

# Corporate Governance and Corporate Social Responsibility: Research on the Interconnection of Both Concepts and Its Impact on Non-Profit Organizations

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## I. INTRODUCTION

**Abstract**—The aim of non-profit organizations (NPO) is to provide services and goods for its clientele, with profit being a minor objective. By having this definition as the basic purpose of doing business, it is obvious that the goal of an organisation is to serve several bottom lines and not only the financial one. This approach is underpinned by the non-distribution constraint which means that NPO are allowed to make profits to a certain extent, but not to distribute them. The advantage is that there are no single shareholders who might have an interest in the prosperity of the organisation: there is no pie to divide. The gained profits remain within the organisation and will be reinvested in purposeful projects. Good governance is mandatory to support the aim of NPOs. Looking for a measure of good governance the principals of corporate governance (CG) will come in mind. The purpose of CG is direction and control, and in the field of NPO, CG is enlarged to consider the relationship to all important stakeholders who have an impact on the organisation. The recognition of more relevant parties than the shareholder is the link to corporate social responsibility (CSR). It supports a broader view of the bottom line: It is no longer enough to know how profits are used but rather how they are made. Besides, CSR addresses the responsibility of organisations for their impact on society. When transferring the concept of CSR to the non-profit area it will become obvious that CSR with its distinctive features will match the aims of NPOs. As a consequence, NPOs who apply CG apply also CSR to a certain extent. The research is designed as a comprehensive theoretical and empirical analysis. First, the investigation focuses on the theoretical basis of both concepts. Second, the similarities and differences are outlined and as a result the interconnection of both concepts will show up. The contribution of this research is manifold: The interconnection of both concepts when applied to NPOs has not got any attention in science yet. CSR and governance as integrated concept provides a lot of advantages for NPOs compared to for-profit organisations which are in a steady justification to show the impact they might have on the society. NPOs, however, integrate economic and social aspects as starting point. For NPOs CG is not a mere concept of compliance but rather an enhanced concept integrating a lot of aspects of CSR. There is no “either-nor” between the concepts for NPOs.

**Keywords**—Business ethics, corporate governance, corporate social responsibility, non-profit organisations, stakeholder theory.

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CG and CSR have been already widely discussed in science. Both concepts got attention in the scientific world through several incidents. The breakthrough for attention to CG was many worldwide crashes of corporations due to a lack of guidance and supervision. CSR got its attention in science due to a changing world. It is no longer enough to know how profits are used but above all how they are made. The concept of CG has been already transferred successfully to NPO. For this purpose, the mere concept has been adapted to the distinctive features of these organizations and their special governing structures.

The author has already made deep investigations in the context of a doctoral study programme of CG for NPO. For this reason, the rough presentation of the field of CG mirrors the gained expertise and knowledge. Now, the purpose of this article is to enrich this research with the ideas of CSR. CSR has not yet been transferred to the non-profit area. It is to find out which function CSR could play in this field. The research should confirm or reject the thesis that CG in NPO is not a mere concept of compliance but rather an already enhanced concept towards CSR.

## II. CORPORATE GOVERNANCE

### A. Corporate Governance - Introduction

CG got its attention in science because of many worldwide crashes of corporations due to a lack of guidance and supervision. Sir Adrian Cadbury put a landmark with his definition of CG as “...the system by which companies are directed and controlled” [1]. The intense scientific discussion about CG resulted in the development of various CG codes. Today, there exist CG Codes in nearly each of the current EU member states. Over the past ten years, the EU has put effort in harmonizing all these country-specific codes [2]. Principles of CG were also published by the OECD (revised version 2015) due to the worldwide importance of the topic. According to OECD, “Corporate Governance involves a set of relationships between a company’s management, its board, its shareholders and other stakeholders” [3]. The result of the scientific discussion is narrower and broader definitions of CG as the two examples clearly reveal: The OECD-definition considers shareholders and stakeholders whereas the definition of Cadbury refers only to the company itself and its structure.

Despite the difference in the definitions, the central idea of CG is always to define the roles, responsibilities, and power among the board, the management and shareholders respectively stakeholders.

