The Unintended Consequences of Stakeholder Scrutiny on Corporate Social Responsibility

The stakeholders of firms engage in a variety of tactics to push firms to behave responsibly in relation to environmental and social issues. For instance, non-governmental organizations (NGOs) organize campaigns and draw media attention to firms' negative impact on the environment and local communities. Similarly, customers boycott products when firms are involved in controversial practices (such as cruelty on animals, long working hours, etc.) directly or indirectly (through their supply chain partners) in development of products. Furthermore, shareholders submit proposals to annual board meetings asking firms to share information on the gender pay gap and the steps taken by firms to address the pay disparity.

Given the rise and prominence of stakeholder scrutiny, various organizational scholars have become interested in examining the effectiveness of stakeholder scrutiny in shaping firms' actions on environmental and social issues (Briscoe & Gupta, 2016; Durand, Hawn, & Ioannou, 2019; McDonnell & King, 2013; Odziemkowska & Henisz, 2021).Whilst the prior studies cover a broad range of stakeholders and social issues, they share a common feature that makes us overlook a distinct way in which stakeholder scrutiny may influence corporate social responsibility (CSR). The common feature is that when studies examine the consequences of activism by stakeholders on a particular social issue, they typically focus on how firms' behaviour changed on that issue (Eesley & Lenox, 2006; Flammer, Toffel, & Viswanathan, 2021; Gupta & Briscoe, 2020). For instance, when examining the impact of protests by NGOs on environmental issues, Hiatt, Grandy and Lee (2015) focus on how firms changed their practices related to oil extraction. Similarly, Briscoe and Safford (2008) and Buchter (2021) focus on firms' diversity practices when studying the impact of activism by employees on diversity issues. In this paper, I depart from this issue-centric approach and highlight that activism may also impact firms' behaviour on non-targeted social issues (i.e., issues unrelated to the issues on which the firms are scrutinized by stakeholders). In other words, I shift attention to an unintended consequence of stakeholder scrutiny on CSR.

In this paper, I hypothesize that exposure to stakeholder scrutiny on a specific social issue will increase firms' performance on unrelated social issues. To develop this hypothesis, I start with emphasising the possibility that firms sometimes may not have sufficient incentives and resources to change their behaviour on the targeted social issue (i.e., the issue on which firms are facing scrutiny from stakeholders). In such circumstances, firms may engage in strategic deflection whereby they improve their behaviour on non-targeted social issues to shift stakeholders' and wider society's attention away from firms' behaviour on the targeted social issue. This strategic deflection can serve as an impression management tactic whereby firms can avoid conceding to activists and yet giving the impression of caring for societal concerns. Furthermore, increasing performance on non-targeted social issues may help firms improve their reputation on those social issues and hence compensate for the loss of reputation on the targeted social issue. In light of the above considerations, I contend that firms may view this issue-oriented strategic deflection as a viable response to increase in stakeholder scrutiny on a social issue.

To test the above hypothesis, I exploit the unexpected leak of Panama Papers and Bahamas Papers in 2016 that increased stakeholder scrutiny of firms on a specific social issue: the use of offshore tax havens. Although prior research on stakeholder scrutiny has not typically focused on the use of offshore tax havens, this issue shares similar features as the other social issues (such as environmental pollution, diversity, human rights, etc.) typically studied. Like other social issues within the umbrella of CSR, using offshore tax havens is not illegal but at the same time questionable as such behaviour deprives government of tax revenue crucial to sustaining the economic development and prosperity of the country. The leak of papers created headlines and exposed the names of various firms making use of shell companies in offshore tax havens. In this paper, I consider the firms mentioned in the leaks of 2016 to be experiencing increased stakeholder scrutiny regarding their use of tax havens. Thereafter, I examine how this stakeholder scrutiny on a targeted social issue influences firms' behaviour on non-targeted social issues (such as environmental policies, diversity, human rights, etc.). Compared to a control group of firms (i.e., firms not named in any leaks), firms named in Panama Papers and Bahamas Papers increased their performance on non-targeted social issues. This empirical finding is based on a quantitative analysis of panel data spanning 2012-2020 and covering 1138 US firms.

Overall, this paper advances our advancing of the relationship between stakeholder scrutiny and corporate social responsibility in two ways. Firstly, this paper shows that the impact of activism by stakeholders on firms' behaviour may extend beyond the social issue on which the activism took place. This finding suggests that without accounting for the unintended consequences of scrutiny on firms' behaviour on non-targeted social issues, we are under-appreciating the impact of stakeholder scrutiny on CSR.

Secondly, this paper adds nuance to the existing claims in the literature regarding how firms use CSR as an impression management tactic (Luo, Kaul, & Seo, 2018; McDonnell & King, 2013; Werner, 2015). Prior studies recognize that activism by stakeholders increases the visibility of firms' negative impact on society, challenges firms' moral standing, and hence threatens firms' reputation among wider stakeholders (Dorobantu, Henisz, & Nartey, 2017; McDonnell & Werner, 2016). As an esteemed image in the eyes of stakeholders is important for firms' access to a wide variety of resources, firms may concede to activists and increase (or commit to increase) their social performance (King, 2008). In this paper, I add a subtle but important extension to this line of reasoning by emphasising the possibility that the increase in social performance may not be issue-specific when appeasing stakeholders and upholding social standing. In other words, I highlight that firms may strategically choose among the social issues when taking actions to diffuse the reputational harm arising from activism. This finding is particularly important from the perspective of activist stakeholders as they rely on the threat of reputational harm to push firms to accede to their demands. When evaluating potential factors that may increase or decrease their ability to get firms to agree to their demands, stakeholders need to be cognizant of this additional impression management tactic – strategic deflection – that firms may employ to counteract the reputational harm posed by activism.

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