UNIVERSITY OF OKLAHOMA

GRADUATE COLLEGE

WHY WON'T THEY LISTEN TO US: STAKEHOLDER PRESSURE,

MANAGERIAL DISCRETION AND CORPORATE SOCIAL PERFORMANCE

A DISSERTATION

SUBMITTED TO THE GRADUATE FACULTY

in partial fulfillment of the requirements for the

Degree of

DOCTOR OF PHILOSOPHY

By

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Norman, Oklahoma
2011

WHY WON'T THEY LISTEN TO US: STAKEHOLDER PRESSURE,
MANAGERIAL DISCRETION AND CORPORATE SOCIAL PERFORMANCE

A DISSERTATION APPROVED FOR THE
MICHAEL F. PRICE COLLEGE OF BUSINESS

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DEDICATION

Dedicated to my father and my mother. You are the force behind me and I will always be grateful to you for keeping me in your thoughts and prayers.

ACKNOWLEDGEMENTS

I would like to thank my dissertation chair, Mark Sharfman. You always listened and had my best interest at heart, and in mind, when providing feedback. From inception to completion of this project, you encouraged my ideas, guided me in my efforts and demanded the best from me in order to make me a better scholar. For all your help and kindness, I am truly grateful and most indebted. I would also like to thank the rest of my dissertation committee: Lowell Busenitz, Laku Chidambaram, Parthiban David, and Lawrence Plummer. I always received excellent advice from all of you which provided unique insights and helped me vastly improve the final product.

A big thank you to all the rest of the faculty at the Price College of Business and the Department of Management and Entrepreneurship in particular. My formal training as a scholar would be incomplete without your efforts. Thank you as well to my fellow doctoral students and to those who have already graduated. All of you provided excellent company, wonderful ideas, and thoughtful suggestions throughout the doctoral program. Not only did it make working with you more fun, but also it allowed us to connect socially. I will surely miss all the good times we had together.

I would like to thank my family, and my wife and kids. Mom and Dad, you gave me the best gift a parent can give their child; an appreciation for knowledge and education. You always wished for me to achieve a terminal degree and you kept me in your thoughts and continually prayed for my success. I appreciate all you have done for me and I hope I can always make you both very proud. My elder sister and my younger brother, both of you set the bar high with your achievements and accomplishments. I

appreciate the encouragement, support, and a bit of sibling pressure that helped me set higher goals and then achieve them. My dear sons, Zayn and Saad, you were always proud of my accomplishments and the fact that your father was studying to become a professor. You always understood when dad worked late or didn't have time to play with you. I owe my sanity and stability during this arduous process to the smiles and cheer your innocence, energy, and laughter brought to me.

Finally Naureen, the love of my life, and the one who truly shares the credit for this dissertation with me. I cannot even imagine undertaking this journey without you by my side. There are no words to express the gratitude I have for your love and constant support throughout the writing of this dissertation and the four years of the doctoral program. You put your own career on hold to allow me to pursue my dreams; I will always remember that gratefully. You rose to every challenge of being the wife of an academic and dealt with my highs and lows while keeping me focused on the important goals and milestones. Any success I will have will be a direct result of you being by my side.

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ABSTRACT

Public corporations are under immense pressure to re-direct resources towards maximizing the value that accrues to non-shareholding stakeholders of the firm. Stakeholders such as employees, customers, suppliers, government, media and the community at large, continually put pressure on firms to improve the corporate social (including environmental) performance (CSP). But do increased stakeholder demands result in subsequent improvements in firms' CSP? In this dissertation, I argue that stakeholder pressure (SP) is successful in enhancing the corporation's sensitivity to stakeholder issues through improvements in the stakeholder governance mechanisms – institutions that safeguard stakeholder interests and maximize stakeholder welfare – within the firm. Using advanced panel-data analysis techniques, I confirm that stakeholder pressure is successful in influencing firms to improve weaknesses in stakeholder governance mechanisms. I also introduce the role of managerial discretion in devising and influencing stakeholder governance mechanisms. I propose and find that stakeholder pressure is less effective in strengthening stakeholder governance mechanisms in organizational and environmental contexts where managers have more room to exercise discretion. Further, stakeholder governance mechanisms partially mediate the relationship between stakeholder pressure and subsequent CSP.

In the second part of the study, I focus on the practical implications of discretionary managerial spending on corporate financial performance (CFP). Stakeholder theory contends that when firms are receptive to stakeholders' demands they can also increase the value accrued to the firms' shareholders. According to this

view, it is possible for a firm to enhance simultaneously both its CSP and its CFP. Yet, after nearly two decades of research on this topic, researchers are divided on the exact nature of the CSP-CFP relationship. I introduce the role of managers in appropriating the benefits arising out of CSP. I propose and test a set of models that include contexts in which managers exercise discretion as moderators of the relationship between CSP and CFP. Results indicate that when rigorous empirical testing is conducted, the CSP-CFP relationship ceases to be statistically significant and is not moderated by managerial discretion contexts.

Finally, I re-investigate the link between CSP and CFP with a particular emphasis on the discretionary nature of CSP spending. Firms may choose to invest in CSP due to a variety of endogenous pressures, and if there is evidence of self-selection by firms to pursue social performance, omission of these antecedents of CSP from an analysis of the CSP-CFP relationship may provide inconsistent results. I propose that researchers investigating the link between CSP and CFP need to correct not only for the endogeneity due to omitted variables, but also for the endogeneity of a firm's decision to engage in CSP. I employ statistical corrections for selection model issues to re-estimate the CSP-CFP link using stakeholder pressure as a predictor of a firm's decision to engage in CSP. I find that once sample selection errors are fixed, CSP is indeed positively related to CFP. Implications, directions for future research and possible extensions are also discussed.

CHAPTER ONE

INTRODUCTION

Overview

Public corporations are under increasing amounts of pressure from society at large to re-direct resources towards the value-maximization of other constituents besides shareholders (Donaldson, 1982). Indeed, in a recent survey, "three-fourths (74%) of Americans say, now more than ever, businesses must show leadership, courage and commitment in keeping corporate citizenship among the top business priorities" (GolinHarris, 2009). In order to ensure that companies do keep corporate citizenship as one of their goals, secondary stakeholders such as government, activist groups, environmental advocates, NGO's and communities attempt to influence a firm's practices and policies through regulatory threats, campaigns, and social movements such as protests and consumer boycotts. There is considerable research that examines the mechanisms of these social movements and their impact on organizational change and outcomes (e.g., Davis, McAdam, Scott, & Zald, 2005; Eesley & Lenox, 2006; Kassinis & Vafeas, 2006; King, 2008; King & Soule, 2007; Lounsbury, 2001; Reid & Toffel, 2009).

Increasingly, researchers have turned their attention towards the primary stakeholders of the firm such as employees, suppliers, buyers and providers of capital who also demand that firms favor their social and environmental interests over pure wealth maximization objectives desired by other shareholders of the firm (Monks, Miller, & Cook, 2004). Because primary stakeholders have direct connections with the firm, they possess legitimate channels such as letter writing, direct communication with

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top management or directors and posing questions at general meetings. These opportunities allow stakeholders to voice their concerns (Hirschman, 1970) regarding strategic decisions which impact the organization's social responsibilities. More formally, those stakeholders of public corporations in the United States who also own shares in the firm, can file proposals on social and environmental issues concerning their firm. Since the 1970's, stakeholders of public corporations in the United States have used these proposals to urge firms to adopt and implement policies that improve corporations' social (including environmental) performance (CSP)[1].