### *B. Corporate Governance - Theories*

The theoretical background of CG is manifold. It depends on the focus which will be put on this concept. There is no doubt that **agency theory** is the predominant theory to explain the mechanism of CG. In the centre of attention is the relationship between a principal and an agent where the principal delegates the execution of an action including decision making to an agent [4]. The focus has to be on the principal as he is the bearer of the residual loss. The problem is that the agent may not act in the best interest of the principal. Different goal-orientation, risk preferences, information asymmetry are described as agency problems. Control will help to solve these agency problems [5].

Agency theory is based on a special type of people. Between both parties, the principal and the agent, it is assumed that there is a trade-off between their goals. Both parties are assumed to be self-interested. In contrast, **stewardship theory** has been developed to show an opposite type of people acting in organizations, above all NPO. Stewardship theory's parties are the principal and the agent, as well, but the agent – better defined as “steward” – maximizes the principal's interest by maximizing his personal goals at the same time [6]. The behavior of a steward in stewardship theory is diametrically opposed to those of an agent in agency theory. This underlying assumption has far-reaching consequences: As already mentioned, the focus in agency theory is on control to cope with the divergent interests over the agent through more or less sophisticated incentive systems and governance structures. Control is also a matter of stewardship theory but with a completely different focus: Trust is an important prerequisite to install a control system which presumes itself high identification with an organization. It gives the managers a high level of autonomy and working-conditions which support trustful decision-making [7].

The attempt to understand CG by using only one theory is hardly one-sided. A comprehensive picture of the basis of CG is only possible by looking at further theories, too. The company or an organization's environment consists of a network of relationships with stakeholders. This focus is also emphasized by the CG definition of the OECD. A company not only has shareholders but also a lot of stakeholders have in mind. In the CG discussion around for-profit organizations, the shareholder is seen as the most important stakeholder, and therefore the focus is concentrated on it. Regardless this focus, stakeholders play an increasingly important role even in for-profit companies. Stakeholders are in the central focus of NPO as they represent the missing owner. The well-known definition of Freeman that *a stakeholder is any group or individual who can affect or is affected by the achievement of the organization's objectives* [8] is central to this paper as it belongs also to the concept of CSR which will be discussed below. **Stakeholder theory's** actors are stakeholders.

Stakeholder of a company or organization can be everybody who is of interest to a company or organization. The number of stakeholders depends on the size, mission and legal form. In theory, there have been developed several methods to reduce the number of stakeholders. The most important concept refers to that of Mitchell/Agle/Wood where power, legitimacy, and urgency are attributes to reduce the number of stakeholders [9].

The comprehensive picture of theories of CG is not thinkable without **business ethics**. The purpose of a business is to create value for all groups and individuals who have a stake in the business [10]. This valuable purpose of business reflects two concepts which are business ethics and stakeholder theory. It becomes obvious that these concepts might be interconnected. But, the assumption exists that ethics do not go together with attaining business goals such as maximizing profits. It is the concept of CSR which will bring both goals together. Details will be discussed below. According to [11], it is surprising that business ethics in the form of applied ethics have the same origin as strategic management. Unfortunately, they grew apart as strategic management focused on profit making, and business ethics have focused on ethics itself. But, by focusing the value creation process, it becomes obvious that effective strategic management includes considerations of ethics [11].

**Managerial discretion and power** are basic elements in all discussed theories. Managerial discretion describes the degree of freedom of the management to make decisions [12]. Managerial discretion and power can only be understood correctly by considering the aforementioned theories. Above all, power is used differently in agency theory, stewardship theory and stakeholder theory.

### *C. CG in NPO*

The adoption of this topic within the non-profit-area dates back to the beginning of the 21<sup>st</sup> century. The overall purpose is also guidance and supervision. The outcome of the discussion within the non-profit area is also a few non-profit governance codes, for example in Germany, Switzerland, and also Austria [13]. The adoption of CG to the non-profit area has been put forward because of large public serving organizations which resemble more firms than typical NPO. The decision-making process in these huge organizations is hierarchical. CG structures have been implemented to increase reliability and accountability to the address of potential stakeholders [14].

