in the society. This will increase the value of the company due to more years of cash flow.	• Milton Friedman states, ***"the business of business of business is business"***, meaning that the main objective of a business is to earn profit and that the managers should focus on maximising the wealth of shareholders. • An argument against CSR is that wealth maximisation is in itself beneficial for the society, because: – Increased returns will increase tax revenues to the state, which can then be used by the government on socially desirable objectives. – Many company shares are owned by pension funds whose ultimate beneficiaries may themselves not be wealthy. • One practical reason for not pursuing CSR is that obtaining materials from ethical sources may prove costly. • CSR planning and implementation can be time-consuming for the management.

Carroll's corporate social responsibility model – the pyramid of corporate social responsibility

Carroll's four-part model of CSR requires an ethical business to fulfil the following responsibilities:

- **Philanthropic responsibility:** to be a good corporate citizen and to improve the lives of others. This responsibility is discretionary.
- **Ethical responsibility:** responsibility to act in a fair and just manner.
- **Legal responsibility:** responsibility to operate according to the applicable laws and regulations.
- **Economic responsibility**: responsibility to be profitable.

Carroll suggests four possible strategies regarding CSR:

- **Reaction:** the organisation denies any social responsibility.
- **Defence:** the organisation accepts social responsibility but fulfils only the minimum requirement.
- **Accommodation:** the organisation accepts responsibility and fulfils the demands of the relevant groups.
- **Proaction:** the organisation goes beyond the society's expectations and attempts to improve the society.

Ethical stances

Johnson, Scholes and Whittington identified four different stances regarding corporate social responsibility:

- **Short-term shareholder interest:** this ethical stance focuses on the short-term responsibilities of the business, i.e. to maximise profits in the financial year. Organisations with this view will only meet the minimum obligations as defined by laws and regulations.
- **Long-term shareholder interest:** organisations with this view are ready to incur additional costs in order to achieve higher returns in the future. This view is taken with the belief that managing good relations with the stakeholders will be beneficial for the organisation in the long run.

- **Multiple stakeholder obligations:** organisations with this stance believe that their role is more than just earning profits. They take into account the interests of all the stakeholders.
- **Shaper of society:** in the view of these organisations, their actions should be such that they benefit the society, and financial and other stakeholder interests are of secondary nature.

Sustainability

Sustainability is an aspect of CSR that means using resources in such a way that the needs of future generations are not compromised. This includes protecting the environment from pollution.

Incorporating ethics and CSR into strategy

CIMA's article on sustainability and incorporating ethics into strategy

The six main points included in the article are as follows:

1. Strong ethical principles can add great value to the brand, while failure to do the right thing can cause social, economic and environmental damage, undermining a company's long-term prospects.
2. Companies that adopt high ethical standards often find that there are bottom-line benefits resulting from these ethical standards.
3. The management accountant has a specific responsibility for promoting an ethics-based culture.
4. The ethical tone is set from the top.
5. Good quality management information on social, environmental and ethical performance is important for monitoring the environmental and social impacts of a company and for compiling the related reports.
6. When reporting on sustainability, the organisation should provide hard evidence of the positive impact of their operations and how any negative impacts are being addressed.

CIMA's report on the 'evolution of corporate sustainability practices'

The drivers of business sustainability are:

- ***Compliance risk****:* the need to comply with regulatory requirements.
- ***Reputational risk****:* the risk of damage to the organisation's reputation if it fails to act in a sustainable manner.
- ***Cost-cutting and efficiency****:* acting in a sustainable manner can help reduce costs.

Ten elements of organisational sustainability:

- **Strategy and oversight**:
  - Board and senior management commitment.
  - Understanding and analysing the key sustainability drivers for the organisation.
  - Integrating the key sustainability drivers into the organisation's strategy.
- **Execution and alignment**:
  - Ensuring that sustainability is the responsibility of everyone in the organisation.
  - Breaking down the sustainability targets and objectives for the organisation as a whole into targets and objectives that are meaningful for individual subsidiaries, divisions and departments.
  - Processes that enable sustainability issues to be taken into account clearly and consistently in day-to-day decision-making.
  - Extensive and effective sustainability training.
- **Performance and reporting**:
  - Including sustainability targets and objectives in performance appraisal.
  - Champions to promote sustainability and celebrate success.
  - Monitoring and reporting sustainability performance.

2. CIMA's Code of Ethics

The code consists of 3 parts (E3 CIMA examines only A and B):

- **Part A:** fundamental principles and general application of the code
- **Part B**: professional accountants in business
- **Part C**: professional accountants in public practice

Business ethics can be described as the standards of behaviour in the world of business.

THE FUNDAMENTAL PRINCIPLES OF ETHICS

CIMA's code of ethics consists of the following five fundamental principles of ethics:

- **Integrity**: requires members to be fair and honest.
- **Objective**: accountants must remain unbiased and not let their professional judgements be influenced in any way.
- **Professional competence and due care**: professionals must maintain professional skills and up-to-date knowledge.
- **Confidentiality**: any information obtained as part of business and professional relationships should not be disclosed to third parties without proper authority or used for personal advantage.

  Such information can be disclosed in the following situations:
  - If it is permitted by law and authorised by the client
  - If it is required by law
  - If there is a professional right or duty to disclose
- **Professional behaviour**: the actions of a professional should not bring discredit to the profession.

Resolving ethical conflicts

Ethical conflicts can be resolved as follows:

1. Gather all the relevant facts.
2. Establish the ethical issues involved.
3. Refer to relevant fundamental principles.
4. Follow established internal procedures.
5. Investigate alternative courses of actions.
6. Consult with appropriate persons within the firm.
7. Obtain advice from a professional institute.
8. If the matter remains unresolved, consider withdrawing from the engagement team/assignment/role.

Threats to the fundamental principles of ethics

- Self-interest threat
- Self-review threat
- Advocacy threat
- Familiarity threat
- Intimidation threat

Safeguards against the threats

There are two main categories of safeguard:

- Safeguards created by legislation, regulation or the profession.
- Safeguards in the work environment.

3. Chapter summary