Although a significant majority of large public corporations in the United States are already "stakeholder oriented" (Agle, Donaldson, Freeman, Jensen, Mitchell, & Wood, 2008), the new millennium has seen a sharp increase in the social and environmental nature of demands made to businesses through stakeholder proposals. Indeed, almost half of all stakeholder proposals filed at US public corporations during the first few years of this decade were concerned with social and environmental issues (Monks et al., 2004). This trend is likely to continue; impending institutional changes approved by the Securities and Exchange Commission (SEC), which regulates stakeholder proposal activity in the United States, are a harbinger of vigorous stakeholder proposal seasons in the future (Sweeney, 2010). Because stakeholder proposal activity is on the rise, organizational researchers are also increasingly interested in stakeholder actions, plus organizational responses to stakeholder proposal

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[1] For the purpose of this dissertation CSP will refer to a corporation's performance on both social and environmental fronts. Managing relations with customers, suppliers, buyers and the community at large, ensuring fair pay, improved work environment, non-discrimination at job etc. are described as social issues. Avoiding business in "sin" industries and countries, reducing emissions, preparing sustainability reports, gearing up for climate change and ensuring corporation's actions do not inflict harm on the general external environment etc are considered environmental issues.

activism (Laplume, Sonpar, & Litz, 2008; Sjöström, 2008). For example, what are the outcomes of stakeholder demands? Is the pressure exerted by stakeholders successful in inducing change in the way businesses operate? What changes in organizational structure does stakeholder pressure induce to succeed in influencing corporate policies and strategy? What are the implications of stakeholder pressure for the target corporation's social and financial performance? Thus far, prior research on the results of stakeholder activism reveals mixed views, provides conflicting results and offers unclear answers to most of the questions raised above.

On one hand, researchers suggest that businesses do factor stakeholder pressures in their decision making (Berry & Rondinelli, 1998). By being responsive to social and environmental concerns, firms garner the support of stakeholders, reduce input costs, acquire legitimacy, and avoid negative publicity and/or adverse regulation (Bansal & Roth, 2000; Chiu & Sharfman, 2009; Sharfman & Fernando, 2008). On the other hand, some researchers conclude that in general, because most proposals are unsuccessful, activism simply "lack[s] the power to create significant corporate change" (Haigh & Hazelton, 2004: 59). Increasingly, it is argued that stakeholder activism may not be an effective tool for influencing firm strategy or outcomes (Sjostrom, 2008). Millions   of people invest in public firms, and in present times, are also increasingly anxious about the prospects of their investment bringing about greater social good. Because links between stakeholder activism and corporate social performance remain mixed, it would be useful to investigate the impact of stakeholder-oriented proposals on a firm's social and environmental "bottom line".

In this dissertation, I explain the conflicting conclusions of prior research by introducing the role of corporate managers in shaping the firm's response to shareholder proposals. Corporate managers control most of the corporate resources which are necessary to achieve the objectives targeted by stakeholder initiatives (Frooman, 1999). Because managers hold a central position in the organization, they usually decide the setting of CSP strategy and the disbursement of funds for CSP investments. Seminal research on top manager strategic decision-making suggests that managers exercise flexibility in decision-making (Sharfman & Dean, 1997), and tremendous discretion or "latitude of managerial action" (Hambrick & Finkelstein, 1987: 371) over strategy formulation and resource allocation activities. Although in public corporations, directors hold the fiduciary responsibility of representing stakeholder interests, top managers have huge informational advantages over directors. CEO's are intricately involved and exercise considerable control over the selection of directors (Monks & Minow, 1995) and subsequent committee decisions sometimes involving even their own compensation (Johnson, Porter, & Shackell-Dowell, 1997). Managers also have their own goals, e.g., minimizing their employment risk (Amihud & Lev, 1981), or maximizing their power, prestige, and salary (Hambrick & Finkelstein, 1995). Therefore, to study the effect of stakeholder activism on CSP requires the inclusion of the "role of managers as a party with specific interests"(Tirole, 2001: 25); interests which may often collide with those of both firm owners and other stakeholders (Jensen & Meckling, 1976).

In this study, I propose that changes in the firm's response to stakeholder pressure are shaped by managerial influences. I also explain that it is possible for

stakeholder pressure directed at the improvement of a firm's CSP to often end up only strengthening the stakeholder governance control mechanisms - "the design of institutions that induce or force management to internalize the welfare of stakeholders" (Tirole, 2001: 4) within the firm. Managerial discretion contexts shapes the creation or effectiveness of stakeholder governance mechanisms resulting from stakeholder pressure. The strength of stakeholder governance mechanisms in turn may impact the subsequent level of CSP by the firm. To test this theory, I model the role of managerial discretion contexts as a moderator between the stakeholder pressure and stakeholder governance relationship. Figure 1 shows the models that were tested in this section of the dissertation.

Next, I focus on the practical implications of the discretionary nature of CSP spending by studying the relationship between corporate social performance (CSP) and corporate financial performance (CFP). Nearly two decades of research on this topic has revealed mixed findings (Orlitzky, Schmidt, & Rynes, 2003) and the debate is still wide open. Studies relying on stakeholder theory argue that satisfied stakeholders are key to improving the organization's overall effectiveness which, in turn, leads to improved financial performance (Donaldson & Preston, 1995). Motivated employees, committed suppliers, and loyal buyers are more cooperative towards firms which project a socially superior image. Accordingly, such stakeholders increase their value-enhancing contributions to the firm enabling a simultaneous increase in CSP and CFP (Dutton, Dukerich, & Harquail, 1994; Greening & Turban, 2000). On the other hand, research from the agency and rent appropriation perspectives suggests that powerful stakeholders may accrue significant unobserved benefits generated by competitively advantaged

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FIGURE 1

Stakeholder Pressure, Managerial Discretion Stakeholder Governance and CSP
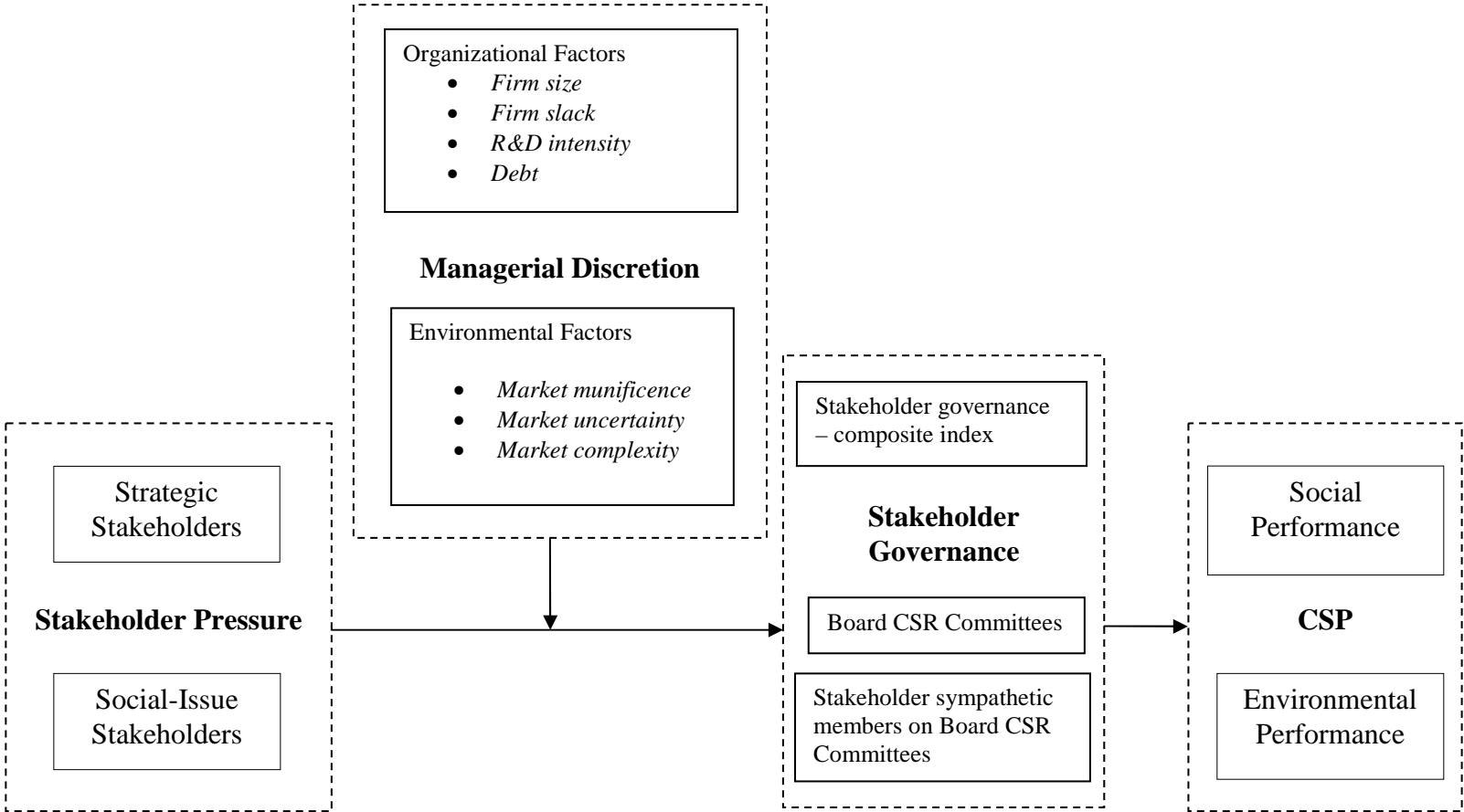
firms, thereby leading to reduced levels of observed financial performance (Coff, 1999; Surroca & Tribó, 2008). Investigations launching on both these views have overlooked at least one theoretical and one empirical consideration. The first issue concerns the role of managers in controlling benefits arising out of CSP. The second issue stems from the discretionary nature of CSP spending and the omission of relevant antecedents to CSP from estimation of models investigating the CSP-CFP link.