### *D. NPO and its Distinctive Features*

In order to understand that the impact NPO might have on the concept of CSR, it is helpful to get to know NPO with its distinctive features. NPO are an important social, political, and cultural part of a civil society. They have received attention as third sector in addition to the profit sector and the government sector. The non-profit sector is huge and the inherent organizations are different regarding scope, mission, social and political importance, and professionalism [15]. Furthermore, there exist several legal frameworks to form

NPO, which are associations as most important legal framework, foundations and cooperatives [16]. The common denominator of such organizations is the provision of services, usually for charitable, religious, educational, scientific, literary, humanitarian or other purposes. Profit is only the basis of its activities and not the mere goal [17]. The common existing misunderstanding of the term “non-profit” is no profit, but it means correctly “not for profit” and this term is only used to distinguish these organizations from profit organizations. NPO are allowed to make profits to a certain extent, but not to distribute them. The demarcation criterion to profit organizations is the non-distribution constraint [18]. Furthermore, NPO are characterized as multiple stakeholder organizations [19]. The consideration of several stakeholders is an important feature as they represent the missing owner. The focus on stakeholders is an important feature with respect to the discussion of the concept of CSR and its interconnection with NPO. The description of distinctive features can be enlarged by the fact that these organizations do not concentrate on a mere financial bottom line. They rather concentrate on task goals, and the economic performance is only the basis and not the goal of their existence [20]. As a consequence, these organizations face the challenge of several bottom lines, and the interconnection between these bottom lines sometimes is even of conflicting nature.

### III. CORPORATE SOCIAL RESPONSIBILITY

#### *A. Corporate Social Responsibility - Introduction*

CSR got its attention in Europe in the years of 1990 although first ideas were released in the US in the late 1800s [21]. Unfortunately, there does not exist any definition which states the unique understanding of the concept. In this respect, CSR faces the same problem as CG. Far a lot of scholars claim the unclear situation regarding the meaning of CSR and try themselves to provide more or less suitable definitions. [22]. As a consequence, it is the responsibility of the author to choose an adequate understanding which suits the discussed context. Carroll is the author which provides the most commonly accepted definition. He defines CSR as the social responsibility of business as encompassing the economic, legal, ethical, and discretionary expectations that society has of organizations at a given point in time [23].

The discussion about CSR has also attracted the European Union (EU) and the EU acknowledged the importance of this concept by providing a green paper. The understanding of CSR in this paper is those that companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis [24].

#### *B. Corporate Social Responsibility – Theories*

The concept of CSR is a far-reaching which offers a wide range of matters to focus on. There exists hardly any more comprehensive overview of relating theories for this concept than those of Garriga and Melé [25]. The authors have classified the approaches and corresponding theories. The

classification is done along underlying theories and has been clustered in four groups: The first group summarizes theories where the economic aspect of the interaction between business and society is focused. Social activity is welcome only for the purpose of creating wealth to the corporation: instrumental theories. The second group of theories emphasizes the social power of the corporation with respect to its responsibility in the political area: political theories. The third group of theories looks at corporations in a way that they might have to integrate social demands in their business: integrative theories. The last group of theories deals with ethics. Whenever a business is done, it takes place in an ethical environment: ethical theories [25].

To put forward these theoretical considerations, it might be helpful to choose one set of theories out of this all-embracing overview. The planned investigation in applying CSR to NPO calls for a concentration on applied theories as well.

### IV. SIMILARITIES AND DIFFERENCES

CG and CSR are intertwined concepts according to various scholars [26]: the starting point of social responsibility is “good governance”. With a lack in vision, leadership, or accountability a company or profit organization will not be able to gain sustainable profit. Obviously, there has taken place a paradigm shift. The single focus on the pursuit, and the financial bottom line with the purpose to satisfy shareholders has been changed to a broader view. Sustainable growth and shareholder value will be achieved by following a so-called triple bottom line which consists of financial, social, and also environmental factors.

