Corporate Social Actions and Reputation:

From *Doing Good* to *Looking Good*

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ABSTRACT

Corporate Social Actions and Reputation:
From *Doing Good* to *Looking Good*

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While corporate social responsibility (CSR) has garnered the attention of scholars over the past three decades, most attention has been focused on a link to financial performance. Grounded in stakeholder theory and a resource-based view of the firm considering the cospecialized intangible assets of CSR and reputation, this research explores the evolution of corporate social actions and firm reputation over time. We draw on data from the KLD database on corporate social actions and concerns, and on the Fortune most-admired company database to examine the relationship between corporate social behaviour and reputation over time.

In the thesis, we argue that starting with the broad premise that any corporate social action or gesture can initially enhance corporate reputation, the firm is then both encouraged and also expected to go further. Accordingly, we propose subsequent actions are needed to meet stakeholder expectations to be able to improve or at least sustain firm reputation. We find that over the

timeframe of our study that corporate social actions do experience the predicted positive linear growth.

Drawing on a sample of 285 major US firms and a 2002-2006 time frame to provide a 1425 firm year panel, we find corporate social actions to be strongly related to corporate reputation, while the change in corporate social actions also predicts a change in corporate reputation. We also found support for the hypothesis that corporate social actions directed to technical stakeholders have the most significant impact on firm reputation. We do not however find the expected influence of concerns over corporate social actions directed to institutional stakeholders on firm reputation, leading to the intriguing question: *why not?*

We provide detailed illustrations with five of the sampled firms and interpret their CSR-reputation relationships. These findings expand our understanding of the effect of the change over time in corporate social actions and the ensuing effect on corporate reputation. We extend the applicability of our findings to management, discuss limitations and propose future research directions.

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I dedicate this thesis to my daughters Francesca and Dominique, and to my Mom, an inspiring, unsung *do-gooder*, who would have been so proud to have a Ph.D in the family!

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1. INTRODUCTION

Some might view corporate social responsibility (CSR) as an oxymoron akin to *military intelligence*, as CSR describes business' discretionary relationship with stakeholders, going well beyond the traditional model concerned only with shareholders and that required by law. Firms in the developed world have widely embraced the need to cohabit with the society around them, so much so that a most recent article by Orlitzky and colleagues (2011: 9) calls for a shift away from research directed to "whether CSR *pays*, but instead when or under what circumstances". This underlines that we no longer need to justify CSR, however there is still much to learn about CSR to address limitations in the literature.

For more than three decades CSR research has primarily focused on a CSR link to financial performance (Lockett, Moon & Visser, 2006; Margolis & Walsh, 2001). The results of the largely cross sectional studies may however be viewed as inconclusive (Waddock & Graves, 1997; Orlitzky, Schmidt & Rynes, 2003) with critics pointing out misspecifications (McWilliams & Siegel, 2000) and even pondering whether it is the lack of a dominant paradigm of CSR that has hampered CSR research progress (Godfrey & Hatch, 2007; Lockett et al., 2006; McWilliams, Siegel & Wright, 2006; Orlitzky, Siegel & Waldman, 2011).

Recognizing the multi-faceted complexity of today's firms and the longer-term impact of CSR, it is not surprising that a direct relationship to financial performance has been hard to substantiate. However, the link from CSR to firm reputation has greater conceptual alignment (Fombrun, Gardberg & Barnett, 2000), consistent with Fombrun and Van Riel's (2004: 105) suggestion that

"perceptions of social responsibility enhance reputation". Prior research on this link is somewhat limited and has focused on the effect of particular types of CSR actions on corporate reputation, such as accidents (Zyglidopoulos, 2001), downsizing or layoffs (Kraatz & Love, 2006; Love & Kraatz, 2009; Zyglidopoulos, 2004, 2005) and quality (Straw & Epstein, 2000). The value of a good reputation (Fombrun & Shanley, 1990; Podolny, 1993) was examined by Roberts and Dowling (2002) to find support for the persistence over time of reputation and financial performance, however they did not consider CSR in building reputation.

More recently, McWilliams and Siegel (2010) have proposed that CSR can be synergistic with other assets, of which they highlight corporate reputation, labeling them as *cospecialized assets*. They integrate a resource based view as a theoretical foundation for the competitive advantage these intangible assets can confer, but remain at a conceptual level.

As noted earlier, another critique has been that of the cross-sectional design of most CSR research. From the earliest reviews of Aldag and Bartol (1978) and Ulmann (1985), the need for longitudinal studies of CSR has been suggested, echoing Cochran and Wood's (1984) call to investigate causality. Given CSR and reputation evolve in a dynamic corporate environment; capturing the change over time is highly pertinent to understanding the interaction that may add to the value of these intangible assets.

The need for a more precise definition of CSR and better adapted CSR measures was stressed by McWilliams and colleagues (2006) as well as Godfrey and Hatch (2007) in discussing a future research agenda on the strategic

implications of CSR, while Mattingly and Berman (2006) advocate that CSR strengths and concerns are not a continuum when interpreting CSR measures. Orlitzky and colleagues (2011) repeat these issues and introduce the need for multi-theoretic grounding of CSR research. Given the inherent ambiguity of how CSR is interpreted and translated into perceptions of reputation, it is logical that no single management theory can provide adequate foundation. While past CSR studies have been overwhelmingly grounded in stakeholder theory, the addition of other theoretical lenses can reinforce the potential for integrating CSR into firm strategy.

Responding to these shortcomings, this dissertation uses a multi-theoretic lens to capture the dynamic relationship of CSR over time on the evolution of corporate reputation. Based on stakeholder theory (Freeman, 1984) and a resource-based view (Barney, 1991 & 2001) of the firm, we explore how corporate social actions (distinguished between strengths and concerns) change over time to influence the change in stakeholder assessments of firm reputation. Using longitudinal data and structural equation modeling, we search for evidence of a causal relationship between corporate social actions and corporate reputation. Starting with the broad premise that any corporate social action or gesture, including merely a symbolic one, can initially enhance corporate reputation, we suggest that the firm is then both encouraged and also expected to go further. Furthermore, "when expectations of CSR increase, the value of the status quo necessarily declines" (Barnett, 2007: 807). Accordingly, we argue in this thesis that subsequent CSR actions will need to expand in order meet stakeholder expectations to be able to improve or at least sustain firm reputation. The

importance to society at large of firms acting responsibly is undeniable, however little is known of how social performance evolves over time, nor the longer-term impact on the favourable consequence of an enhanced firm reputation, a most valuable, albeit intangible, competitive resource.

While we have proposed that firms must engage in further corporate social actions than the status quo to maintain or enhance reputation, the stakeholder perception of the firm's underlying rationale is an additional input to their reputation assessment. Remembering that the distinction of whether a CSR initiative is symbolic or substantive is in the eye of the stakeholder, it is the stakeholder's access to sufficient information to develop expectations as well as to evaluate the outcomes that informs their interpretation of the corporate social action. For example, in situations where stakeholders' CSR expectations are adequately met one interpretation may be that the corporate social actions were substantive or alternatively, that stakeholders expected lip-service and given the context were satisfied with symbolic actions. Furthermore, where "in symbol-intensive industries there is a very fine line between image and substance" (Cappetta & Gioia, 2006: 217), stakeholder interpretations of firm CSR initiatives may be further blurred. Another consideration that may affect the stakeholders' access to information is in the interaction they have with the firm. When stakeholders contract or transact with a firm they enter into an exchange with formulated expectations, while when a stakeholder is peripheral or involuntary they may not have formulated such expectations. Furthermore, the access to information on the firm's corporate social actions is most likely available to those stakeholders transacting with the firm than those affected by the firm's actions.

In other words, stakeholders such as employees or suppliers who regularly exchange services/goods with the firm are likely to know more about the firm's CSR than would more distant stakeholders such as neighbours to one of the firm's plants. Accordingly, the type of interaction the stakeholder holds with the firm will be influential to information asymmetry as well as establishing expectations. As the same initiative may be viewed as substantive by one stakeholder and symbolic by another, it is not the objective of this research to measure or classify CSR initiatives as symbolic or substantive.

The overarching foundation of the resource-based view is used to frame the relationship of corporate social actions and corporate reputation as viewed through institutional, resource dependence and stakeholder theoretical lenses. This research focuses on the corporate social actions of major US firms directed to a broad array of stakeholders to identify the impact on corporate reputation over time. The research question we pose is: How do corporate social actions affect corporate reputation and how do changes over time in corporate social actions affect a change in firm reputation?

This dissertation will examine the evolution of firm reputation with CSR over time, considering the stickiness of reputation and other temporal effects in a resource-based view of the firm where the synergy between CSR and reputation creates cospecialized intangible assets (McWilliams & Siegel, 2010). The challenge in interpreting these relationships lies in the "unpredictable and sometimes immeasurable elements that come into play as time unfolds" (Ketchen, Jr., Boyd & Bergh, 2008). The impact of the external environment (i.e. natural disasters of earthquakes, warfare or civil unrest, global recession,

etc.) as well as firm or industry-specific events (i.e. sale/purchase of major lines of business, judicial inquiries, destructive innovation, etc.) are factors that may distort annual comparisons on a case-by-case basis across the years. Through select illustration we delve into some of these possibilities in interpreting the relationship of five individual firms' corporate social actions with the evolution of their reputations.

A resource-based view of the firm considering the value of CSR and reputation, underpins this research, drawing on stakeholder, institutional and resource dependence theories. CSR creates a synergy with reputation, something that "makes other assets more valuable than they other-wise would be. The clearest example of this is firm reputation" (McWilliams & Siegel, 2010: 12). This research expands our understanding of the effect of the change over time in corporate social actions and the ensuing effect on corporate reputation over time, contributing to resource-based view research on intangible assets.

We establish that corporate social actions have a positive linear growth over the period of our study as a starting point to then consider how the change in corporate social actions affects corporate reputation. We find a change in corporate social actions predicts a change in corporate reputation, supporting our hypothesis that improvements in corporate social actions are positively related to an improvement in corporate reputation. We also find corporate social actions directed to technical stakeholders to have an impact on firm reputation beyond those directed to institutional stakeholders.

In recognition that a model may not "be simultaneously general, accurate, and simple" (Weick, 1979: 35, c.f. Miller & Dess, 1993), often referred to as the

GAS trade-off, this research utilizes a generic model which may be applied to all manner of firms and draws on a sample of major US public corporations. While much existing research is based on a pre-2000 time frame, this study is based on a post Sarbanes-Oxley time period from 2002 to 2006 where markets were generally improving. This has the advantage of avoiding the technology bubble and crash; however, stakeholder awareness and access to information have been accelerated with the internet and globalization. Skepticism and distrust of corporate America has also been fuelled, as captured in accusations of *green-washing*. The advent of social media and the barrage of blogs, twitter posts and other instantaneous stakeholder feedback have significantly altered the information horizon to reduce the often advocated influence of firm advertising to communicate CSR activities (McWilliams & Siegel, 2010).

The literature review in Chapter 2 will start with a retrospective on the origins of CSR, we will then distinguish the various CSR and reputational constructs to establish clear definitions as a rigorous foundation for the theory development and provide the theoretic and conceptual frameworks. The proposed model and hypothesized relationships will also be discussed. The methodology presented in Chapter 3 will identify the dependent and independent variables, describe the data sources, as well as support the choice of control variables in the model and the rational for the sample selection. The analysis of the empirical tests and results is presented in Chapter 4, with a discussion of results and limitations following in Chapter 5. The concluding Chapter 6 reviews the direction for future research and the applicability to management in assessing CSR and reputation strategies.

2. THEORY DEVELOPMENT

2.1 Preamble

We set the stage for our theoretical model with a retrospective on the origins attributed to corporate social responsibility (CSR). Taking this very long horizon accentuates how gradual the shift toward CSR had been during the past century, particularly in North America. This sets the stage for understanding how slowly the origins of CSR were to take root, but which today have been so broadly embraced that there is no longer a debate as to whether CSR pays (Orlitzky et al., 2011).

A discussion of the definitional landscape follows for the broadly related CSR and reputation concepts. A synopsis of various interpretations concludes with the working definitions that have been chosen for this research. This is a key building block to avoid any confusion as to what interpretations are intended of the focal concepts before proceeding to develop the theoretical model.

We will then assess drivers and motivations behind corporate social actions and corporate reputation to ground these key constructs. Then, encompassed in the resource-based view we will elaborate on the interaction of stakeholder, institutional and resource dependence theories shaping the relationship between corporate social actions and corporate reputation.

This will complete the theoretical framework upon which the proposed model will reside. Building upon the theoretical and conceptual models the anticipated relationships will be formulated in the hypotheses that will be subsequently tested in the next section

2.2 A retrospective on the history of corporate social responsibility[1]

While corporate social responsibility (CSR) is now a widely accepted domain, it was almost sixty years ago that Peter Drucker's conclusion entitled "The Responsibilities of Management", included the captions "the social impact of business decision, making a profit the first social responsibility and the ultimate responsibility: to make what is for the public good the enterprises' own self-interest" (Drucker, 1954: 381).

In this chapter we will explore the antecedent and subsequent business classic works that influenced and embodied the concept of CSR. We will draw on these authors, largely using their own words, to develop the foundation of what we now term CSR, recognizing that "business and society are interwoven rather than distinct entities" (Wood, 1991: 695). Before expanding on our more contemporary view of CSR, examining how the firm's focus on shareholders is extended to consider other internal and external actors today known as *stakeholders* provides an appreciation for the roots of CSR. To recognize the temporal context the retrospective is subdivided by decades which are categorized for their primary influence on business and society. The voice of these early scholars is largely maintained to provide insights into the interpretation at the time of business' actions, thus capturing the temporal context against which the perspectives are framed.

[1] This first chapter is an extract of portions of the author's article published in the Journal of Management History (2009) and reflects the thinking of the time of influential business and academic leaders.

2.2.1 1930's – The Great Depression

The corporate revolution described by Berle and Means in *The Modern Corporation and Private Property* (1932) is chosen as the starting point for this review. Epstein (1999) argues that strategy was founded on their intellectual base, while Novicevic and colleagues (2006) identify the limited liability corporation as giving birth to corporate responsibility. It is Berle and Means' recognition of the transformation from the traditional owner-managed firm to widely held stock ownership, where a new class of managers exercises considerable control that frames new expectations of corporations and their executives. Berle's original preface (1932: xli) lamented, "Accepting the institution of the large corporation (as we must), and studying it as a human institution, we have to consider the effect on property, the effect on workers, and the effect upon individuals who consume or use the goods or services which the corporation produces or renders". The new concept of the corporation is viewed to have "placed the community in a position to demand that the modern corporation serve not alone the owners or the control but all society" (Berle & Means, 1932: 312, revised 1968 edition). This vision is essentially today's stakeholder theory.

In a 1967 revision Means noted the lack of a corporate performance measure, other than profits. He then posed the following questions: "Should the problems of bad performance be worked on piecemeal, as has been done by the laws concerning theft and breach of contract, drug distribution, and auto safety? Or can criteria for good performance be developed to guide corporate management and inducements be provided to encourage the good? What

changes would be needed to make it true that action by corporate management in its own self-interest serves the public interest?" (Berle & Means, 1932: xxxv, revised 1968 edition). More than forty years after Means' revision these questions are still being debated.

Concurrent with Berle and Means' reflections on the corporate revolution, Elton Mayo, a highly influential researcher perhaps best noted for the Hawthorne Experiment, was also very conscious of the interaction of business with society as described in *The Human Problems of an Industrial Civilization* (1933). As his name is often noted as a source of inspiration by scholars such as Barnard (1938), Homans (1950) and Roethlisberger (1977), an insight into his view of social responsibility provides an additional perspective on some of the influences of the day. In Mayo's (1933) description of worker morale at the Western Electric Company, Hawthorne plant, he notes the high esteem with which the employees hold the Company and how much they appreciate the considerate hours, affordable restaurant and good hospital, as well as vacation entitlements and company sponsored investment plans.

The generous employee benefits are perhaps even more impressive in the context of the Great Depression and could serve as an example of highly responsible corporate behaviour, even today. In 1936 the Western Electric Company applied the experiment findings by adding an employee-counseling program with the help of another of the experiment researchers, Fritz Roethlisberger. Roethlisberger credits Mayo's interaction with the executives and unrelenting inquisitiveness as the driving force in having the results fully

understood, calling them the "double-whammy Hawthorne effect. Today the condition is called synergy, that is, when 2 + 2 = 5" (Roethlisberger, 1977: 51).

While these academics were helping the Western Electric Company to implement socially responsible improvements, Chester Barnard, a thirty-year veteran corporate executive was writing about cooperation and leadership. His *The Functions of the Executive* (1938) seminal work is one of the most quoted business perspectives on the organization's top managers. He notes the complex morality accompanying executive positions, given the executive is also defining morals for others within the firm. Similarly, as the executive's rank increases so does the moral complexity in addressing conflicts of codes.

Relating the impact of the executive's morals to the organization, Barnard (1938: 282) goes on to say, "Organizations endure, however, in proportion to the breadth of the morality by which they are governed. Thus the endurance of organization depends upon the quality of leadership; and that quality derives from the breadth of the morality upon which it rests." The onus is clearly on the executive to not only establish the corporate values, but to ensure these values form the foundation of corporate actions throughout the organization. In the spirit of today's stakeholder management, Barnard argues (1938: 255), "This philosophy of giving as little as possible and getting as much as possible in the *other man's values* is the root of bad customer relations, bad labor relations, bad credit relations, bad supply relations, bad technology". Barnard has been credited as a visionary in recognizing stakeholders external to the firm (Schwartz, 2007).

2.2.2 1940's & 1950's– World War II through to the Cold War

Building on the work of Barnard whose influence he acknowledges, Herbert Simon's *Administrative Behavior* (1945) also recognizes the social values to which organizations must respond. With organizations assuming broader roles, Simon notes however, that traditional institutions, like religion or the family, are at the origin of fundamental values against which corporate actions will be judged.

Roethlisberger (1977: 111) recounts the attitude toward responsibility in the mid 1940's "that responsibility was a property of an executive in the same sense that wisdom was a property of a sage. That is to say, an irresponsible executive was a contradiction in terms; he could not exist". Clearly the executive was held in high esteem with unquestioned authority based on the position occupied within the organization. The acceptance of this authority was however somewhat mitigated since "unless an executive's function reported directly to the president, he could not get people to do what they were supposed to" (Roethlisberger, 1977: 171). This observation that the chief executive officer's authority extended to immediate subordinates recognizes the influence of the executive group, currently referred to as the top management team (TMT).

Relating his experiences in a post war retraining program, Roethlisberger (1977: 112) decided his "goal was not to make persons into better executives but instead to make executives into better persons", focusing on "a class of phenomena - the interactions between persons – that I called social space" (1977: 115). Surprised at a context that appeared to be missing in the case studies taught, Roethlisberger (1977: 130) noted "these societal and cultural factors had

ruled them *out of existence*", furnishing the students with a narrow view of the world. Roethlisberger (1977: 147) went on to note "what an organization *needed* in order to realize its purposes was something entirely different from what a person *needed* in order to be satisfied", however he identified a gap in how management and workers looked at each other's behaviour which Roethlisberger (1977: 167) identified as the "man-in-the-middle syndrome". Only decades later did upper echelons theory recognize the cognitive biases of executives (Hambrick, 2007) which influenced perceptions and subsequent actions.

Peter Drucker's *The Practice of Management* (1954) is the birth of what will be coined as corporate social responsibility, directing managers' attention to ensure the corporation does "not undermine our social beliefs and cohesion" (Drucker, 1954: 387). He clearly assigns leadership to managers in establishing objectives and meeting performance commitments, with the bottom-line that when "an enterprise fails to perform, we rightly hire not different workers but a new president" (Drucker, 1954: 13). Managers are told it is their "public responsibility to *make* what-ever is genuinely in the public good *become* the enterprise's own self-interest" (Drucker, 1954: 390).

The responsibility to shareholders, often used by managers as justification for profit maximization, is responded to by the fact shareholders of public companies can sell their stock, "society, however is stuck with the enterprise" (Drucker, 1954: 387). As to the goal of profit maximization, Drucker (1954: 36) asserts that the goal of business is "the achievement of sufficient profit to cover the risks of economic activity and thus to avoid loss", going on to say "the profit motive and its offspring, maximization of profits, are just as irrelevant to the

function of a business, the purpose of a business and the job of managing a business".

Drucker's (1954: 388) concluding arguments remind management to "realize that it must consider the impact of every business policy and business action upon society. It has to consider whether the action is likely to promote the public good, to advance the basic beliefs of our society, to contribute to its stability, strength and harmony". This recognition of the social power granted to the corporation corresponds to expectations of additional corporate responsibilities (Schwartz, 2007).

Going beyond just the role of the chief executive officer, or the president, it is the "job of a team of several men acting together" dubbed the "chief-executive team" upon whom the responsibility for the corporation's attention to social responsibility lies (Drucker, 1954: 169). This reflects the growing importance of the corporation in America, where the task exceeds that of one person alone to be able to manage all of the stakeholder interests. It also recognizes that “leadership of a complex organization is a shared activity, and the collective cognitions, capabilities, and interactions of the entire TMT enter into strategic behaviours” (Hambrick, 2007: 334).

While Drucker promotes the management team approach to leadership, Philip Selznick's *Leadership in Administration* (1957: 4) focuses on the argument, "The executive becomes a statesman as he makes the transition from administrative management to institutional leadership." He highlights how the treatment of others comes from the administrator's "code of ethics" which "is as significant a part of his equipment as an administrator as is his knowledge of

administrative behavior", quoting from a 1950 collaboration of Simon's *Public Administration* (Selznick, 1957: 80). He then goes on to note that the challenge to leadership is "*to choose key values and to create a social structure that embodies them"* (Selznick, 1957: 60), reinforcing the role of the executives in "building special values" (1957: 27) into the organization to ensure its stability.

With respect to organizations, Selznick notes they "do not so much create values as embody them" (1957: 20) while "from the standpoint of social systems rather than persons, organizations become infused with value as they come to symbolize the community's aspirations, its sense of identity" (1957: 19). This firmly places a social responsibility of purpose and responsiveness on the organization. Selznick (1957: 121) also defines social values as "objects of desire that are capable of sustaining group identity", while "*the maintenance of social values depends on the autonomy of elites*", where *elites* could be matched to Drucker's management teams. Selznick's criteria of autonomy reflects the importance he attaches to protecting values from being compromised, as noted in one of his concluding arguments that the "characteristics of the responsible leader can be summarized under two headings: the avoidance of opportunism and the avoidance of utopianism" (Selznick, 1957: 143).

2.2.3 1960's – Cold War & civil rights

Roethlisberger's (1977: 259) teaching of business policy provoked a reflection on the CEO's position and the realization that the challenge was to "get people *not* in this position to practice the administrative point of view" and the importance of "group rather than individual performance" (1977: 313).

Chandler's *Strategy and Structure* (1962) reflects on corporate structure development of major American firms to 1960 in relationship to their environment and chosen strategies, where *structure follows strategy* is often repeated. In addressing the role of senior executives, Chandler (1962: 382) stressed the importance of the longer-term planning aspect and the need to remove the executives from the day-to-day activities, balancing management's attention to echo Selznick's emphasis on critical decision making. The complexity of integrating often ambiguous or conflicting stakeholders' concerns when evaluating strategic choices underlines the need for comprehensive executive review of the longer-term consequences of corporate decisions. This focus on future stakeholder needs has been integrated into current definitions of corporate sustainability (Zink, 2007).

David Braybrooke and Charles Lindblom's *A Strategy of Decision* (1963) relate ethics, morals and values within public policy formulation, which could also be applied to corporations. Warning "ethical theory cannot make bad actions impossible" Braybrooke and Lindblom (1963: 209) point out that some moral judgments can contradict other equally moral decisions. Considerable emphasis is placed on the ethical and moral underpinning of public policy decisions to achieve a concept of justice. However, as "values change with time and experience" (Braybrooke & Lindblom, 1963: 26) the difficulty of public policy setting or strategy determination for the firm is accentuated. The divergent public interests to be considered by governments may be seen as an analogy to the divergent stakeholder interests to be taken into account by the firm.

Richard Cyert and James March's *A Behavioral Theory of the Firm* (1963) viewed the organization as "a coalition of individuals" (1963: 27) where the coalition would establish objectives through bargaining, controlling and adjusting to respond to changes, including those within the environment of the firm. This suggested that both internal and external stakeholders, beyond just shareholders, would influence the firm's choice of direction. They also go on to note that within the goal setting "side payments, far from being the incidental distribution of a fixed, transferable body, represent the central process of goal specification. That is, a significant number of these payments are in the form of policy commitments" (Cyert & March: 30). This has interpreted firm objectives to be "in reality a negotiated consensus of objectives of the influential participants" (Ansoff, 1965: 35), leading Ansoff to credit Cyert and March with "the ring of the stakeholder theory" as his inspiration. Cyert and March viewed business decisions to be taken based on economics but in consideration of social behaviour and noted (1963: 237) "the modern business firm is an impressive social creation", suggesting the role of social networks in influencing decisions.

An illustration of a large corporation's goal to have a better safety record than other plants in the industry stressed the importance to safety engineers of eliminating fatal accidents and time lost due to injuries (Cyert & March, 1963: 35), recognizing a social responsibility to the workers as well as an economic benefit to the corporation.

Igor Ansoff's *Corporate Strategy* (1965: 34) combined responsibilities and objectives into a "stakeholder theory of objectives. This theory maintains that the objectives of the firm should be derived balancing the conflicting claims

of the various *stakeholders* in the firm: managers, workers, stockholders, suppliers, vendors. The firm has a responsibility to all of these and must configure its objectives so as to give each a measure of satisfaction" going on to say, "profit which is a return on the investment to the stockholders is one of such satisfactions, but does not necessarily receive special predominance in the objective structure". Ethical criticism of the profit objective prompt other doctrines such as "equal responsibility to stock-holders, long-term survival, or a negotiated consensus among various participants of the firm" to be suggested, noting that, "some have branded profit as immoral and socially unacceptable" (Ansoff, 1965: 31).

In identifying major influences on the firm, Ansoff (1965: 64) notes two categories of social responsibility*, "philanthropy* and *enlightened self-interest*" where "a sense of personal obligation by management or owner to serve larger purposes of society is sometimes expressed". He recognizes that the social objectives "are the result of interaction among individual objectives of the firm's participants", however that they "exert a secondary modifying and constraining influence on management behavior", where *"constraints* are decision rules which exclude certain options from the firm's freedom actions" (Ansoff, 1965: 38). While Ansoff has been credited as the origin of the term *stakeholder* (Freeman, 1984: 49), his view of stakeholders included the above noted *constraints*, as opposed to today's view that stakeholders are integral to strategy development.

James Thompson's *Organizations in Action* (1967: 11) places the organization as "part of a wider social system which is the source of the *meaning,* legitimation, or higher-level support which makes the implementation of the

organization's goals possible" where in "its *rights* to command resources and to subject its customers to discipline, it is never wholly independent".

2.2.4 1970's – Technology

Russell Ackoff's *A Concept of Corporate Planning* (1970) provides general planning insights, which may be applied to social responsibility issues. Ackoff (1970: 21) notes "adaptive planning also requires understanding of the dynamics of values: the way values relate to needs and their satisfaction, how changes in needs produce changes in values, and what produces changes in needs", highlighting the importance of "building responsiveness and flexibility into an organization" (1970: 17). The need to understand stakeholders' concerns and priorities was never more evident as media reporting shrunk the information gap, fuelling stakeholders' expectations and enabling stakeholders to assess firm behaviours. In addressing one stakeholder, the consumer, Ackoff (1970: 53) quotes a marketing executive's advice to view the consumer as rational, while the marketer may be irrational, to conclude "dramatic changes in a business can be suggested by an understanding of why people consume what they do, when they do, where they do". Reflecting the old adage that *the customer is always right,* responsiveness can only be achieved when stakeholder motivation is fully understood. This search for the underlying rationality is a key feature in today's stakeholder management.

Joseph Bower's *Managing the Resource Allocation Process* (1970: 302) identifies all projects to be "organizationally interdependent", so that the definition and conception of a project should take into account the entire

structural context. He points out "the choice of business goals must reflect management's aspirations, attitudes toward risk, and sense of social responsibility" (Bower, 1970: 285), the sole reference to other than economic responsibilities.

Graham Allison's *The Essence of Decision* (1971: 145) describes organizations as creating *"capabilities* for achieving humanly-chosen purposes and performing tasks that would otherwise be impossible"; constraining *"behavior*, namely, they address it already oriented toward doing whatever they do"; and developing a culture "to shape the behavior of individuals within the organization" where (1971: 153) "organizational culture is thus the set of beliefs the members of an organization hold about their organization, beliefs they have inherited and pass on to their successors". These beliefs can also be seen as framing social responsibility. Echoing Cyert and March's (1963) role of negotiations, Allison (1971: 170) explains "by arranging a *negotiated environment,* organizations try to maximize autonomy and regularize the reactions of other actors with whom they must deal", once again alluding to stakeholders.

In developing the stakeholder management concept, Freeman's (1984: 81) analyses levels of "*rational, process*, and *transactional* parallels Graham Allison's (1971) three levels of organizational analysis. However, the three levels are not mutually exclusive as is often interpreted from Allison's account. Each level of analysis offers a different *lens* for viewing the organization and offers different kinds of explanation for some underlying phenomena broadly called

organization behavior. While the explanations at each level need not be identical, they do need to be consistent".

Kenneth Andrews' *The Concept of Corporate Strategy* (1971) is essentially an executive handbook of values, ethics, morality and social responsibility. He very clearly attributes heavy responsibilities to the chief executive officer to be fully accountable for results and fully aware of all corporate activities. Andrews (1971: 8) notes "enthusiasm for meeting ethical problems head on and avoiding shoddy solutions comes not so much from a system of rewards and punishments as from the sentiments of loyalty or courage stimulated by the personal deportment of the chief executive. By the persons they are, as much as by what they say and do, presidents influence their organizations and affect the development of the individuals" and that "ethics, like preference, may be considered a product of values" (1971: 88).

With respect to the formulation of corporate strategy, including its objectives and goals, Andrews (1971: 18) emphasizes that it also defines "the kind of economic and human organization it is or intends to be, and the nature of the economic and noneconomic contribution it intends to make to its shareholders, employees, customers, and communities", reflecting an awareness of the diversity of stakeholder interests to be addressed by the firm. When considering strategic decisions, coherent with the firm's environment, he links firm success to the ability to capitalize on firm strengths, including its identity. Andrews (1971: 26) goes on to explain the examination of ethics within strategic choices is made "against the standards of responsiveness to the expectations of society that the strategist elects. Some alternatives may seem to the executive considering them

more attractive than others when the public good or service to society is considered" and that "coming to terms with the morality of choice may be the most strenuous undertaking in strategic decisions" (1971: 89). He puts strategy into context by stressing: "strategy is a human construction; it must in the long run be responsive to human needs" (Andrews, 1971: 85).

Like Drucker (1954) and Ansoff (1965), Andrews (1971) saw the firm as having distinct responsibilities to society. Andrews (1971: 99) also recognized the "personal values of the managers making the decision" would orient a choice of strategic alternatives, and in cautioning "a company should not venture into good works that are not strategically related to its present and prospective economic functions" (1971: 100) recognized the lack of necessary resources. The integration of ethical, moral and stakeholder considerations into strategy decisions is the essence of today's CSR.

2.2.5 A contemporary view of CSR: 1980's and beyond

Edward Freeman's seminal 1984 *Strategic Management: A Stakeholder Approach*, is the basis for stakeholder theory and stakeholder management. His research (Freeman, 1984: 33) found the word "stakeholder" first used by "Stanford Research Institute in 1963", who defined it as a survival mechanism as "*those groups without whose support the organization would cease to exist",* and next appeared in Ansoff's *Corporate Strategy (*1965). Freeman (1984: 46) defined stakeholders to include "any group or individual who can affect or is affected by the achievement of the organization's objectives", with his stakeholder concept embracing corporate planning, systems theory, corporate social

responsibility and organization theory to form strategic stakeholder management (1984: 32).

With respect to the aspect of CSR, Freeman (1984: 40) laments the popular view of *"corporate social responsibility is fine, if you can afford it",* while noting the potential to "redefine the notion of enterprise level strategy to more closely align *social and ethical concerns* with traditional *business concerns*" (1984: 90). Drucker (1984: 62) also modernized his advice to managers that "the proper *social responsibility* of business is to tame the dragon, that is to turn a social problem into economic opportunity and economic benefit, into productive capacity, into human competence, into well-paid jobs, and into wealth", making the link explicit and echoing Andrews (1971).

2.2.6 Current stakeholder themes

Some subsequent refinements to stakeholder theory focus on requiring legitimacy to be considered a stakeholder (Rowley, 1997); on segregating primary from secondary stakeholders based on their necessity to firm survival (Clarkson, 1995); and in utilizing urgency, power and legitimacy to determine stakeholder salience (Mitchell, Agle & Wood, 1997).

While it would be altruistic for firms to be intrinsically committed to stakeholder interests because it is the right thing to do, a more instrumental approach views stakeholder management as a strategic tool to improve financial performance and provide a sustainable competitive advantage over the long term (Donaldson & Preston, 1995; Harrison & Freeman, 1999; Wood, 1991).

The institutional view of the corporation's legitimacy is developed in relationship to how a corporation manages its stakeholders (Wood, 1991), with any loss of legitimacy seen as a withdrawal of stakeholder support. While "legitimacy is a *perception* or *assumption* in that it represents a reaction of observers to the organization as they see it; thus legitimacy is possessed objectively, yet created subjectively" (Suchman, 1995: 574), making it both the Achilles' heel and cornerstone of the stakeholder relationship.

Even today, while linked to sustainability, stakeholders and ethics, there is no single, universal definition of corporate social responsibility. One that exemplifies the underlying partnership is The World Business Council for Sustainable Development's definition of corporate social responsibility as "the commitment of business to contribute to sustainable economic development, working with employees, their families, the local community and society at large to improve their quality of life" (WBCSD, 2000: 10).