First, the central role of managers in controlling CSP investments provides a compelling argument for including managerial discretion contexts in a model investigating the CSP-CFP relationship. I address this issue by testing a model of the CSP-CFP link with managerial discretion contexts as a moderator. Second, firms may choose to invest in CSP based on a variety of relevant antecedents (Chiu & Sharfman, 2009). Some of these antecedents may in turn influence corporate financial performance. Omission of relevant CSP antecedent variables from an investigation of the CSP-CFP relationship introduces a specification error in our models inducing a sample-selection bias in our estimates (Heckman, 1979). Proceeding to estimate such models without applying proper statistical corrections would lead to an endogeneity problem and results in incorrect inferences drawn from inconsistent estimates (Greene, 2008). I therefore explicitly include the decision to invest in CSP by using the Heckman selection model (Heckman, 1979). Specifically, in the first stage, I test whether the decision to invest in CSP is indeed endogenous. If statistical tests confirm my hypothesis, I model the CSP-CFP relationship after controlling for the factors impacting the CSP investment decision. Figure 2 shows the models tested in this section of the dissertation.

FIGURE 2

CSP and Performance: The Role Of Managerial Discretion and CSP Antecedents

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Organizational Factors
Firm size
Firm slack
R&D intensity
Debt

Managerial Discretion

Environmental Factors

Market munificence
Market uncertainty
Market complexity

Organizational Factors
- *Firm size*
- *Debt*
- *Performance*
- *Firm slack*
- *R&D intensity*

CSP Antecedents

Stakeholder pressure

Social
Performance

CSP

Environmental
Performance

ROA/ROS/ROE

**Financial
Performance**

Tobin's Q

Importance of This Research

The first contribution of this study is a clarification of the role played by managers in devising and implementing CSP initiatives proposed by stakeholders. Most previous research implicitly assumes away this role or fails to explicitly model it in empirical investigations. In this study, I include managerial discretion contexts as a moderator of the stakeholder pressure and CSP relationship. In effect, I attempt to answer the question of not only whether managers matter, but illustrate how exactly do they matter. Activist stakeholders are desirous of engendering change within the organization; this study informs stakeholders of the consequences of their efforts and why they may or may not see the results of their activism.

The second contribution of this study is to show that although stakeholder proposals are targeted at improving the firm's ultimate CSP, change takes the path through the design and enhancement of stakeholder governance mechanisms; a process which is influenced by managerial discretion. Specifically then, this study confirms the direct effects of stakeholder pressure on the stakeholder governance mechanisms and the moderating role of managerial discretion. Research often focuses on corporate governance mechanisms as indicators of how well the firm governs issues related to stakeholders. This study clarifies why these two may not be synonymous, and why stakeholder governance should be treated as a distinct construct in studies of stakeholder activism and CSP. In testing the activism and stakeholder governance relationships, this study includes measurable indicators of stakeholder governance which may benefit future research on the topic.

The third contribution of this research is to provide further empirical clarity to the ambiguity surrounding the CSP-CFP relationship. If the decision to invest in CSP is determined to be endogenous, this study will provide evidence that prior empirical investigations using similar data may suffer from a specification error. This may help explain the non-significant relationship observed in many studies and offer compelling reasons for future researchers investigating the CSP-CFP link to explicitly model the endogeneity of the CSP decision in addition to the endogeneity due to omitted variables. A resolution to this debate also has theoretical and practical implications. For management researchers, evidence of a positive relationship between CSP and CFP will provide empirical support to arguments made in favor of instrumental and agency stakeholder perspectives (Donaldson & Preston, 1995; Freeman & Evan, 1990). A negative relationship between these two constructs will provide more credence to agency theory perspectives (Friedman, 1970; Jensen, 2001). Finally, if a relationship does not exist, the rent appropriation perspective would seem to provide the best theoretical lens to further examine the CSP and CFP relationship. For management professionals, shareholders and stakeholders, evidence of the exact implications of CSP spending on CFP will help untangle the gridlock in which these groups often find themselves battling over resource allocation decisions.

The fourth and final contribution of this research is the specific acknowledgement of the role of managers in impacting the value that accrues to stakeholders. Again, the intent of this study is to show that even if sometimes the CSP-CFP relationship is inconclusive, it is not because there is no underlying association between the two constructs. It is because managers possess tremendous latitude in their

actions and can appropriate the excess value generated by satisfied stakeholders, thereby reducing the levels of observed CFP.

Overall then, this study highlights the central role of managers in devising and implementing corporate strategies such as CSP. Contexts in which managers possess greater latitude in decision making are shown to impact not only the formation and strength of stakeholder governance mechanisms, but the resulting corporate social performance and the ensuing benefits accrual into corporate financial performance.

Organization of This Dissertation

This dissertation proceeds as follows. In Chapter Two (Literature Review and Hypotheses), I present a review of relevant stakeholder pressure, stakeholder management, managerial discretion and corporate social performance literatures. After presenting the literature reviews, I develop two sets of hypotheses. The first set of hypotheses link stakeholder pressure with stakeholder governance. I present hypotheses for the moderating role of managerial discretion on the relationship between stakeholder pressure and stakeholder governance and on the relationship between stakeholder pressure and corporate social performance. In the second set of hypotheses, I propose that the relationship between CSP and CFP is moderated by managerial discretion contexts, and that the decision to invest in CSP is endogenous. In Chapter Three (Methods), I describe the data, sample, and variable construction and the general analysis techniques I employed. In Chapter Four (Results) I explain the research methodology applied to test each hypothesis and present the results of the analysis. Finally, in Chapter Five (Discussion), I provide a discussion of the findings, some avenues for future research and a conclusion.

CHAPTER TWO

LITERATURE REVIEW AND HYPOTHESES

In this chapter, I present a review of the literature on stakeholder activism and its outcomes. In the first section of this chapter, I specifically address the most formal type of stakeholder activism: stakeholder pressure on the organization through proposal writing. I introduce the concept of stakeholder governance mechanisms – institutions designed to align managers' interests with those of stakeholders, as a distinct concept from corporate governance which describes control mechanisms designed to oversee managers for the purpose of safeguarding shareholder wealth. I develop hypotheses to link stakeholder proposal activism with the strength of stakeholder governance mechanisms. I then introduce the moderating/mediating role of managerial discretion in shaping the stakeholder governance mechanisms. I complete the first section of this chapter with development of hypotheses linking stakeholder pressure, stakeholder governance mechanisms and corporate social performance using hypotheses that model the moderating role of stakeholder governance mechanisms and managerial discretion. Figure 1 displays the layout of the proposed theoretical model.

In the second section of this chapter, I revisit the debate on the nature of the link between corporate social performance (CSP) and corporate financial performance (CFP). I explain that previous research may have overlooked the possibility of CSP investment decisions being endogenous. I offer methodological suggestions on how to obtain more consistent estimates of the impact of CSP on CFP. I argue that managerial discretion contexts can allow managers to shape or even absorb the "good" that comes

out of a firm's CSP. Figure 2 displays the layout of the proposed theoretical model for this section of the chapter.