CG itself has been developed due to big worldwide crashes of companies. Sustainable growth was not in the general awareness shareholders. The focus was on profit maximization. These crashes called for a new “good governance” in a growing meaning till today. Schmidpeter [27] provides an overview to classify and demarcate several concepts of CSR. He classifies CG as part of CSR, but its meaning is narrowed only to compliance, anti-corruption and transparency, or boni for the management. Compliance means to obey relevant rules, standards, and laws for an organization. Compliance is a prerequisite for good governance. It can be called the “hard law” [28]. Good governance comprises the whole set of rules, i.e. laws and firm-specific standards, upon which an organization is governed. CG Codes, for example of Austria and Germany, state in their preambles that the rules refer to international standards of “good governance” in a broadened sense including not only the shareholders but also stakeholders [29].

Schmidpeter shows with his draft that also corporate citizenship and responsible lobbying will be part of the bigger concept of CSR.

Today CSR with its triple bottom line has already inspired CG Codes [30]. And depending on the applied focus or used definitions, there is hardly any difference between the concepts. The drawback of CSR is that their appliance is voluntarily, and therefore, these ideas might not have really reached the reality of profit-organizations. The awareness till

consideration of multiple stakeholders and the environment still has high potential to grow.

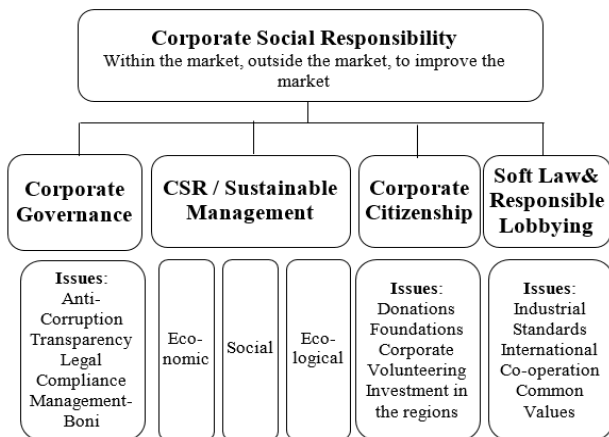


Fig. 1 Fields of CSR

### V. CSR IN NPO

The thesis for this research is that CG in NPO is not a mere concept of compliance but rather an already enhanced concept towards CSR. The question is, if NPO have to put effort in adapting also CSR as a second concept or they enhance their exiting governance concepts with valuable aspects of CSR. The first step is to get evidence that CG in NPO is more than a concept of compliance.

The cornerstone to start the discussion about an enriched CG for NPO is the fact that these organizations are NPO and pursue special missions. NPO are multiple stakeholder organizations. NPO have no owner but founders. The stakeholders represent the missing owner. A narrow definition of CG is concerned with the enhancement of shareholder value and protection of shareholder interest. The consideration of other stakeholders is not the first interest. The daily business of NPO is the consideration of complementary, conflicting or concurring stakeholder interests. CSR concepts have the range of stakeholders in their attention. In this respect, CG in NPO is in line with CSR.

NPO face the challenge of multiple bottom lines. According to their characteristic as a *not-for-profit-organization*, the financial or economic perspective is the basis of activity, but the main goal is to reach defined task goals which are most of social nature. CSR claims also to reach ecological goals. Such goals could be a prerequisite of the activity of NPO, for example Alpine Clubs in merely all European countries have a statutory commitment to protect the Alpine environment [31]. An environmental interest as basis of all activities of NPO might have to be adopted consciously in statutes or further organizational rules.

NPO as associations have three functions, i.e. the service function for members and further stakeholders. Within this function, non-profits provide services according to their constitution, e.g. education in sport. With the representation of interests, NPO' duty is to represent the interest of minor

groups and as a consequence, influence politics and save availability of special collective goods. Community building as social function and integration of volunteers are vital functions of associations [32]. These three functions resemble the idea of corporate citizenship and are again daily business of NPO.

### VI. CONCLUSION

CG and CSR are two important concepts, and their intertwining has been shown up. Despite this fact, all efforts regarding CSR are of voluntary nature for profit organizations. This means in the end that, without legal pressure, profit organizations are not forced to apply the features of a triple bottom line. They still can focus on the sole profit making goal. On the other hand, NPO already apply several characteristics of the concept of CSR due to their distinctive features and their mission. The thesis that NPO already apply and enriched concept of CG is confirmed.

This scientific paper is the starting point of a deeper investigation in this field. It is to find out why this topic has yet got any interest in the non-profit research.

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