The diversity and breadth of the elements included in CSR range from marketing dangerous or harmful products to uninformed customers and unfair labour practices to environmental degradation and pollution (Harrison & Freeman, 1999). While corporate social performance has often been linked to financial performance, findings remain inconclusive (Griffin & Mahon, 1997; Margolis & Walsh, 2001; Waddock & Graves, 1997), however the longer-term profitability of environmental and social initiatives has been recognized by many major corporations (Epstein & Roy, 2003).

With respect to management attitudes, "today's captains of industry place no greater importance on social responsibilities than the individuals who

occupied their positions thirty years ago" (Kinard, Smith & Kinard, 2003: 89), a finding the researchers described as "unexpected" given the more widespread acceptance of CSR.

Philip Selznick's *The Communitarian Persuasion"* (2002) draws upon the author's later reflections on many of the topics of his earlier works, as well as exploring new avenues. On the theme of accountability, Selznick (2002: 29) offers a broader view of responsibility where the question is "whether and how much you care about your duties", looking to "ideals as well as obligations, to values as well as rules". In questioning whether a corporation has a conscience, Selznick (2002: 101) notes, "a corporate conscience is created when values that transcend narrow self-interest are built into the practice and structure of the enterprise", becoming an "organizational culture" and accepting the "realities of interdependence".

2.2.7 Summary on 75 years of lessons learned

Most of the business classics reviewed have provided the underpinnings of what has become stakeholder management and CSR. The notion of *authentic leadership* essentially sets out the need for executives to balance their responsibilities to stakeholders to obtain the cooperation necessary for corporate and personal success (Novicevic et al., 2006). The determination of stakeholder salience has been attributed to power, legitimacy and urgency (Mitchell et al., 1997), while Wood (1991) proposed corporate social responsiveness to be processes of assessing the environment, identifying the issues and managing stakeholders.

This exploration of the contributions from the business classics integrates the antecedents to stakeholder theory and CSR. The institutional and population ecology views of isomorphism and the minimal impact of corporate executives on the evolution of firm processes and outcomes offer alternative interpretations for the direction of CSR initiatives. From the classic works of Barnard and Drucker, we are reminded that to achieve firm goals leadership that rallies the full cooperation of internal and external stakeholders is required. With the increased complexity of the often conflicting perspectives of diverse stakeholders on the global stage, current CSR decisions cannot be taken lightly.

While some of today's thriving companies such as Apple and Google may be renowned for unique employee perks, harkening back to the Western Electric Company's employee-friendly policies is a reminder of the distinctiveness that some firms carved out for themselves three-quarters of a century ago in a bleak economic context. In certain industrial sectors, such as the high tech of Apple and Google, today's challenge may come in attracting and retaining the best employees, while in others it is in strategically downsizing without destroying employee morale. We will consider how corporate social actions may achieve these diverse objectives, as well as how perceptions of CSR influence the reputation of the firm in the marketplace. Accordingly, we will next review the definitional landscape of CSR and reputation, as well as the management theories behind their relationship.

2. 3 Definitional landscape of key constructs

2.3.1 Corporate social actions and related constructs

While the terms CSR, corporate social performance, corporate social responsiveness, corporate social actions, corporate social initiatives, corporate social gestures and corporate citizenship are often used interchangeably; there are subtle differences that merit discussion. Each of these *corporate* constructs applies to a firm level of analysis (Griffin, 2000), however the actions, initiatives or gestures may also represent individual transactions. Whether they are viewed as policies, principles, programs or processes (Carroll, 1999) also influences interpretation. Fuelling some of the confusion and lack of agreement is the absence of a single recognized definition (Carroll, 1999 & 2000; McWilliams et al., 2006), leading some scholars to question the absence of a dominant paradigm in the " ill and incompletely defined " (Baron, 2001: 9) or embryonic conceptualization of CSR (Lockett et al., 2006; McWilliams et al., 2006; Orlitzky et al., 2011; Windsor, 2006). The following table outlines a selection of some of the definitions that have been attributed to CSR constructs. These will be compared and contrasted in the discussions that follow to lead to the working definition of corporate social actions that is adopted for this research.

Figure 1. Selected definitions of CSR constructs

	Author(s) quoted
Corporate Social Responsibility (CSR):	
"a discretionary allocation of corporate resources toward improving social welfare that serves as means of enhancing relationships with key stakeholders"	Barnett (2007: 801); also adopted by Bertels & Peloza (2008: 58)
"meeting the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time"	Carroll (1979: 500)
"obligation to evaluate in its decision-making process the effects of its decisions on the external social system.... social responsibility begins where the law ends"	Davis (1973: 312)
"actions that appear to further some social good, beyond the interests of the firm and that which is required by law"	McWilliams & Siegel (2001: 117); also adopted by Janney & Gove (2011: 3)
"the private provision of public goods".... "any "responsible" activity that allows a firm to achieve sustainable competitive advantage, regardless of motive"	McWilliams & Siegel (2010: 2)
"business and society are interwoven rather than distinct entities"	Wood (1991: 695)
Corporate Social Performance (CSP):	
A firm's actions in the promotion and configuration of social responsibility processes, policies, programs, and observable outcomes that are beyond the immediate interests of the firm and beyond that which is required by law	Chiu & Sharfman (2009: 6)
broad construct comprised of stakeholder management and social issues management	Hillman and Keim (2001: 126)
broad array of strategies and operating practices that a company develops in its efforts to deal with and create relationships with its numerous stakeholders and the natural environment	Surroca, Tribo & Waddock (2010: 464)
configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships	Wood (1991: 693)
Corporate Social Responsiveness:	
the capacity of a corporation to respond to social pressures, complements but does not replace responsibility	Frederick (1978: 6)
Corporate Social Actions:	
behaviours and practices that extend beyond immediate profit maximization goals and are intended to increase social benefits or mitigate social problems for constituencies external to the firm	Marquis, Glynn & Davis (2007: 926)

CSR may be viewed as an umbrella term that recognizes "business and society are interwoven rather than distinct entities" (Wood, 1991: 695), representing policies or principles, while the corporate social actions, initiatives or gestures are the vehicles through which CSR is enacted. Another characterization of CSR is “the private provision of public goods” (McWilliams & Siegel, 2010: 2), rooted in I/O economics yet highly pertinent to strategy (Bagnoli & Watts, 2003; Orlitzky et al., 20111). Corporate social responsiveness as "the capacity of a corporation to respond to social pressures, complements but does not replace responsibility" (Frederick, 1978:6, c.f. Wood, 1991: 703). Responsiveness may also be viewed as subsumed within corporate social performance (CSP) which Wood (1991: 693) defines as a "configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships". However Mitnick's (2000) extensive discussion on the measurement of CSP notes the important distinction between outputs and outcomes, questioning the underlying metric for performance. Chiu and Sharfman’s (2009) CSP definition includes a specific reference to *observable* outcomes, while Surroca and colleagues (2010) distinguish CSP as constituting stakeholder relation strategies. Hillman and Keim (2001) also note the lack of a definitional consensus; however their construction of CSP links the management of social issues and stakeholders. The extension to corporate citizenship includes a yet broader role of the firm in "administering citizenship rights for individuals" (Matten & Crane, 2005: 173) or in treating its stakeholders (Heugens, Lamertz &

Calmet, 2003), while the World Economic Forum adds involvement in public policy in its definition (Gardberg & Fombrun, 2006).

Davis' "classic definition of CSR" (Wood, 1991: 694) centers on business' "obligation to evaluate in its decision-making process the effects of its decisions on the external social system.... social responsibility begins where the law ends" (Davis, 1973: 312). Carroll's (1979: 500) definition of CSR expands to meeting "the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time". McWilliams and Siegel (2001: 117) "define CSR as actions that appear to further some social good, beyond the interests of the firm and that which is required by law", clearly attaching voluntarism to CSR as well as actions. Burke and Logsdon (1996) linked voluntarism to proactivity, management discretion and non-imposed compliance as characteristics of strategic CSR. One of the noteworthy characteristics of CSR is that it is at the discretion of the firm (Barnett, 2007).

Some of the more narrow definitions include Barnett’s (2007: 801) formulation of CSR’s focus on “improving social welfare that serves as means of enhancing relationships with key stakeholders”, while Marquis and colleagues’ (2007: 926) corporate social actions are defined as “behaviours and practices that extend beyond immediate profit maximization goals and are intended to increase social benefits or mitigate social problems for constituencies external to the firm”. These restrictions to social aspects ignore the importance of environmental considerations, as well as the multiple stakeholder dimensions whereby employees or shareholders may also be consumers of firm products, neighbours or suppliers.

Linking Wood's (1991) CSP with McWilliams and Siegel's (2001) CSR, we conceptualize corporate social actions to be the expression of the organization's discretionary relationships with stakeholders. When from the perspective of the stakeholder these actions are viewed negatively they constitute detrimental corporate social actions and will be identified as *concerns*. This is the working definition we use when referring to corporate social actions; remembering that CSR is an umbrella term that encompasses the business and society relationship (Wood, 1991) and thus the corporate social actions of business directed to society.

2.3.2 CSR and corporate social irresponsibility

CSR research by Strike, Gao and Bansal (2006) is premised on the separate constructs of CSR and corporate social irresponsibility (CSiR), arguing that in certain activities firms act responsibly while in others they may be irresponsible, echoing McGuire, Dow and Argheyd's (2003) suggestion that a firm may be both strong and weak within a single dimension or across dimensions of CSR. Strike and colleagues (2006: 852) define CSiR as "the set of corporate actions that negatively affects an identifiable social stakeholder's legitimate claims (in the long run)". Schuler and Cording (2006: 550) propose that CSiR firms "will be evaluated negatively by all stakeholders, whereas support for positive CSP will depend on the consumer's moral values", building on Sen and Bhattacharya's (2001) experimental study of consumer purchasing behaviour which found no difference in CSiR by omission or commission. This underlines CSiR's broad stakeholder alienation and resultant hazards. While there is no conceptual foundation to support any offset of desirable corporate social actions

directed to particular stakeholders against undesirable actions directed to the same or other stakeholders, prior research has largely treated CSR as a continuum from responsible to irresponsible (Mattingly & Berman, 2006; Orlitzky et al., 2003). Recognizing firm deficiencies in the relationship with particular stakeholders are "not simply the converse of social strength" (Mattingly & Berman, 2006: 38), further underlines the lack of conceptual basis for a CSR continuum.

Strike and colleagues (2006) allude to, but have not tested, the relationship of reputation and organizational learning on both CSR and CSiR, in their link with international diversification. Following their logic, Doh and colleagues (2010) considered CSiR in their event study of deletions from social responsible indexes however did not find any statistically significant relationship of CSiR with market returns. Mattingly and Berman (2006: 20) have cautioned "that positive and negative social action are both empirically and conceptually distinct constructs and should not be combined in future research". They also propose a taxonomy further segregating the strengths (CSR) and weaknesses (CSiR) between institutional and technical stakeholders in pursuit of more accurate CSR measures to assess other valuable outcomes, such as enhanced corporate image or reputation.

McGuire and colleagues' (2003) examination of executive compensation incentives (a governance mechanism) used separate constructs of desirable and undesirable CSR. While their research found different dynamics in the distinct constructs, they show generous CEO salary and incentives more likely to be associated with poor CSR. Godfrey and Hatch's (2007: 95) reflection on how

"investment among one group of stakeholders to overcome deficiencies with another" may influence strategy, further brings into question "the marginal utility of various CSRs by firms", offering another perspective for an over-investment.

Campbell (2007) notes the difficulty in ascribing the characteristics which will give rise to a firm being judged as socially irresponsible as they vary over time and depending on the stakeholders' perspectives. He postulates that only by failing to meet a minimum behavioral standard does a firm's social behaviour become irresponsible. This may explain why Brammer and Millington (2008: 1341) found "unusually poor social performers doing best in the short run", as they benefit from information asymmetry making stakeholder assessment difficult, compounded by not publicizing their under-performance to their stakeholders, to conceal their poor performance (Doh, Howton, Howton & Siegel, 2010). Recent research on corporate disaster donations following Hurricane Katrina (Muller & Kräussl, 2011) also segregated CSiR in determining the likelihood that irresponsible firms would suffer market share losses, while also making subsequent donations as a possible reputation management strategy.

Widely publicized corporate irresponsibility, such as the BP oil spill in the Gulf of Mexico, informs stakeholders who categorize the environmental disaster as CSiR, resulting in a significant deterioration in BP's corporate reputation. However, many lesser known irresponsible actions may not capture broad stakeholder attention, particularly when firms suppress or deny their involvement in CSiR. While firms seek immediate visibility for their good deeds, they largely delay acknowledging irresponsible actions to distance themselves in the hopes that stakeholder interests will have shifted. For the purposes of this

research we will consider detrimental corporate social actions which we have termed as *concerns* to not be a continuum from corporate social actions, but rather a distinct construct.

2.3.3 Symbolic versus substantive CSR

No discussion of corporate social actions would be complete without recognizing that depending on the stakeholder perspective, a firm's CSR may be perceived to be genuine or merely window-dressing. "Goodness is in the eye of the beholder" (Godfrey, 2005: 784) is a phrase that aptly describes stakeholder views of all aspects of CSR, going beyond Godfrey's (2005) theoretical posturing on philanthropy's ability to generate a resultant intangible asset. His contention that "good deeds earn chits" (p.777) is founded on the long-standing view held in management scholarship (Barnard, 1938; Selznick, 1957) that stakeholders reward firms held in high esteem. Godfrey proposes to anthropomorphize the firm's actions as ingratiating or genuine, in a suggestion that stakeholders question whether a firm action represents "a genuine manifestation of the firm's underlying intentions, vision and character, or is the activity designed to ingratiate the firm among the impacted community?" (2005: 784.). He adopts Jones' (1964: 4) definition of ingratiating as "a class of strategic behaviors designed to influence a particular other person (or group) concerning the attractiveness of one's personal qualities". This ascribes a tone of deception to ingratiation, highlighting the underlying motive as one to purposefully deceive the stakeholder (Godfrey, 2005). Godfrey and colleagues (2007) also caution that CSR may be seen as ingratiating when firms with negative social impact by

virtue of their industry (i.e. pornography, tobacco, nuclear, etc.) or their own actions (i.e. BP) attempt an offset by engaging in CSR such as philanthropic contributions. Similarly, Muller and Kräussl (2011) found that investors viewed the minimizing of a firm's CSiR as a more genuine indicator of trustworthiness than any disaster response philanthropy. To repair damaged reputations Rhee and Valdez (2009: 165) suggest "crisis managers can also benefit from many other symbolic communication strategies", however these may risk further alienating stakeholders. Likened to a "shotgun wedding between marketing communications and CSR" (Jahdi & Acikdilli, 2009: 111), public skepticism is commonly voiced in social media (McWilliams & Siegel, 2010). Campbell (2007) notes the rhetoric or lip service given to CSR that firms build into their corporate image or advertising, suggesting the difficulties in distinguishing hollow claims from substantive actions in considering different cultural contexts.

Aguilera and colleagues (2007) suggest firm response to evolving CSR expectations leads to "decoupling effects so that some companies introduce CSR practices at a superficial level for window-dressing purposes, whereas other companies embed CSR into their core company strategy" (p. 838). In considering the risk of a strategy of symbolic corporate social actions Barnett (2007) postulates the destruction of stakeholder trust to detract from the desired impact of the CSR. However, extending his model of stakeholder influence capacity which proposes past experiences with the firm fuel expectations, then consistently symbolic CSR actions could temper expectations to, for example, maintain *green-washing* rather than substantive environmental initiatives. However, should the actions be CSiR transgressions, any repeat offenses are

likely to fuel stakeholder skepticism as to the sincerity of the firm to reintegrate stakeholder relations or whether they constitute mere window-dressing (Pfarrer, DeCelles, Smith & Taylor, 2008).

Westphal and Zajac (1994: 382) lamented, "while institutional and symbolic action theorists commonly invoke the separation of substance and symbol in organizational activity, large-scale empirical observation of this phenomenon is relatively rare". Their empirical governance research on CEO's long-term incentive plans (Westphal & Zajac 1994, 1995 & 1998) found both symbolic and substantive explanations of these plans, where even symbolic actions were favourably received by the stock markets. They also found firms that followed later than earlier movers to be more likely to seek legitimacy by implementing, but not utilizing, these plans. Based on event history analysis they identified the adoption of the plans distinct from their application, then used multiple regression analysis to find support for their hypotheses of the symbolism of these plans separate from their substance.

In interpreting why symbolic actions were adopted, they suggest "signalling to stakeholders" was adequate as just by appearing to be aligned with stakeholder interests "CEOs are better able to manage their reputation"(Westphal & Zajac, 1994: 370). Similar to the individual level of CEOs, organizations use impression management, which Schlenker (1980: 6) defined as "the conscious or unconscious attempt to control images that are projected in real or imagined social interactions", such as symbolic corporate social actions to influence firm reputation.

David and colleagues (2007) found symbolic management responses to shareholder activism led to deterioration in subsequent CSP. This contradicts the generally held expectation that management's acceptance of a shareholder proposal on enhancing CSP indicates their willingness to improve their CSR. They thus concluded that when shareholder proposals were settled while the CSR performance deteriorated, that a symbolic response had been demonstrated. They do however also recognize limitations related to "aggregation of these (KLD) data into an overall corporate social performance measure could be obfuscating behavioral responses to activism" (David et al., 2007: 98), as they used a composite measure netting CSiR against CSR, combining all stakeholder dimensions. This also reinforces our decision to not consider CSR to be a continuum from positive to negative social actions.

Using quality management standards as a proxy for CSR, Christmann and Taylor (2006) used survey data from ISO 9000 certified firms in China to examine the conditions under which the application of the certification would be substantive. They found "supplier certification programs contribute to symbolic standard implementation by suppliers" (Christmann & Taylor, 2006: 873) based on firm survey responses that they did not integrate into their daily operations the certified management system, relying on last-minute efforts to pass required audits. This decoupling of obtaining certification from actually implementing the procedures permits a symbolic management. They also found that only frequent monitoring by those customers in whom the supplier had made specific investments resulted in a substantive implementation. They thus highlight the

importance of building a relationship with the stakeholder as a key ingredient to a substantive application of quality standards.

On a similar theme, Hillman and Keim (2001: 127) note "transactional interactions can be easily duplicated and thus offer little potential for competitive advantage", going on to emphasize the importance of reputation in relationships and the time that must be invested. While catastrophes and scandals have often forced a reaction to CSiR, but whether the response has maintained substantive CSR as suggested by Aguilera and colleagues' (2007) illustration of Shell is debatable. Similarly they point to the successful achievement of social change with proactive CSR gestures built on the implementation of reporting structures, adoption of standards and attribution of senior executives to lead CSR, however these may also be viewed as trappings which are only initiated to follow the leaders (Bertels & Peloza, 2008).

While it is not our intention to measure or classify corporate social actions as symbolic or substantive, understanding the stakeholder information asymmetries in building expectations is a foundation to interpret the likelihood of how an initiative will be perceived, depending on the interaction between the firm and the stakeholder. In addressing the influence of stakeholder theory on the relationship between corporate social actions and corporate reputation, we will expand on how stakeholders with a relation with the focal firm differ from those who have exchange transactions with the firm, identifying the former as institutional stakeholders and the latter as technical stakeholders. We will build on the previously discussed research in looking at transactional (i.e. technical) and relational (i.e. institutional) stakeholders (see Chapter 2.4.3.2 for details on

these stakeholders) to anticipate whether they will view a focal firm's corporate social action as symbolic or substantive. The perception of the stakeholder is the key to classifying the corporate social action as symbolic or substantive, such that the same action may be viewed differently depending on the stakeholder and the context with which they frame their assessment. For example, two employees may view their firm's support of employee volunteering very differently, depending on their individual attitudes on volunteering and their perception of the impact of this CSR on themselves. A hypothetical situation is that of two coworkers: one with a commitment to a student mentoring program who is able to leave two hours early once a month to supervisor a homework program in a neighbouring school and another who doesn't have an interest in volunteering, but who will be required cover for the two hours that their coworker is absent. Multiple interpretations are possible: the first worker may view the initiative as substantive, while the coworker may consider it to be that their firm is just *looking good* or engaged in a symbolic gesture; or alternatively, the first worker views it to be symbolic since they expect to be able to volunteer weekly so that only once a month is inadequate, but makes their employer look good. The coworker who does not participate may be impressed that the firm facilitates employee volunteering at a reasonable pace (i.e. two hours a month is not much to cover for a coworker), perceiving the firm to be engaged in a substantive action.

2.3.4 Corporate reputation and related constructs

Corporate reputation is often referred to interchangeably with corporate identity, corporate image, corporate legitimacy or corporate status. However, the distinctions tend to be better nuanced than those surrounding CSR. Corporate identity is internal to the firm (Logsdon & Wood, 2002; Scott & Lane, 2000) and is a self-definition, while image is externally projected (Whetten & Mackey, 2002). Legitimacy comes from conforming to societal expectations thereby justifying the firm's right to exist (Rindova, Pollock & Hayward, 2006; Suchman, 1995), while status is relative to a peer group (Rindova et al., 2006) and "captures differences in social rank that generate privilege or discrimination" (Washington & Zajac, 2005: 283).

Although Lange, Lee and Dai (2011: 155) suggest there is no "definite definition of the construct" of reputation, the most widely used management definition of reputation (Wartick, 2002) is "a perceptual representation of a company's past actions and future prospects that describes the firm's overall appeal to all of its key constituents when compared with other leading rivals" (Fombrun, 1996: 72), and is the definition we adopt in this dissertation. The suitability is further supported by a recent reputation literature review (Walker, 2010: 369) confirming "the predominance of Fombrun's (1996) definition is consistent with Wartick's (2002) narrative assessment of the corporate reputation literature". Other disciplines such as marketing, sociology and economics use a variety of definitions. However, the focus on *perception* is universal, as categorized by Rindova and colleagues (2005: 1036) to be equated with either "assessments of a relevant attribute(s)" or "collective knowledge and

recognition". Reputation is rooted in stakeholders' comparisons of firms, rather than against the societal standard of legitimacy (Deephouse & Carter, 2005; Wartick, 2002). Reputation is enhanced in the eyes of stakeholders when they perceive the firm's actions to be consistent with their expectations and compare favourably against those of other firms (Logsdon & Wood, 2002; Mahon, 2002; Wartick, 2002; Whetten & Mackey, 2002). Miller noted, "capability and reputation cycles reinforced one another", underlining the value of creating these "reputation resources" (2003: 970) over time. Like capabilities, reputation is an intangible asset embedded in the firm (Roberts & Dowling, 2002; Granovetter, 1985).

Thus a firm's reputation is the "overall estimation in which a company is held by its constituents" (Fombrun, 1996: 37), and will evolve over time (Hall, 1992 & 1993; Mahon, 2002). While the short-term influence of advertising may enhance recognition in the marketplace, the esteem component of reputation with which a firm is held may only be built over the longer term (Hall, 1992 & 1993). However, a firm's individual reputation is also nested in that of the industries within which it is associated (Shamsie, 2003). The relative influence of an excellent industry reputation on that of an average firm may infer free-riding reputation advantages, while a good firm may be held back, captive by a poor industry reputation (Mahon, 2002).

While Barnett, Jermier and Lafferty (2006) analyzed definitions of reputation segregating them into three clusters (asset, assessment and awareness), we identify firm reputation as an intangible asset that within a resource-based view can provide a sustainable competitive advantage (Barney,

1991; Carter & Ruefli, 2006; Frombrun, 1996; Lange et al., 2011; Roberts & Dowling, 2002). While reputation is built over time, it is highly vulnerable to being tarnished and risks being lost in no time at all (Carter & Ruefli, 2006; Davies, Chun, Vinhas da Silva & Roper, 2003; Hall, 1992 & 1993). For firms whose stakeholders accord them a strong reputation, any CSR breach may incite a serious backlash since expectations are high (Dawkins & Lewis, 2003; Lewellyn, 2002; Mahon, 2002; Rhee & Haunschild, 2006). When considering how firm reputation may benefit the firm over time, the various advantages of a good reputation include being able to charge premium prices to generate superior margins, cost savings as suppliers and employees seek to be associated with the firm, as well as favourable access to capital given the perception of lower risk (Carter & Ruefli, 2006; Frombrun, 1996, 2001; Fombrun & Shanley, 1990; Lange et al., 2011; Roberts & Dowling, 2002). An extensive review of indicators and antecedents of reputation across disciplines highlighting reputation's multidimensionality is documented by Rhee and Valdez (2009: 147-150), while Lange and colleagues (2011) present a similar review drawing only from the management literature.

Attributed as key to firm success (Hall, 1992 & 1993), but only durable to the few (Carter & Ruefli, 2006) and rarely over a long time-frame (Wiggins & Ruefli, 2002), understanding the evolution of reputation with corporate social actions is integral to firm strategy.

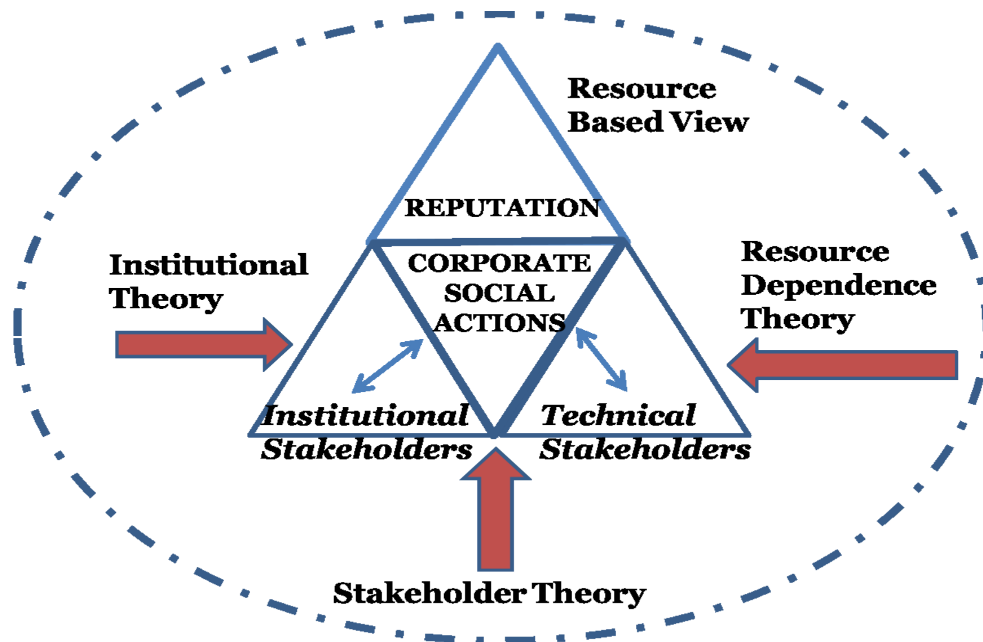
2.4 Theoretical foundations

2.4.1 Overview of theoretical model

Freeman's (1984: 46) classic definition of stakeholders as "any group or individual who can affect or is affected by the achievement of the organization's objectives" underpins stakeholder theory which is the foundation for stakeholder management. However the inherent complexity in stakeholder management draws on multiple theoretic lenses to understand how organizations interact with their stakeholders, so that stakeholder theory is but the starting point. We will also draw upon Pfeffer & Salancik's (1978) resource dependence theory for the firm's reliance on stakeholders for access to resources and institutional theory's isomorphism (DiMaggio & Powell, 1983) as firms mimic each other in their stakeholder relations, embedding them within firm processes (Granovetter, 1985), as well as within industry practices. These are linked together with the resource-based view (Barney, 1991) of a firm's bundle of unique capabilities that provide competitive advantage, adopting McWilliams and Siegel's (2010) identification of the synergy of CSR and reputation as cospecialized assets. The bundling of capabilities in CSR and reputation reinforces their value beyond what they contribute independently to add further ambiguity, creating a resource bundle that can be rare, valuable, inimitable and non-substitutable (Barney, 1991). As CSR improves or deteriorates, the impact on corporate reputation creates a dynamic model of change over time this being the primary focus of this research. We recognize that no model of stakeholder interaction can be stagnant, as time, context and stakeholder salience influence stakeholder perceptions which translate to their assessment of firm reputation.

Before examining the drivers of corporate social actions and corporate reputation the following figure situates the theoretical relationship that will be the foundation for the proposed conceptual model. The outer circle represents the firm as seen from a resource-based view, with the other theories captured within the inner circle. At the core diamond are the cospecialized intangible assets of reputation and corporate social actions. CSR is both focused on and influenced by stakeholders as defined by stakeholder theory. As discussed in greater detail in Chapter 2.4.3.2, *technical stakeholders* are those who transact or hold exchange relations with the firm, while *institutional stakeholders* are those affected by the firm. It is then institutional theory that frames the interaction with institutional stakeholders and resource dependence theory that explains the interaction with technical stakeholders. Each theory will be subsequently discussed in greater detail.

Figure 2. Theoretical foundation for corporate social actions and reputation



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2.4.2 Perspectives on corporate social action and reputation drivers

Before elaborating on the theoretical framework depicted in Figure 2, alternative interpretations of the drivers of corporate social actions and corporate reputation will be explored. There are multiple theories underlying the motives for engaging in corporate social actions, aligned with Brammer and Millington's (2008) observation that "fundamentally different aspects of CSP may be expected to be differently motivated", which we extend to those actions giving rise to CSP. Multiple dimensions of reputation are proposed by Lange and colleagues (2011: 163) reflecting: "being known, being known for something, and generalized favorability". The following table summarizes the underlying theories that

explain the motives that incite investments in corporate social actions and the mechanisms that explain corporate reputation. These theories provide insights into why firms engage in CSR as well as how the resultant reputation may be interpreted by stakeholders.

Figure 3. Underlying theories for corporate social actions and reputation

Corporate Social Actions
Signalling theory
Insurance
Over-investment
Conformity
Reputation
Character trait
Technical efficiency
Status by association
Conformity

2.4.2.1 Theories of motives behind corporate social actions

Signalling theory is often evoked in that a firm's discretionary choice of corporate social actions sends a message to stakeholders, indicating that the firm's behaviour will be aligned with expectations (Brammer & Pavelin, 2006; Surroca et al, 2010). Godfrey, Merrill and Hansen (2009: 427) argue "CSR signals a willingness to act *altruistically* (other considering) as opposed to purely *agonistically* (self considering)", while Bergh and colleagues (2010) note the role of signalling to assist stakeholders to distinguish between high and low quality firms. Inclusion in or deletion from benchmark CSR indices were found to signal to investors a competitive advantage to create shareholder value over the long-

term (Ramchander, Schwebach & Staking, 2011). The visibility of the corporate social action (Chiu & Sharfman, 2009; Tetrault Sirsly & Lamertz, 2008) as well as the informational source reporting the action (Godfrey et al., 2009) contribute to how the signal will be interpreted (Barnett,2007). Mackey and colleagues (2007: 829) caution that a too frequent change in CSR strategy may signal "a firm's commitment to social responsibility is not genuine", while Wang and Choi (2010) found consistent CSP or CSR over time to benefit financial performance.

For example, the recession's devastation of retirement savings has focused attention on the issue of employer sponsored pension plans, particularly those where employee benefits are guaranteed (i.e. generally a formula of years of service and age). Firms offering such pension plans signal to stakeholders their engagement to their employees, as well as in a broader sense to the communities in which they operate as they provide for their retirees' financial independence. Conversely, those firms not funding actuarial deficits or otherwise jeopardizing current and future pensions do signal a breach of trust to stakeholders. This signal (be it positive or negative) may directly influence employee recruitment and retention, while may indirectly be extrapolated by stakeholders as a signal of the firm's commitment in other areas, such as product warranty guarantees. In choosing CSR initiatives, understanding that what the organization signals to stakeholders may be more far-reaching underscores the need to thoroughly consider possible interpretations as well as the coherence of the signals sent by multiple CSR initiatives.

Insurance considerations may be attached to corporate social actions, as CSR is aligned with a risk-management strategy. Godfrey and colleagues (2009:

428) note “firms accrue positive attributions or moral capital to the extent these outsiders see the firm engaging in activities they deem socially or morally desirable”, so that engaging in CSR may be seen as key to creating this moral capital. This imputation of moral value by stakeholders has a long-standing history (ref: Barnard, 1938; Selznick, 1957) as stakeholders judge the intentions and motivation of organizations. The value of this moral capital may be considered to have an insurance-like quality, as stakeholders are likely to be more forgiving of firms with strong CSR histories, particularly where motives are ambiguous (Chiu & Sharfman, 2009; Godfrey, 2005; Godfrey et al., 2009; McWilliams & Siegel, 2010), and may pardon CSR missteps. Choi and Wang (2009) find that CSP helps under-performing firms recover, suggesting the importance of a prior engagement in CSR to stockpile this social insurance, while Doh and colleagues (2010) find it shelters firms from deletions from social indexes. The focus of a corporate social action may be segregated between social issues and stakeholder management (Barnett, 2007; Hillman & Keim, 2001), while Aguilera and colleagues (2007: 838) distinguish between “reactive and proactive CSR initiatives”. Campbell (2007) takes an alternative perspective in setting a minimal threshold where no harm is done by the firm, with anything less considered to be social irresponsibility. While endorsing the possible benefit of CSR as an insurance against “bad deeds”, we do not integrate this motivation into our model of corporate social actions.

Returning to our example of corporate pension plans, this employee benefit may provide a form of insurance against future concessions. This has been widely used in the airline industry where pilots have agreed to operational

changes to their work requirements to guard against modifications to their pension plans. The insurance provided by a corporate pension plan may also be key to retaining valuable human resources, thus fending off competitor targeted recruitment.

Over-investment offers an alternative perspective on the insurance rationale for CSR in that firms may also over-invest in CSR to achieve anticipated financial (Barnea & Rubin, 2010; Harrison, Bosse & Phillips, 2010; Orlitzky et al., 2011) or reputational benefits (Bertels & Peloza, 2008; Rehbein, Waddock & Graves, 2004). This over-allocation of resources to satisfy particular stakeholders may also serve to create dissatisfaction on the part of other stakeholders (Barnett,2007). While not a *motivation* in itself, firms may place themselves in this situation due to imperfect environmental scanning or a flawed assessment of issues or identification of salient stakeholder concerns leading to an excessive investment in corporate social actions.