Stakeholder Activism – Why Now?

Economic growth in the United States has led to improved standards of living, quick dissemination of information, increased awareness and high societal expectations of the responsibilities of corporations towards the larger environment within which they operate (Reilly, 1990). Public corporations are under increasing amounts of pressure from society at large to re-direct their resources towards the value-maximization of other constituents besides their shareholders (Donaldson, 1982). Despite the recent downturn in the economy, public perception of the role of business remains squarely focused on the social and environmental responsibilities of the firm. Indeed, in a recent survey, "three-fourths (74%) of Americans say, now more than ever, businesses must show leadership, courage and commitment in keeping corporate citizenship among the top business priorities" (GolinHarris, 2009: 2). Organizations are accountable to their stakeholders more today than ever and cannot just turn away from societal demands by treating them as a cost of doing business (Wood, 1991). Indeed the long term viability of corporations depends on addressing the needs of all stakeholders, which makes social and environmental issues an essential component of the modern corporation's new "bottom line" (Heath & Palenchar, 2009).

In order to ensure that corporations remain cognizant of their social and environmental responsibilities, and stay committed to resolving social and environmental issues, secondary stakeholders such as activist groups, environmental advocates, NGO's and communities attempt to influence a firm's practices and policies

through regulatory threats and social movements such as protests and consumer boycotts. Past research has closely examined the mechanisms of social movements and their impact on corporate decision-making (Davis et al., 2005). For example, research suggests that it is possible for social movements to influence organizational policies towards their employees (Scully & Segal, 2002). Secondary stakeholder groups, such as communities, can influence organizations to become more cognizant of their environmental footprint, adopt recycling programs and reduce pollution (Eesley & Lenox, 2006; Kassinis & Vafeas, 2006; Lounsbury, 2001; Reid & Toffel, 2009). Social movements such as protests and consumer boycotts, attempt to influence corporate policies by threatening to draw negative attention towards the organization's lack of corporate social performance. Negative publicity for the firm is a hurdle to recruiting top talent or to attract investments from socially concerned investors (Turban & Greening, 1997). Research confirms that consumer boycotts and protests can indeed negatively impact corporate financial performance indicators such as stock prices (King, 2008; King & Soule, 2007; Pruitt, Wei, & White, 1988).

However, not all external pressures are successful in influencing organizations and in achieving activists' goals (Johnston, 1994). Members of stakeholder groups often vary in their awareness, ability and initiative in championing social causes (Rowley & Berman, 2000). Activist groups may have divergent or even competing interests which complicates the attainment of broad agreement on the priority of issues to be raised, and the exact mode of pressure to apply on target organizations to achieve desired objectives (Mark, Irene Hanson, & Kimberly, 2004; Wolfe & Putler, 2002). There is a high probability of a lack of commonality in goals, economic interests, vision, and the

assessment that the organization will be receptive to activism, which further impedes collaboration among stakeholder groups (Butterfield, Reed, & Lemak, 2004). Because secondary stakeholder do not control valuable resources required by the organization to operate, succeed or survive, they may lack the visibility, legitimacy and salience in the minds of managers and hence may lack the power to bring about change within the organization through activism (Agle, Mitchell, & Sonnenfeld, 1999; Frooman, 1999; Mitchell, Agle, & Wood, 1997). For all these reasons, scholars are increasingly turning towards alternate mechanisms that stakeholder groups employ to make their demands more salient to the organization; stakeholder activism through proposal writing is one such mechanism.

Stakeholder Proposals

Stakeholders desirous of voicing their concerns regarding an organization's CSP can engage in social activism through a variety of ways. They can directly communicate with top management or directors, ask questions at general meetings, write letters, or, if they own shares in the company, formally file stakeholder proposals. A stakeholder proposal[2] is a written (not exceeding 500 words) recommendation, requirement or demand that the company (board of directors and/or top management) take certain actions. For example:

> *"A proposal can ask a company to adopt a human rights policy, to issue a report on how it plans to mitigate risks pertaining to greenhouse gas emissions or to implement ethical codes of conducts for its supply chain"* (Sjöström, 2008)

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[2] For the purpose of this dissertation, the term "stakeholder proposals" will refer to those proposals which raise social and environmental issues. These proposals are filed by equity holders with the express aim of pressuring the firm to maximize its CSP. By contrast, the term "shareholder proposals" will be used for proposal activity that targets corporate governance issues within the firm with the ultimate aim of safeguarding shareholder wealth.

Stakeholder proposals can be filed by individuals and groups who hold at least $2000 or 1% of shares of a public corporation continuously for one year; owners of share have to demonstrate their eligibility for filing the proposals (Logsdon & Van Buren, 2008; O'Rourke, 2003). Once a properly filed proposal is received, firms may decide to accept or reject it based on its relevance to the firms' mission and objective, and the feasibility of acting upon the suggestions. If accepted, the issue raised in the proposal has to be included in the proxy reports of the firm and is voted upon by all shareholders in the company's next general meeting. A proposal which receives a majority vote from all shareholders is still non-binding, and may be implemented subject to the approval of management and the board of directors.

Stakeholder activism through proposal writing has at least four benefits over stakeholder activism through social movements. First, anyone who owns the requisite number of shares in the organization can submit a stakeholder proposal, which holds the same legal importance as proposals submitted by large stakeholders. This empowers stakeholders to attempt to bring social change through individual action without having to create a consensus among a broader group for collective action. Second, activism through proposal writing is a legal channel of communication (Mathiasen, 2004). Managers have a fiduciary responsibility to attend to the demands of those stakeholders who own equity in the firm (Eisenberg, 1976). Written proposals require a response by managers which forces them to acknowledge the issues being raised and to submit their responses on record. The proposal mechanism thus allows stakeholders to extract formal written responses from managers to issues managers may not otherwise address directly. Third, managers are known to be more receptive to the demands of salient

stakeholders than those of stakeholders who do not command importance in their view (Agle et al., 1999; Mitchell et al., 1997). Through proposals, activists can communicate and garner the support of other shareholders which increases the bargaining power of the stakeholders behind the initially submitted proposal and enhances the salience of the issue under consideration. Proposals are an efficient method of achieving this objective because regulation requires corporations to bear all costs of disseminating proposals through proxy statements using the corporation's communication channels. Finally, research suggests that stakeholder activism through proposal writing is also a preferred vehicle for social movement stakeholders. Activists, NGO's, unions, and special interest groups often purchase shares in organizations they are targeting for protests in order to alert managers to their demands and to make their demands more salient and legitimate in the eyes of top management and other stakeholders (Anderson, Ramsay, Marshall, & Mitchell, 2007; Guay, Doh, & Sinclair, 2004; Hoffman, 1996).

Outcomes of stakeholder proposals. Prior literature provides a mixed picture of the success of stakeholder proposals in bringing about changes in corporations' social performance. On one hand, some researchers have expressed optimism over the influence of stakeholder activism on corporate policy. Research suggests that firms garner the support of stakeholders, acquire legitimacy, reduce input costs, and avoid negative publicity and/or adverse regulation when they demonstrate responsiveness to social and environmental concerns (Bansal & Roth, 2000; Chiu & Sharfman, 2009; Sharfman & Fernando, 2008). The expectation of such benefits compels businesses to factor stakeholder pressures in their decision making (Berry & Rondinelli, 1998). Specially, since institutional investors increasingly pressure firms to address social

issues, the salience of CSP issues for firms has also increased (Sparkes & Cowton, 2004). This has led some scholars to opine that the more stakeholders press organizations for CSP, the more likely it is that organizations will increase their CSP (Campbell, 2007).

On the other hand, some researchers argue that because suggestions included in stakeholder proposals are non-binding and subject to process-constraints, passage of proposals remains difficult, if not impossible (Engel, 2006). Indeed, when put to a vote, the majority of stakeholder proposals fail to get even 10% support from other shareholders (Logsdon & Van Buren, 2008). Other researchers suggest that it matters little whether a proposal gets accepted, rejected or settled outside of the voting process; "no real changes to core policies are made" in response to stakeholder activism (David, Bloom, & Hillman, 2007: 98). These dismal results have led some researchers to conclude that most proposals go unsuccessful and can hence be declared a failure. In short, shareholder activism 'lack[s] the power to create significant corporate change' (Haigh & Hazelton, 2004: 59). There is therefore a growing doubt among some researchers concerning stakeholder activism as an effective tool for influencing corporations' strategies towards improving their social and environmental performance (Lawrence & Morrell, 1995; Sjöström, 2008).