In the pension plan arena, the high cost of generous defined benefit plans has garnered considerable attention as firms struggle to viably fund their obligations. The legacy pensions of the US auto industry are one example of an over-investment in a social action of benefit to employee stakeholders. While these US manufacturers provided comparable benefits, the arrival of global competition changed the competitive landscape so that in retrospect these employee benefits appear to be an over-investment.

Conformity to social expectations is another motivator to corporate social actions as increasing stakeholder expectations place pressure on firm managers to keep up with similar firms, as well as firms within the same

geographic community (Bertels & Peloza, 2008; Marquis et al., 2007). Post (1978: 23; c.f. Zyglidopoulos, 2003: 72) notes "a gap develops between the actual performance of a corporation and public expectations about what that performance should be" so that corporate behaviour must be modified to align with the expectations of its stakeholders.

Returning to our example of pension plans, it was traditionally expected that major corporations would provide for their retired employees, who most probably devoted their entire working lives to a single employer. This was the 20th century pattern in many industries such as automotive, banking, transportation, telecommunications, etc. For this reason defined benefit plans prevailed, with very similar conditions within a given industry (i.e. early retirement penalties, maintenance of ancillary benefits). However, stakeholder expectations have been shifting as employee mobility has replaced the single employer and competitive pressures come from developing nations devoid of employee benefits. The expectations of employees may be less than homogeneous (i.e. depending on length of service, employability, union affiliation), while the diverse context of other stakeholders generally reduces their support of such pension plans. This shift in expectations, coupled with the economic environment and increased longevity, may explain the reviews and revisions many firms are instigating to conform to their perceptions of where their industry peers will orient themselves. However, returning to the signal the firm provides via its pension plan, while any changes may draw on its insurance value or be viewed as correcting an over-investment, it is the conformity to expectations that will determine the stakeholder's interpretation of the signal.

As we have seen, CSR may signal motivations to stakeholders or may provide insurance with the attribution of moral capital, while it may also be an over-investment or conform to what similar firms are doing to meet stakeholder expectations; all possible motivations for engaging in CSR which will influence stakeholder perceptions of how well corporate social actions meet expectations. These perspectives lay the groundwork for firms' motives for engaging in CSR which stakeholders will interpret when they attribute reputation to the firm in the mechanisms to be discussed in the following chapter. Additional discussion of specific stakeholder relationships will continue in the section on stakeholder theory that follows, as well as an expansion of mimicry and isomorphism in the following discussion on institutional theory.

2.4.2.2 Theoretical mechanisms explaining reputation

According to Kraatz and Love, three distinct insights on the mechanisms guiding stakeholders in attributing reputation to a firm are that firm's character traits, conformity to social norms or technical efficiency (Kraatz & Love, 2006; Love & Kraatz, 2009). A further mechanism focused on the relational profile of the focal firm with central high status firms or individuals is an additional network perspective of how a firm can enhance its reputation by association (Kraatz & Love, 2006). In considering a firm's reputation, stakeholders' evaluations may be based on any combination of these perspectives, recognizing that information asymmetries and imperfect knowledge of the firm will influence their evaluative logic and interpretation of firm actions (Washington & Zajac, 2005).

Lange and colleagues (2011: 163) propose reputation to be three dimensional: "being known, being known for something, and generalized favorability", however they map their *being known for something* as Love and Kraatz's (2009) technical efficiency and their *generalized favorability* as the character traits and conformity identified by Love and Kraatz.

Character traits of a favourable nature undoubtedly enhance personal reputation. Extending this explanation to corporations is based on the tendency for individuals to attribute human traits to organizations, known as anthropomorphization (Davies et al., 2003; Love & Kraatz, 2009). Accordingly much of the literature on corporate reputation promotes the reputational benefits gained by firms based on their desirable character traits, most notably integrity, reliability and trustworthiness (Davies et al., 2003; Fombrun, 1996; Kraatz & Love, 2006; Love & Kraatz, 2009).

The coherence over time of a firm's valued character traits with its demonstrated actions, such as corporate social actions, can be seen as enhancing firm reputation, while inconsistencies are most likely to damage firm reputation (Davies et al., 2003; Kraatz & Love, 2006; Love & Kraatz, 2009). Beyond CSR or philanthropy, character traits may also be imputed from product quality, innovation and creativity (Godfrey, 2005). Davies and colleagues (2003) extend human personality traits, often described by the *Big Five* dimensions, to corporate personality traits to consider in managing firm reputation. The character trait perspective suggests stakeholders will interpret signals from firm actions to make judgments on how these actions correspond to those firm attributed characteristics, "*as if* they were indicative of organizational character

traits, whether or not this is actually the case" (Kraatz & Love, 2006: 348). Furthermore, based on limited information stakeholders rely on these signals to impute intentions and predict future firm behaviour (Fombrun & Shanley, 1990; Rao, 1994). For example, the *green movement* has gained momentum in defining trustworthiness as a reduced environmental footprint, reflecting reliability and accountability for the use and disposal of resources. Accordingly, a recycling initiative would reflect positively as a desirable trait of environmental stewardship.

Technical efficiency essentially bases reputation on superior results, be they financial, product or service quality, focusing on the outputs, rather than the firm itself (Kraatz & Love, 2006; Love & Kraatz, 2009). This approach echoes the financial halo effect criticized by researchers such as Fryxell & Wang (1994) and Washington and Zajac (2005) and others who claim financial performance is a predictor of reputation (Brown & Perry, 1994; Fombrun & Shanley, 1990). This reflects a utilitarian view that firm reputation is dependent on how well a firm delivers valued outputs or is technically efficient in the eyes of its stakeholders.

Returning to the previous example of the *green movement*, stakeholders may interpret recycling as going beyond trustworthiness to provide a more efficient input to a production process for a cost saving that can be redirected to further *green initiatives*. Offering a parallel to the signalling of CSR, such corporate social actions may also be interpreted by stakeholders as a signal of the firm's engagement with the *green movement* and commitment to pursue further beneficial initiatives. This technical efficiency viewpoint also balances the firm's investment in corporate social actions with anticipated returns so that reputation

is enhanced for wisely investing, while diminished for tangential or over-investment which fail to meet stakeholder expectations.

S***tatus by association*** *(*relational status) explains the assessment of reputation to go beyond the focal firm to be based on the status of the firm's external partners or network of clients and suppliers, and is grounded in social network research (Kraatz & Love, 2006; Podolny, 1993 & 1994; Stuart, Hoang & Hybels, 1999). Effectively, this perspective envisions reputation to be gained by association with high status actors, or to be lost when associated with low status actors, where "status refers to a more global assessment of the prestige, desirability, or esteem of the firm itself" (Bergh, Ketchen, Boyd & Bergh, 2010: 629). Rindova and colleagues (2006) invoke status as an instigator of stakeholder attribution of quality as they interpret other firms' association to be an endorsement. This situation is most likely to arise when the quality of the firm or the nature of its business is sufficiently ambiguous as to make reputational assessments difficult for stakeholders (Kraatz & Love, 2006).

Washington and Zajac (2005) however note the sociological foundation of status in ascribing a social rank that does not have to be earned, distinguishing status from reputation which they consider to be a "fundamentally economic concept that captures differences in perceived or actual quality or merit that generate earned, performance-based rewards" (p. 283). They recognize the role of historical legacy and audience perception in attributing both reputation and status to an organization, although they claim to be able to explain the evolution of status without referring to *merit*, but to social class. Accordingly the prestige

of high status actors in a firm's network aids the focal firm's reputation by inference as to the firm's quality (Kraatz & Love, 2006).

In an event study around the addition and deletion of firms to prestigious social indexes, Doh and colleagues (2010) found only a removal had negative effects, speculating that market anticipation was already factored in for well performing firms. Conversely, Ramchander and colleagues (2010) found that not only did inclusions benefit the focal firm share price, but that it also detracted from rivals, with the reverse being true when deleted from the index (i.e. a negative share price reaction for the focal firm, to the benefit of rivals). They also found these responses most pronounced for industries where intangible assets dominated, such as services and R&D focused firms.

Returning to the example of the *green movement*, affiliation with firms included in the Dow Jones Sustainability Index (high status actors recognized for their environmental record) can confer reputational benefits beyond those directly attributable to the recycling initiative.

Conformity to social norms is grounded in neo-institutionalism where conformity, including symbolic conformity, garners stakeholder approval (Kraatz & Love, 2006; Love & Kraatz, 2009; Meyer & Rowan, 1977). Conforming to industry norms establishes similarities between industry actors, lending credibility to stakeholders (Basdeo, Smith, Grimm, Rindova & Derfus, 2006). "Institutional perspectives generally emphasize the role of social factors rather than economic or efficiency factors in driving organizational action" (Westphal, Gulati & Shortell, 1997: 366), a reflection of how stakeholders attribute reputation according to their perceptions of how well the firm conforms to their

expectations (Rao, 1994; Straw & Epstein, 2000). This confirmation of fit with their cultural beliefs is expressed in stakeholders' approval through the esteem they attribute to a firm's reputation (Love & Kraatz, 2009).

In studying the effect of popular management techniques, such as total quality management (TQM), Straw and Epstein (2000) found that announcing adhesion to TQM or actually implementing TQM enhanced firm reputation, in spite of the fact that such management techniques were not proven to enhance financial performance. They interpreted their findings to support "both rhetoric and reality" (Straw & Epstein, 2000: 548) in conforming to the beliefs and normative values of the surveyed audience (Love & Kraatz, 2009). Completing the *green movement* example, societal values and beliefs have evolved to embrace environmental sustainability. Beyond technical efficiency, or the status of being associated with firms recognized by a prestigious index, the recycling initiative would be seen as conforming to social values, and thus incur reputational benefits.

In summary, the theoretical mechanisms explaining corporate reputation as imputed character traits or signals of technical efficiency, status or conformity to social norms, link firm actions (with corporate social actions being our focus) to stakeholder perceptions upon which reputation is attributed. As will be seen in the following discussion on stakeholders, conformity will largely guide institutional stakeholders' assessments, with technical efficiency influencing technical stakeholders' assessments.

2.4.3 Stakeholder theory and stakeholder management

Returning to the theoretical foundation depicted earlier in Figure 2, stakeholders have been generalized as primary, secondary, voluntary and involuntary (Clarkson, 1995), while stakeholder categories include employees, customers, community, suppliers, shareholders and the environment, with stakeholders possibly belonging to multiple groups, such as employees owning company shares, purchasing firm products and living in the same community as the firm.

Clarkson (1995: 106) defines primary stakeholders as those "without whose continuing participation the corporation cannot survive as a going concern", while (1995: 107) "secondary stakeholder groups are defined as those who influence or affect, or are influenced or affected by, the corporation", going on to note that a firm is not dependent on them for survival.

There are multiple categorizations possible of stakeholders based on whether stakeholders are related (internal) or unrelated (external) to the firm, as well as distinctions between those stakeholders that affect the firm (technical) and those that are affected by firm actions (institutional). Underlying these distinctions are information asymmetries inherent in developing expectations and assessing the impact of firm actions relative to those of their peers.

Rindova and colleagues (2005) note where customers have difficulty to evaluate product quality they rely on strategic signals to formulate their expectations, consistent with the role of signalling discussed earlier.

It is the stakeholders' perceptions of the quality of past interactions that forms future expectations and frames the stakeholders' images of the firm

(Lewellyn, 2002; Logsdon & Wood, 2002; Mahon, 2002; Scott & Lane, 2000; Wartick, 2002). The firm's legitimacy as an institution comes from how it is perceived to manage its stakeholders, with any withdrawal of stakeholder support signifying a loss of legitimacy (Suchman, 1995; Wood, 1991). This withdrawal signifies a distinct dynamic with a message to the firm from the stakeholder, as communicated in the form of reputation (Lewellyn, 2002).

Inevitably there are trade-offs required between stakeholders as social conditions change and good causes emerge (Godfrey, 2005). Also consistent with the theory of over-investment in social actions is the need for firms to recognize when stakeholder interests have shifted to align their attention to meet issues pertinent to their stakeholders. However, engaging this social responsiveness must be balanced against demonstrating consistency in CSP to avoid alienating stakeholders. Godfrey (2005) suggests adapting philanthropic activities to focus on pressing societal needs, a practice that has been evident in firm social actions directed to recovery after hurricanes, earthquakes and other natural and man-made disasters. However, Muller and Kräussl's (2011) research on corporate responses to Hurricane Katrina suggests that disaster response giving may also be seen as ingratiating, particularly for organizations viewed as irresponsible where such philanthropy is viewed to be inconsistent.

2.4.3.1 Stakeholder salience

Stakeholder attributes such as legitimacy, power and urgency (Mitchell et al., 1997) determine the salience to management and ultimately whether management will ignore stakeholder pressures and maintain the status quo, offer

a compromise or comply with the stakeholders' request (Rowley, 1997). Peloza and Papania (2008) propose that these salient stakeholders will follow and be more aware of corporate social actions than stakeholders lacking the Mitchell and colleagues' (1997) attributes. Accordingly salient stakeholders will likely engage in more exchanges with the firm to generate exchange capital, defined by Godfrey and colleagues (2009: 429) as "the potential to create more advantageous exchanges between the firm and its primary stakeholders".

Considering primary stakeholders to be legitimate, when they have power and urgency the ensuing corporate social actions are likely to produce *exchange capital* rather than *moral capital* building on a lens of power-exchange (Godfrey et al., 2009). Alternatively, secondary stakeholders while legitimate may have urgency, but lack any power, so that corporate social actions on their behalf are likely to create *moral capital* (Godfrey et al, 2009).

Stakeholders seeking to influence firm policies or actions may operate independently, within a group (Rowley & Moldoveanu, 2003) or in a network (Rowley, 1997), to directly or indirectly withhold resources from the firm as predicted by both exchange theory and resource dependence (Frooman, 1999). As the primary stakeholders have power in the exchange relationship, the firm is dependent on these stakeholders for resources critical to accomplishing their objectives (Pfeffer & Salancik, 1978).

2.4.3.2 Technical and institutional stakeholders

Building on stakeholder salience, we will characterize primary stakeholders as technical, and secondary as institutional, considering the

following distinguishing features. *Technical stakeholders* are viewed to hold exchange relations with the firm and consistent with resource dependency theory (Pfeffer & Salancik, 1978) the firm requires inputs from these stakeholders to achieve its objectives. These are generally viewed as employees, suppliers, shareholders and customers who furnish labour, input goods, capital and purchasers, respectively. However with respect to *institutional stakeholders* it is the firm that can affect these stakeholders' interests, albeit while mimicking others within their industry or geographic domain as predicted by institutional theory. These stakeholders include the community, environment and regulatory bodies. These terms generalize the firm's interactions with its stakeholders, which depending on context and issues may be both transactional and relational at a point in time, recognizing that stakeholders may simultaneously have multiple interests (i.e. an environmental activist employed by the firm, holding company shares and also a customer living in the community within which the firm operates). In other words, while generally technical stakeholders transact with the firm they may also have relational interactions. Similarly, while institutional stakeholders' interactions with the firm may be largely relational, this does not exclude the possibility of transactions with the firm.

Furthermore, relating primary stakeholders to Mattingly and Berman's (2006) technical stakeholders and secondary stakeholders to their institutional stakeholders, Godfrey and colleagues (2009) found a CSR insurance value after a negative event (i.e. a legal or regulatory action against a firm) for institutionally directed CSR but not for technically directed CSR, consistent with the creation of *moral capital*. This underlines the different paths to influence technical and

institutional stakeholders with technical transactions creating *exchange capital*, while institutional relations create *moral capital*. The choice of stakeholder to which a social action is directed will influence the creation of *exchange* or *moral* capital. Similarly, the target of a detrimental social action may accept that exchange capital is bartered or traded off against other actions, this being the case of the technical stakeholder, with their ability to withhold essential goods or services from the firm. However, when directed to the institutional stakeholder the buffering anticipated by the insurance value may only slow the erosion of moral capital, as these stakeholders have no other recourse to show their displeasure with the detrimental social actions. With more avenues to influence the firm, the exchange capital built with technical stakeholders is thus interpreted to be less influenced by CSiR than is the moral capital held by institutional stakeholders.

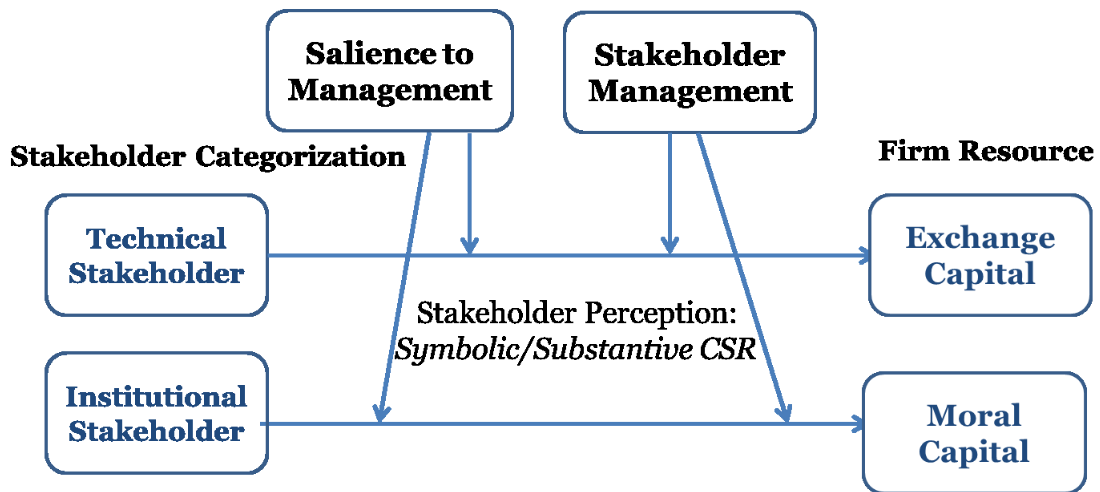
In summary, the firm's exchanges with technical stakeholders creates exchange capital which builds with corporate social actions, while a similar mechanism with institutional stakeholders creates moral capital, however acting as an insurance moral capital is depleted in the case of CSiR.

2.4.3.3 Reactive to proactive stakeholder management

Carroll's (1979) RDAP scale (reactive, defensive, accommodative, proactive) predicts firm processes to position themselves from doing less than required to anticipating beyond actual requirements. Firm management may use Mitchell and colleagues' (1997) criteria of salience in assessing how to manage technical and institutional stakeholders, thus creating exchange and moral

capital, respectively. As discussed previously, these stakeholders will perceive the firm's corporate social actions to be symbolic or substantive as a result of how they are treated by management, thus influencing the quality of the exchange or moral capital created. Relating this characterization of firm stakeholder management to the above discussed stakeholder salience of technical and institutional stakeholders, the following interpretations may be drawn as depicted in Figure 4 below.

Figure 4. Integration of stakeholder management



Depending on the stakeholder type and access to the characteristics that garner attention from management, the firm may choose to be reactive/defensive which may represent mainly symbolic actions or accommodative/proactive which are more likely to be substantive social actions. These are however generalizations for which there may be actual or perceived contradictions, remembering that the perception of whether CSR is symbolic or substantive is in the eye of the stakeholder. Should the firm's social actions correspond to technical stakeholder expectations exchange capital will be created, while conforming to institutional stakeholder expectations moral capital that provides insurance value will be generated. However failure to respond to technical stakeholder expectations of social actions will only fail to create further exchange capital, and not deplete the accrued value of this exchange capital. Technical stakeholders are able to withhold essential resources so that they do not need to draw down on the exchange capital to send a message to the firm of their displeasure with CSiR. On the other hand, institutional stakeholders have no option other than to fall back on the insurance value of the moral capital. Accordingly, a failure to meet institutional stakeholder expectations has them draw down on the insurance value of the moral capital to deplete its accrued value. This is consistent with Godfrey and colleagues' (2009) findings that institutional stakeholders' moral capital acted as an insurance against CSiR, but was not the case for technical stakeholders. Thus institutional stakeholders express their concern in the only way open to them by reducing moral capital. In other words, although moral capital has an insurance value there is a cost of drawing down on it in terms of the remaining value of this intangible asset after a

CSiR misstep. The stock of exchange and moral capital as valuable firm resources is generated by stakeholder perceptions of CSR. We will now briefly relate resource-dependence theory to technical stakeholders, followed by an examination of institutional theory related to institutional stakeholders.

2.4.4 Resource dependence theory

Returning to the theoretical foundation depicted in Figure 2, technical stakeholders have exchange transactions with the firm to provide resources essential to the firm to enable it to achieve its objectives. Pfeffer and Salancik's (1978) resource dependence theory explains how organizations are dependent on resource providers over which they have limited control, but upon which their survival depends. It is this asymmetry between the exchange of resources and the relative power of the exchange partners that are the focus of resource dependence theory (Pfeffer, 1981). Bode and colleagues (2011: 835) summarize the major thrust of resource dependence as "a firm's need for scarce external resources creates a dependence on its exchange partners and, hence, a potential source of adversity for the firm, and that firms strive to minimize this dependence, which is tantamount to maximizing power".

As was seen earlier, power is a key consideration in determining stakeholder salience, such that when a firm is vulnerable to the power of a stakeholder it predicts management's attention will be turned toward the stakeholder, with a strong likelihood that the actions taken will be accommodative or proactive. Maignan and McAlister (2003: 83) note "the

ability of stakeholder communities to withdraw needed organizational resources gives them power over the firm".

Taking the example of employer-employee relations, when there are powerful unions representing essential employees the organization may have to acquiesce to labour demands for above market conditions, thus over-investing in this particular stakeholder group to ensure its survival by avoiding an even more costly labour disruption. Resource dependence emphasizes competing, often incompatible demands, for which management must allocate scarce resources (Oliver, 1991) in selecting among the choice of corporate social actions. As these allocations vary over time, so too will stakeholder assessments of CSR.

Furthermore, technical stakeholders' exchange transactions with the firm provide them with information upon which their expectations are based so they are less likely to be taken in by reactive or defensive actions resembling lip-service. Given the social construction of reality upon which stakeholders base their interpretation of corporate actions as symbolic or substantive (Pfeffer, 1981), "resource dependencies are probably more useful for understanding substantive outcomes in organizations" (Pfeffer, 1981: 8).

This grounding of technical stakeholders in resource dependence theory integrates the essential exchange transactions they engage in with the firm, leading to accommodative and proactive actions by management to meet their expectations for substantive corporate social actions. We will now contrast this with institutional stakeholders as viewed by institutional theory.

2.4.5 Institutional theory

The relationship of the firm with its institutional stakeholders seen earlier in Figure 2 is built on institutional theory. Early foundations are attributed to Selznick's (1957) reflections on transforming organizations into institutions, focusing on routines, roles, beliefs and the processes by which value is infused. His discussions on institutional leadership are described in greater detail in Chapter 2.2.2.

Institutional rules as myths and isomorphic structures to garner legitimacy (Meyer& Rowan, 1977) are interpreted by DiMaggio and Powell (1991) as providing a symbolic role to organizational structures. Three pillars of institutions are described by Scott (1995) as regulative, normative and cultural-cognitive, with their respective sources of legitimacy attributed as legal, moral and cultural. From a cultural-cognitive perspective, institutionalism is based on scripts built on taken-for-granted understandings that mimic those in the environment and also places a value on symbolism (Scott, 1995). Institutional activities are viewed as multilevel interrelated processes which define behavioral expectations, so that conforming gains legitimacy for the firm, however at the same time has firms resembling each other.

When there is no evident technical or financial reason for an institutional activity, such as how corporate social actions might be viewed, the absence of a rational choice explanation makes institutional theory particularly interesting (Oliver, 1997). Although corporate social actions are entirely at the discretion of the firm, from an institutional theory perspective it is societal expectations that

place pressure on firms to behave in a socially acceptable manner, leading to isomorphism (Oliver, 1997).

Interactions of institutional stakeholders with the firm are viewed to be based on relationships that are built over time and create moral capital. Their assessment of CSR evolves over time as perceived urgent issues are replaced by those perceived to be yet more urgent. As these stakeholders are primarily affected by the firm's actions while they may have legitimacy and urgency, a lack of power may prevent them from capturing management attention (Mitchell et al., 1997). Furthermore, a firm's strategy to respond to institutional stakeholders may be to seek a compromise by balancing or bargaining (Oliver, 1991), so that only partially meeting expectations suffices. Oliver (1991: 155) also notes that "the appearance rather than the fact of conformity is often presumed to be sufficient for the attainment of legitimacy". Extending this perspective to when there is ambiguity in stakeholder preferences, as seen in the broader categorization of institutional stakeholders, their inability to discern the value of organizational outcomes allows firms "to get by with symbolic action" (Pfeffer, 1981: 29).

Oliver (1991) also proposes two conditions that may incite a defiance strategy whereby a firm dismisses, challenges or attacks the institutional norms or stakeholder expectations. She notes "when dependence is low, both defiance and manipulation represent minimal risks to organizational interests" (Oliver, 1991: 164), as well as when the cost to conform is significantly more than the expected benefits that would accrue from conforming. The results of such a defiance strategy could be interpreted to be the corporate social concerns

addressed to institutional stakeholders. Given their power and economic asymmetry with the firm, the only affordable response available to institutional stakeholders is in the devaluation of their assessment of firm reputation, depleting moral capital.

This grounding of institutional stakeholders in institutional theory integrates the relationship these stakeholders hold with the firm, suggesting that reactive and defensive actions by management may be adequate to meet their expectations and that symbolic corporate social actions may suffice. However, detrimental social actions directed to institutional stakeholders are likely to have negative consequences . We will now examine the resource-based view to complete the theoretical foundation.

2.4.6 Resource-based view

The resource-based view's answer to why performance varies between firms contends that it is a firm's unique bundle of valuable, rare, non-substitutable and costly to imitate resources and capabilities that provides competitive advantage (Barney, 1991 & 2001). Capabilities become embedded in the firm's processes (Madhok, 1996), and unlike resources may not be distinctly valued or traded (Hoopes, Madsen & Walker, 2003; Makadok, 2001; Teece, Pisano & Schuen, 1997). A firm’s CSR practices may represent such a capability when the value is recognized by the firm’s stakeholders, as attested to in their affirmation of firm reputation, and becomes a dynamic capability (Teece et al., 1997) as it is reinforced over time.

McWilliams and Siegel (2010: 12) integrate the resource-based view of CSR and reputation to identify CSR as “a cospecialized asset that makes other assets more valuable than they other-wise would be. The clearest example of this is firm reputation”. They go on to speculate that CSR best qualifies as this cospecialized asset at those firms producing experience goods or where the cost of irresponsible social behaviour may be significant. The potential for value creation in an intangible asset such as corporate reputation is inherent in the difficulty to replicate a competitor’s reputation due to the ambiguity as to how it was derived (Roberts & Dowling, 2002), and more so how it changes over time.

Bergh and colleagues (2010) also note the social complexity in building reputation, as well as the need to have in place appropriate support to exploit the value of reputation. This is of particular importance in innovation-based industries or knowledge-based services where intellectual property is the intangible competitive advantage (Ang & Wright, 2009; McWilliams & Siegel, 2010), confirmed by Ramchander and colleagues’ (2011) findings of more pronounced share price responses to index reconstitutions for industries they labeled as *informationally opaque*.

Similarly, Janney and Gove (2011) note firms operating in industries with perceived poor CSR have greater reputation benefits when their CSR can signal good quality, however governance lapses such as stock options back-dating were found to have more severe negative impacts on firms with strong governance-related CSR.

A firm's CSR practices may represent such a capability to generate a sustainable competitive advantage when the value is recognized by the firm's

stakeholders, as attested to in their affirmation of firm reputation. In considering shareholder reaction to a firm's recognition for exemplary CSR when it is added to a benchmark index, Ramchander and colleagues (2011) found not only did the added firm's share price benefit from significant improvement, but the share price of their competitors was negatively impacted, providing a competitive advantage in enhancing the relative desirability of their shares.

Examining CSR through the resource-based lens may find the corporate social actions to be vulnerable to imitation due to the inherent visibility if they are to convey positive reputational advantage (McWilliams & Siegel, 2010). It is however the linkage between the intangible assets of CSR and reputation that causal ambiguity is created, with the public visibility of the corporate social action having the potential to provide priceless advertising. This is however a double edged sword, as media and social-media attention is drawn to both good and bad corporate deeds (McWilliams & Siegel, 2010).

Branco and Rodrigues' (2006) resource-based view proposes voluntary CSR disclosure as a leverage of corporate social actions to enhance reputation, however Cho and colleagues (2010) found biased environmental disclosure, with poor environmental performers utilizing highly optimistic language to deflect blame. When stakeholders' primary source of information on corporate social actions was from the corporate annual report, no contradictory information was available for stakeholders to obtain external validation. However, as disclosure has been significantly facilitated by the Internet and social media, these tools provide multiple alternative informational sources for stakeholders, placing greater importance on the accuracy of management claims (Scott & Lane, 2000)

to avoid accusations of half-truths or data manipulation. As controversy over impression management which exaggerates corporate social actions gives rise to public skepticism, the proposed advantages of CSR disclosure are considerably devalued (Jahdi & Acikdilli, 2009).

As noted previously with a resource-based view, firm reputation is likely to provide sustainable competitive advantage when the firm's business processes exploit distinct reputation characteristics (Ray, Barney & Muhanna, 2004), maintaining or improving them based on stakeholder feedback (Mahon, 2002). A resource-based view for CSR research links the firm's abilities with the opportunities offered (Russo & Fouts, 1997). This is also reflected in Podolny's (1993) image of a virtuous cycle between salient actions and firm reputation, to constantly reinforce each other in a dynamic fashion. This logic of continual advancement by taking advantage of opportunities is built on by Roberts & Dowling (2002: 1079) to support their findings that *"reputation differences should demonstrate a relatively high degree of persistence over time"*.

An alternative interpretation of CSR within the resource-based framework cautions that the evolution of CSR has made it less rare while more readily imitated (Orlitzky et al., 2011). The ability of firms to differentiate their corporate social actions is limited, when essentially all major firms are engaged in a broad array of CSR initiatives, which some researchers have found to lead to an overinvestment in CSR (Bertels & Peloza, 2008; Rehbein et al., 2004). Orlitzky and colleagues (2011) suggest that 21st century CSR may in fact no longer bestow a reputational advantage due to the public distrust of CSR manipulations. They point out the British Petroleum (BP) horrific 2010 Deepwater Horizon

environmental disaster, despite universally high CSR recognition of BP as one such example. Similar violations of public trust may be seen in Toyota's product recalls (Diermeier, 2010; Lange et al., 2011), the financial melt-down of sub-prime lending and board scandals over stock option backdating at Apple and other major corporations (Janney & Gove, 2011), all affecting firms with otherwise strong CSR records. However, the attention that these relatively isolated detrimental corporate actions attract may also be interpreted as reinforcing the importance stakeholders attach to being a good corporate citizen.

Furthermore, a firm "may act responsibly not because of any direct link to a positive organizational outcome (e.g. greater prestige or more resources) but merely because it would be unthinkable to do otherwise" (Oliver, 1991: 149). By conforming to stakeholder expectations of acceptable corporate behaviour, firms distinguish themselves to acquire social capital, which Oliver (1996: 177) defines as "a strategic resource distributed by the institutional environment that signifies a firm's credibility and legitimacy". She also proposes that the value of social capital "exists whenever a firm's ability to implement its strategies successfully is affected by its reputation" (Oliver, 1996: 177), while Adler and Kwon (2002: 21) qualify social capital as "a long-lived asset", going on to note the "expectation of a future (albeit uncertain) flow of benefits". This social capital constitutes a dynamic resource that accrues value over time to contribute to competitive advantage. We consider social capital to encompass exchange capital earned with technical stakeholders and moral capital of institutional stakeholders. As pointed out earlier, a key distinction is the cumulative nature of exchange capital while the insurance value of moral capital introduces the risk of depletion over CSiR.

Returning to the basic premise of the resource-based view; rare, valuable, inimitable, idiosyncratic resources are the source of a sustainable competitive advantage (Barney, 1991; Oliver, 1997). The cospecialized assets of corporate social actions and corporate reputation (McWilliams & Siegel, 2010) offer the potential to provide such a resource bundle when they demonstrate persistence over time as "socially endorsed routines that become ratified by their longevity" (Oliver, 1997: 703). In other words, when over time CSR and reputation are consistently strong they can provide a greater value to the firm than should their performance be more sporadic.

This now leads us into a discussion on the temporal dynamics to be considered as a backdrop to the theoretical model depicted in Figure 2.

2.4.7 Temporal dynamics

The enduring quality of reputation that has been referred to as *sticky* (Kraatz & Love, 2006; Roberts & Dowling, 2002; Schultz, Mouritsen & Gabrielsen, 2001) highlights the importance of studying the change over time in a firm's reputation (Muller & Kräussl, 2011). The resilience of reputation, particularly where a strong reputation has been cultivated (Fombrun et al., 2000), indicates that a lag effect may exist before changes in corporate social actions are translated into reputation revisions. Godfrey (2005) also proposes the insurance-like quality of previously acquired positive stakeholder goodwill in dampening the ill effects of CSR missteps. However, where a firm has a reputation for irresponsibility the reduction in those bad deeds is more likely to

matter more than a good deed such as corporate philanthropy (Muller & Kräussl, 2011).

Fombrun (2001: 294) refers to the "winner-take-all" nature of the reputational markets, where attention is given to the most noticeable firms, making it more difficult for competitors to challenge and to improve their reputations. However he also notes how corporate reputation may plunge when a crisis strikes and how recovery will depend on both the pre-crisis reputation and how well the firm is perceived to deal with the situation. This may be viewed as a long uphill battle to build reputation with well received deeds, but a slippery slope to destroy reputation with a misstep.

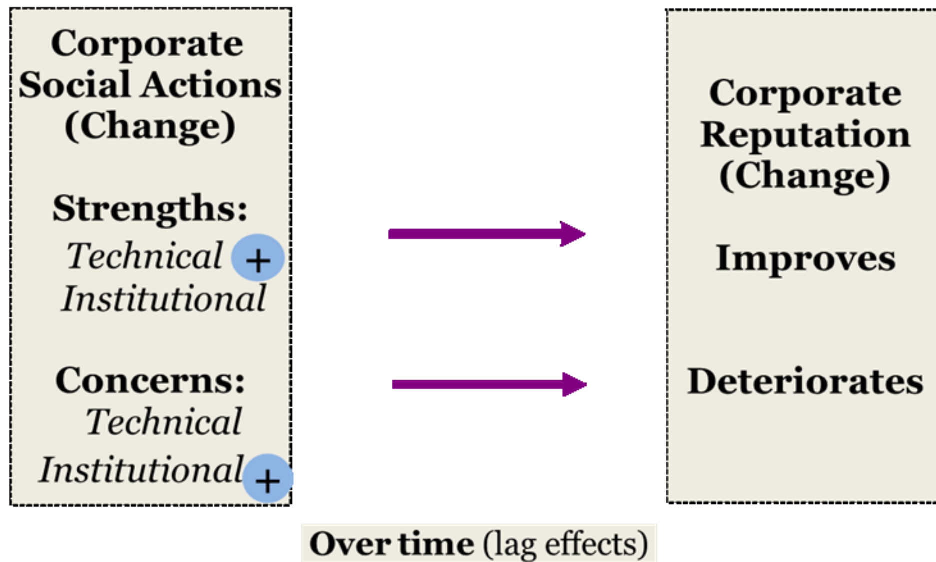
Also to be considered as evolving over time are corporate social actions for which Harrison and colleagues (2010) caution the need for the firm to have been engaged in the CSR for sufficient time for the stakeholders to understand the actions to be able to then reciprocate with for example, a positive reputational assessment. However, from a practical perspective "it is likely impossible to come up with a set of objective and commonly agreed on time lags to examine the causal relationships in the CSP research because isolating the potential confounding factors becomes more challenging as the time lag increases between variables" (Chiu & Sharfman,2009: 21). Godfrey (2005) proposes the strategic value of a consistent pattern of philanthropy as signalling a genuine commitment. In examining the relationship of corporate philanthropy on financial performance, Brammer and Millington's (2008) ten year time period (1990 to 1999) found financial returns to be significantly better for consistently philanthropic major U.K. firms.

As suggested by Ployhard and Vandenberg (2010), to capture the dynamics of expected reputation changes over time, more than three repeated observations are necessary, with the key considerations being the adequacy of the number of repeated measurements and the likelihood of change occurring over the time period selected. Recognizing that both reputation and corporate social actions evolve over time in an idiosyncratic manner, it is necessary to understand the relative positioning of each of these constructs at the beginning of the period under study as well as their movement with the ensuing years. This now leads to our proposed model of corporate social actions and reputation.

2.5 Model of corporate social actions and corporate reputation

Now that the theoretical foundation has been laid, the proposed dynamic interaction of corporate social actions on firm reputation will be developed. Remembering that stakeholders' perception of corporate social actions influences their perception of corporate reputation, it is this dynamic interaction that will take place over time where previous reputation will be revised by interpreting the ensuing corporate social actions in an ongoing feedback loop. Now, building on Godfrey's (2005) conceptual model of good deeds benefiting reputation and Mattingly and Berman's (2006) categorization of stakeholders as institutional or technical, we depict their relationship on the schematic that follows.

Figure 5. Corporate social actions and corporate reputation overview



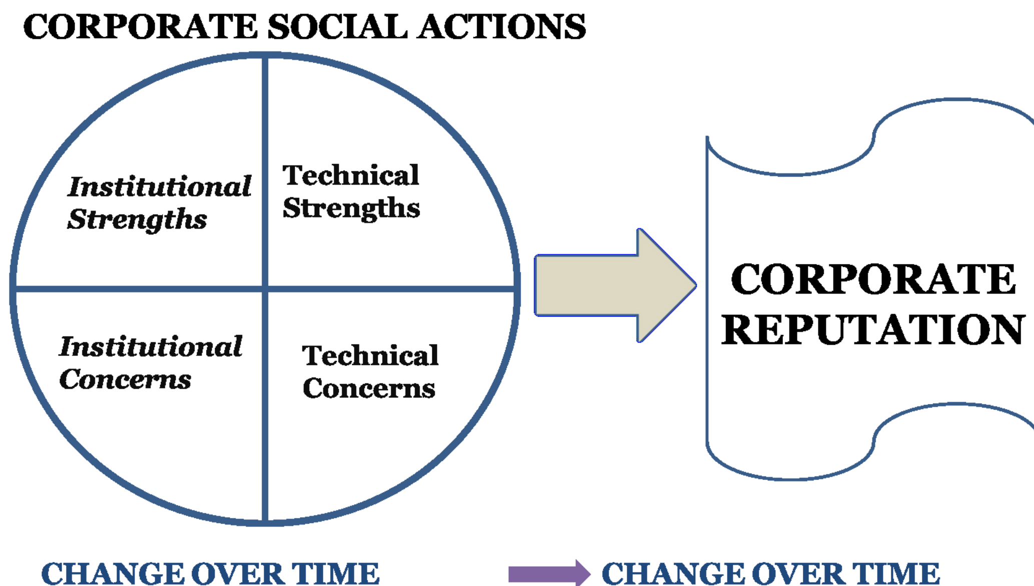
Our model proposes that when stakeholders' perception of corporate social actions is favourable they will reward the firm with positive reputation assessments. Likewise, stakeholder concerns over shortcomings in corporate social actions will be reflected in negative reputation assessments. This dynamic cycle will continue over time. The category of stakeholder as institutional or technical will contribute to whether it is strengths or concerns which will primarily influence the change in reputation as a result of the change in CSR.

Refining the distinction between CSR strengths and concerns, there are differences in the relative importance of assessments by technical and institutional stakeholders. We have already identified the power in exchange transactions as providing technical stakeholders with greater ability to establish expectations as well as more accessible CSR information to assess how well the

firm's corporate social actions meet with their expectations to establish their perception of the firm's reputation. For institutional stakeholders their dependence on the firm provides neither power nor ready access to information, however in the case of concerns over CSR it is institutional stakeholders who sanction the firm with a diminished reputation assessment as they draw down on the moral capital held with the firm. While both stakeholder groups contribute to firm reputation, technical stakeholders will more strongly influence the perception of corporate social strengths, while institutional stakeholders will more strongly influence the perception of concerns over corporate social actions. In Figure 5 above, this is portrayed by the plus sign next to technical stakeholders for strengths and to institutional stakeholders for concerns.

In summary, as per institutional and resource dependence theories, institutional stakeholders will have a stronger impact on the relationship between corporate social concerns and reputation, while technical stakeholders will dominate the relationship between corporate social actions and reputation. This is highlighted above in Figure 5. The overall dynamics of changing corporate social actions' influence on changing corporate reputation is depicted below in Figure 6.

Figure 6. Model of corporate social actions and reputation dynamics



This builds on the premise that stakeholder expectations increase over time, prompting the firm to do more to sustain or improve its corporate reputation. As pointed out earlier, there is a decline in the status quo of CSR when expectations have risen (Barnett, 2007). This need to continue adding to corporate social actions to improve the status quo implies an increase in CSR over time. We have no reason to believe that either CSR or reputation are time invariant, but rather that to meet stakeholder expectations CSR will grow over time as the status quo becomes acquired so that more responsive CSR is needed to maintain reputation.

In other words, after a firm's stakeholders assess its initial CSR efforts these stakeholders perceive the firm's reputation at an initial level and then for the subsequent years are expecting the corporate social actions to be extended.

In year two, the firm has a choice to make with respect to whether it will maintain, diminish or increase its CSR. Recognizing that stakeholder expectations are for the firm to go beyond what was done the previous year, a responsive firm will choose to do more to thus maintain or improve its reputation. This cycle continues on year after year as the firm assesses its CSR efforts and the implications these choices have on their corporate reputation. This is not to suggest that CSR spending grows without limit, but rather the firm makes choices in its CSR initiatives that go beyond the status quo for those elements that are of importance to its stakeholders while perhaps previous or older CSR efforts become less relevant or are regulated, and thus no longer considered to be discretionary CSR. An example of this would be a country's legislation for mandatory company pensions which today are a CSR choice made by some firms, but if required by law would no longer be CSR.

As identified by Orlitzky and colleagues (2011), with CSR having become widely accepted it is no longer a question of whether a firm will engage in corporate social actions. Consistent with stakeholder theory (Freeman, 1984) and identifying the stakeholder salience (Mitchell et al., 1997), the choice of stakeholder to which corporate social actions are directed will however change over time (Godfrey, 2005). Building on the need to go beyond the status quo (Barnett, 2007), a firm will enhance its corporate social actions to meet salient stakeholder expectations (Peloza & Papania, 208) since standing still would effectively be falling behind.

In considering the synergy generated by the cospecialized assets of corporate social actions and corporate reputation (McWilliams & Siegel, 2010), each of these intangible resources are enhanced from a perspective of the RBV (Barney, 1991) so that they contribute to a sustainable competitive advantage. The good deeds performed by corporate social actions within a particular sphere extend beyond that domain to embellish other components considered by stakeholders in assessing overall corporate reputation. For example, when a consumer happy with the good value for money of their purchases is aware of the favourable working conditions a retailer provides its employees, their estimation of firm reputation may be enhanced while they may also attribute greater quality to the services provided by the firm. This compounds the benefits of good customer value and attention to employees to distinguish the firm via a strong reputation which constitutes a competitive advantage. As noted earlier, stakeholder expectations of *what have you done for me lately* effectively discount the status quo, as subsequent corporate social actions are expected to take on additional weight. Accordingly, to maintain or enhance corporate reputation the synergy of these intangibles must escalate so that more responsive corporate social actions are enacted over time. In considering the changes that occur in corporate social actions, our initial hypothesis is:

Hypothesis 1: During the time period of this study, positive change occurs in corporate social actions.

Building on having established that changes do occur over time in corporate social actions, we now consider the direct relation of the change in social actions predicting a change in corporate reputation. This is derived from our earlier explanation of stakeholders' expectations of better than status quo CSR to maintain or enhance reputation. Returning to our initial premise, firms are encouraged to increase their corporate social actions to improve corporate reputation, thus implying a continuing improvement in CSR to maintain or continue to enhance reputation. After having established the changes over time in CSR , we now expect the following relationship with reputation:

Hypothesis 2: During the time period of this study, the greater the positive change in corporate social actions, the greater the positive change in reputation. In other words, improvements in corporate social actions are positively related to an improvement in corporate reputation.

Now that we have established the relationship of the change of corporate social actions improving corporate reputation over the five years of our study, we will now consider the stakeholders to whom CSR is directed. Mattingly and Berman's inductive research on a taxonomy of social actions at the firm level found corporate social actions to depend "on whether stakeholder groups provide institutional or technical resources" (2006: 37). They interpret institutional social actions as built on normative expectations, while resource exchange comes from the technical foundation. Expanding this we further refine institutional social actions as fundamentally relationship based and technical as more

transaction based, adopting Mattingly and Berman's (2006) segmentation of institutional from technical stakeholders in researching corporate social actions. As noted previously, institutional stakeholders are deemed to hold normative expectations of firm behavior and generate moral capital, while technical stakeholders have economic exchange relations with the firm and create exchange capital. Accordingly, the institutional stakeholders may also be viewed as predominantly non-market to include the community and the environment, while technical stakeholders aligned with markets include employees, suppliers, customers and shareholders.

As discussed earlier, stakeholders may be categorized in a variety of ways relative to the firms which influence or may be influenced by stakeholders (Freeman, 1984). We have chosen to expand upon Mattingly and Berman's (2006) view of technical and institutional stakeholders, which may alternatively be categorized as voluntary and involuntary stakeholders or primary and secondary stakeholders (Clarkson, 1995).

While the terminology used to segment stakeholders may be interchangeable, it is the underlying relationship with the focal firm that is paramount to determining the theoretical foundation which may explain the interaction. Building on stakeholder salience (Mitchell, et al., 1997) with a particular emphasis on the element of *power* that the stakeholder exercises, it is those stakeholders who provide essential goods/services to the firm that are likely to command significantly greater management attention than those stakeholders who are dependent on the firm. Resource dependency theory

(Pfeffer & Salancik, 1978) highlights the importance of critical resource providers in capturing management attention and influencing transactions with the focal firm. As technical stakeholders engage in exchange transactions (which may or may not be in addition to developing relationships with the focal firm), they have first-hand knowledge to build expectations as well as to assess how well they are met. Accordingly, when corporate social actions are directed at technical stakeholders their appreciation may be translated into an enhanced corporate reputation. Conversely, should technical stakeholders be the object of any corporate social concerns their ability to withhold valuable goods/services provides them an option other than merely diminishing corporate reputation of the focal firm. With resource dependency theory explaining the relationship between technical stakeholders and the focal firm, this balance of power enables technical stakeholders to positively improve corporate reputation over corporate social actions, while they may engage in a withholding strategy over corporate social concerns as an alternative to merely decreasing reputation. The firm's resource dependency on technical stakeholders thus suggests:

> *Hypothesis 3: Strengths in corporate social actions directed to technical stakeholders more strongly influence corporate reputation than those directed to institutional stakeholders.*

However, when considering "one of the important ways of generating external support for a given organization is to make that organization's

operations and outcomes appear to be consonant with prevailing social values and useful to the larger social system" (Pfeffer, 1981: 21), any failure to meet such normative expectations would be found in institutional stakeholder directed concerns and their negative effects on firm reputation. Furthermore, the insurance value of institutional stakeholders' moral capital is eroded, with the result that technical stakeholders are less influenced by CSiR than are institutional stakeholders.

Institutional stakeholders are largely involuntary or secondary, and as such at are at a power imbalance. As discussed earlier, while institutional stakeholders have relationships with focal firms (which may or may not be in addition to transacting with the focal firm) for which they hold normative expectations (Oliver, 1997), they often lack direct knowledge of firm behaviour and must rely on second-hand reports. According to institutional theory (Scott, 1995), conforming to stakeholder expectations provides legitimacy, or society's moral license to operate. However, given the disparity of institutional stakeholder perspectives, in the event the focal firm fails to meet some normative expectations the only avenue available to institutional stakeholders is to draw down on moral capital (Godfrey et al., 2009) by devaluing corporate reputation.

Institutional stakeholders' (comprising the community, environment, media and NGOs) response to a focal firm's corporate social misdeed is likely to be more homogeneous as shared norms are violated (Oliver, 1991), than to a corporate social action where expectations are ambiguous (Pfeffer, 1981). As noted previously, technical stakeholders' power to withhold essential resources

provides insulation against corporate social concerns. Accordingly, institutional stakeholders' reactions to concerns over corporate missteps will translate to a diminished corporate reputation, leading us to propose:

> *Hypothesis 4: Concerns over corporate social actions directed to institutional stakeholders more strongly influence corporate reputation than those directed to technical stakeholders.*

2.6 Summary of theory development

Drawing on stakeholder, resource dependence and institutional theories, as well as the mechanisms explaining CSR and corporate reputation, we have hypothesized the relationship of corporate social actions and corporate reputation within a resource-based view of the firm. Remembering that reputation is a perception, it is in the technical and institutional stakeholder perceptions of a focal firm that assessments of reputation are formulated. As such, information asymmetry may account for differences in the development of stakeholder expectations and subsequently in the perception of corporate social actions as well as firm reputation. Building on resource dependence, technical stakeholders' exchange transactions provide them greater information to both formulate expectations of and then assess the corporate social actions. Substantive corporate social actions are more likely to be exchanged to obtain favourable reputation assessments. However institutional stakeholders' relationships with the firm may provide more ambiguous information on which they may formulate expectations and subsequently assess conformity. The firm's

relationship with institutional stakeholders may thus allow their corporate social actions to be symbolic yet still be well received. However, should a firm defy institutionally expected social behaviour it jeopardizes the moral capital it has earned from institutional stakeholders, expressed by a devaluation of their reputation assessments.

Returning to the fundamental characteristic that CSR and reputation are perceptions in the eye of the beholder reminds us that the same corporate social gesture may invoke different perceptions related to context (i.e. time, location, etc.), as well as stakeholder interest and knowledge, to influence a variety of assessments of firm reputation. Similarly, various firm stakeholders will value as more important certain types of corporate social actions in formulating their assessment of the focal firm's reputation, so that not all corporate social actions will attract the attention of certain stakeholders. Furthermore, we view corporate social actions to not be a continuum from strengths to concerns, but rather as distinct constructs.

As stakeholders form their opinions and expectations based on previous exchange transactions (technical stakeholders) or previous relationships (institutional stakeholders), corporate social actions will build over time to enhance corporate reputation. The preceding hypothesis suggests such changes in corporate social actions, segregated by the intended recipient, can predict the evolution of corporate reputation. We have also identified the synergies that CSR may yield with corporate reputation, as stakeholders express their satisfaction with CSR with a better perception of the firm as expressed in their assessment of corporate reputation.

Remembering that the perception of reputation compares overall firm appeal (Fombrun, 1996), not all stakeholders have access to the same comparatives against which to assess relative appeal, however industry experts do share a common background of competitor knowledge. While assessing reputation from representative stakeholders corresponds to capturing *the eye of the beholder,* the perception of industry experts assesses competing firms knowledgably, but from only a single stakeholder perspective. In this trade-off for assessing reputation we have chosen the perception of industry experts who also broadly assess firm performance across multiple domains in considering relative firm reputation. The methods by which these hypotheses will now be empirically tested are described in the following chapter.

3. Methods

3.1 Overview of methods

The hypothesized relationships between corporate social actions and corporate reputation will be tested on a sample of major US corporations over a five year period from 2002 to 2006. The data sources include the proprietary database of KLD, Inc.[2] for the corporate responsibility measures, *Fortune's* America's Most Admired Companies (MAC) annual rating of reputation compiled from published information available from *Fortune* and from the OSIRIS database from Bureau van Djik Electronic Publishing available from JMSB, Concordia University for financial data used for control purposes. The control variables will include industry, profitability, asset size, risk and slack. They are drawn from past research and will later be described in greater detail.

Before elaborating on each aspect of the methods adopted a brief explanation of the measurement of the focal constructs of corporate social actions and corporate reputation follow to frame the description of methods. The predictor, corporate social actions, is measured from the historical statistical spreadsheets purchased from KLD. Since 1991, starting with only 600 firms, KLD's annual coverage increased to 1100 firms by 2001 and then to 3300 by 2003; drawn from the S&P 500 and Russell 3000 index of major US public firms. There is relatively little attrition from year to year with coverage terminating due to bankruptcy, corporate restructuring or no longer being publicly listed. KLD analysts using corporate self-reported answers and publicly

[2] The PhD. Thesis grant accorded by John Molson School of Business was the source of funding to acquire access to the KLD historical stats up to 2006. Appreciation for this financial support is extended to Concordia University.

available reports review a series of considerations which have remained largely unchanged over the years to examine aspects of the firms social responsibility strengths and weaknesses, which they term as *concerns*. These are grouped under the categories of community, diversity, employee, environment, governance, human rights and product. According to the aspects under review (see Appendix A for KLD ratings criteria), they assign a *one* (1) for meeting the criteria or otherwise a *zero* (0). These are reported on the historical spreadsheets, with the any modification or addition to the criteria clearly explained to allow researchers to ensure the comparability of data across years.

The dependent variable, corporate reputation, is measured by *Fortune's* MAC rating, published annually in a spring edition of the magazine to rate and rank within industries the corporate reputation at the end of the preceding year on a scale of 1 to 10. The raters are industry knowledgeable analysts and insiders who rate only firms within their industry sector on eight attributes (quality of management, quality of products and services, innovation, long-term investment value, financial soundness, people management, use of corporate assets and social responsibility). *Fortune* does not make available all component scores, reporting only the simple average MAC rating from 1 to 10 (see Appendix B for *Fortune* methodology). Only the top ten or so firms within each industry category are reported upon. Accordingly, from year to year not all firms will maintain their top ten ranking, and as such may have years for which no rating is publicly available.

As will be described in greater detail, both the KLD and *Fortune* MAC are established measures which have been extensively used in previous research, having their critics but nonetheless are precious sources of longitudinal data.

3.2 Sample

With a firm level of analysis, we focus on major US firms for our sample. The period under study was chosen as 2002 to 2006. The universe from which the selection was drawn is those firms included in Standard and Poor’s *S & P* 500 and those firms included in the *Fortune 1000* index. Standard and Poor's ranks the top 500 US firms based on market capitalization. However, Standard and Poor's also screens to ensure a majority public float and adequate stock price, as well as financial viability indicated by four consecutive positive quarterly earnings. To compensate for this performance bias, we also included those firms appearing on *Fortune's 1000*, a ranking of US firms by revenues. Given the objective of a representative sample of the largest US firms, once a firm appeared on either the *S & P 500* or *Fortune 1000* ranking in any of these years they were considered for the entire period.

We started with all the largest U.S. firms from the S & P 500 and Fortune 1000 for which evaluations of social actions were available from KLD (see section 3.4.1 for a detailed explanation of the KLD measures) for 2001 to 2006. While the KLD ratings also include firms in the Domini 400 Social Index and the Russell 1000 (the Russell 3000 since 2003), these represent the highest social performers and specifically exclude all firms significantly involved in tobacco, alcohol, gambling, firearms, military weapons and nuclear power (KLD, 2009).

Similar to Mattingly and Berman (2006), to avoid prejudicing the sample's generalizability we included those firms identified by KLD as *S & P 500* firms. From the remaining KLD firms we identified those included in the Fortune index and eliminated those not recognized on either the *S & P* or *Fortune* indexes.

Accordingly, the sample was drawn from the 1107 firms rated by KLD in 2001, reduced by the non-qualification of 460 firms for the previously noted reasons, leaving a sample universe of 647 firms which represent the 500 *S & P* and the additional 147 *Fortune* ranked firms.

While KLD increased its coverage of firms over time, for a variety of reasons some of the firms rated in 2001 were dropped from subsequent ratings in any of the years from 2002 to 2006. Corporate reorganizations (mergers or acquisitions), bankruptcies and privatization were some of the reasons for which the sample universe suffered from a slight attrition over time.

From the 647 firms for which KLD ratings of CSR were available throughout the period, not all were consistently included in the reputation measure from Fortune *America's Most Admired Companies* ratings. Reasons similar to those noted for KLD attrition were compounded by the limited number of firms whose annual reputation ratings were published (see section 3.4.3 for a detailed explanation of the Fortune reputation ratings). Attrition over time is a common feature affecting all longitudinal studies and was compensated for by the large number of firms in the initial sample universe (Ployhard & Vandenberg, 2010). The final sample of firms for which all data was available was 285 firms, and constitutes the number of cases with no missing data across the time frame (2002-2006 for CSR and controls; 2002-2007 for reputation).

3.3 Data sources

The KLD academic spreadsheets covering 1991-2006 (as of December 31st of each year) are the source of the strengths and concerns ratings indicated by a "1", where the absence of a rating, signified by a "0" indicates that the firm did not meet the criteria for a strength or a concern. For example, in assessing strengths related to the environment KLD has six criteria, therefore strength ratings for this category range from 0 to 6, while the product strengths are assessed on four criteria for a range in strength ratings from 0 to 4. (For details on the specific criteria used by KLD see Appendix A.)

KLD describes their research evaluations to come from five distinct data sources which include direct communications with firm officers, global media sources reviewed on a daily basis, public documents as filed with the SEC, input from ten global socially responsible investment research firms and information gathered from various branches of the U.S. government and non-governmental organizations. Their research process has analysts who specialize by sector, are mentored by senior analysts who also perform quality reviews and a KLD Ratings Review Committee to critically evaluate methodology and assessment criteria. The KLD ratings are also "among the oldest and most influential, and, by far, the most widely analyzed by academics" (Chatterji, Levine & Toffel, 2009: 125) and as such are a well-recognized data source characterized by Deckop and colleagues (2006: 334) as "the largest multidimensional CSP database available to the public".

The measure of corporate reputation, *Fortune's* America's Most Admired Companies (MAC), has a history dating to 1982 of obtaining reputation

assessments from industry executives as well as financial analysts covering those industries. Based on eight equally weighted categories (for details see Appendix B), the average of the 1 to 10 ratings and an industry ranking are published in a spring edition. Using the *Fortune* publications for the years 2002 to 2007, where the publication of the March list represents the previous year-end's ratings, we compiled the ratings assigned to the top firms representing some 60 industries in each of those years. For 2008 the ratings were revised to a common survey for the former America's Most Admired Companies and the former World's Most Admired Companies (Fortune, 2009). As this change significantly reduces the number of American companies, eliminating those relatively smaller when compared to global firms, the 2007 ratings published in March 2008 are the last comparable reputation ratings.

The OSIRIS database from Bureau van Djik Electronic Publishing is the source of all financial data to be used as controls.

3.4 Measures

3.4.1 Corporate social actions

The KLD ratings consider seven broad categories: community, governance, diversity, employee relations, environment, human rights and product. KLD also has exclusionary screens for which only concerns are noted in the areas of alcohol, gambling, firearms, military, nuclear power and tobacco. The single-sided nature of the exclusionary screens are industry focused rather than aligned with stakeholders (Strike et al., 2006), and as in prior studies using KLD (Griffin & Mahon, 1997; Hillman & Keim, 2001; Mattingly & Berman, 2006;

McGuire et al., 2003; Shropshire & Hillman, 2007; Strike et al., 2006) we do not consider these ratings.

The specific criteria for which KLD awards a strength or posts a concern are included in Appendix A. While KLD's naming convention may have changed over the years, they provide clear descriptions and explanations of the ratings criteria to enable a consistent matching. For example, in 2000 they began assigning strengths for exemplary and concerns for problematic indigenous peoples relations within the community category and then moved these to the human rights category in 2002.

Mattingly and Berman (2006) develop a taxonomy of social actions at the firm level within the KLD qualitative social ratings. Using exploratory factor analysis over five years of data, they identified four distinct categories of corporate social action: institutional strengths, institutional weaknesses, technical strengths and technical weaknesses. The institutional stakeholders are the KLD categories of community and the environment, while the technical stakeholders are KLD categories of employees, customers and shareholders. The KLD category of diversity strengths is related to the community, while KLD's diversity concerns are linked to KLD's employee relations. Mattingly and Berman (2006) note the complexity of the relationship with diversity-related employees who in addition to being resource suppliers (i.e. technical stakeholders) also have normative expectations, as do all diversity-related community stakeholders (i.e. institutional stakeholders). They also note that environmental strengths and concerns are highly correlated, offering as a possible explanation that those firms responsible for environmental harm are

also those that rely heavily on the environment in exploiting their business. Delmas and Blass (2011) also found significant correlation between KLD's environmental strengths and weaknesses, concluding that strong management practices do not translate into better environmental compliance, while Chatterji and colleagues (2009) suggest that having more environmental strengths also means that there will be more environmental concerns related to the firm.

Building on Mattingly and Berman's (2006) findings (Appendix E), as confirmed by a confirmatory factor analysis of our data sample (see Chapter 4.3 for details), we adopt their stakeholder categorization of the KLD data, as follows:

Figure 7. Stakeholder categorization

Institutional Strength *Community* *Diversity*	**Technical Strength** *Employee* *Customer (product)* *Shareholder (governance)*
Institutional Weakness *Community* *Environment (including strengths)*	**Technical Weakness** *Employee* *Diversity* *Customer (product)* *Shareholder (governance)*

While the split classification of diversity as an institutional strength but a technical weakness might appear an anomaly, further examination of the specific criteria utilized can support this interpretation with face validity. Remembering the premise that corporate social strengths and weaknesses are not a continuum,

the eight criteria assessing diversity strengths cover a broad spectrum of considerations such as provisions for women/minority contracting, disabled persons, women/ minority directors, etc., most of which are policy based initiatives which can readily be interpreted to be institutional. The three diversity concerns represent affirmative action and other controversies, as well as the non-representation of women on the board, which may be interpreted as more closely aligned with governance and employee concerns and thus classification as technical weaknesses is coherent.

As the number of criteria used by KLD in assessing strengths and concerns varies considerably by category, a built in dominance of either strengths or weaknesses is inherent in a simple summing (Strike et al., 2006) and has been identified as skewing results (Hillman & Keim, 2001). However, we have followed Chatterji and colleagues' (2009), Cho and colleagues' (2010) and Walls and colleagues' (2011) summing of the KLD environmental strengths and/or concerns as a representative measure of institutional and technical strengths and concerns. As their findings also noted a significant number of companies within their sample had KLD scores of zero, the disparity between the number of questions within the various categories is less likely to skew results. Furthermore, utilizing the same summation in each of the five years is unlikely to affect any variance in the ratings over time.

These four categories of corporate social actions are the independent variables, constituting the overall measure of CSR. The construct of corporate social actions as a formative, rather than a reflective construct, has implications on assessments of validity which will be discussed next.

3.4.2 Reflective and formative constructs

A key element to assess whether a construct is reflective or formative is the direction between the variables (Williams, Gauvin & Hartman, 2004). The more common reflective indicator represents the manifestation of a construct (Roberts & Thatcher, 2009; Williams et al, 2004) Formative measures are those that produce or form the construct to which they are associated (Williams, Edwards & Vandenberg, 2003). The importance of making the distinction between reflective and formative constructs lies in how they may be modeled, as well as the assessment of their validity. Williams and colleagues (2004) caution that strategy researchers incorrectly categorize as reflective, constructs that are better represented as formative.

Using Roberts and Thatcher's (2009: 12) framework of conceptualizing a formative indicator, the corporate social actions construct may be viewed as described in the following Figure 8.

Figure 8: Formative indicators

Concept	Formative indicators	Applied to construct of corporate social actions
Causality	Viewed as causes; construct formed by its measures	A series of actions directed to a variety of stakeholders forms the construct of corporate social actions; Corporate social actions may be defined as the institutional and technical strengths and the institutional and technical weaknesses of the focal firm
Interchangeable	Not interchangeable, unlike reflective where removal of items doesn't change construct's essential nature	The 4 factor composite represents corporate social actions so that by removing any one would remove a theoretically relevant element of the construct
Validity	Exogenously determined; correlations not explained by measurement model (taken as given)	"Reliability in an internal consistency sense is not meaningful for formative indicators" ….. "construct intercorrelation is less than .71" (Diamantopoulos, Riefler & Roth, 2008: 1215 & 1216)

As a formative construct, traditional indicators of validity such as Cronbach alpha are not relevant. Validating formative constructs relies heavily on face validity and on identifying structural relations (Williams et al., 2003). In consideration of KLD's underlying structure of assessing CSR, the comprehensiveness of the stakeholder categories, the consistency over time of the aspects of CSR that are examined, as well as the appropriateness of the issues considered, we find this measure of CSR to have face validity. As seen in Appendix A, each strength and concern is distinctly formulated without ambiguity, further reinforcing face validity. The wide acceptance of the KLD

measures by both the academic and social investment research communities attests to this face validity.

3.4.3 Reputation

Fortune's ranking of *America's Most Admired Companies* (MAC) is based on an annual survey of senior executives and board directors of Fortune 1000 companies, as well as financial analysts, where they rate the major companies in their industry on eight reputation drivers. These include the quality of management, product and service quality, innovation, use of corporate assets, personnel development and ability to attract talent, long-term investment value, financial performance and social responsibility. The published 2008 ratings were based on fourth quarter, 2007 survey responses from over 3,300 executives, directors and analysts representing over 600 companies in almost 70 industries. See Appendix B for a more detailed description of the data collection methodology.

Roberts and Dowling's (2002) longitudinal examination of the link of reputation to persistent superior financial performance found evidence "that *Fortune*'s reputation measure is a global firm attribute that allows stakeholders to fill in the blanks when full information about firm particulars is not readily available" (Roberts & Dowling, 2002: 1082), confirming earlier findings by Fombrun and Shanley (1990: 245) "that the eight attributes elicited from respondents were components of an underlying and stable construct of reputation". While the criticisms of using individual components of the MAC ratings focus on the financial halo (Brown & Perry, 1994) and its rating of

reputation "as an investment" (Fryxell & Wang, 1994: 13), our use of the aggregation is as an indicator of overall firm-level reputation. A more recent study by Flanagan, O'Shaughnessy and Palmer (2011) replicated Brown and Perry's 1991 sample along with one drawn from 2006 data to conclude the "impact of financial variables on reputation is much weaker today than it was in the past" (Flanagan et al., 2011: 13), going on to reinforce the use of MAC ratings as a valid measure of corporate reputation. To explain this deflation of the link between reputation and financial performance they suggest both constructs to be more dynamic today, as well as the greater information sources available to 21st century raters to provide data beyond the reported financial results upon which raters base their assessments (Flanagan et al, 2011).

Although one of the *Fortune* MAC considerations is *social responsibility* it is the respondents' overall estimations of this aspect within their perception of the reputation of a firm and not the structured analysis of KLD. Kraatz and Love (2006) note the importance of using reputation measures which are of importance to firms, singling out Fortune's ratings for special consideration. One example of how the Fortune placing forms part of the strategic goals may be found in General Electric's proxy statement where the CEO's compensation related to risk and reputation management is assessed as "GE remains one of the most admired companies...Fortune (#1)" (GE, 2007: 19).

3.4.4 Industry

The significance of industry in all strategy research is well recognized (Waddock & Graves, 1997), however the diversification of many large firms is

reflected in their multiple standard industry codes (SIC), leading researchers to often assign an industry category based on the primary SIC determined by revenue source. While extremely simple distinctions such as service or manufacturing (Christmann & Taylor, 2006) or broad category one-digit SIC (Strike et al., 2006) may represent attractive options to compress industry categories, the use of the two-digit SIC (Hillman & Keim, 2001; Johnson & Greening, 1999) provides adequate distinction for our purposes, without the undue fine-tuning of the four-digit SIC (McWilliams & Siegel, 2000; Russo & Fouts, 1997). While the firms' designation of the primary SIC recognizes their principal revenue/profit source, the relative proportion of earnings derived from this industry sector may fluctuate over time as firms acquire/divest operating units, however this is not captured in the stagnant SIC reported by most firms.