In general, past research on the affect of stakeholder pressures on firms to increase their corporate social performance has adopted a social-movement theoretical lens and largely predicted outcomes based on institutional perspectives. However, the mixed findings in the literature reveal that existing theoretical approaches may be insufficient to fully explain the impact of stakeholder pressure on CSP. Whether

stakeholders have been insisting on the wrong set of outcomes (Kerr, 1995) or researchers have ignored other possible outcomes besides an improvement in CSP also remains an open question. Research on the outcome of shareholder activism – proposals filed by equity holders to improve the corporation's financial performance, holds the potential to inform these questions. As previously stated, in this dissertation, I draw a distinction between stakeholder and shareholder activism; thus far, both have largely been treated as homogenous types of investor activism.

Some intriguing parallels can be drawn between research on stakeholder activism – equity holders' pressure on firms to focus on social and environmental issues, and shareholder activism – suggestions by shareholders directing management and directors towards safeguarding shareholder wealth. Both kinds of activism emanate from an inherent difficulty of measuring the effectiveness of managerial strategy in implementing the desires of the owners of the firm. Below, I describe briefly the similarities and differences between these two types of activism, provide a brief overview of the literature on stakeholder pressures and explain how adopting the more agency-theoretic predictions from the shareholder literature can help us predict possible outcomes of stakeholder pressure on firms.

Shareholder Activism – Purpose and Outcomes

In contrast to the stakeholder activism literature, shareholder activism literature has largely viewed activism antecedents and outcomes through an agency theory lens. In public corporations, shareholding owners (or principals) are separated from organizational control and decision-making activities (Berle & Means, 1932). Professional managers (or agents of shareholders), usually hold information

superiorities over shareholders and are therefore entrusted to make strategic decisions for the firm. A central tenet of agency theory is that managerial agents and shareholding principals have divergent predilections towards the allocation of firm resources (Ross, 1973). Agency theorists argue that not all managerial decisions maximize shareholder wealth; because managerial pay and prestige is tied to firm growth, self-interest compels them to minimize their employment risk and maximize their own compensation by often engaging in projects that destroy shareholder value (Amihud & Lev, 1981; Baumol, 1967; Hambrick & Finkelstein, 1995; Jensen, 1986; Jensen & Meckling, 1976; Marris, 1964). Shareholders therefore appoint a board of directors delegated with a fiduciary responsibility to represent shareholder interests within the organization, and to oversee and advise managers in setting corporate strategy (Easterbrook & Fischel, 1991). All publicly held corporations in the United States, regardless of size, are required by the various corporate laws of their state of incorporation to have a board of directors. Thus the board of directors, with its power to hire, compensate and fire managers, has assumed the central role in the corporate governance of US firms (Finkelstein & Hambrick, 1996; Jensen, 1993).

The ultimate goal of shareholders is the protection and maximization of their wealth, but it is difficult, or too costly, for non-specialist shareholders to ascertain the real consequences of professional managers' strategic decisions for shareholder wealth protection and maximization. In search of an optimum solution to "control" managers, shareholders entrust the board of directors to both incentivize and monitor managers. Directors in turn employ means ranging from salaries, commissions, and stock options to conducting regular meetings to discuss strategies plus review objectives and

performance targets (Eisenhardt, 1985, 1989). To this end, various corporate governance mechanisms that address the structure of managerial compensation, board-compensation independence and diversity, and safeguards against managerial entrenchment have been enacted and perfected within the firm (see Shleifer & Vishny, 1997 for a review). These mechanisms are specifically designed to protect shareholders by ensuring that managerial actions and board oversight are harmonious with shareholder desires of protecting and growing their investments in the firm.

If shareholders suspect that despite the existence of these corporate governance controls, the actions of board members or management threaten shareholder goals, they engage in activism through proposal writing to inform directors (and top management) of their concerns. A review of the shareholder activism literature indicates that while activism may not always result in the long term improvement in operational and financial efficiency of the firm, it may be successful in achieving governance changes within companies (Gillan & Starks, 2007). This has led to the conclusion that rather than achieve directly the primary objective of protecting and maximizing shareholder wealth, activism can help strengthen corporate governance mechanisms within the firm. Corporate governance mechanisms in turn help shareholders monitor and incentivize managers to keep shareholder goals paramount in managerial decision making (Davis & Thompson, 1994). For example, shareholder proposals can "call for firms to rescind poison pills, reject paying "greenmail", require confidential voting, or make other changes in the rules that govern relations between shareholders, directors, and top-level managers" (Karpoff, Malatesta, & Walkling, 1996: 366). Shareholder activism is hence best understood as a conduit for both dispersed and organized shareholders to

strengthen the corporate governance mechanisms within the firm for the ultimate goal of safeguarding shareholder wealth.

Below, I describe how theoretical approaches employed in shareholder activism research can be applied to stakeholder activism to better understand its outcomes. Stakeholder activism research has so far focused on the ultimate improvement in CSP as the primary result of stakeholder pressure. Perhaps other internal changes within the firm are a more plausible outcome of stakeholder activism.

Stakeholder Activism - Purpose and Outcomes

Stakeholders desirous of bringing social changes through firm actions are relatively more dispersed than those shareholders interested in safeguarding their wealth. While shareholder activism is dominated by large blocks of shareholders such as pension funds, mutual investment groups, and insurance funds, stakeholder activism is usually spearheaded by individuals, religious organizations such as the Interfaith Council on Corporate Responsibility (ICCR), NGOs, or other groups acting on behalf of a group of stakeholders with common interests (Campbell, Gillan, & Niden, 1999; Monks et al., 2004). It is much harder for individual stakeholders to measure quantitatively the true impact of a firm's efforts to maximize the welfare of its constituents such as employees, suppliers, or buyers than to assess its financial performance (Coff, 1999; Tirole, 2001). Whereas, volatility in the income stream or market value of firms instantly draws attention from analysts, only egregious departures from stakeholder social and environmental agendas are punished by litigation (Kassinis & Vafeas, 2002). This allows managers to pursue stakeholder value-destroying initiatives without much concern for being reprimanded for their actions.

From an agency theory perspective, the information asymmetry between management and stakeholders is even more egregious than that between shareholders and managers. Recall that shareholder activism attempts to minimize this information asymmetry by designing and strengthening several corporate governance mechanisms within the firm which serve to monitor and incentivize managers. Similarly, I propose that in order to investigate the impact of stakeholder activism, it is reasonable to turn our attention towards those corporate governance mechanisms within the firm which facilitate the monitoring and incentivizing of managers to minimize the information asymmetry and to maximize the corporate social and environmental performance of the firm. Next, I describe why internal control mechanisms directed exclusively at improving the social performance of firms are required to supplement the prevailing corporate governance mechanisms, which are designed specifically for the purpose of safeguarding shareholder wealth in the firm.

Stakeholder Pressure and Stakeholder Governance

Since social and environmental issues have gained increasing importance, visibility, and legitimacy in the minds of stakeholders, pressure is mounting on firms to be better corporate citizens (Chiu & Sharfman, 2009; Sharfman, 1994). In response, organizations are scrambling to alter their corporate governance mechanisms to also address social issues. However, a conflict remains in the objective function between these two modes of governance (Jensen, 2001). While both normative and instrumental stakeholder theorists contend that shareholder wealth maximization and stakeholder welfare are mutually achievable goals, and by extension, corporate governance mechanisms can also be helpful in fostering socially responsible behavior (Donaldson

& Preston, 1995; Freeman, 1984; Freeman, Wicks, & Parmar, 2004), agency theorists of a more rational leaning argue otherwise (Friedman, 1970; Jensen, 2001; Sundaram & Inkpen, 2004). Ambiguity in understanding the causal mechanisms through which CSP is linked with financial performance (Orlitzky et al., 2003), and evidence that managers often "hide" behind such spending to earn personal benefits, often banishes CSP to the realm of an agency problem for the firm (Jensen, 2001). Thus, from a stakeholder perspective, traditional corporate governance mechanisms are paradoxically ineffective in controlling supposedly wasteful spending by encouraging the same.