With reputation being a comparison against competitors (Frombrun, 1996) and the Fortune respondents specialized by industry, we propose an adequate categorization by industry is achieved using the primary SIC. Flanagan and colleagues' (2011) findings maintain that industry influences corporate reputation, and suggest the use of industry dummy variables when modeling corporate reputation.

The final sample of 285 companies had the following SIC distribution as shown in Figure 9. Initially to control for industry 44 industry dummy codes were created to represent the 45 two-digit SIC codes, however then a more simple 7 industry dummy codes representing the 8 one-digit SIC codes were considered, however to not to remove power the categorization of industry was further reduced to four broad categories, represented by 3 dummy codes. Our structural

equation models used the four broad industry categories of manufacturing, services, retail/transportation and other.

Figure 9. Industry distribution by two-digit SIC

SIC	Number	**%**		**SIC**	Number	**%**
10-19	16	6		50-59	51	18
20-29	61	21		60-69	44	15
30-39	63	22		70-79	19	7
40-49	25	9		80-87	6	2
Summary of 4 codes		%				%
20-39	Manufacturing	43		40-47, 50-59	Retail & transportation	22
60-87	Services	24		10-19, 48-49	All other	11

3.4.5 Financial controls

We include control variables to eliminate possible confounding variables that could provide alternative explanations and in response to McWilliams and Siegel's (2000) criticism of model misspecifications.

Prior research studies have shown a variety of financial factors to have an effect on CSR and we address the pertinence to control for each of these factors in our analysis. Using the table that follows we indicate prior operationalizations (including references), as well as the measure we have chosen for this research.

While our objective is to examine the largest corporations, the issue of firm size has long been seen as affecting both CSR and reputation. Similarly, profitability and prior period profitability have been seen as precursors that warrant controls. Other more random factors have included asset age, slack

resources, and leverage and R&D intensity. The fact that our sample includes both services and manufacturing within a broad cross-section of industries indicates we consider both physical resources and human capital to capture a comparable indicator of size.

To further greater comparability of period to period results by excluding taxation regulations that underwent changes over time, we focused on pre-tax income as the foundation of performance or profitability in determining the various financial returns. This had the advantage of not only enhancing comparability, but of excluding the tax corrections that were imputed when the prospective of future earnings changed underlying accounting assumptions to distort declared net income.

Figure 10. Summary of financial controls measures

Firm size:

Prior operationalizations	**References**	**Rationalization and choice for this research**
Number of employees	Christmann & Taylor, 2006	Based on Boyd et al.'s (2005) call for multiple indicators, and on the previous uses, we have selected the natural log of total assets and the natural log of total employees as best quantifying *firm size*. Given our sample includes both service and manufacturing, employees and assets constitute a true measure of "size" of the organization. Adding the two logs is equivalent to the log of assets x employees, resulting in a weighted average which is our proxy for size.
Net sales & net income	Hillman & Keim, 2001	
Average log of total assets, total firm sales & total employees	Johnson & Greening, 1999	
Log of number of employees	McGuire et al., 2003	
Natural log of total assets	Strike et al, 2006	
Total assets & total sales	Waddock & Graves, 1997	

Firm profitability (financial performance):

Prior operationalizations	References	Rationalization and choice for this research
2 year averages of return on sales, return on assets & return on equity Prior return on assets, two year average Return on sales (1 year lag) Return on sales, return on assets & return on equity	Johnson & Greening, 1999 McGuire et al., 2003 Strike et al., 2006 Waddock & Graves, 1997	Based on Boyd & al.'s (2005) call for multiple indicators, and on the previous uses, we have selected the pre-tax return on shareholder funds & pre-tax return on assets as best quantifying *firm profitability*.

Slack, R & D, risk & asset age:

Prior operationalizations	References	Rationalization and choice for this research
Slack and R & D: Ratio of current assets over current liabilities, log transformation Leverage and times interest earned ratios Industry average R&D as % of sales, log transformed	Bansal, 2005; Strike et al., 2006; McGuire et al., 2003 Strike et al., 2006	Following Lawson's (2001) argument for the role of slack in innovation, and McWilliams & Siegel's (2000) call for controlling for R & D, we use slack as a proxy for R & D, using the ratio of current assets over current liabilities.
Risk: Beta reported in Standard & Poor's Coefficient of variation of daily stock price for each firm in each year, log transformed Long-term debt to total assets ratio	Hillman & Keim, 2001 Strike et al., 2006 Waddock & Graves, 1997	Following Waddock & Graves' (1997: 309) "proxy for management's risk tolerance" we use their ratio of long-term debt to total assets, operationalized as one minus the solvency ratio (shareholder funds to total assets) to capture the indebtedness of the firm, long viewed under agency theory as a control over management.
Asset age: Ratio of net and gross plant, property & equipment	Cochran & Wood, 1984; Strike et al., 2006	We explored this control, however given the mix of services and manufacturing firms chose to exclude as non-representative.

3.4.6 Years

The time frame 2002 to 2006, for a total of five years provides ample data to achieve necessary power for a longitudinal and structural equation modeling analyses. In discussing environmental performance measurement, Delmas and Blass (2011) favour multi-year data as change is a lengthy process and any one year may not be representative.

3.5 Reliability and validity

The KLD data have been used extensively and are well acknowledged as representing the construct of corporate social actions (Sharfman, 1996; Walls et al., 2011) despite their critics (Entine, 2003), they are reliably constructed to ensure internal, external and construct validity (Chatterji, Levine & Toffel, 2009; Sharfman, 1996). The Mattingly and Berman (2006) four factor regrouping of the KLD data has not been widely utilized in its entirety. For example Bear, Rahman and Post's (2010) study focuses only on the two strength dimensions (institutional and technical), while Muller and Kräussl (2011) attempted to replicate the exploratory factor analysis but were unable to match the factor loadings of Mattingly and Berman, and so did not choose to use the four factors. We encountered similar difficulties when using the unrestricted exploratory factor analysis, however a more appropriate test is confirmatory factor analysis (Kaplan, 200; Maruyama, 1998). Having established face validity (see Chapter 3.4.2) to validate the four factor model as proposed by Mattingly and Berman (2006) we performed a confirmatory factor analysis which fitted our data, the details of which follow in the Chapter 4.3 on results.

As an overall global measure of reputation, Fortune's America's Most Admired Companies is considered to be "one of the most reliable data points to measure corporate reputation" (Lee, Fairhurst & Wesley, 2009), with empirical evidence "which support validity and reliability of the *Fortune* survey data (Flanagan, O'Shaughnessy & Palmer, 2011: 5). It has also been used extensively in prior research on reputation (e.g. Brown & Perry, 1994; Carter & Ruefli, 2006; Fombrun & Shanley, 1990; Lee et al., 2009; Love & Kraatz, 2009; Roberts & Dowling, 2002; Straw & Epstein, 2000). As noted earlier, a recent study by Flanagan and colleagues (2011) found the more recent *Fortune* ratings (e.g. 2006) to not be unduly influenced by performance and suggest that *Fortune* continues to be a very appropriate data source.

The financial controls are coherent with previous research in their use, application and source. As suggested by Flanagan and colleagues (2011), the importance of industry effects on firm reputation must be taken into account, for which they suggest including industry dummy variables. Bureau van Djik's OSIRIS is a reputable, well-respected source of comprehensive financial data (Bener, M. & Glaister, K.W, 2010; Muino, F. & Trombetta, M, 2009; Shao, L., Kwok, C.C. & Guedhami, O., 2010). OSIRIS includes some 65,000 listed and major unlisted/delisted companies with data sourced from over a hundred specialist information providers, such as D&B, EIU, S&P and Thomson Reuters among others (Bureau van Djik, 2011). A review of peer-reviewed journal articles using ProQuest found increasing references to OSIRIS as a data source, with six such articles for 2011, equal to the number for all of 2010. As recommended by Boyd and colleagues (2005),multiple indicators have been selected.

3.6 Summary of all variables to be considered

The following table summarizes the proposed variables of interest and identifies how they will be operationalized.

Figure 11. Summary of variables

Independent variables:

Corporate social action strengths	
Institutional	KLD strengths assigned for community (7) and diversity (8) for a possible 15 captions as a sum of strengths.
Technical	KLD strengths assigned for employee (7), governance (3) and product (4), for a possible 14 captions as a sum of strengths.
Corporate social action weaknesses	
Institutional	KLD concerns assigned for community (6) and net environment (7 possible concerns, reduced by a possible 6 strengths by reverse coding strengths), as a sum of concerns.
Technical	KLD concerns assigned for employee (6), governance (4), product (4) and diversity (3), for a possible 17 captions as a sum of concerns.
Industry	Primary SIC code reduced to 4 broad categories (manufacturing, services, retail/transportation and all other), represented by 3dummy codes.
Firm size	OSIRIS, total assets transformed to natural log, plus total employees transformed to natural log
Firm profitability	OSIRIS average of pre-tax return on shareholder funds and pre-tax return on total assets
Slack resources, R&D proxy	OSIRIS current ratio calculated as current assets divided by current liabilities
Risk	OSIRIS solvency ratio calculated as total shareholder funds divided by total assets, then subtracted from one, to equal the percentage of assets not financed by equity.

Dependent variable:

Reputation	Fortune's America's Most Admired Companies actual rating for each individual year from 2002 to 2007.

3.7 Data screening

The KLD, FMA and OSIRIS data were extracted and examined to ensure comparability year over year, as well as to ensure an exact match at the firm level. Corporate name changes were identified to reduce attrition. Wherever possible when financial data were missing from OSIRIS, the firm's annual reports and SEC filings were consulted to extract the data and perform the ratio calculations. To ensure consistency and correct interpretation, these calculations were also performed for other periods reported by OSIRIS as a further validation.

The changes effected by KLD in the categorization of certain questions were examined to best attribute the characteristic to a stakeholder classification and to ensure a consistent treatment across the period under study. Alternative interpretations of classifications were examined to assess the best ideological fit, such as the reintegration of the human rights categories into their previous community or employee classifications.

To ensure comparability across the years, only the KLD questions that were asked for the entire five years were included in the scoring. However, given the *all other* question within each strength or concern it was also deemed necessary to examine the KLD questions added after 2002 to ensure true comparability between years. The underlying rationale being that at the outset a

particular CSR action might be fairly rare and thus be captured in the *all other* category, however if a trend of acceptance was noted that provoked KLD to add a distinct caption the same CSR gesture might now be recognized in the new category and no longer in the *all other*. As new questions were not considered it would be necessary to reintegrate the observation into the *all other* tabulation. An example of one such detailed review of new captions added is the 2006 recognition of a firm's commitment to environmental management systems within KLD's environmental strengths. The unusually large increase in *all other* environmental strengths in 2005 was obviously a precursor of the new 2006 *commitment to environmental management systems* category which was not considered in the earlier coverage from 2002 to 2004. Within the sample there were 54 firms recognizing a 1 in *other environmental strengths* in 2005. These were compared individually to the 2006 ratings for *commitment to environmental management systems* to identify those firms receiving a 1, as well as compared to the 2004 *other environmental strengths* ratings. Where a firm did not rate a 1 in the 2006 *commitment to environmental management* category the 2005 rating of 1 in the *other environmental strength* category was considered to be a true measure of the constant measure from 2002 and was maintained. This is coherent with maintaining a stable measure over the period as formal environmental management systems were generally not in place in 2002. Of the 54 firms with an *other environmental strength* in 2005 only 4 were maintained as consistent with previous years, while the other 50 related to a new measure so were eliminated. As noted earlier, the policy nature of certain of the KLD ratings favour a constant rating and underlie the data screening undertaken.

3.8 Temporal effect

The five year time period from 2002 to 2006 is viewed as an ample window upon which to capture the effect of the change in corporate social actions on the change in corporate reputation. Based on our expectations of the evolution of corporate social actions the chosen sample is expected to provide adequate change, however we have no guarantee as to whether this data sample will capture the anticipated change (Ployhard & Vandenberg, 2010).

Given the role of stakeholder management in developing CSR initiatives it is logical to expect stakeholder expectations to change over time in response to shifts in social issues as well as their perceptions of how business has behaved. The classic stakeholder salience model of urgency, legitimacy and power attributes (Mitchell et al., 1997) would predict change over time, as at least urgency by its very definition is unlikely to be stable over the years, providing somewhat of an assurance of variability over time.

As the element of change over time in both the dependent and independent variables is of vital interest to our study, the measurement of such change is a key methods decision. The use of change scores, while common in strategy research, has its critiques who note severe limitations (Bergh & Fairbank, 2002). Chan (1998: 423) observes that "limited information on individual change over time can be obtained from a difference score analysis".

Williams and colleagues (2004: 329) identify "latent growth modeling has the potential for many applications in strategy research when repeated observations are collected across observational units", generating growth trajectories across firms over time. We will now examine some of the underlying

considerations before latent growth modeling (LGM) may be undertaken, followed by a discussion of the appropriateness of LGM.

3.8.1 Measurement equivalence or invariance

In order to attest that the same construct is being measured in each of the selected years, with the same precision, measurement invariance tests are a prerequisite to LGM (Bentein, Vandenberg, Vandenberghe & Stinglhamber, 2005; Chan, 1998; Chan & Schmitt, 2000; Ployhard & Vandenberg, 2010). To ensure corporate social actions from 2002 to 2006 are consistently measured, following Chan (1998) our four factor model was replicated for each of the five years. "Invariance is said to exist if (a) each time point has the same single factor with the same specific items loading on each factor, (i.e. configural invariance) and (b) the factor loadings correspond to the identical items are equal across time points (i.e. factorial invariance)" (Chan & Schmitt, 2000: 195). As reputation is a single item measure, no measure invariance test is required. "Evidence of measurement invariance establishes the meaningfulness of the analysis" (Chan, 1998: 433) for modeling the growth trajectories. The results of the measure invariance tests are reported in the next chapter.

3.8.2 Latent growth modeling (LGM)

Bentein and colleagues (2005) provide a comprehensive analysis for operationalizing change to conclude the superiority of LGM. They note LGM's capacity to capture individual change for each subject across time, along with the subject's initial relationship between constructs and the trajectory of change.

Williams and colleagues (2003) observe the scarcity of empirical applications of LGM, and note that although at the time only completed at the individual level that "LGM is equally applicable to other units of observation and analysis" (Williams et al, 2003: 926). The LGM framework followed in the subsequent chapter's results is that advocated by Chan's (1998) often cited discussion and example of LGM.

3.9 Summary of methods

The relationship between corporate social actions and corporate reputation will be empirically tested for 285 major US firms using five years (2002-2006) of data from KLD (corporate social actions) and six years (2002-2007) of data from *Fortune* (corporate reputation), with industry dummies and financial controls from OSIRIS. The reliability and validity of these data sources have been established and the Mattingly and Berman (2006) four factors of KLD supported by a confirmatory factor analysis. The industry and financial controls conform with those used in previous studies, while the KLD and *Fortune* measures have been utilized extensively by other organizational researchers.

To measure the effect of changes in corporate social actions on changes in corporate reputation latent growth modeling (LGM) is the best suited technique, as difference scores are an inadequate alternative (Chan, 1998). The measure invariance of the KLD data is established as a precursor to LGM to ensure the comparability of the measure/interpretation of corporate social actions across time. The next chapter will address the data analysis strategy in greater detail as well as report the results of the empirical testing of the hypotheses.

4. Results

4.1 Overview of analysis of results

The five year data set of 285 firms' complete information will first be reported as descriptive statistics, including relevant correlations, to provide an insight into the variables which will be utilized for hypothesis testing. Extensive use of structural equation modeling (SEM) using EQS6.1 is employed to perform the data analysis, along with multivariate regression analysis using IBM's SPSS, version 19.

A confirmatory factor analysis (CFA) of the four-factor model (institutional strengths, weaknesses; technical strengths, weaknesses) proposed by Mattingly and Berman (2006) will then be presented. The acceptable fit indices obtained provide support for the use of the four-factor model with this research dataset.

To capture the effects of change over time in the focal constructs, a SEM technique, latent growth modeling (LGM), will constitute the primary analysis vehicle. The data analysis techniques follow those detailed by Chan (1998), as well as utilized by Bentein and colleagues (2005). LGM requires the confirmation that the same constructs are being measured with the same precision across the time period. This was performed for corporate social actions, but given the single reputation rating was not relevant for reputation (Chan, 1998).

Thus an examination of measurement invariance is reported which confirms this prerequisite condition necessary to undertaking LGM. The good fit

of all of the models confirms that the four factors are constant across the five years with the same elements loading on each of the factors across each year.

Having established this precursor condition, the LGM which captures a growth trajectory for each firm over the period is analysed. The acceptable model fit supports the linear change found in corporate social actions and corporate reputation. Then a second-order factor LGM was developed introducing the industry and financial control variables. Once again, the acceptable model fit supports that the change in corporate social actions predicts a change in corporate reputation.

To test the relative importance of technical strengths and institutional concerns, regression analysis including the control variables was performed. The regression model confirmed the significance of technical strengths, but not that of institutional concerns on the relationship between corporate social actions and corporate reputation. A summary of findings against the hypotheses tested concludes the analysis.

Finally, to translate the statistical models into more tangible examples, a selection of sampled firms were illustrated and related to the hypothesized relationships. The implications of these results will be discussed in Chapter 5.

4.2 Descriptive statistics

The descriptive statistics that follow present the 285 firms year by year, while further descriptive details may be found in Appendix C. A year by year review shows relatively little variability. As expected, profitability generally has

the largest standard deviation due to corporate losses which may extend to the negative range, along with the greatest volatility.

Table 4.2.1 Descriptive statistics by year

Year / **Statistics**	**2002** Mean	SD	**2003** Mean	SD	**2004** Mean	SD	**2005** Mean	SD	**2006** Mean	SD
Institutional Strength	1.70	1.97	2.02	2.13	2.12	2.20	2.32	2.15	2.45	2.26
Technical Strength	0.86	1.10	0.82	1.10	0.85	1.16	1.03	1.30	1.05	1.32
Institutional Concern	6.48	1.33	6.47	1.23	6.58	1.26	6.58	1.43	6.52	1.51
Technical Concern	2.17	1.75	2.60	1.90	2.78	1.80	2.89	1.85	3.18	2.03
Size	26.77	2.16	26.85	2.15	26.97	2.13	27.07	2.14	27.16	2.16
Profitability	13.58	36.93	13.24	19.30	14.81	21.48	16.86	20.33	15.44	22.72
Slack	1.57	1.09	1.61	1.08	1.61	1.06	1.577	0.98	1.55	0.92
Risk	66.06	19.92	65.01	19.81	63.78	19.41	63.52	20.01	63.85	19.33
Reputation*	6.17	1.06	6.47	1.03	6.50	0.93	6.41	0.97	6.36	0.94

*In 2007 reputation mean = 6.39; SD = .96

While technical strengths and concerns as well as institutional strengths all have a minimum of zero (see Appendix C for ranges), the reverse coding of environmental strengths added to environmental and community concerns results in a minimum of two. This reverse coding achieves the netting of strengths against concerns and is similar to Kempf and Osthoff's (2007: 911) transforming of KLD "concerns into strengths by taking the binary complements". While reverse coding has its particularities when developing survey questions on a range of scales, the operationalization of this reverse

coding is similar to converting yes/no questions and less likely to build in misinterpretations (Spector et al., 1997), however reverse coded items are sometimes thought to be more difficult to interpret (Pallant, 2007). For more information on the frequencies of each strength/concern, see Appendix C.

A review of the distribution of the primary industry SIC codes for the 285 firms covers a range from industry code 10 to 87 as shown earlier in Figure 9. To visualize how these 45 distinct industry codes relate to each other, a broad regrouping into four categories shows that the sample represents manufacturing (SIC 20-39) for 43%, services (SIC 60-87) for 24%, retail and transportation (SIC40-47 & 50-50) for 22%, with all other constituting the remaining 11%. Using these broad industry grouping to generalize on how they compare, there are no major distinctions (see Appendix C for details).

A correlation analysis was performed for each year as well as the panel, with the key results summarized in tables found in Appendix D. Given the relatively large data set, although there are some statistically significant relationships, the correlations are generally small, however most are in the expected direction.

The year-by year relationship of the institutional and technical strengths and concerns to firm reputation found significant correlations only for the strengths, as detailed in Appendix D. The panel found significant relationships for all but the technical concerns. There was no consistent pattern of which time frame had the strongest relationships. The institutional and technical strengths produced significant relationships to reputation over all time periods however,

there were no significant relationships for technical concerns over any of the time periods, while institutional concerns had modest correlations.

These preceding statistics are for descriptive purposes only. The hypothesis testing will follow the preliminary data reliability/validity tests reported in the next section.

4.3 Confirmatory factor analysis (CFA)

As indicated in the earlier Figure 7, the four-factor structure of institutional strengths/weaknesses and technical strengths/weaknesses proposed by Mattingly and Berman (2006) is the manner in which we will operationalize corporate social actions. To ensure the validity and reliability of these factors with our data we undertook a CFA. All of the SEM modeling used maximum likelihood (ML) estimators which Nyle and Drasgow (2011: 550) note "in large samples, ML estimates are (nearly) unbiased with the smallest possible standard errors".

There are a number of tests of overall SEM model fit, known as fit indices, however "there is no agreement about a single optimal test or even set of optimal tests" (Maruyama, 1998: 238), leading Hu and Bentler (1998) to suggest that researchers report multiple indicators. Starting with the chi-square (χ^2) statistic and its degrees of freedom (df) as an absolute index (Maruyama, 1998) provides an indication of acceptable fit as long as it is less than 3*df. There are then a number of comparative fit indexes generally scaled to fall between 0 and 1, with "one representing perfect fit relative to baseline; usual rule of thumb is that .95 is

indicative of good fit" (Kaplan, 2000: 107), while an acceptable fit is better than .9 (Bentler, 1988). Bentler (2004: 118) suggests selecting one or two fit indices as "these indices are very highly correlated and hence redundant", while Williams and O'Boyle (2011: 354) "focus on two of the most popular global fit indices, the comparative fit index (CFI) and the root mean square error of approximation (RMSEA)".

The CFI was developed by Bentler to adjust McDonald and Marsh's relative noncentrality index (RNI) to lie in the range of 0 to 1 (Kaplan, 2000). As the popular CFI is reputed to have good performance (Bentler, 2004), it will be one of the indices reported when examining model fit.

Another perspective on model fit takes into consideration the residual errors in approximating a model solution. Two such indicators are the standardized root mean-square residual (SRMR) and the RMSEA, where the objective is to have as small as possible a value of error (Kaplan, 2000; Williams & O"Boyle, 2011). While generally this is less than .05, values "between .05 and .08 indicate reasonable fit, .08 to .10 indicating mediocre fit" (Williams & Boyle, 2011: 355). Bentler (2004: 118) claims "if the SRMR value is very small, the model fits the data well regardless of what other measures of fit may imply", while Kaplan (2000: 113) points to the advantage of RMSEA's 90% confidence interval (C.I.) "enabling an assessment of the precision of the estimate".

Building on these model fit criteria, the CFA four-factor model yielded an excellent statistical fit: χ^2 (df) = 38.2 (37), CFI = .995 and RMSEA = .01, C.I. .00 - .04. As seen in Table 4.3.1 an alternative one factor and two factor models

demonstrated a less optimal statistical fit to further reinforce our conclusion of the viability of the four-factor model.

Table 4.3.1 CFA nested models for CSR dimensionality in 2002

	Chi-sq (χ^2) (df)	**CFI**	**SRMR**	**RMSEA 90% C.I.**	**Δ Chi-sq (Δdf)**
4 Factor (baseline) Model	38.2 (37)	.995	.048	.011 .0-.044	
2 Factor Model (strengths vs concerns)	48.8 (43)	.977	.057	.022 .0 - .047	10.6 (6)^{T}
2 Factor Model (institutional vs technical)	57.5 (42)	.940	.061	.036 .0 - .057	19.3 (5)**
1 Factor Model	59.6 (44)	.939	.060	.035 .0-.057	21.4 (7)**

**p<.01; ^{T}p<.10

Further discussion of the model structure consistency over time (in 2002-2006) follows in the next section on measurement invariance.

4.4 Dimensionality of corporate social actions

An essential precursor to longitudinal analysis is to ensure the constructs being measured across time are consistent in their factor structure (configural invariance) as well as the interpretation of what is being measured (Bentein et al., 2005; Chan, 1998; Chan & Schmitt, 2000; Lance, Vandenberg & Self, 2000). This was accomplished using CFA and a nested models technique at time 1 (i.e. 2002), given the "first one being most critical, since it tests whether the same

conceptual frame of reference was used to interpret items across occasion" (Lance et al., 2005: 110).

As demonstrated by the preceding CFA, Mattingly and Berman's (2006) four factor (institutional/technical - strengths/weaknesses) is confirmed for our data, the details year by year which follow in Table 4.4.1.

Table 4.4.1 CFA model fit by year

	2002	**2003**	**2004**	**2005**	**2006**
Chi-sq (χ^2) (df = 1)	7.920	1.283	0.687	0.117	0.156
CFI	.930	.996	1.000	1.000	1.000
SRMR	.052	.025	.019	.008	.010
RMSEA 90% C.I.	.156 .069-.265	.032 .0-.166	.000 .0-.147	.000 .0-.113	.000 .0-.119
Std. Factor Loading					
Institutional Strength	.726	.440	.425	.929	.903
Technical Strength	.452	.630	.687	.380	.371
Institutional Concern	.263	.265	.229	.028	.101
Technical Concern	.578	.903	.866	.443	.465
Std. Solution - R-sq.					
Institutional Strength	.61	.162	.143	1.0	.994
Technical Strength	.24	.804	1.0	.116	.106
Institutional Concern	.01	.058	.042	.072	.151
Technical Concern	.23	1.0	1.0	.157	.167

(Least squares – elliptical distribution used for all models)

Furthermore configural and metric invariance were established by estimating separate baseline models for corporate social actions in 2002 to 2006. As indicated by the Lagrange multiplier test for adding parameters, minor modifications such as correlations of some error terms were implemented to the

models across each of the five years. All of these baseline CFAs demonstrated a good fit to the data, as shown in the following table 4.4.2.

To test for invariance of factor loadings requires that an equality constraint be imposed on all factor loadings across the five time periods (Bentein et al., 2005; Chan,1998; Lance et al., 2000). Results from this test yielded an appropriate fit as indicated in the following table 4.4.2.

Table 4.4.2 Invariance models fit

	Configural Invariance	**Measurement Invariance**
Chi-sq (χ^2) (df)	10.16 (5)	41.46 (17)
CFI	.985	.929
Std. RMR	.028	.058
RMSEA 90% C.I.	.061 .0-.115	.072 .044-.10

However, as may be seen in a comparison of the two models above, there is a statistically significant difference in the chi-squares (Δ31.3 (12), $p<.05$) and the CFI difference exceeds .05, suggesting the presence of non-invariance loadings (Cheung & Rensvold, 2002). To address this indication, a Lagrange Multiplier test which assesses the validity of the model restrictions was implemented and identified two non-equivalent factor loadings. These are technical strengths at 2002 not equivalent to 2003 and technical concerns at 2002 not equivalent to 2004. However, as Lance and colleagues (2000: 111) note this "is less serious because partial measurement inequivalence may be modeled in the LGM parameterization. As such, sources of inequivalence are controlled for in the LGM". Hence partial measure equivalence was established.

Accordingly, we may conclude that the measures of corporate social actions across time are configurally and metrically invariant and that the four-factor structure of corporate social actions is optimal. The non-equivalent factor loadings were controlled in the further analysis. Further details on the models are included in Appendix F. We have now met the prerequisite conditions to proceed with LGM, as described in the following section.

4.5 Latent growth modeling (LGM) of growth trajectories

A second-order factor LGM technique was utilized to test the change over time hypotheses of corporate social actions, as well as the relationship with corporate reputation. Following Bentein and colleagues (2005), a first phase of the analysis was to specify a linear trajectory of change over time of corporate social actions. With only a five-year horizon, within a relatively stable external context we have no reason to believe CSR change to be anything other than linear.

This model included the repeated measure for each of the four corporate social action dimensions as indicators of a latent intercept variable (initial status, as measured at 2002) and a latent slope variable (change over the period). The two latent variables were permitted to covary. The intercepts for each indicator were fixed at 1.0 and the change factor loadings were fixed to 0, 1, 2, 3, and 4 for 2002 to 2006, respectively. The factor loadings were fixed this way in order to represent the time intervals in between measurements of the variable creating a linear model that accounted for the annual measures. The linear change model represented a good fit to the data: χ^2 (df) = 336.7 (146), CFI = .989, RMSEA

=.049, C.I. .036-.060. As a comparison or alternative to the hypothesized linear change, quadratic and cubic LGMs were tested, but demonstrated significantly worst fit. Hence, the model representing a positive linear change in corporate social actions is retained for the analysis, and Hypothesis 1 predicting a positive change in corporate social actions is confirmed.

As corporate reputation is a single item measure, we are unable to perform a second-order factor LGM, so that a base LGM was used to assess the trajectory of change for corporate reputation. A good fit was achieved with a beginning, middle and end of period measure of reputation, specifying a linear growth and fixing the change factor loadings to 0, 1, and 2, respectively. Given the sample size of only 285 firms, using a more parsimonious model of three data points was preferable. The linear change model represented a good fit (χ^2=28.3 (1), CFI = .994, SRMR = .014) and demonstrated statistical significance in both intercept and change parameters, thus indicating a positive linear change in corporate reputation.

4.6 Multivariate LGM analysis

To test the dynamic relationship between corporate social actions and corporate reputation, a multivariate second-order factor LGM was utilized. This allowed us to introduce the industry and financial control variables discussed earlier in our theory development. In an effort to create a parsimonious model of the sample of 285 firms, we examined the control variables to establish the appropriateness of introducing only the initial (2002) variables based on their comparability with the subsequent years. As preliminary analysis had failed to

find any significance in the relationship with slack, this control variable was excluded from further LGM analysis. The initial state of size, industry, profit and risk were treated as time invariant variables based on the following reasoning. We had tested the profit and risk variables for linear growth; however the fact that they did not demonstrate any change/growth allowed us to consider them to be stable. Company size demonstrated a positive linear growth, however when considering only the employee component (log employees[3]) there was no change/growth, so that only the initial state of firm size was considered in further analysis. Industry is time invariant by definition as firms' primary SIC codes are constant. The control variables measured in 2002 were introduced into both the intercept and parameters change equations predicting the dynamic relationship between corporate social actions and corporate reputation. All of these year 2002 control factors were found to be a significant predictor of the initial state of corporate reputation, however only initial profit was found to influence a change in reputation. Hence only profit was maintained in the final model of reputation change, however the other factors were retained as a predictor of the initial state (intercept) of corporate reputation.

The final model exhibited a good fit (χ^2=819.3 (272), CFI = .965, RMSEA = .067, (C.I. .06-.07). Furthermore, the change in corporate social actions was found to significantly and positively relate to the change in corporate reputation. This demonstrates that a positive change in corporate social actions can predict a positive change in corporate reputation, while controlling for profit, confirming Hypothesis 2.

[3] In running these LGM analysis using log employees only for size, the results were very similar.

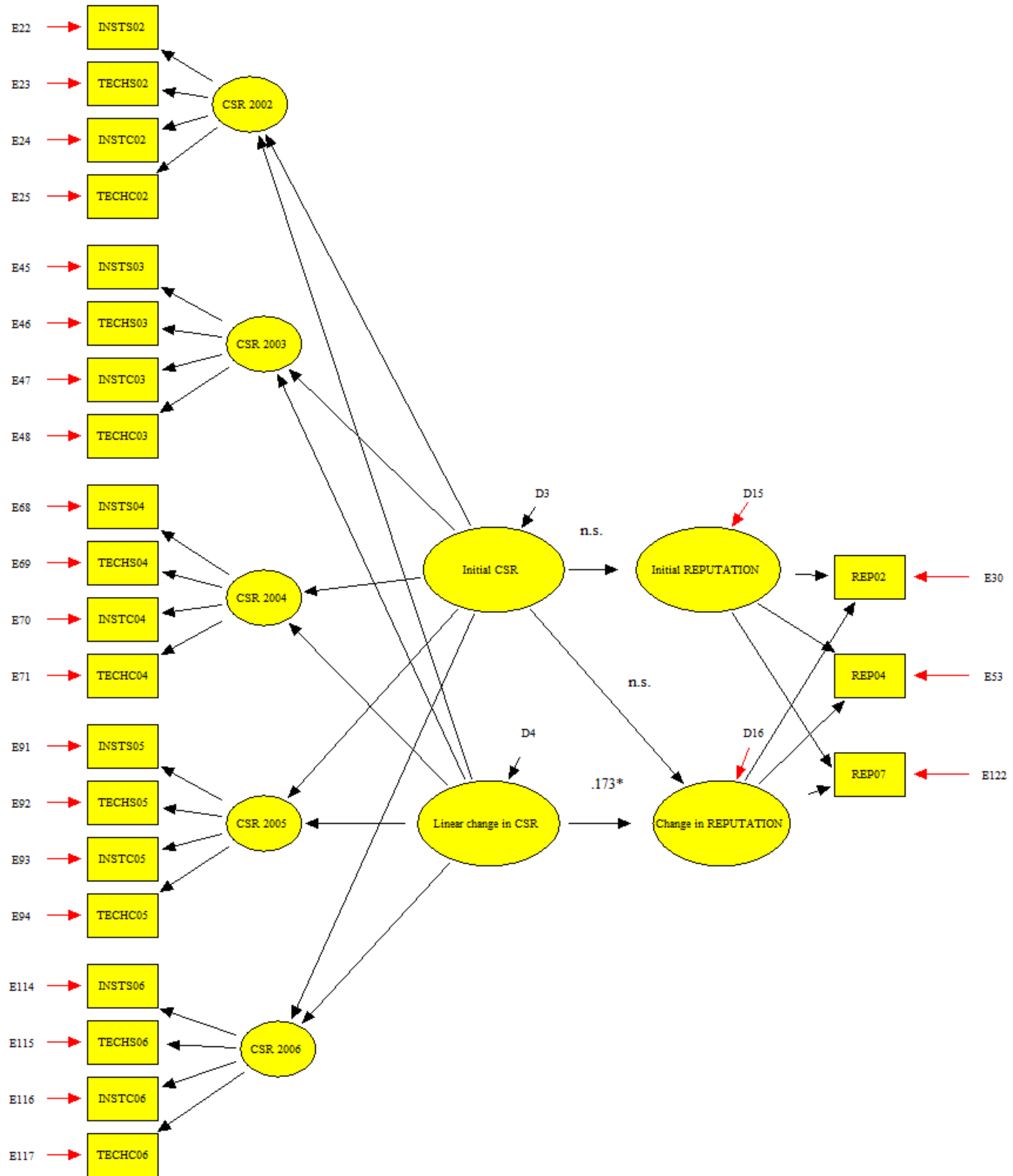
Accordingly, the predictive equations (standardized solution) for corporate reputation are as follows:

Reputation at t (intercept represents initial state) = .081*industry +.159*$size_t$ + .264*$profit_t$ - .290*$risk_t$ - .09 corporate social $actions_t$ + .894error

Reputation change 2006-2002 (slope represents change) = .236*industry + .096* $size_t$ -.234 $profit_t$ - .065*$risk_t$ + .179*change in corporate social actions + .919error

The SEM model is depicted in the following figure.

Figure 12. Representation of Latent Growth Second Order Factor Model: Corporate social actions predicting linear change in corporate reputation



*p<.05

X^2 = 819.2 (272), CFI=.965, RMSEA=.067 (C.I. .06-.07)

4.7 Multiple regression analysis

To ensure there was no problem of multicollinearity with the data set, the SPSS calculations of tolerance and the variance inflation factor (VIF) were reviewed and found to be well within the cut-off points of multicollinearity which exists when tolerance<.10 or VIF>10 (Pallant, 2007: 156). Normality was established through a review of the Normal P-P Plot as well as the scatterplot of the standardized residuals which both corresponded to the distribution expected for a normal distribution. Furthermore, a review of the scatterplot identified only 7 outliers out of the total of 1425 (defined as those cases with a standardized residual of +/- 3.3, c.f. Pallant, 2007: 156). Also verifying the Mahalanobis distances and Cook's distance reaffirmed the absence of any significant outliers requiring further action (Pallant, 2007). The absence of autocorrelation was established using the Durbin-Watson test which at 1.971 is very close to the value of 2 which indicates non-autocorrelation (Bartels & Goodhew, 1981).

Regression analysis to test Hypotheses 3 and 4 was performed. The industry and financial controls were introduced at the first step of the analysis, followed by the institutional and technical strengths and institutional concerns at the second step, and finally the last step considered technical strengths as a predictor of reputation at time one, midpoint and the final measure in 2007. The significance of technical strengths confirms Hypothesis 3. The Hypothesis 4 considering institutional concerns was tested in a similar manner. The lack of significance of institutional concerns was contrary to Hypothesis 4. The regression results follow.

Table 4.7.1 Results of regression analysis of predictive power of technical strengths and institutional concerns in relation to corporate reputation

2002	Reputation 2002		
	Model 1	Model 2	Model 3
Constant:	4.26**(.82)	4.78** (1.02)	5.02** (1.02)
Industry	Yes	Yes	Yes
Size	.12** (0.3)	.09* (.04)	.08 * (.04)
Profit	.01** (.002)	.01** (.002)	.01** (.002)
Risk	-.02** (.003)	-.02** (.003)	-.02** (.003)
Slack	.03 (.06)	.04 (.06)	.04 (.06)
Institutional Strength		.09* (.04)	.07^T (.04)
Technical Concerns		-.04^T (.04)	- .05(.04)
Institutional Concerns		.01 (.05)	- .01 (.05)
Technical Strength			.13*(.06)
F	6.6**	5.3**	5.3**
R^2	.14	.16/.18	.17/.18
ΔR^2		.02/.03*	.01*/.00

2002	Reputation 2004		
	Model 1	Model 2	Model 3
Constant:	4.02**(.75)	4.24** (.94)	4.50** (.94)
Industry	Yes	Yes	Yes
Size	.11** (0.3)	.1** (.04)	.09 * (.04)
Profit	.004** (.001)	.003* (.001)	.004* (.001)
Risk	-.01** (.003)	-.01** (.003)	-.01** (.003)
Slack	.03 (.06)	.03 (.05)	.04 (.06)
Institutional Strength		.06* (.03)	.04(.03)
Technical Concerns		-.04^T(.04)	- .05(.04)
Institutional Concerns		.03 (.05)	- .01 (.05)
Technical Strength			.14*(.06)
F	4.9**	3.9**	4.2**
R^2	.11	.12/.14	.14/.14
ΔR^2		.01/0.3*	.02*/.00

2002	Reputation 2007		
	Model 1	Model 2	Model 3
Constant:	3.64**(.78)	3.85** (.97)	4.09** (.98)
Industry	Yes	Yes	Yes
Size	.13** (0.3)	.11* (.04)	.09 * (.04)
Profit	.002 (.002)	.002 (.002)	.002 (.002)
Risk	-.01** (.003)	-.01** (.003)	-.01** (.003)
Slack	-.003 (.05)	.001 (.05)	.003 (.05)
Institutional Strength		.06^T (.03)	.04^T (.04)
Technical Concerns		-.04^T(.04)	- .04(.04)
Institutional Concerns		.06 (.05)	.04 (.05)
Technical Strength			.13*(.06)
F	4.7**	3.8**	3.9**
R^2	.11	.12/.13	.14/.13
ΔR^2		.01/0.3*	.02*/.00

Values shown are the unstandardized regression coefficients with standard errors in parentheses. Values provided after a slash mark represent R^2 and ΔR^2 of the model where Institutional Concerns are introduced as a final step, after controls and the three dimensions of CSR.
$^T p < .10$, $^* p < .05$, $^{**} p < .01$

The significance of technical strengths in the above results confirm Hypothesis 3, while the lack of significance of institutional concerns in the above results is contrary to Hypothesis 4. We also reproduced the analysis using the log of employees as the proxy for firm size and obtained very similar results.

While technical concerns marginally affect 2002 and 2004 reputation, they have no significance in predicting final reputation.

4.8 Summary of LGM and regression analyses

The preceding LGM analyses have examined the dynamic relationship between corporate social actions and corporate reputation, while the regression analysis has explored the moderating effect of stakeholder orientation of corporate social actions on the relationship with reputation. Relating these conclusions to the hypotheses developed in Chapter 2, the following table summarizes the results achieved.

Table 4.8 Summary of results of hypotheses testing

Hypothesis	LGM **Δ** Regression	Pg. ref. to test	√ or **X**
1. During the time period of this study, a positive change will occur in corporate social actions.	**LGM Δ**	124	√
2. During the time period of this study, the greater the rate of increasing change in corporate social actions, the greater the rate of increasing change in reputation. In other words, improvements in corporate social actions are positively related to an improvement in corporate reputation.	**LGM Δ**	125	√
3. Strengths in corporate social actions directed to technical stakeholders will more strongly influence corporate reputation than those directed to institutional stakeholders.	**Regression**	129	√
4. Concerns over corporate social actions directed to institutional stakeholders will more strongly influence corporate reputation than those directed to technical stakeholders.	**Regression**	129	**X**

4.9 Illustrations drawn from the sample

4.9.1 Introduction to illustrations

To bring the statistical analyses back to an individual firm level, we will examine five firms in our sample drawn from a variety of industries. Consistently good reputation as well as consistently improving reputation firms are included, as well as the opposite with consistently deteriorating reputation firms. Similarly, these firms illustrate different patterns of corporate social actions directed to institutional and technical stakeholders. The purpose of this section is to bring to light some of the anomalies in assessing corporate social actions across time. This also allows a more specific discussion of some of the individual

elements considered behind the corporate social actions directed to institutional and technical stakeholders.

These are not related to any hypotheses testing, but will provide some insights into the inherent limitations of measuring corporate social actions across time. The count of the number of strengths/concerns each year are segregated into those directed to institutional and to technical stakeholders. For the purposes of these illustrations institutional concerns are represented as conceived to be the sum of community concerns and net environmental concerns (i.e. environmental concerns less environmental strengths), rather than the reverse coding utilized in the results analyses. This presentation aligns with the conceptual identification of institutional concerns, rather than the technical operationalization of environmental concerns net of strengths.

The reputation horizon has been extended to include more recent years of *Fortune's* World's Most Admired Companies, which has been the rating scheme since 2008. These later ratings are provided for information purposes only, recognizing the limited comparability. As subsequent KLD ratings have not been purchased it is not possible to provide a similar extension on more recent corporate social actions.

As was noted in testing the dynamic corporate social responsibility – corporate reputation relationship, while controls influenced the initial state (i.e. 2002) with size showing some growth, the only control variable that contributed to the change in reputation was profit. Accordingly, these factors were examined for each of the examples however size (log value of assets and log value of number of employees) demonstrated very little variability, ranging from a decrease of

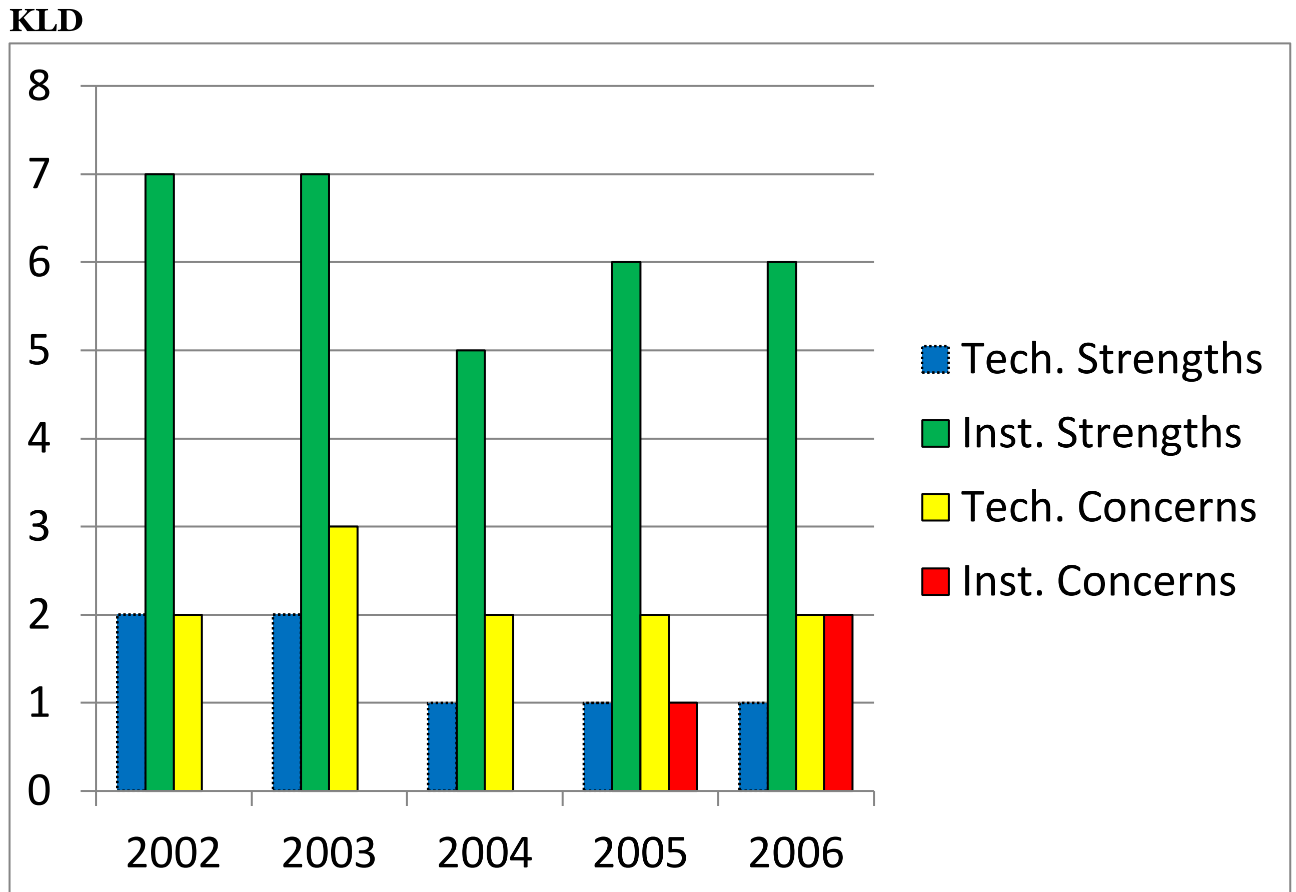
2.6% (International Paper) to an increase of 5.2% (Procter & Gamble) over the five year period. Profit (average pre-tax return on shareholder funds and on average assets) on the other hand reported more fluctuation, however with the illustration firms generally demonstrating an inconsistent pattern, with the exception of Wendy's International which steadily fell from 10.14% in 2002 to 3.13% in 2006.

We will now illustrate Procter & Gamble, Southwest Airlines, International Paper, Wendy's International and Tribune for insights on the dynamic relationship of corporate social actions and corporate reputation. In addition to the KLD ratings, we draw on corporate web disclosure as well as annual financial, sustainability and social responsibility reports from these firms.

4.9.2 Procter & Gamble

A consistently Fortune MAC star firm was Procter & Gamble (P&G), having ranked first in its industry since 1997 up to the most current 2010 rankings. However, for the period under study P&G's 2007 reputation rating was a six year low of 8.20, yet still top of its industry as it is through to 2010, despite the lower rating. The increase in CSR concerns and the decrease in CSR strengths can be seen in the following chart:

Figure 13 . Procter & Gamble corporate social actions and reputation



Fortune MAC ratings:

2002	2003	2004	2005	2006	2007
8.31	8.83	8.33	8.45	8.48	8.20

(Fortune World MAC ratings: 2008- 7.69; 2009- 7.94; 2010- 7.43)

One of the technical strengths present in all years includes a notably strong program of retirement benefits. As might be expected, once this is in place it would be maintained. In 2002 and 2003 the other technical strength was strong employee involvement.

Five institutional strengths are present in all years. They are all in the Diversity category and recognize four or more minorities, women or the disabled on the Board; outstanding programs oriented to family/work concerns; more than 5% subcontracting with women or minorities; employment of the disabled; and notably progressive gay/lesbian policies. In 2005 and 2006 P&G was further awarded an additional Diversity strength for notable progress in promoting women and minorities, particularly to line positions with profit and loss responsibility. This focus on diversity is not surprising as P&G senior management have diversity results tied to their stock option awards (P&G, 2006: p.59). The two additional institutional strengths in 2002 and 2003 were in the community area related to support for education and the making of charitable contributions abroad.

One technical concern found across all years is related to high executive compensation defined by KLD as CEO salary over $10 million or director remuneration over $100,000. While this might be a relevant definition for national firms applying it to all global firms lacks nuance, particularly without any relationship to profitability or other performance measures. Given the complexity of P&G, the long-serving CEO (A.G. Lafley) and their financial situation, these KLD concerns might well be expected across all periods. In 2002 and 2003, a significant reduction in the workforce gave rise to a concern, while from 2003 on, a concern was raised related to a substantially underfunded pension plan. The irony is that having strong retirement benefits counted as a technical strength!

Institutional concerns only came to light in 2005 related to regulatory or environmental controversies as well as toxic waste emissions. While technical strengths were diminishing, institutional concerns were rising, generating an overall deterioration in CSR, which when compared to the reputation ratings showed a similar pattern. Consistent with the proposed model, the strong technical strengths may have helped establish the sterling reputation, however the rise of institutional concerns may have influenced the deterioration in reputation. The parallel overall trends of CSR and reputation support an interpretation that P&G's corporate social actions are substantive, rather than symbolic.

Throughout the period, P&G had no other concerns noted, however EU regulators have fined P&G €211.2 million in April 2011 for participating in a laundry detergent price fixing cartel operating between 2002 and 2005 (Business News Network, 2011). This highlights the difficulty in accurately assessing CSR compliance as the due process of investigations, particularly related to complex issues, can be very lengthy.

P&G has long been recognized as a leading socially responsible company and has published an extensive sustainability report for over a decade. One striking feature is however how the composition of the business lines has changed over the years with significant acquisitions and divestitures. P&G identified 12 *Billion$ brands* in 2002, which by 2006 had grown to 22 such brands. Even in the 2002 to 2006 period there were several acquisitions such as Clairol, Wella and Gillette, while subsequent divestitures include Folgers, the European family care business and the global pharmaceutical business, as well as

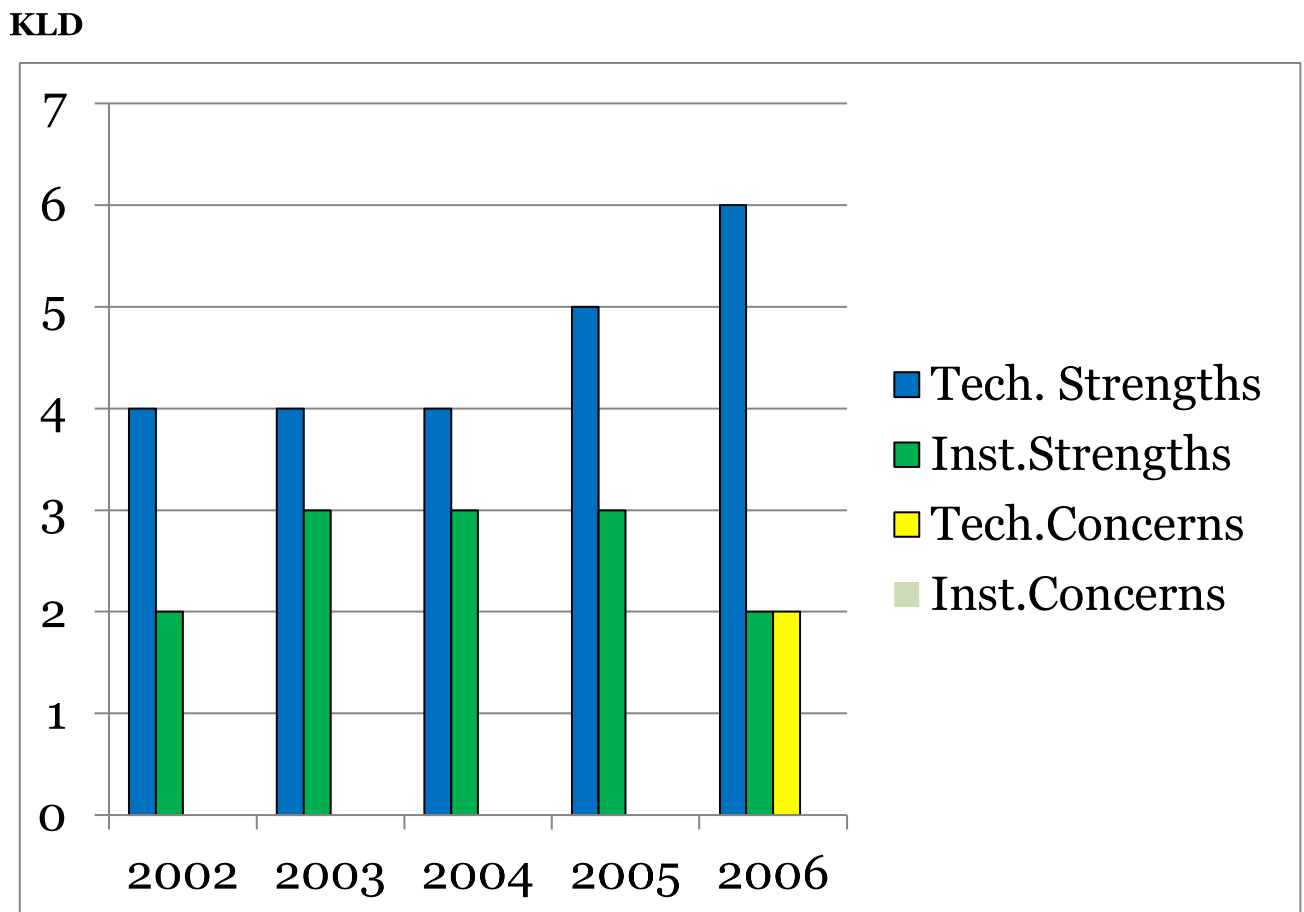
the recently announced Pringles line. Shifting away from food and beverage to the higher yielding beauty product lines not only account for increased margins, but may also be seen as an explanation for the previously noted institutional concerns related to environmental issues. All the while the primary SIC code for P&G remains 28 (Manufacturing, grouped within *chemicals and allied products*). These comments are raised to highlight subtleties in comparing performance (financial, social and reputational) over a number of years, as even the same corporate entity does not represent the same sphere of operations. Furthermore, the broad nature of the KLD ratings questions may not adequately nuance CSR performance for firms with highly diversified product lines. For example, within the product category P&G had no strengths or concerns awarded from 2002 to 2006. However a review of the P&G sustainability reports over these years highlight product innovation as attested to by the organic growth in brands, as well as their water purification tablets (PUR) offering notable social benefits, both KLD product strength categories for which no 1's were assessed. This is not meant to second-guess the KLD raters, but to underscore the diversity of interpretation possible, as well as substantiate our interpretation that corporate social actions of P&G are substantive.

4.9.3 Southwest Airlines (LUV)

With reputation ratings suggesting a rising star, Southwest Airlines, the LUV airline (the Southwest ticker symbol affectionately used as an identifier) saw a significant improvement in its 2007 Fortune MAC score to 8.02, ranking it in first place in its industry category. This was unfortunately short lived as it fell to

third place the following year with a then declining trend in subsequent reputation ratings (remembering that these are not exactly comparable to the period under study due to changes in Fortune's methodology to report World rather than America's MACs).

Figure 14. Southwest Airlines corporate social actions and reputation



Fortune MAC ratings:

2002	2003	2004	2005	2006	2007
6.98	7.01	7.35	7.19	7.08	8.02

(Fortune World MAC ratings: 2008- 6.89; 2009- 6.26; 2010- 6.17)

There is a striking absence of any concerns from 2002 to 2005, with only two technical concerns raised in 2006 related to an *other category* in Diversity and to employee workforce reductions.

The four technical strengths present over the entire period were Product Quality and three employee strengths (strong union relations, strong retirement benefits and other noteworthy commitments to employees' well-being). To these were added *strong encouragement of worker involvement* (2005 and 2006) and in 2006 the corporate governance strength of limited executive compensation (defined by KLD as CEO salary less than $500,000 and directors less than $30,000).

This illustration is consistent with the proposed model in that improved technical strengths may be interpreted to have contributed to the improvement in reputation assessments, albeit with certain lags. Also, overall strengths in social actions showed consistent improvement from six in 2002 to eight in 2006 that corresponds with the improvement in reputation rating from 6.98 in 2002 to 8.02 in 2007. Once again, this pattern directs our interpretation of Southwest Airline's corporate social actions as substantive.

A review of the LUV sustainability reports found a focus on many environmental initiatives which did not earn any recognition in the KLD ratings. Perhaps the consistency of operations and single line of business of Southwest Airlines may have facilitated the link between corporate social actions and corporate reputation. Southwest Airlines is often used as an exemplar and as a successful outlier in its industry it has somewhat of a celebrity status which might also have influenced the reputation assessments. Another unusually consistent

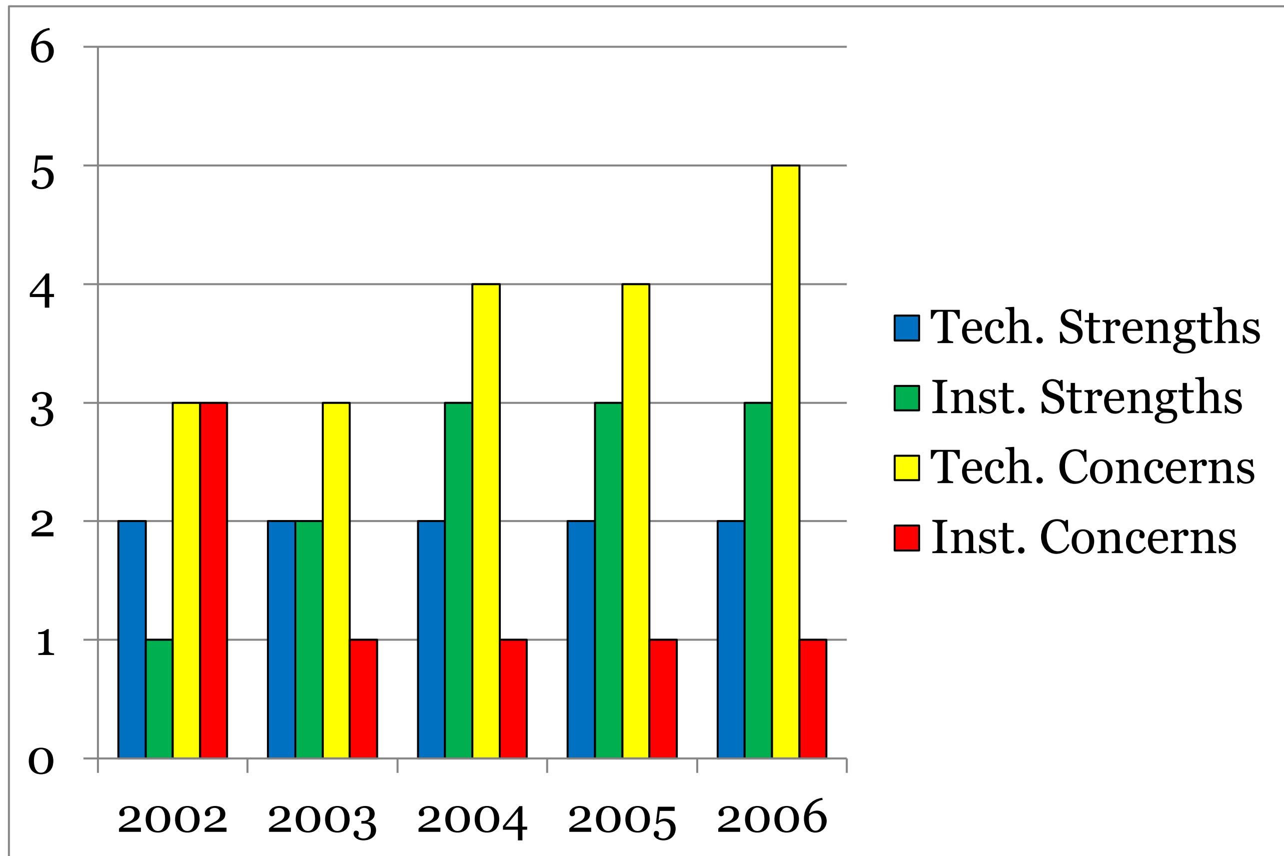
performance feature, particularly within the airline industry, has been the LUV quarterly profitability which may be interpreted to reflect not only on management but on consumer acceptance/support of their airline services and value for money. Capturing the volatile industry dynamics, where successive and repeated bankruptcies are the norm, is undoubtedly a challenge for any longitudinal evaluation of one of the few surviving USA based airlines. The impact on LUV reputation related to the morose industry outlook may also be a factor on the subsequent decline in reputation. An inherent conflict of interest exists between the consumers' expectation of quality service at low prices and the airlines' financial performance to avoid bankruptcy restructuring, further complicating overall assessments of both CSR and reputation.

4.9.4 International Paper

Looking to the only firm that consistently improved its reputation rating from 2002 to 2007 and continued to so under the 2008 World's Most Admired rating is International Paper.

Figure 15 . International Paper corporate social actions and reputation

KLD



Fortune MAC ratings:

2002	2003	2004	2005	2006	2007
6.92	6.95	7.31	7.45	7.60	8.07

(Fortune World MAC ratings: 2008- 8.56; 2009- 6.12; 2010- 6.58)

Although International Paper has all manner of strengths and concerns, the overall trend is for improving institutional strengths, but also more technical concerns spread across employee, diversity, product and governance categories.

The technical strengths relate to employee health and safety and governance communications, and are constant over the five years. The institutional strengths include five years of community support of education, four years of diversity policies favouring gays and lesbians, along with notable promotion of women and minorities from 2004 to 2006.

The institutional concerns in 2002 included two community concerns over negative economic impact and another unidentified (one of the rarely used "other" categories), while the net environmental concerns were maintained at one throughout the five years.

Technical concerns were more far-ranging, as well as less consistent, with only high compensation being maintained over the five years, while antitrust violations and underfunded pension liabilities were of concern from 2003 to 2006. Health and safety concerns were first noted in 2002 and then recurred in 2005 and 2006, while there was only one occurrence of a marketing incident in 2002, an affirmative action controversy in 2004 and an "other" corporate governance concern in 2006.

While the model proposes technical strengths (a constant 2 over the period) as a driver of reputation improvement, the greatest increase is in technical concerns (from 3 to 5), however the increasing institutional strengths (from 1 to 3) and decreasing institutional concerns (from 3 to 1) may cause an interaction effect to propel reputation improvements until 2008. Although International Paper's reputation consistently rose over the period its CSR gestures did not trend as cleanly. While institutional strengths and technical concerns were on the rise, aligned with the proposed model decreased

institutional concerns may support the improving reputation. A further aspect not explored by the model is the role of industry associations or networks founded on CSR issues, such as the highly respected Forestry Stewardship Council (FSC) of which International Paper is a member and whose products hold certifications (FSC, 2011). Although FSC is generally accepted as the gold standard of sustainable forest management, Driscoll (2006: 343) cautions that for some firms "certification can be more symbolic than a reflection of substantive change". Interpreting the consistently improved reputation against the mixed CSR performance, a symbolic or substantive distinction is not readily apparent.

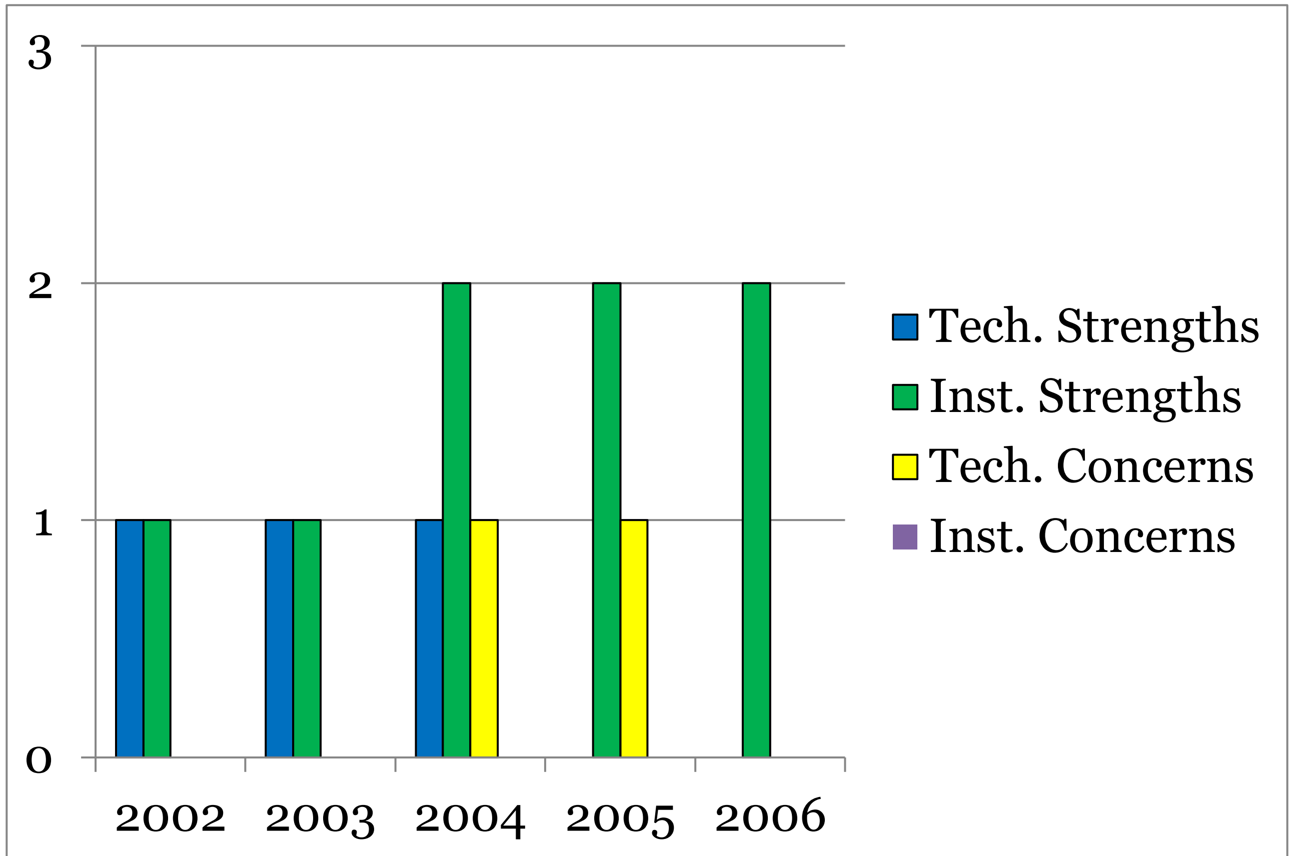
In perusing the International Paper press releases they prominently noted their first place Fortune ranking in Forest and Paper products for the fifth straight year and made particular reference to their good CSR performance (International Paper, 2007). Considerable corporate attention is given to sustainability and the environmental issues facing the forestry industry, however the KLD environmental rating considerations do not address any industry specific issues. Once again, in terms of the corporate composition, International Paper notes a considerable number of divestitures and acquisitions of various properties, business lines and subsidiaries, for an ever evolving corporate structure.