The ambiguity over the efficacy of corporate governance mechanisms in enhancing firms' CSP also adds to the complexity in understanding the outcomes of stakeholder's activism. Corporate governance mechanism have evolved to further only one agenda; the protection and maximization of shareholder wealth (Shleifer & Vishny, 1997). Most corporate governance measures, by design, do not help stakeholder activists' broad social and environmental causes. For example, research indicates that strong corporate governance, such as ownership and general board structure, plus safeguards against managerial entrenchment, work to reverse investments in CSP and steer them towards the corporate goal of shareholder wealth protection (Barnea & Rubin, 2010; Brammer & Millington, 2005; Surroca & Tribó, 2008). Other evidence suggests that even when corporate governance mechanisms are successful in inducing better social outcomes, they may only be effective in eliciting firm responses along narrow strategic dimensions which may only help a select few stakeholders (Johnson & Greening, 1999; Kacperczyk, 2009). It follows then that corporations' conception of governance structures for corporate social responsibility, or "the design of institutions

that induce or force management to internalize the welfare of stakeholders" (Tirole, 2001: 4), should be treated separately from studies of the effect of existing corporate governance mechanisms on firms' CSP. Next, I briefly describe the limited existing work on the topic of governance mechanisms designed exclusively to improve the corporate social performance of firms.

Stakeholder governance mechanisms. Research on stakeholder activism targeting organizations' corporate social performance is still growing (Sjöström, 2008). A literature review indicates that most studies that have addressed the emergence of those corporate governance measures which explicitly safeguard the social interests of stakeholders, use a case analysis methodology (e.g., De Wit, Wade, & Schouten, 2006; Lovdal, Bauer, & Treverton, 1977; Mackenzie, 2007; Ricart, Rodríguez, & Sánchez, 2005; Spitzeck, 2009)[3].

Earlier in this dissertation, I pointed out that the shareholder activism literature indicates that not all proposals are accepted; some proposals are withdrawn because stakeholders manage to acquire some support from the firm for making the requested changes. Because institutional and social pressures are usually successful in creating structural changes within the organization (Greening & Gray, 1994), often the changes agreed upon by managers occur in those mechanisms within the firm which are designed to ensure that a particular social objective is met in the future. Prior research shows that stakeholder proposals usually ask for general changes in codes within organizations rather than focus on specific desired outcomes (Proffitt & Spicer, 2006). Stakeholder activists themselves do not anticipate the entire proposal to be accepted and

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[3] Of these studies the only empirical study was conducted by Spitzeck (2009) on firms in the United Kingdom.

implemented; they are prepared to accept a thoughtful response and indication that the firm will continue to pursue the issues raised (IRRC, 1993: 1). There is also evidence that even if proposals are successful, rather than creating long term change, they force the organization to make minor internal adjustments (O'Rourke, 2003). Specifically, the argument is that the greater the pressure of stakeholders on the organization, the more the organization will strengthen its internal control systems. It follows then that rather than directly achieve the objective of increased CSP, stakeholder pressure may be successful in achieving changes in internal control mechanisms that govern managerial interests and behaviors such that they become more aligned with stakeholders than shareholders.

H1: Stakeholder pressure is positively associated with the subsequent

overall strength of stakeholder governance mechanisms within the firm.

Somewhat similar to corporate governance mechanisms, stakeholder governance can also encompass several mechanisms of incentives and allocation of control rights which may each help re-align managerial interests with those of stakeholders demanding social changes. Absent any large legal restrictions on managers to pursue social and environmental initiatives, and an unclear impact of CSP spending on firm financial performance (Orlitzky et al., 2003); it is reasonable to consider that stakeholders might prefer control mechanisms to align managers with stakeholder demands. Drawing on research on the impact of corporate governance mechanisms on CSP, I present two such control mechanisms that might improve the monitoring of social issues within the firm and hence hold the potential to become an outcome of stakeholder pressure.

Corporate social responsibility (CSR) board committees. From an agency theoretic perspective, dispersed stakeholder principals are in no position to assess correctly the impact of managerial agents on the social and environmental performance goals of the firm. The board of directors thus becomes a de-facto tool for stakeholders to evaluate and compensate managers for their role in furthering stakeholder objectives. However, "[t]he work of the board is done in committees" (Lorsch & MacIver, 1989: 59). Board committees allow the delegation of board responsibilities to smaller groups of board members facilitating the separation of tasks and functions. For example, the compensation committee is ubiquitous in modern public corporation boards. Together with the audit committee, the compensation committee performs the role of evaluating CEO performance and designing appropriate incentives to ensure CEO's do not stray from the shareholder wealth protection objectives of the firm (Conyon & Simon, 1998; Laux & Laux, 2009). Special board committees have been a favorite tool of shareholder activists to ensure specialist board members can oversee professional managers, and for organizations to signal their legitimacy to regulatory bodies such as the SEC (Harrison, 1987).

Evidence from UK suggests that the use of corporate responsibility board committees to incorporate corporate responsibility issues is on the rise (Spitzeck, 2009). An examination of board composition of US corporations also indicates the emergence and prevalence of committees for the purpose of augmenting existing committee board structures (Evan & Freeman, 1993). CSR board committees are entrusted with insuring that the corporation complies with its social responsibility policies and standards and that adequate controls are in place to monitor management is complying with social

objectives (Cochran & Wartick, 1988). Mackenzie (2007) explains that CSR board committees are responsible for reviewing CSR issues, specially issues that may have a potentially negative impact on the company's business and reputation plus which pose financial risks to the firm (Ricart et al., 2005). CSR committees also review company's external reporting on issues of social concern (Lovdal et al., 1977).

Stakeholder proposals are intended to highlight social issues and regular board committees are generally designed to provide traditional corporate governance oversight. Therefore, it is likely that stakeholders attribute the firm's lack of attention to social and environmental performance to an absence of concern within the firm for social and environmental issues. Research shows that the mere existence of special board committees directed towards improving CSP can signal to concerned stakeholders that the firm is indeed responsive to their demands (Greening & Gray, 1994). It follows then, that under pressure from stakeholder activists, the firm may find it beneficial to create committees that specifically address stakeholder issues. Stakeholder pressure may thus result in the creation of dedicated CSR committees. Or formally,

H2: Stakeholder pressure is positively associated with the subsequent presence of CSR board committees in the firm.

CSR board committee composition. The composition of the board of directors is instrumental in assessing the effectiveness of managerial strategy (Baysinger & Hoskisson, 1990). Likewise, the composition of the committee could also be seen as a legitimate target for shareholder activism. Most committee members are appointed by managers and are more likely not to objectively evaluate or critically scrutinize managerial actions. CEO's seek to appoint members who are demographically similar,

and share the same management philosophies as themselves because such directors are more sympathetic to CEO's (Westphal & Zajac, 1995). Most committee members appointed by management are also beholden to the corporate wealth maximization objective of other large shareholders and may not necessarily pursue stakeholder issues as diligently; the votes cast by such committee members often reveal their allegiance to corporate management (Zajac & Westphal, 1994). Therefore, scholars have long argued for the importance and necessity of stakeholders to be represented on the board of directors in public corporations (Jones & Goldberg, 1982).