4.9.5 Wendy's International

Now turning to a firm in reputational collapse as its rating consistently deteriorated from 2002 to not even be rated by 2008, is Wendy's International.

Figure 16. Wendy's International corporate social actions and reputation

KLD



Fortune MAC ratings:

2002	2003	2004	2005	2006	2007
7.22	7.05	6.63	5.58	5.45	4.74

(Fortune World MAC ratings: 2008- below 4.88 cutoff; 2009-4.83; 2010- 4.08)

Surprisingly, there is a striking absence of institutional concerns, while there was only one technical concern in 2004 and 2005 in the diversity area related to affirmative action controversies. However, turning to Wendy's profitability, this showed a consistent decline from 10.1% to 3.1% over the five

years, while change in size (combination of assets and employees) was less consistent but was lower in 2006 than 2002.

The only technical strength from 2002 to 2004 was employee involvement, while the institutional strength came in the diversity area related to notable progress in the promotion of women and minorities from 2002 to 2005, as well as strong representation from these communities on the Board of Directors from 2004 to 2006, while in 2006 a female CEO provided the second strength. However, similar to Walls and colleagues' (2011) speculation that KLD measures may be artificially inflated when an issue is captured in multiple areas (in their study it was KLD concerns in environmental and other categories), the promotion of a female to CEO is highly likely to translate into an additional female on the Board, as the CEO position is generally appointed to the Board. This may account for the inability of these institutional strengths to promote corporate reputation, however the deterioration in profitability may also be somewhat reflected in the declining reputation, possibly a reverse financial halo effect. While the model predicts institutional concerns to drive a deterioration in reputation, the constant decline despite no institutional concerns and stable CSR strengths may be interpreted as symbolic CSR. Going beyond the KLD ratings the following considerations may reinforce this interpretation.

In reviewing Wendy's press releases they have concentrated significant attention on the nutrition debate and have given customers healthy choices, eliminated transfats and encouraged healthy eating. However, as these are newer issues of specific interest to the food services industry, they do not fall into any particular KLD categories. Ironically, Wendy's started publishing a CSR report in

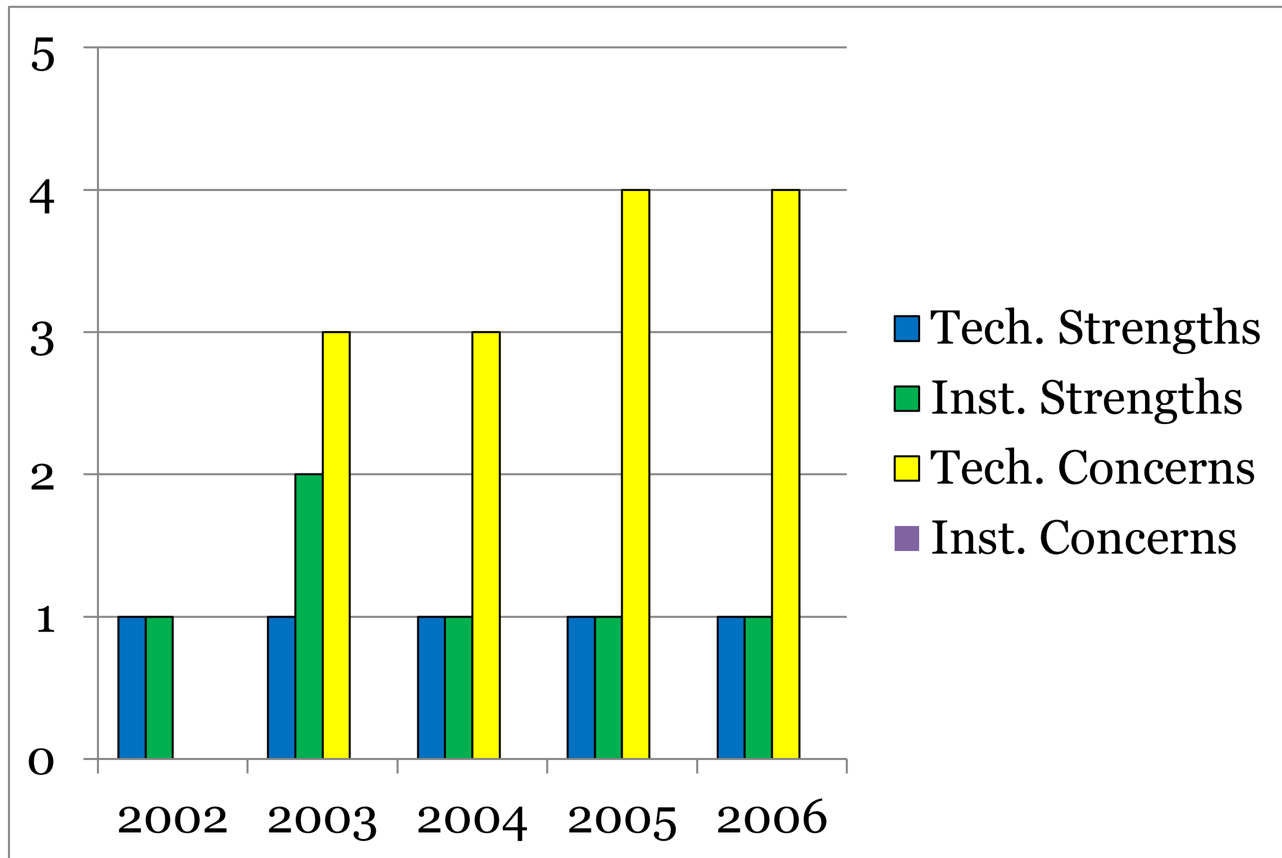
2005, however they were also fending off a public relations disaster which their president noted "our brand reputation has been affected nationally" related to a foreign object (alleged to be a human finger) found in a bowl of chilli on March 22, 2005 in San Diego (Wendy's/Arby's, 2005). Given the reputational collapse Wendy's experienced it might be inferred that stakeholders interpreted Wendy's CSR actions to be symbolic given the contradictory reports of tainted products.

Also, in examining Wendy's corporate reports other factors come to light that may impact interpretations of the factors influencing their reputation. During the 2002 to 2006 period Wendy's also included newly acquired Baja Fresh and Tim Horton's (spun off by fourth quarter 2006), while a subsequent take over in September 2008 by Triarc gave rise to the Wendy's/Arby's Group, all the while still under the same ticker symbol, WEN. Most recently, they have indicated that selling off Arby's is being aggressively pursued in 2011 to refocus on Wendy's. This remixing of brands within the corporate banner may also be a factor in the constant deterioration of the reputation rating as well as of profitability.

4.9.6 Tribune

Another firm in reputational decline since 2003 to the point of Chapter 11 restructuring in 2008 is the Tribune Company. Once again, there are no institutional concerns.

Figure 17. Tribute corporate social actions and reputation



Fortune MAC ratings:

2002	2003	2004	2005	2006	2007
7.11	7.52	7.17	6.56	5.82	5.28

(Fortune World MAC ratings: 2008- 2.85; no subsequent ratings)

While a technical strength for a quality program was maintained over the five years, the institutional strength in 2002 and 2003 was for support of education while from 2003 to 2005 progressive gay and lesbian policies were in place.

The technical concerns commenced in 2003 with governance concerns over excessive compensation and employee concerns over union relations and workforce reductions, which were repeated in 2004. However while the workforce reductions no longer rated a concern, for 2005 and 2006 additional concerns over tax disputes and marketing controversies were noted to increase the technical concerns from none in 2002 to four in 2006. Consistent with the proposed model, increasing CSR concerns correspond to decreasing reputation as CSR strengths are negligible.

While a pre-existing tax dispute that came with an earlier acquisition was decided against the Tribune in 2005, upon appeal the Tribune was vindicated and received a significant tax refund at the end of 2007 (Tribune, 2007). It would also appear that the marketing controversy over the inflation of paid circulation which likely gave rise to the 2005 and 2006 concern were also settled with "no fines or other sanctions levied against the company" (Tribune, 2006), as the Tribune's remedial actions more than satisfied the SEC. These reversals of situations flagged by KLD as concerns cannot be integrated into the prior year ratings as KLD does not restate. While significant reversals are probably rare, the double occurrence at the Tribune raises questions of measurement integrity. Given the time lapse before resolution of these concerns, they still most likely contributed to the decline of the Tribune's reputation.

4.9.7 Summary of insights from illustrations

The intent of the illustrations was to personalize the statistical model and highlight some of the possible sources of noise or measurement error across the

various components of the proposed model. Starting with the industry classification and financial controls, the shifting composition of subsidiaries, business lines and brands over five years in some of these major corporations complicates true comparisons. As new facts come to light, none of the historic data is restated, while subsequent accounting periods may record charges related to prior periods so that trends are obscured or volatility amplified. Even firms with a history of stable profitability, such as Tribune, subsequently fell into bankruptcy protection not predicted by the earlier financial controls. Furthermore, issues of the timing of settlements of disputes, fines and the like can significantly distort annual comparisons.

The highly subjective assessment of corporate social actions is framed with consistent considerations over time; however this consistency may constrain recognition of evolving issues relevant to particular industries. Applying the same series of corporate social actions across highly disparate industries may ignore significant social issues of importance only to a small segment (i.e. obesity and nutritional value of fast foods). Also, similar to the timing issues affecting the financial controls, attributing strengths or concerns over social actions is also subject to delays in being detected as well as reversals on appeals for which no restatement of past assessments is performed. Also, the KLD presence (a rating of 1) or absence (a rating of 0) measurement model lacks nuance in how well a firm meets a condition or how much it may have changed from one year to another.

With an overall reputation rating which reflects a comprehensive perception of each firm compared to their competitors, our understanding of the

changes over time of corporate reputation has been placed in the perspective of the changes in corporate social actions. The *Fortune* single rating does provide an insight into year over year change in reputation, although some of these modest changes did not affect the firm's ranking against its peers (i.e. Procter & Gamble's consistent first place industry ranking despite ratings fluctuations).

These insights are not meant as a criticism of the reputable data sources utilized in this research, but as a reminder that the accuracy of any single data point may be subject to interpretation based on events subsequent to the date of record. The large number of firm years of data does however compensate for the types of anomalies discussed in the illustrations. While there may be some under reporting or over reporting of corporate social actions, the overall portrait provides a valuable lens into the dynamic relationship to corporate reputation. We will now proceed to a discussion of the results of this research and a recognition of the limitations faced in capturing dynamic change of perceptual cospecialized intangible assets.

4.10 Summary of key results findings

The dynamic relationship of corporate social actions and corporate reputation were tested using LGM to find support for that the trajectory of change in corporate social actions is positively related to the trajectory of change of corporate reputation. Furthermore, the corporate social actions directed to technical stakeholders were found to have a significant positive effect on corporate reputation, while the relationship of concerns related to corporate

social actions directed to institutional stakeholders and corporate reputation were not statistically significant.

To rule out the alternative model that it is the change in corporate reputation that predicts the change in corporate social actions we revised the LGM predictor variables to test this alternative relationship, however the model did not converge so that there were no reliable estimates, leading us to conclude that the inverse is not supported. Thus no reverse causality is suspected.

Our research makes an important contribution in substantiating firstly that corporate social actions demonstrate linear change over time. The proposed feedback loop of corporate social actions inciting further actions to maintain or improve reputation is thus substantiated. Secondly we supported our hypothesis that the change in corporate social actions is positively related to the change in corporate reputation; in other words improvements in corporate social action improve reputation.

Furthermore, in examining the components of corporate social actions we confirmed the four-factor model of Mattingly and Berman (2006). Controlling for industry and financial performance, corporate social actions directed to technical stakeholders were found to positively influence corporate reputation more than those actions directed to institutional stakeholders. While our theory building predicted concerns over social actions directed to institutional stakeholders would have a negative impact on corporate reputation, we did not find support for this expectation. We will go into greater discussion of these results in the following chapter.

5. DISCUSSION OF RESULTS AND LIMITATIONS

This research focuses on the evolution of overall firm corporate social actions over time, as operationalized for a period of five years from 2002 to 2006. Given the role of stakeholder management in developing CSR initiatives it is logical to expect stakeholder expectations to change over time in response to shifts in social issues as well as their perceptions of how business has behaved.

Returning to the hypothesized changes over time in corporate social actions and corporate reputation, finding support for the improvement in CSR over the five-year time period of our study laid the foundation for interpreting the relationship between these constructs. This supported our initial premise that rising expectations would prompt an increase in corporate social actions. Our hypothesis that improvements in corporate social actions will be positively related to an improvement in corporate reputation was supported by the LGM with statistically significant fit indices. While LGM has become a common analytic technique in psychology and organizational behaviour, it is more novel in strategy research. Using the change of firm corporate social actions to predict a change in corporate reputation makes a contribution to our understanding of the dynamic relationship and supports the feedback loop that we propose managers be aware of in assessing corporate social actions.

We then predicted that strengths in corporate social actions directed to technical stakeholders will more strongly influence corporate reputation than those directed to institutional stakeholders. Finding support for this hypothesis built on stakeholder and resource dependence theories contributing to the resource-based view of intangible assets makes a theoretical contribution in

providing an integrated lens. From a managerial perspective, understanding the importance of the perception of technical stakeholders on improving firm reputation may guide the choice of corporate social actions.

While we did not find support for our prediction that concerns over corporate social actions directed to institutional stakeholders will more strongly influence corporate reputation than those directed to technical stakeholders, we are not alone in being unable to find evidence of the role of institutional concerns. In summary we found support for the following hypothesis:

H1 – During the time period of this study, a positive change will occur in corporate social actions.

H2 - During the time period of this study, the greater the rate of increasing change in corporate social actions, the greater the rate of increasing change in reputation. In other words, improvements in corporate social actions will be positively related to an improvement in corporate reputation.

H3 - Strengths in corporate social actions directed to technical stakeholders will more strongly influence corporate reputation than those directed to institutional stakeholders.

Before considering some of the limitations, a return to the theory development underlying these hypotheses confirms that CSR increases over time as firms recognize stakeholders expect more than the status quo (Barnett, 2007). While the motives prompting firms to engage in CSR have been identified as

sending signals to stakeholders, conforming to social expectations, managing risk by building insurance value, or alternatively over-investing in CSR, these could all be interpreted to incite firms to expand their corporate social actions over time. Although motives were not captured in our empirical model, our theoretical model advocated an increase in CSR to maintain or advance firm reputation. By establishing the growth in corporate social actions, we are then able to relate this positive change to an improvement in reputation over time.

Going back to the earliest conceptions of CSR, scholars such as Drucker (1954) advocated businesses' need to respond to society's expectations to maintain legitimacy as well as to engage in social actions which demonstrated that corporations were committed to addressing societal concerns to which they devoted firm efforts (Drucker, 1984). As stakeholders' attentions shift over time (Godfrey, 2005), so do firms' attentions as predicted by Mitchell and colleagues' (1997) conditions for salience to management (power, legitimacy and urgency) of which clearly urgency exhibits a temporal component. By providing empirical support for the increase in CSR over the five years of this study, we effectively show that firms go beyond the status quo as their CSR performance is enhanced over time.

Although at the outset CSR was not found to be related to corporate reputation this is not surprising, given the complexity with which corporate reputation is formed. The legacy effect of past actions (Fombrun, 1996) is one of the components influencing reputation as some of the mechanisms that explain reputation include character traits, technical efficiency, conformity to norms or

status by association (Kraatz & Love, 2006; Love & Kraatz, 2009). The attribution of any or all such characteristics based on prior actions may have influenced corporate reputations at the time this study was undertaken, so that initial CSR was but one contributor to initial corporate reputation. As stakeholder expectations of future corporate social actions are built on perceptions of past behaviour (Fombrun, 1996) subsequent corporate social actions would have to improve to at least maintain reputation. This is consistent with the empirical support found for the improved reputation that corresponded with the positive change in CSR over the time frame of the research. We examined an alternative model for reverse causality but found no support. Accordingly, we may therefor rule out that it is having a consistently good reputation that provokes a firm to engage in increasing corporate social actions. This reinforces that it is the improvement in CSR that contributes to improved corporate reputation.

Now turning to the segmentation between institutional and technical stakeholders and the underlying theoretical drivers of institutional and resource dependence theories, respectively, our data is consistent with Mattingly and Berman's (2006) classification. Recognizing the power that technical stakeholders have in providing resources critical to firm survival as well as the inherent legitimacy of technical stakeholders, our hypothesis that corporate social actions directed to technical stakeholders will dominate the relationship to reputation is consistent with Mitchell and colleagues' (1997) predictions that stakeholders salient to management receive management's attention. As

technical stakeholders have both legitimacy and power (as indicated in resource dependency that the firm holds with such stakeholders), when there is any urgency they will attract management interest. This is consistent with our findings that corporate social actions directed to technical stakeholders improve corporate reputation.

While any violation of legitimacy or non-conformity with societal expectations was expected to detract from corporate reputation to the extent that social concerns directed to institutional stakeholders were expected to be a deterrent to reputation, our empirical results did not provide substantiation. One interpretation may be that information asymmetry is sufficient to camouflage concerns or that firms deliberately dismiss institutional stakeholder expectations as they assess the costs to conform to be excessive or the risk to be minimal (Oliver, 1991). The ambiguity of institutional stakeholder preferences (Pfeffer, 1981) may have also been demonstrated as concerns did not create the anticipated decrease in reputation. Returning to Fombrun's (1996) definition of corporate reputation as a comparative against rivals, the lack of backlash over corporate social concerns may reflect a stakeholder malaise over post Enron bad deeds. With so many major US firms having a tainted history of bad behaviour, perhaps stakeholders discounted their expectations of future actions to be less sensitive to the concerns. In other words, the concerns identified by institutional stakeholders may not have been a surprise so that they imposed no reputational penalty for expected poor behaviour.

Substantiating change in corporate social actions is particularly encouraging given the KLD measures, as examining the underlying KLD foundation for the CSR ratings finds a number of the questions biased against change. This is consistent with findings of other researchers (Cho et al., 2010). It was only through the use of LGM techniques that the change over time in corporate social actions was captured.

While as pointed out earlier, considerable research has utilized the KLD ratings for a single year as a measure of social responsibility or irresponsibility, somewhat less use has been made in longitudinal studies. Furthermore, while suitable to many researchers' needs on specific aspects of CSR such as the environment (Cho et al., 2010; Delmas & Blass, 2011; Post, Rahman & Rubow, 2011; Walls, Phan & Berrone, 2011), the KLD assessments have been less utilized in their entirety as an overall CSR measure. The appropriateness of global ratings has been questioned as not reflecting the issues of importance related to ethics and compliance, for example (SustainAbility, 2011). Furthermore, the industry particularities are not captured in a *one size fits all* ratings approach, which while having the advantage of being able to generalize findings does not support a deeper comparison of industry-specific issues as they evolve (SustainAbility, 2011).

While earlier studies netted concerns against strengths, Mattingly and Berman's (2006) assertion that strengths and concerns are not a continuum have yet to be embraced. Rather than a summing and netting, Kempf and Osthoff (2007) created an overall CSR score by reverse coding concerns. Chiu and Sharfman's (2009) research compiled only the KLD strengths for each area to

focus on two CSP aspects which they entitled social and strategic. Godfrey and colleagues' (2009) summarization of institutional or technical CSR participation strengths found that only institutional strengths were significantly related to abnormal cumulative annual returns, while technical CSR was not significant, concluding that the insurance-like effect of CSR is captured only by institutional CSR participation. Our study found only technical strengths, but not institutional concerns, to be significantly related to reputation, which when paired with the just noted Godfrey results may suggest that transactional stakeholders discount the insurance effect of CSR as they form their expectations and monitor outcomes on more accessible information than institutional stakeholders. It may also be that the *Fortune* reputation assessments are more heavily weighted in favour of considerations identified with technical stakeholders.

Our research sought to remedy some of the criticisms of earlier CSR research by following the Mattingly and Berman (2006) suggestion to avoid netting concerns against strengths, as well as to develop a longitudinal perspective. We were able to confirm the suitability of their four-factor model via CFA, allowing us to then base our analyses accordingly. Their *institutional concerns* factor is the only one which loaded environmental strengths and concerns together, along with community concerns. This was operationalized in reverse scoring environmental strengths, however as noted earlier, reverse coding can be problematic in truly capturing the respondents' intensions (Pallant, 2007; Spector et al., 1997). In retrospect this may partially account for our lack of support for the expected impact of institutional concerns on corporate

reputation. This also echoes Walls and colleagues' (2011) findings focused only on environmental issues, which found KLD's environmental strengths to lack reliability, while KLD's environmental concerns found no statistically significant association to environmental performance. They suggest "the KLD *concerns* measure may be artificially inflated because a firm with one environmental problem could be captured in several of the KLD concerns categories" (Walls et al., 2011: 96), an artifact further distorted by reverse coding. Orlitzky and colleagues (2011: 16) conclude the Walls and colleagues' study "convincingly demonstrate the superiority of their proposed new measure to the extant proxy measures of KLD", pointing to "critical limitations of widely used data sets in the study of CSR". Similarly, Post and colleagues' (2011) lack of significant relationship between board composition and KLD's environmental concerns prompted them to posit that the difference in time required to address environmental concerns was perhaps more significant than to act on strengths. Our findings not supporting institutional concerns' (of which the environment is a primary component) relationship to corporate reputation would concur with the Post speculation that addressing institutional concerns takes longer than the five year period under study. Furthermore, Doh and colleagues (2009) were also not able to find any statistically significant relationship summing KLD's *concerns* into a CSiR measure. The ability of the KLD *concerns* to accurately capture environmental and CSR missteps is well challenged by these studies, reinforcing our absence of any significant relationship of KLD institutional concerns on corporate reputation. Orlitzky and colleagues (2011: 14) raise the issue of the "inconsistencies between CSR ratings and actual outcomes (which) raise

fundamental questions about the credibility and accuracy", further putting into question the overall predictive capability of the KLD ratings. As was noted in the illustrations, when additional information comes to light subsequent to the period being rated no modification or restatement is brought to the KLD ratings.

Although we did find a linear growth curve for corporate social actions, to better understand the less variable elements of institutional concerns and technical strengths, a further review of the underlying questions reveals the inherent policy nature of some of the responses. While in theory any corporate policy that is implemented may be reversed, a practical application calendar would preclude a full cycle within five years. That said, the KLD attribution of a 1 for having a policy in place is likely to be constant thereafter, and as such will not provide for variability as there is no nuance to the question or expectation of further improvement. Suggestions such as developing better metrics to assess CSR investments (Godfrey et al., 2009) may provide greater insight and differentiation by considering actual CSR spending. Although standardized information may be difficult to obtain as such disclosure is entirely voluntary, evolution over time might better be captured.

Similarly, some of the rating items touch upon the very nature of the business, such as for example the community concern "the company is a financial institution whose lending or investment practices have led to controversies, particularly ones related to the Community Reinvestment Act" (KLD, 2009). This particular concern, classified in institutional concerns, was noted between 9 and 12 times from 2002 to 2006 (touching a total of only 19 companies over the

period), with 7 companies rating a 1 in at least 4 of the 5 years, thus further compounding the limited applicability with limited variability.

A further consideration for the institutional concerns category is that this is the only incidence of reverse coding environmental strengths to sum to environmental concerns, which for most firms results in a larger score than the other categories of technical strengths/concerns or institutional strengths. While the larger number of rating parameters might on the surface offer greater potential for variability, once again the nature of the company's business is a key determinant. For example, environmental strengths are noted when the firm provides environmental services or is a recycling firm, while environmental concerns are registered if it manufactures ozone depleting or agricultural chemicals or sells coal, oil or fuel.

While true variability is most likely to be found in those concerns which represent acts of commission, that because of fines or other retribution are unlikely to be repeated year after year, the institutional concerns include few such categories, with only two environmental questions related to fines for hazardous waste or for violating air, water or other environmental regulations. Furthermore, the incidence of actions or events that would constitute a concern might be considered as *outliers* in that they are seldom recorded in the entire population of major US firms, for example representing less than 5% of the KLD universe in the two environmental categories just noted. As was highlighted in the P&G illustration, the time lag before which fines are imposed may be so significant as to be beyond the scope of a five-year analysis.

The sample of 285 firms had a significant proportion of firms with relatively few ratings of either strengths or concerns. As noted, some of the KLD questions were unlikely to be widely applicable, such as the product strength of serving the economically disadvantaged for which only 3 firms in the sample (11 in the 2006 universe or less than 0.4%) ever had a strength over the 5 years. Within each major category, there was always an "other" question to recognize a strength or concern not covered by the other ratings. While rarely utilized in most categories except the product concern dimension, comparability is difficult to interpret, however given the judicious assignment of such ratings ignoring or eliminating them from the compilation would taint the overall assessment of a focal firm's CSR.

Returning to the hypotheses testing, corporate social actions were found to have a positive linear growth trend over the period under study. We then established that the improvements in corporate social actions were positively related to the improvements in corporate reputation over time. Having also examined an alternative model reversing the causality (i.e. corporate reputation predicting corporate social actions) for which no convergence was achieved, further supports our findings that changes in corporate social actions are positively related to changes in corporate reputation. The LGM model demonstrates the significance of the relationship in the change of corporate social actions and corporate reputation. Utilizing regression analysis to look at the moderating effect of technical stakeholders also found support for the positive relationship of corporate social actions directed to technical stakeholders on corporate reputation. Following the LGM model a regression analysis for 2002

corporate social actions was undertaken for reputation at 2002, 2004 and 2007, all confirming the strongly positive relationship, albeit with a modest r-squared.

Using these same analysis techniques, we did not find support for institutional concerns in the regression analyses. We might speculate that less information asymmetry may explain the greater significance of transactional stakeholders to recognize technical strengths to then influence corporate reputation. While institutional stakeholders' expectations were anticipated to have greater influence when concerns were raised given the universality of impact on the community (Brammer & Pavelin, 2006), perhaps the lack of support for this assertion reflects these stakeholders' limited access to information. Once again, the time required for due process investigations and subsequent penalties may exceed the five-year time frame of this study. Furthermore, the reverse coding of environmental strengths to aggregate with environmental and community concerns to constitute institutional concerns may also have proved problematic.

While we did achieve good CFA model fit to confirm Mattingly and Berman's (2006) aggregations of institutional and technical strengths and concerns, an alternative factor analysis was not tested. Earlier we did attempt exploratory factor analyses for each of the years but were unable to obtain any consistent factor structure other than that confirmed by the CFA. The limited quantitative research utilizing Mattingly and Berman's composite KLD factors may also suggest certain difficulties. While Chiu and Sharfman (2009) both criticize and vindicate the KLD measures, they "chose to use the dataset because

of its comprehensiveness and objectivity over other CSP measures" (p. 12), however focused only on the strengths for 2002.

While the consistency of the KLD universe over the period attenuated a common longitudinal challenge of participant attrition, the Fortune MAC measure of reputation's concentration on only the best performing firms within each industry did limit the sample to those consistently "good" performers. Also, newcomers not appearing until after the 2002 Fortune MAC were excluded from the sample, thus biasing against younger firms. Furthermore, in selecting only major US firms across a variety of industries to favour the generalizability of findings, the industry control reflected only the primary industry code. As the nature of the sample firms is often more diversified, including a change of composition over time, the measures utilized may not have sufficiently addressed the industry(s) or the components over the periods. An example is the sale/purchase of lines of business seen in the insurance/ reinsurance sector or the restaurant brands discussed in the Wendy's illustration, as well as the consolidation/divestment of business lines in consumer goods as detailed in the P&G illustration. While the MAC respondents' expertise may have considered these issues in their ratings, the control variables could not integrate these complexities. The shift over time in the comparability within each of the sample firms' financial, social and reputational performance may have also influenced the statistical results. However as Chiu and Sharfman (2009) note that with increasing time lags between variables there is a greater risk of confounding factors, adding to the difficulty in establishing causal relationships or obtaining agreement between researchers on a most appropriate time line.

Capturing overall perceptions of both the social responsibility initiatives and the corporate reputation from different evaluators at different times may have overcome any common method variance, however it may also not have adequately captured evolution over time. The contextual background of the social initiatives/ missteps and any events surrounding their implementation (i.e. natural or man-made disaster, fraud, etc.) may not have been sufficiently integrated in the measures used. Although publicly available documentation was a significant source of the KLD rating evaluations, independent reading of this information may give rise to differences in interpretation, as was noted in the P&G illustration of product categories, as well as the revised legal outcomes discussed in the Tribune illustration.

Reconsidering the perspectives taken by the respondents to the MAC survey and by the compilers of the KLD data may bring to light some of the limitations of only select stakeholder viewpoints. Although the KLD measures are characterized by stakeholder, no broad stakeholder input is sought as most of the underlying data are firm self-reports, including those to regulatory agencies, without any external validation or audit. As external to the focal firm, only publicly available information without any internal context fuels the opinions expressed by these respondents. Recognizing that employees and contractors working within a firm's walls are privy to a closer observation of corporate culture and thus consistency with demonstrated CSR, the absence of their input may ignore critical interpretations. While management may externally project a very strong CSR focus, their internal actions may not carry through with stated policies. One such example is KLD's diversity strength related to life-balance

programs, which is easily publicized in formal documentation but is practically subject to discretionary application which may effectively deny many categories of employees such options. Developing more fine-tuned measures, such as tracking the number and location of employees requesting and then receiving particular types of accommodations, might better differentiate firm commitments and the evolution over time of such actions.

The issue of reputation to whom, for what, also carries with it the limitations that the MAC ratings originate from within the investment community and direct competitors in the eyes of relatively senior respondents. While undoubtedly well informed by industry published documentation and media reports, there may be inherent biases and knowledge gaps tainting responses. The halo around celebrity firms created by the media (Rindova et al., 2006) may afford greater recognition for the same corporate social action as a lesser known firm, further enhancing corporate reputation without tangible justification. The attention given CSR initiatives is inherently linked to the respondents' attitudes about the relevance of such actions which influence their expectations as well as their assessments of the relative strength of CSR against their industry competitors. Accordingly, not all corporate social actions are of comparable interest across stakeholders, however no such weighting is incorporated into the KLD dimensions as all aspects are considered equal. Conceivably the MAC respondents' alignment with shareholder interests might elevate corporate governance as a dimension of greater interest than others such as diversity. Had another stakeholder group such as customers formed the survey pool, the product dimension would have dominated over other CSR

aspects such as corporate governance. Furthermore, many CSR gestures directed to technical stakeholders tend to attract more media attention on a stand-alone basis, compared to corporate social actions directed to the community or the environment which are often overshadowed by disastrous events or catastrophes. For example, while the support offered by many firms to victims of Hurricane Katrina captured momentary media attention as a commendable corporate movement, social actions directed to customers, shareholders and employees tend to benefit from more prolonged attention due to the distinct corporate identify tailored to entice media follow-up.

We do not find the expected influence of concerns over corporate social actions directed to institutional stakeholders on firm reputation, leading to the intriguing question of "why not"? Is it because there is no disconnect between stakeholder expectations due to general cynicism about corporate behaviour, or have reputational assessments already been discounted for inevitable "bad behaviour"? An alternative explanation may be the methodology of reverse coding or even the Mattingly and Berman (2006) factor loading of environmental strengths and weakness onto institutional concerns. Spector and colleagues (1997) caution negating positive worded items may not produce appropriate negatively worded items. Returning to the KLD environmental strengths, they do identify distinctively different criteria than the environmental concerns, with the exception of the little used "other" category. Accordingly, adding to the KLD environmental concerns would be that the firm does not produce a beneficial product/service; it does not engage in pollution prevention; it does not recycle; it does not use alternative fuels; it has not signed the CERES Principles and finally

it does not demonstrate any other strong attributes not covered elsewhere by KLD. Combining these items into one factor via reverse coding may have distorted the sought after *net environmental concerns* which was added to community concerns to reflect concerns over social actions directed to institutional stakeholders.

The asymmetry of the control over the visibility of CSR actions may also present a factor in stakeholder awareness. While firms strategically promote their CSR strengths and tend to be silent or excusive of CSR weaknesses, thus favouring the diffusion of only positive gestures (Doh et al., 2010), social media is more likely to become viral over missteps than good deeds. Traditional research in the early internet and pre-social media era has operationalized media visibility with news media article counts and various finite measures of how often or what key words were utilized to communicate information on corporate actions. Comparisons of corporate annual and more recently CSR/sustainability report disclosures have also become less meaningful as global reporting standards are voluntarily adopted. However, the 21st century poses significantly greater research challenges on identifying and measuring stakeholder sources of information that influence their expectations as well as their assessments of how well CSR actions measure up, both absolutely and against competitors. The advent of blogs, twitter, consumer reviews and a multitude of on-line constantly updated global sources, with varying levels of credibility or authenticity, have yet to be integrated into a viable research model. While previously the challenge was to find informed stakeholders, the going forward challenge may be to weed out

misinformed stakeholders as even unsubstantiated accusations of wrong doings may degrade firm reputation.

6. CONCLUSIONS AND FUTURE RESEARCH DIRECTIONS

This research path has witnessed many detours since first proposed. High expectations of the suitability of the KLD data for longitudinal CSR measures led to initial disappointment with the lack of variability, then to the pleasure of LGM techniques' detecting growth in both corporate social actions and corporate reputation over the five years under examination. The theoretical foundation answered the call of integrating multiple theoretical lenses, as the over-arching resource-based view linked to institutional, stakeholder and resource dependence theories. The dynamic loop of improving corporate social actions leading to improved reputation was successfully demonstrated with change substantiated for each construct as well as the relationship between them.

This research has broadened the theoretical lenses with which we view CSR and has empirically tested for a growth in CSR over time, then linking the improvement in CSR to an improvement in corporate reputation. Under the resource-based view of the firm, we have considered the synergy created by the cospecialized assets of CSR and reputation. We have examined technical stakeholders as resource providers who under resource dependence theory create exchange capital while rewarding the firm with reputation enhancements. Using institutional theory we have outlined how institutional stakeholders create moral capital, which is drawn-down upon when there are concerns over CSR, however as previously discussed we were not able to find empirical support for this relationship. We have also contributed to understanding how the change in CSR over time is evidenced by a change in corporate reputation over time. The longitudinal design of our research with LGM analytics provides these insights on

the dynamic relationship between CSR and reputation which cannot be captured by traditional cross-sectional studies.

We integrated stakeholder theory with stakeholder management to develop divergent expectations for corporate social actions directed to institutional and technical stakeholders; supporting the significant role of actions directed to technical stakeholders, while concerns related to institutional stakeholders were not supported. Much has been learned and will be integrated in future research.

The findings of this study emphasize the dynamic relationship between corporate social actions and corporate reputation. Although no initial relationship was expected, the findings that an improvement in corporate social actions improved corporate reputation over time imply that only maintaining corporate social actions may see reputation decline. Future research into the consequences of constant or decreasing social actions on corporate reputation is warranted. Furthermore, when looking at changes in corporate social actions future research might distinguish between firms with initially high or low reputation to compare the evolution of the relationship over time.

In earlier research we have proposed that firms can achieve a first-mover advantage when corporate social actions are central to the firm's mission, provide some firm-specific benefits and are visible to stakeholders (Tetrault-Sirsly & Lamertz, 2008), however without continued attention to improving on this CSR, the first-mover advantage on corporate reputation could be very short-lived. Any testing of these propositions should consider the sustainability of the various

advantages attached to the speed of implementation of corporate social actions, along with the impact of improvements over time.

Returning to the role of stakeholder expectations in formulating reputation expectations, a background of time, place and culture should be integrated to future research. The all-important context against which societal norms are developed was discussed in Chapter 2 and serves as a reminder that issues of importance to stakeholders evolve over time, in addition to being culturally grounded. While racial discrimination existed long before the civil rights movement it did not preoccupy stakeholder attention during the depression years when other priorities, such as a lack of employment, were at the forefront. The taken-for-granted gender equality of the Western world is not the reality found in countries like Saudi Arabia where women are denied what we view to be basic human rights. As corporate social actions are discretionary and go beyond that which is required by law (McWilliams & Siegel, 2001), when legislation changes (either over time or by the nation of reference) the scope of required gestures will evolve and so need to be considered in future research designs.

Integrating firm legitimacy into stakeholder assessments of reputation might extend the risk-management motivation for CSR (Godfrey et al., 2009) as well as provide a deterrent for bad behaviour. Building on Oliver's (1991) defiance strategy of ignoring or manipulating stakeholders, when could this provoke a withdrawal of stakeholder approval of the firm's license to operate? This understanding could provide valuable insights for both expanding theory

and for practice. Furnishing managers with tools to weigh choices in corporate social actions against possible reputational benefits can assist in building the business case for CSR options as well as directing CSR to influential stakeholders.

This study's support of the dominant influence of technical stakeholders provides a starting point for future research to refine stakeholder segmentation to determine when CSR directed to which technical stakeholder(s) is most likely to improve corporate reputation. Similarly, perhaps it was the aggregation of institutional stakeholders which failed to provide support for reputation decline over concerns. Accordingly, determining which institutional stakeholder(s)' disapproval over social concerns can damage reputation is of importance to both academics and managers when establishing a CSR strategy or making choices between possible corporate social actions.

Strategy research relies on many proxies for hard to quantify attributes, however just because a measure has been used extensively in the past may not make it suitable for all research designs. Ironically, both key measures, the Fortune MAC and KLD have undergone significant make-over, rendering the time-frame utilized in this study as effectively the latest date upon which comparable longitudinal data are available. Fortune now focuses on the World's MACs, while KLD's new ownership has completely revised scoring to go beyond the 0,1 of the academic spreadsheets available since 2002. The consolidation and growth of the ESG (environmental, social and governance) reporting and tracking industry will complicate comparable longitudinal ratings, however the

critical mass of the merged MSCI group (owners of KLD) may lead to more comprehensive firm assessments.

The GAS (generalizability, accuracy and simplicity) challenge persists and may have to compromise generalizability to obtain greater accuracy. Of particular note is the comparability of results over time, given changes in the composition of business lines, contextual factors and the consolidation of disparate operating results under common headings. Future research might avoid conglomerates or look at individual business lines due to the disparate reputations that may be attached to individual brands operating under a corporate umbrella with global CSR policies.

The pertinence of the research question posed by this dissertation warrants continued exploration, as corporate social initiatives and corporate reputation undoubtedly influence strategy and contribute to overall corporate performance. However, recognizing the complexity of the relationship and the ambiguity to building corporate reputation, other research methodologies might be considered such as event studies or comparative case analyses. To integrate external context an event-study design around a provocative issue, integrating an assessment of various media coverage, might provide a starting point. Access to relevant stakeholders and the corporate decision makers for repeated survey or interview could also provide invaluable input in triangulating the intersection of corporate social actions and reputation. Capturing the dynamic relationship and evolution over time will provide a valuable piece to the puzzle of corporate and stakeholder value creation.

Returning to the role of the CEO in championing corporate social actions offers interesting cross-level research possibilities, such as using the retirement or firing of CEOs as an event study on the stakeholder attention of corporate social actions. Furthermore, examining the origin of the successor CEO (from within the organization, within the industry or outside industry) and the subsequent changes on firm CSR orientation may offer an opportunity to examine whether CSR is embedded within corporate culture or transferred with CEO. As we saw in the early origins of CSR, the values embraced by the CEO laid the foundation for corporate social actions and may still do so today in the choice of both implementation of new policies or cessation of existing orientations.

The current economic recession will offer a unique research context for examining a reduction in corporate social actions as some firms take-back benefits such as defined benefit pension plans, scale back on community involvement and product recalls become more prevalent. Stakeholder reactions to these gestures and the ensuing impact on firm reputations offer fertile research avenues. The recent announcement by The Royal Bank of Canada (Shecter, 2011) to end defined pension benefits for new employees has thus far received minimal attention yet no other Canadian financial institution has followed suit. While institutional theory might suggest mimicry within the banking oligopoly, the contentious issue of not only retirement benefits, but two-tiered benefits between existing and future employees, may find RBC alone its proposal. Whether or not RBC goes ahead with the planned changes, the reaction of a variety of stakeholders (i.e. not just employees) would provide an interesting insight into the acceptability of such expense cutting by a profitable bank on its reputation.

Building upon case studies of particular improvements/ deteriorations of CSR may unlock insights as to their underlying causes which may inform researchers and managers. Concentrating on single industry or more mature firms may also provide a more stable research setting within which to compare year over year evolution in a comparable setting. Another area of interest is the interaction between industry and the firms comprising an industry, strategic groups and the role of membership in industry associations. Exploring the notion of reverse reputational gains as large firms piggy back on reputational gains made by smaller niche firms, such as the organic foods market, may offer additional insights. Alternatively, understanding how firms in poorly regarded or *sin* industries can distance themselves to create reputational capital may also be another research avenue. Ultimately, identifying how to build reputation and avoid reputation shocks must be meaningful to the corporate managers entrusted with navigating the reputational landscape. Our findings of the significant relationship of improving corporate social actions to improving reputation assessments can assist managers in justifying, maintaining or extending CSR initiatives to nurture the valuable resource of reputation.

The motivation behind CSR initiatives might also provide a rich multi-level research agenda as the motives behind CSR actions engaged by individual managers, firms and industries digress or overlap under what conditions, locations and contexts. Integrating stakeholder assessments of corporate CSR motives may also help guide CSR agendas. Going beyond large North American public companies, there is fertile research territory in small or privately owned firms, cooperatives and public corporations. The geographic distance between

CSR beneficiaries and influential stakeholders may also be considered by global firms in selecting their CSR initiatives in consideration of the markets within which they are managing their reputation.

Corporate managers' focus on financial performance is largely assured by compensation plan alignments, while many such schemes also refer to reputational achievements, however inserting corporate social performance into the management equation is perhaps key to future success. Exploring the role social media plays in diffusing and critiquing CSR gestures is also undoubtedly of interest to managers hoping to economically leverage positive comments while minimizing the visibility of negative comments. An integral component of superior management, strategic CSR can contribute to enhanced financial and reputational performance.

Throughout the business literature many references are made to the importance of protecting corporate reputation, however the presence of CSR concerns has not been found to be immediately detrimental to reputation. Of interest to managers is distinguishing between CSR concerns that menace reputation and those which stakeholders are more likely to forgive, thus maintaining reputation intact without over CSR spending. The cumulative and longer-term outcome of CSR performance on firm reputation requires further exploration to understand how and why CSR concerns take their toll.

What role does mimicry play when all participants in a market are equally guilty? Does this serve to manage stakeholder expectations so that the lack of corporate social irresponsibility provides reputational advances without investing in further CSR? Remembering that the perception of whether a corporate social

action is symbolic or substantive is in the eye of the stakeholder, how do firms signal CSR motives, to which stakeholders, to most influence these assessments? Public skepticism over insincere corporate social gestures, such as many of the pink products sold during October's breast cancer awareness campaigns, must also be considered by managers when planning their CSR initiatives.

The issue of reputation measures and CSR scales cries out for research attention, as directing management attention to the broader reputational outcomes of CSR initiatives may provide justification for CSR investments over time. There is a need to develop practical tools to assist managers to choose those CSR initiatives that will leverage relevant stakeholder attitudes to enhance corporate reputation. This would allow firms to measure the on-going pertinence of their CSR gestures as well as guard against a repeat of the status quo when stakeholder interests may have evolved in new directions. Akin to the old *zero-based budgeting* concept where tomorrow's investments/spending had to be justified, perhaps CSR choices may also benefit from a more structured relationship to stakeholder expectations and reputational outcomes. The role of social media in diffusing *good deeds* also opens new opportunities for informing relevant stakeholders and monitoring perceptions. Expanding our understanding of the synergies between CSR and reputation provides a tool for managers to create sustainable competitive advantage by investing in *doing good* to reap the benefits of *looking good!*

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KLD Ratings Criteria* **Appendix A**

The following questions were used by KLD Research & Analytics, Inc. to rate the 1100 Socrates companies listed on the S&P 500, Domini 400 Social Index or Russell 1000 Indexes as of December 31st, 2001 and 2002. As of 2003, some 3300 Socrates companies (includes Russell 3000 index) were rated. Each strength or concern identified is included as a 1 on the academic spreadsheet.

Strengths	Concerns
Community and Human Rights 1. ***Generous Giving**:* consistent charitable donations of more than 1.5% of net income before taxes (trailing 3 years), or otherwise notably generous in giving. 2. ***Innovative Giving**:* notable program of innovative giving to support not for profit organizations (especially those aimed at the self-sufficiency of the economically disadvantaged). 3. ***Indigenous Peoples Relations:*** established relations in actual or proposed operations that respect the indigenous peoples' land, sovereignty, human rights, culture and intellectual property. 4. ***Support for Housing:*** prominent participant in public/private initiatives favouring the economically disadvantaged (i.e. National Equity Fund or Enterprise Foundation). 5. ***Support for Education:*** notably innovative in supporting school education at the primary and secondary levels in programs that advantage the economically disadvantaged, or prominent support of youth job-training programs. 6. ***Other human rights***: exceptional human rights initiatives or leadership not covered elsewhere. 7. ***Other:*** Exceptional in-kind giving program, strong volunteer or other community program.	 1. ***Negative Economic Impact**:* major controversies related to the economic impact on the community of firm actions. Possibilities include water rights disputes, environmental contamination, "put-or-pay" trash incinerator contracts, plant closings or other actions that adversely affect the community's tax base, quality of life or property values. 2. ***Investment Controversies:*** controversial practices of financial institutions (lending or investments), particularly related to the Community Reinvestment Act. 3. ***Indigenous Peoples Relations:*** serious controversies where the indigenous peoples' land, sovereignty, human rights, culture or intellectual property were not respected. 4. ***Burma***: operations or investments. 5. ***Other human rights***: operations subject of major human rights controversies not covered elsewhere. 6. ***Other:*** strong community opposition to firm's business or other aspects of operations.

<table>
<tr><th>Strengths</th><th>Concerns</th></tr>
<tr><td><u>Corporate Governance</u>

1. Limited Compensation: notably low levels of top management or board compensation recently awarded (CEO less than $500,000 per annum; outside directors less than $30,000).
2. Ownership: owns 20%-50% of another company that KLD has rated as having social strengths, or is more than 20% owned by a firm rated by KLD as having social strengths. (Over 50% ownership represents a controlling interest, such that the other company is treated as a division of the parent company by KLD).
3. Other: (no specific criteria given).</td><td>

1. High Compensation: notably high levels of top management or board compensation recently awarded (CEO more than $10 million per annum; outside directors more than $100,000).
2. Ownership: owns 20%-50% of another company that KLD has rated as having social concerns, or is more than 20% owned by a firm rated by KLD as having areas of concern. (Over 50% ownership represents a controlling interest, such that the other company is treated as a division of the parent company by KLD).
3. Tax Disputes: recent major tax disputes at the Federal, state or local level involving more than $100 million.
4. Other: (no specific criteria given).</td></tr>
</table>

<table>
<tr><th>Strengths</th><th>Concerns</th></tr>
<tr><td><u>Product</u>

1. Quality: has well-developed, long-term company-wide quality program or one recognized in its industry as exceptional in the U.S.
2. R & D / Innovation: industry leader for R & D, particularly distinguished for notably innovative products.
3. Benefits to Economically Disadvantaged: part of basic firm mission is to provide products or services for the economically disadvantaged.
4. Other: (no specific criteria given).</td><td>

1. Product Safety: recent substantial penalties or fines paid, or regulatory actions or major recent controversies surrounding the safety of products or services.
2. Marketing/Contracting Controversy: recent major controversies over contracting or marketing or substantial penalties / fines relating to consumer fraud, advertising practices or government contracting.
3. Antitrust: recent major antitrust allegation controversies or regulatory actions, substantial penalties or fines paid for antitrust violations (i.e. collusion, price fixing, predatory pricing).
4. Other: (no specific criteria given).</td></tr>
</table>

Strengths	Concerns
<u>Environment</u> 1. ***Beneficial Products & Services:*** substantial revenues from innovative remediation products, products that promote energy efficiency, environmental services or innovative products that it has developed that provide environmental benefits. (KLD notes that "environmental service" excludes those services with questionable environmental effects (i.e. landfills, waste-to-energy plants, incinerators and deep injection wells). 2. ***Pollution prevention:*** notably strong pollution prevention programs (includes toxic-use reduction & emissions reductions programs). 3. ***Recycling:*** either a substantial user of recycled materials in its manufacturing processes as raw materials or a major player in the recycling industry. 4. ***Alternative Fuels:*** substantial revenues are derived from alternative fuels (includes natural gas, solar energy and wind power). Exceptional commitment to energy efficiency programs (or the promotion of energy efficiency) has been demonstrated. 5. ***Communications:*** signatory to the CERES Principles, has a notably effective internal communications systems to communicate its best practices related to the environment or publishes a notably substantive environmental report. 6. ***Other:*** demonstrates a strong environmental attribute that is not covered by KLD ratings criteria.	 1. ***Hazardous Waste:*** liabilities for hazardous waste sites exceeds $50 million or substantial fines/penalties have been paid for waste management violations. 2. ***Regulatory Problems:*** recent substantial fines/penalties have been paid for violations of water, air or other environmental regulations, or regular controversies under the Clean Water Act, Clean Air Act or other major environmental regulations have been noted. 3. ***Ozone Depleting Chemicals:*** among top manufacturers of ozone depleting chemicals (i.e. HCFC, methylene chloride, methyl chloroform or bromines. 4. ***Substantial Emissions:*** toxic chemicals (as defined by and reported to the Environmental Protection Agency) legal emissions into the water and air from individual plants are among the highest of the KLD followed companies. 5. ***Agricultural Chemicals:*** substantial producer of agricultural chemicals (i.e. chemical fertilizers or pesticides). 6. ***Climate Change:*** substantial revenues are derived from the sale of oil or coal, including derivative products, or substantial revenues are indirectly derived from the combustion or oil or coal and derivative fuel products. Included are such companies as transportation firms with fleets, truck and automobile manufacturers and other transportation equipment companies. 7. ***Other:*** environmental problems not otherwise covered in KLD ratings categories (i.e environmental accident).

Diversity	
1. ***CEO:*** a minority group member or a woman. 2. ***Promotion:*** notable progress in promoting women and minorities, particularly to those line positions that have responsibilities for profit and loss. 3. ***Board of Directors:*** Minorities, women and/or the disabled hold 4 or more of the board seats (without any double counting), or at least one-third of the total board seats when there are less than 12 members of the board. 4. ***Family Benefits:*** outstanding employee benefits or other programs oriented to family/work concerns (i.e. elder care, childcare or flextime). 5. ***Women/Minority Contracting:*** at least 5% of subcontracting is with women/minorities, or demonstrated significant purchasing/subcontracting with women/minority owned businesses. 6. ***Employment of the Disabled:*** innovative hiring or other human resource programs for the disabled, or otherwise has maintained a superior reputation for being an employer of the disabled. 7. ***Progressive Gay/Lesbian Policies:*** notably progressive gay/lesbian policies, particularly in providing benefits to domestic partners of employees. 8. ***Other:*** noteworthy diversity achievements that are not covered under other KLD ratings categories.	1. ***Controversies:*** affirmative action controversies that have resulted in substantial fines or civil penalties, or other major controversies due to affirmative action issues. 2. ***Non-Representation:*** no women in senior management nor on the board of directors. 3. ***Other:*** notable diversity problems not covered elsewhere.

Strengths	Concerns
<u>Employee Relations</u> 1. ***Strong Union Relations:*** notably strong union relations over the long-term 2. ***Cash Profit Sharing:*** recent distributions from a cash profit-sharing program have been made to a majority of the workforce. 3. ***Employee Involvement:*** strong encouragement of worker involvement and/or ownership via stock options for a majority of employees, stock ownership, gain sharing, participation in management decision-making or sharing of financial information. 4. ***Strong Retirement Benefits:*** notably strong program of retirement benefits. 5. ***Health and Safety:*** U.S. Occupational Health and Safety Administration has noted firm for its safety programs (criteria first introduced in 2003). 6. ***Labour Rights:*** outstanding transparency on monitoring and disclosing overseas sourcing, or outside the U.S., particularly good union relations. 7. ***Other:*** good employee safety record or other noteworthy commitments to employees' well-being demonstrated.	1. ***Poor Union Relations:*** history of poor union relations. 2. ***Workforce Reductions:*** reduction or announcement of a reduced workforce of 15% in the most recent year or 25% over the past two years. 3. ***Pension/Benefits:*** substantially underfunded defined benefit pension plan, or a retirement benefits plan that is inadequate. 4. ***Health and Safety:*** recent substantial fines/penalties for wilful violations of employee health and safety standards, or other involvement in major controversies over health and safety. 5. ***International Labour:*** major recent controversies over non-U.S. operations related to labour standards and employee relations. 6. ***Other:*** notable employee problems not covered elsewhere.

The final coding examined each of the above categories to regroup international human rights related to employment relationships with employees, etc., and regrouped to the following number of categories:

Community Strengths	7	Community Concerns	6
Diversity Strengths	8	Diversity Concerns	3
Environmental Strengths	6	Environmental Concerns	7
Employee Strengths	7	Employee Concerns	6
Product Strengths	4	Product Concerns	4
Governance Strengths	3	Governance Concerns	4

* These questions are taken from the KLD Research & Analytics, Inc. 2003 "*KLD Ratings Data: Inclusive Social Rating Criteria"* and 2008 *"Getting Started with KLD STATS and Ratings Definitions"*.

Appendix B

Fortune's Most Admired Companies Data Collection Methodology**

Fortune started rating 200 U.S. companies in 1982 based on a September 1981 survey of industry experts (analysts) and industry executives with a response rate of 51% of those polled (Makin, 1982: 34), to become an annual survey based on the Fortune 1000, of which the more recent data is utilized in this research. While the respondents have changed over time, and the industries have evolved, an essentially stable methodology has been employed, although since 2001 Fortune has partnered with the Hay Group to conduct this annual survey.

Based on Fortune's information on the 2008 survey (Fortune, 2008), over 600 companies in some 70 industries were included in a fourth quarter 2007 survey of over 3,300 executives, board directors and securities analysts. Fortune determines the industry groupings by using the Fortune 1000 listing and based on revenues selects the ten largest companies in each industry, at the time the required revenue level to be included on the list was $1.2 billion (Fortune, 2008).

The 2009 survey merged the former World's Most Admired Company with the former America's Most Admired Company, to cover some 40 primarily US industries, along with 25 international industries, increasing the minimum required revenue level to $10 billion (Fortune, 2009). Given the significance of the change in methodology, for the purposes of this longitudinal research the 2008 survey based on the fourth quarter 2007 reputation ratings are the last

usable reputation measures. These rating represent a one year lag from the last 2006 CSR measures, two years from 2005 and three years from 2004.

Fortune does not provide detailed response statistics, but indicates that they receive a satisfactory response rate. Up to ten firm executives and board directors from each eligible company were surveyed as to their own company and the nine largest competitors. For financial analysts, they were asked to assess the ten largest industry competitors they monitor. Each respondent rated each of the following categories (equally weighted) from zero (poor) to 10 (excellent), to yield an overall estimation of firm reputation:

Quality of management

Quality of products and services

Innovation

Long-term investment value

Financial soundness

People Management: Ability to attract, develop and keep talented people

Social responsibility

Use of corporate assets

** Description of Fortune methodology was obtained from sample industry reports (no longer available on their web site) and from their web site (last accessed December 19, 2009) at: http://money.cnn.com/magazines/fortune/mostadmired/2009/faq

Appendix C

Descriptive Statistics

	Minimum	Maximum	Mean	Std. Deviation
	Statistic	Statistic	Statistic	Statistic
2 Dig Industry SIC	10	87	43.737	17.638
2002				
Institutional Strength 2002	0	8	1.702	1.973
Technical Strength 2002	0	5	0.856	1.099
Institutional Concern 2002	4	12	6.479	1.325
Technical Concern 2002	0	8	2.168	1.748
Size 2002	21.810	33.246	26.767	2.161
Profitability 2002	-208.045	431.860	13.580	36.927
Slack 2002	0.032	8.110	1.571	1.096
Risk 2002	15.660	109.644	66.055	19.921
2003				
Institutional Strength 2003	0	9	2.021	2.126
Technical Strength 2003	0	5	0.821	1.097
Institutional Concern 2003	4	12	6.473	1.231
Technical Concern 2003	0	9	2.596	1.901
Size 2003	22.041	33.399	26.853	2.148
Profitability 2003	-87.555	147.655	13.236	19.300
Slack 2003	0.040	7.720	1.605	1.079
Risk 2003	13.870	103.857	65.005	19.807
2004				
Institutional Strength 2004	0	10	2.123	2.197
Technical Strength 2004	0	7	0.853	1.159
Institutional Concern 2004	3	13	6.575	1.258
Technical Concern 2004	0	9	2.782	1.796
Size 2004	22.193	33.685	26.974	2.131
Profitability 2004	-146.975	219.250	14.809	21.482
Slack 2004	0.040	8.080	1.605	1.059
Risk 2004	10.680	121.166	63.783	19.406

2005				
Institutional Strength 2005	0	9	2.323	2.150
Technical Strength 2005	0	6	1.032	1.301
Institutional Concern 2005	2	13	6.575	1.434
Technical Concern 2005	0	9	2.890	1.848
Size 2005	22.175	33.733	27.070	2.139
Profitability 2005	-60.605	245.665	16.863	20.327
Slack 2005	0.011	7.280	1.577	0.981
Risk 2005	10.900	115.752	63.515	20.009
2006				
Institutional Strength 2006	0	10	2.453	2.263
Technical Strength 2006	0	6	1.049	1.323
Institutional Concern 2006	2	14	6.520	1.510
Technical Concern 2006	0	11	3.175	2.029
Size 2006	22.121	34.055	27.163	2.162
Profitability 2006	-210.280	81.895	15.444	22.717
Slack 2006	0.014	5.820	1.548	0.915
Risk 2006	11.850	108.683	63.854	19.330
Dependent Variable: Reputation				
Reputation 2002	2.33	8.41	6.171	1.064
Reputation 2003	2.63	9.04	6.468	1.032
Reputation 2004	3.50	8.52	6.503	0.934
Reputation 2005	3.20	8.60	6.407	0.968
Reputation 2006	3.09	8.53	6.362	0.936
Reputation 2007	3.79	8.44	6.389	0.962

Descriptive Statistics - 5 Year Panel

n=1425	Minimum	Maximum	Mean	Std. Deviation
	Statistic	Statistic	Statistic	Statistic
2 Digit Industry SIC	10	87	43.737	17.613
Institutional Strength	0	10	2.124	2.157
Technical Strength	0	7	0.922	1.202
Institutional Concern	2	14	6.400	1.435
Technical Concern	0	11	2.723	1.894
Size	21.810	34.055	26.965	2.150
Profitability	-210.280	431.860	14.786	25.007
Slack	0.011	8.110	1.581	1.027
Risk	10.680	121.166	64.442	19.692
Reputation at *T*	2.33	9.04	6.382	0.994
Reputation at *T+1*	2.63	9.04	6.426	0.967
Reputation at *T+2 (n=1140)*	3.09	8.60	6.416	0.950
Reputation at *T+3 (n=855)*	3.09	8.60	6.386	0.955

Frequencies for 5 year panel

Frequencies (# in 1425)	**Institutional Strengths**	**Technical Strengths**	**Institutional Concerns**	**Technical Concerns**
None (i.e. 0)	392	728	0	128
1	329	397	0	294
2	210	190	14	312
Cumulative 2 or less	931	1315	14	734
% represented				
None (i.e. 0)	27.5%	51.1%	0%	9.0%
1	23.1	27.9	0	20.6
2	14.7	13.3	0.98	21.9
Cumulative 2 or less	65.3%	92.3%	0.98%	51.5%

Illustrative industry groupings for 5 year panel

Manufacturing (SIC 20-39)

(*n=620*)	Minimum	Maximum	Mean	Std. Deviation
Institutional Strength	0	10	2.274	2.243
Technical Strength	0	7	1.290	1.359
Institutional Concern	2	13	6.434	1.536
Technical Concern	0	9	2.777	1.835
Size	22.121	33.071	26.666	1.924
Profitability	-174.073	431.860	16.758	31.749
Slack	0.060	8.080	1.722	0.925
Risk	10.680	121.166	62.731	19.402
Reputation T+1	3.09	8.83	6.429	0.966

Services (SIC 60-87)

(*n=345*)	Minimum	Maximum	Mean	Std. Deviation
Institutional Strength	0	10	2.519	2.386
Technical Strength	0	6	.652	.937
Institutional Concern	4	9	6.149	1.152
Technical Concern	0	9	2.620	1.756
Size	22.591	34.055	27.873	2.259
Profitability	-210.280	38.330	11.579	14.718
Slack	.014	8.110	1.356	1.293
Risk	19.950	101.590	75.259	20.201
Reputation T+1	2.63	8.6	6.328	.927

Retail & Transportation (SIC 40-47 & 50-59)

(n=315)	Minimum	Maximum	Mean	Std. Deviation
Institutional Strength	0	7	1.641	1.566
Technical Strength	0	6	0.549	0.961
Institutional Concern	3	10	6.203	0.887
Technical Concern	0	11	2.549	2.038
Size	21.810	33.294	26.516	2.100
Profitability	-208.045	80.165	14.145	20.819
Slack	0.120	5.940	1.555	0.763
Risk	15.660	104.848	57.737	16.595
Reputation T+1	3.890	9.040	6.518	1.007

All Other Industries (SIC 10-19 & 48-49)

(n=145)	Minimum	Maximum	Mean	Std. Deviation
Institutional Strength	0	8	1.593	2.036
Technical Strength	0	3	0.634	0.873
Institutional Concern	4	14	7.607	2.161
Technical Concern	0	8	3.110	2.082
Size	22.171	32.042	27.062	2.277
Profitability	-57.871	110.070	15.383	18.588
Slack	0.280	7.440	1.571	1.131
Risk	26.910	114.965	60.592	15.330
Reputation T+1	3.570	8.440	6.449	0.963

Appendix D

Correlations by Year

(Spearman's rho)

2002

(N=285)	1	2	3	4	5	6	7	8
1. Institutional Strength 2002	1							
2. Technical Strength 2002	.368***	1						
3. Institutional Concern 2002	.024	.121*	1					
4. Technical Concern 2002	.342***	.230***	.331***	1				
5. Reputation 2002 (*t*)	.823	.176**	-.094	-.038	1			
6. Reputation 2003 (*t+1*)	.151**	.204***	-.102	.014	.823***	1		
7. Reputation 2004 (*t+2*)	.194***	.261***	-.057	.047	.704***	.796***	1	
8. Reputation 2005 (*t+3*)	.258***	.241***	-.076	.058	.609***	.660***	.791***	1

*p<.05 **p<.01 ***p<.001 (two-tailed)

2003

(N=285)	1	2	3	4	5	6	7	8
1. Institutional Strength 2003	1							
2. Technical Strength 2003	.369***	1						
3. Institutional Concern 2003	.048	.150*	1					
4. Technical Concern 2003	.366***	.226***	.226***	1				
5. Reputation 2003 (*t*)	.144*	.281***	-.095	-.001	1			
6. Reputation 2004 (*t+1*)	.177**	.303***	-.043	.017	.796***	1		
7. Reputation 2005 (*t+2*)	.229***	.273***	-.059	.025	.660***	.808***	1	
8. Reputation 2006 (*t+3*)	.173*	.264***	-.087	.054	.611***	.684***	0.755***	1

*p<.05 **p<.01 ***p<.001 (two-tailed)

2004

(N=285)	1	2	3	4	5	6	7	8
1. Institutional Strength 2004	1							
2. Technical Strength 2004	.407***	1						
3. Institutional Concern 2004	-.038	.153*	1					
4. Technical Concern 2004	.312***	.180**	.230***	1				
5. Reputation 2004 (*t*)	.168**	.264***	-.011	-.055	1			
6. Reputation 2005 (*t+1*)	.233***	.262***	-.078	-.060	.791***	1		
7. Reputation 2006 (*t+2*)	.184**	.278***	-.105	-.038	.697***	.808***	1	
8. Reputation 2007 (*t+3*)	.173***	.205***	-.029	-.008	.547***	.684***	.755***	1

*p<.05 **p<.01 ***p<.001 (two-tailed)

2005

(N=285)	1	2	3	4	5	6	7
1. Institutional Strength 2005	1						
2. Technical Strength 2005	.387***	1					
3. Institutional Concern 2005	-.009	.1548*	1				
4. Technical Concern 2005	.339***	.138*	.258***	1			
5. Reputation 2005 *(t)*	.239***	.273***	-.067	-.010	1		
6. Reputation 2006 *(t+1)*	.187**	.305***	-.068	-.032	.808***	1	
7. Reputation 2007 *(t+2)*	.180**	.218***	.017	.054	.684***	.755***	1

**p<.05 **p<.01 ***p<.001 (two-tailed)*

2006

(N=285)	1	2	3	4	5	6
1. Institutional Strength 2006	1					
2. Technical Strength 2006	.384***	1				
3. Institutional Concern 2006	-.132*	.073	1			
4. Technical Concern 2006	.331***	.142*	.222***	1		
5. Reputation 2006 *(t)*	.181**	.276***	-.086	.000	1	
6. Reputation 2007 *(t+1)*	.174**	.233***	-.020	.056	.755***	1

**p<.05 **p<.01 ***p<.001 (two-tailed)*

5 year Panel

Institutional and Technical strengths, concerns & Reputation from T to T+3

(N=1425 for 1-6)	1	2	3	4	5	6	7	8
1. Institutional Strength	1							
2. Technical Strength	.344***	1						
3. Institutional Concern	-.010***	.043	1					
4. Technical Concern	.351***	.162***	.197***	1				
5. Reputation *T*	.171***	.250***	-.077**	-.005	1			
6. Reputation *T+1*	.179***	.255***	-.076**	-.007	.788***	1		
7. Reputation *T+2 (n=1140)*	.189***	.251***	-.070*	.016	.673***	.787***	1	
8. Reputation *T+3 (n=855)*	.201***	.231***	-.070*	.031	.582***	.681***	.784***	1

*p<.05 ** p<.01 ***p<.001 (two-tailed)

Appendix E

KLD Factor Structure subject to CFA

Mattingly and Berman (2006: 32)

Table 3
Factor Solution for All 293 Firms in Sample

	Component			
	Institutional		Technical	
	Weakness	Strength	Weakness	Strength
Environment—weakness	0.83			
Community—weakness	0.74			
Environment—strength	0.61			
Diversity—strength		0.80		
Community—strength		0.70		
Employee—weakness			0.61	
Diversity—weakness			0.61	
Product—weakness			0.59	
Governance—weakness			0.59	
Product—strength				0.78
Governance—strength				0.66
Employee—strength				0.50

Appendix F

Configural and measurement invariance model factors

Configural invariance model factors

n= 285	**2002**	**2003**	**2004**	**2005**	**2006**
Standardized Solution					
Institutional Strength	.781	.402	.378	1.0	.997
Technical Strength	.487	.896	1.0	.340	.326
Institutional Concern	.103	.242	.204	.278	.389
Technical Concern	.484	1.0	1.0	.396	.409
R-sq.					
Institutional Strength	.609	.162	.143	1.0	.994
Technical Strength	.237	.804	1.0	.116	.106
Institutional Concern	.011	.058	.042	.077	.151
Technical Concern	.235	1.0	1.0	.157	.167

Measurement invariance model factors

n= 285	**2002**	**2003**	**2004**	**2005**	**2006**
Standardized Solution					
Institutional Strength	.730	.695	.684	.724	.741
Technical Strength	.474	.513	.504	.469	.497
Institutional Concern	.201	.231	.229	.202	.207
Technical Concern	.545	.557	.573	.543	.537
R-sq.					
Institutional Strength	.533	.483	.468	.524	.549
Technical Strength	.225	.263	.254	.220	.247
Institutional Concern	.041	.054	.052	.041	.043
Technical Concern	.297	.310	.328	.294	.289