From an institutional perspective, representation of stakeholders on key board committees may provide a perception of legitimacy to organizations and enhance their normative approval by government and society (Luoma & Goodstein, 1999; Meyer & Rowan, 1977). The legitimacy of board committees is strengthened if board members are truly recognized by society as experts on social issues or are known to be sympathetic to stakeholder causes. Committee members, who are more cognizant and sympathetic towards stakeholder causes, can use their experience and knowledge to provide better advice to managers on social and environmental issues. Such board members are also desirable to most large stakeholder groups which decry the prevalence of a homogenous group of shareholder-centric directors in most firms. Stakeholders demand board members who are different in their background, experience and perspective than other members of the board. For example, CALPERS is a large pension fund which is known for its activism on board diversity issues. Just recently, a top executive at CALPERS bemoaned:

> *"On most boards, everybody looks the same and thinks the same"*
> *(Chon, 2010)*

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CALPERS is demanding that committee members be elected from a list of directors compiled by the pension fund itself. To that end, CALPERS is compiling a list of stakeholder-sympathetic professionals such as union leaders, environmental activists, NGO members etc. to be nominated to the board of directors of target firms with poor corporate governance (Chon, 2010). Shareholder activism research indicates that such appointments are a mutually beneficial arrangement. Those board members who implement shareholder proposals have lower chances of losing their board seat and directorships than those who go against shareholder initiatives (Ertimur, Ferri, & Stubben, 2010). In sum, it is likely that stakeholder activism will also be successful in changing the composition of the CSR committee towards a more stakeholder-friendly committee, or formally:

> H3: Stakeholder pressure is positively associated with the subsequent presence of stakeholder sympathetic members on board CSR committees.

Thus far, I have relied on institutional theory and agency theory to predict that stakeholder activism results in changes in internal control mechanisms within the firm. Next, I address the question whether stakeholder pressure is *always* successful in creating change within the organization, or, there are factors within the organization that may mitigate this impact. In effect, I define and establish the boundary conditions of the theory presented above. In doing so, I explain that institutional and agency theory assumptions of principals being successful in alleviating information asymmetries by designing effective control mechanisms may not always hold true. Relying on upper-echelons research (Hambrick, 2007; Hambrick & Finkelstein, 1987), I relax institutional theory assumptions when I explore the possibility of managerial discretion contexts in influencing the outcomes of stakeholder pressure. In contexts where managers exercise

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more discretion in firm decisions, their impact on firm outcomes is stronger (Crossland & Hambrick, 2007; Finkelstein & Boyd, 1998; Finkelstein & Hambrick, 1990). Resulting control mechanisms within the firm may therefore be shaped or even thwarted by managerial intervention.

Managerial Discretion

Much of the research on stakeholder proposal activism is grounded in resource dependence and institutional theories. Scholars espousing the resource dependence and institutional views have long argued that primary stakeholders possess resources which are required by firms to operate successfully, acquire legitimacy, succeed competitively, and perhaps even survive (DiMaggio & Powell, 1983; Pfeffer & Salancik, 1978). The reliance of the firm on key stakeholders creates an organizational resource dependence relationship between stakeholders and the firm (Pfeffer, 1978). Specially, according to the institutional perspective, organizations acquiesce to stakeholders demands in order to maintain legitimacy and align their practices and policies to conform to the social pressures placed on them (Deephouse, 1999; Meyer & Rowan, 1977).

However, research from a strategic choice perspective indicates that managers use their discretion in combating various stakeholder pressures exerted on the firm, and in structuring the firm's relationships with its stakeholders (Oliver, 1991; Pfeffer & Salancik, 1978). In doing so, managers try to find ways to increase their own bargaining power, which denotes the potential for strategic choice (Child, 1997; Salancik & Pfeffer, 1978). Some resource dependence scholars concede that institutional pressures may not be entirely deterministic; even under external pressure managers make strategic choices which allows managerial behavior to range from symbolic to discretionary

(Hrebiniak & Joyce, 1985; Pfeffer & Salancik, 1978). Indeed, external institutional pressures create opportunities for managers to be "both strategic and opportunistic" (Hoffman, 1999: 366) in exploiting the uncertainty caused by institutional change.

Those managers, who are under pressure from stakeholders to pursue social issues, exhibit a similar range of strategic behavior. To date, research on stakeholder activism and CSP has largely focused on the direct relationship between the two constructs with a particular emphasis on the divergence of shareholder and stakeholder goals (see Sjöström, 2008 for a review). A practical reality of the modern public corporation is that it is managers, not shareholders or stakeholders, who set CSP strategy, determine social and environmental investment thresholds, and control all other resources vital to the fulfillment of stakeholder demands (Frooman, 1999). Because professional managers have strategic informational advantages over other members of the organization, especially stakeholders, they enjoy the most "autonomy of choice" within the organization (Child, 1997: 53). Therefore, it is likely that managerial responses to stakeholder activism are determined by both the institutional pressure on the firm, and circumstance which determine the "latitude of managerial action" allowed to top managers over resource allocation decisions (Hambrick & Finkelstein, 1987: 371; Hrebiniak & Joyce, 1985).

Managerial discretion theory explains that there are several organizational and environmental contexts that might determine the extent to which CEO's matter to organizations strategy and policy (Finkelstein & Hambrick, 1990; Haleblian & Finkelstein, 1993). Management research has subsequently used both the organizational and environmental indicators of these

contexts to demonstrate the role they play in impacting managerial discretion's relationship with various organizational phenomena. For example, research has used these contexts to investigate the moderators of the relationship between CEO compensation and firm performance (Finkelstein & Boyd, 1998), top management team tenure and organization outcomes (Finkelstein & Hambrick, 1990), internal alignment under regulatory constraints (Peteraf & Reed, 2007) and managerial hubris and risk taking (Li & Tang, 2010).

Likewise, in this dissertation, I propose that certain organizational and environmental contexts affect managerial discretion. In organizational and environmental contexts which allow greater latitude to managers in decision-making, managers have a greater impact on firm outcomes (Hambrick & Finkelstein, 1987). In such situations, the agency costs of managerial discretion are also high (Lang, Poulsen, & Stulz, 1995). For example, excess cash flows available to managers are a positive indicator of a high-discretion situation (Jensen, 1986). Similarly, research indicates that debt is an organizational level indicator of a low-discretion situation because debt reduces the agency costs of high managerial discretion (Stulz, 1990). Thus, I leverage managerial discretion theory as a conceptual bridge between the predominantly deterministic institutional and power dependence theories and the overwhelmingly managerial agency theory to explain the role of high-discretion situations in shaping the outcomes from stakeholder pressure.

Stakeholder pressure, stakeholder governance, and the moderating role of managerial discretion contexts. Corporate social responsibility is often understood as

the "management of discretion" (Ackerman, 1975: 32-33) within the sphere of managerial actions. In other words, managerial discretion extends to the realm of those managerial actions which are taken in pursuit of increasing a corporation's social performance (Carroll, 1979). For example:

> *Management can almost always rationalize any action by invoking its impact on the welfare of some stakeholder. An empire builder can justify a costly acquisition by a claim that the purchase will save a couple of jobs in the acquired firm; a manager can choose his brother-in-law as supplier on the grounds that the latter's production process is environmentally friendly - (Tirole, 2001).*

Thus any study of the effects of stakeholder activism on CSP requires the inclusion of the "role of managers as a party with specific interests" (Tirole, 2001: 25). As discussed earlier, often these managerial interests can collide with the interests of the owners of the firm and other stakeholders (Jensen & Meckling, 1976). In such circumstances, it is expected that stakeholder pressure will not remain the sole force that determines the design and strength of stakeholder governance mechanisms within the firm. Specifically, organizational and environmental contexts which present opportunities to managers to exercise discretion will influence the existence or strength of stakeholder governance mechanisms resulting from prior stakeholder pressure.

Managerial discretion assumes supremacy at the very beginning of the stakeholder proposal submission process. Stakeholder proposals are required to be submitted to the company's executive office which allows managers to prepare their responses before other organizational constituents can provide their input. Managerial responses to stakeholder proposals stem out of legal discretion (determined by the

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regulatory environment) that allows managers tremendous leeway in responding to stakeholder criticism of their shortfalls in pursuing items of social significance.

One of the many different reasons stakeholder proposals fail is because they can be declared "non-strategic" by management. The determination is based on managerial assessments that the proposal is not significantly related to the operations of the company because it concerns itself with less than 5% of the company's total assets, net earnings and gross sales (Ingram, Coco, Cummins, & Gumbs, 2001). Managers are not only privy to the operations within the firm but also exercise control over the various accounting decisions that lead to the reporting of financial performance to stakeholders (Murphy, 1996). In high-discretion situations, managers gain even more control over these processes (Bowen, Rajgopal, & Venkatachalam, 2008) and can arbitrarily over-rule stakeholder demands. Even when voted upon and accepted by a majority of stakeholders, stakeholder proposals are non-binding. Because most managers are more committed to the status-quo (Hambrick, Geletkanycz, & Fredrickson, 1993) it is not surprising that top management is often in defiance or even outright denial when stakeholders accuse them of some wrongdoing (Vandekerckhove *et al.*, 2007)

High-discretion situations also mean that CEO's have the freedom to pick and choose some causes and then champion them inside the firm. For example, in response to pressure from stakeholders to improve the social performance of the firm, managers may create specialized departments within the firm and staff them with professional managers to signal their commitment to social issues without actually improving the bottom line on social performance (Brammer & Millington, 2003; Saiia, Carroll, & Buchholtz, 2003) . Managers are also known to deploy a barrage of tactics to buffer

their organization from stakeholder pressure; these tactics range from reputation management and impression management to pure rhetoric and imagery (Carter, 2006; Snider, Hill, & Martin, 2003; Ulmer & Sellnow, 2000). In such cases where managerial action is disconnected with any substantial structural changes within the firm which might serve to monitor managers, we will likely see no change in stakeholder governance mechanisms stemming from stakeholder pressure on the firm. Recent research posits that stakeholder pressure on firms may in fact be a "catalyst for wider discretion" (Phillips, Berman, Elms, & Johnson-Cramer, 2010: 178) afforded to managers.

Often managers enhance their discretion by pitting one political coalition (stakeholders) against another (owners). For example, managers can deny the payment of overtime pay by appealing to shareholder instructions of economizing on labor costs. Managers are also known to adopt an instrumental approach towards salient stakeholders. In response to stakeholder pressure, managers settle with large stakeholders, however, even when they do acquiesce to powerful stakeholders, change is often more symbolic than substantial (David et al., 2007). It follows then that the creation of stakeholder governance mechanisms within the firm will also be influenced heavily by situations in which managers exercise discretion. Or,

> *H4. Managerial discretion contexts weaken the positive relationship between stakeholder pressure and subsequent overall stakeholder governance*
>
> ***Managerial discretion contexts and board CSR committees.*** Even though the

board of directors holds the fiduciary responsibility of representing stakeholder interests and oversees managerial strategy, top managers have huge informational advantages

over most directors. To the extent that CEO's are intricately involved and exercise considerable control over the selection of directors (Monks & Minow, 1995) and subsequent committee decisions sometimes involving even the CEO's own compensation (Finkelstein & Boyd, 1998; Johnson et al., 1997). Managers are known to insert themselves into key committees in order to ensure no decisions tilt the balance of power against them. Although outside directors are often used to bring in some neutral perspectives, research indicates that managers are often successful in installing outside directors who are instrumental in further entrenching managers within the firm (Wade, O'Reilly, & Chandratat, 1990). Managers make every effort to appear to conform to demands of board independence, yet these efforts are purposely designed to be ineffective (Westphal & Graebner, 2010).

I therefore argue further that it is likely that high discretion situations in which managers exercise tremendous influence over setting of corporate governance policy within the firm, will also offer managers a chance to influence change in stakeholder governance policies resulting from stakeholder pressure. Resulting stakeholder governance mechanisms will therefore be shaped more by managers' decisions than external pressures. It is likely that stakeholder-oriented change in the board composition, such as the strength of board CSR committees, is also impacted by the high discretion situations. The essence of these arguments is captured in the following hypothesis:

> *H5: Managerial discretion contexts moderate the relationship between stakeholder pressure and the strength of board CSR committees such that the higher the managerial discretion, the weaker the board CSR committees.*

Stakeholder pressure and corporate social performance. In the previous sections, I have explained how stakeholder pressure is not always successful in achieving the desired objective of maximizing firms' CSP. In a striking parallel to the outcome of shareholder activism, stakeholder activism possibly looses most of its steam impacting the stakeholder governance mechanisms within the firm. If this is true, and stakeholder pressure manages to transform the stakeholder governance measures within the firm, then any relationship between stakeholder pressure and CSP should at least weaken when stakeholder governance is used as a control variable in the model.

> *H6: Stakeholder governance mediates the relationship between stakeholder pressure and CSP such that any relationship between stakeholder pressure and subsequent CSP is weakened when stakeholder governance is introduced as a mediating variable in the model.*

Managerial discretion plays a somewhat similar role in possibly altering any improvements in CSP that may arise out of stakeholder pressure. Earlier I explained how certain organizational and environmental contexts might allow managers tremendous latitude of action. As a result, managers gain discretion in dealing with pressures exerted by stakeholders. Managers use their discretionary powers to weaken stakeholder governance mechanisms. In high discretion contexts, managers are more likely to weaken the CSP resulting from stakeholder pressure. The following hypothesis formally capture the essence of the arguments made in the preceding sections:

> *H7: Managerial discretion contexts weaken the positive relationship between stakeholder pressure and CSP*

Corporate Social Performance and Corporate Financial Performance

Having traced the links between stakeholder pressures, corporate governance mechanisms, managerial discretion and corporate social performance in the previous section, I now turn towards the relationship between a corporation's social performance (CSP) and its financial performance (CFP). The link between CSP and CFP has been a contentious topic in much of prior research; to date, scholars are divided on the exact nature of the relationship and the debate is ongoing. A better understanding of the impact of CSP on CFP can help resolve apparent conflicts between stakeholder theory and corporate governance theories. For example, if research is able to confirm that increased CSP does indeed benefit the financial performance of firms, then stakeholders may find it easier to pressure organizations to direct more resources towards the maximization of the general welfare of stakeholders. A resolution of this debate may also help organization craft better and more balanced governance mechanisms which incentivize and monitor managers to enhance both the social and financial performance of the firm. Much criticism of stakeholder literature stems from the inability of research to clearly guide decision-makers on how to balance competing stakeholder demands; additional insight into the nature of the CSP-CFP relationship holds the potential to address this concern.

Motivated by the significance of this debate, in this section of the dissertation, I will re-explore the relationship between CSP and CFP. I will argue that in order to understand the nature of the relationship, researchers must include the moderating role of managerial discretion. In addition, I will explain that empirical investigations of the CSP-CFP relationship could benefit from an additional methodological consideration. It is my effort that through a consideration and resolution of at least one theoretical and

one methodological concern respectively, research will be able to better understand the true underlying relationship between corporate social performance and corporate financial performance.

CSP and CFP – Theoretical and methodological considerations. Nearly three decades of research examining the link between CSP and CFP has revealed mixed findings and conflicting results (Brammer & Millington, 2008; Griffin & Mahon, 1997; Margolis & Walsh, 2003; McWilliams & Siegel, 2001; Orlitzky et al., 2003). In this hotly contested debate, research launching on normative and instrumental stakeholder theories has argued that improvement in CSP can result in satisfied stakeholders who are key to improving the organization's overall effectiveness (Donaldson & Preston, 1995). Firms which project a socially superior image attract motivated employees, committed suppliers and socially conscious buyers and investors who feel more positive and are more cooperative towards such firms (Dutton et al., 1994; Fombrun & Shanley, 1990; Greening & Turban, 2000; Hillman & Keim, 2001; Turban & Greening, 1997). Some scholars have also advanced the notion that balancing the needs of a diverse group of stakeholders constrains management from making self-serving investments thereby economizing on agency costs (Freeman & Evan, 1990). Researchers conclude that improvements in CSP may increase the value-enhancing contributions from stakeholders and minimize agency costs which may collectively increase the corporation's financial performance (Hill & Jones, 1992; Jones, 1995).

On the other hand, some researchers have argued that the corporation's primary goal is to protect and maximize the wealth of shareholders (Easterbrook & Fischel, 1991; Friedman, 1970; Levitt, 1958). Researchers declare that requiring managers to

pursue two seemingly disparate objectives of shareholder wealth protection and stakeholder welfare maximization may divert valuable resources to ill-defined causes, detract managers from efficiently running the firm, and may eventually serve neither stakeholders nor shareholders (McWilliams & Siegel, 2001). Investing in CSP comes at some costs to the firm and resource diversion towards unclear social goals may have an adverse effect on a firm's financial performance (Alexander & Buchholz, 1978; McWilliams & Siegel, 2000). Challenging the notion that better stakeholder management reduces agency costs, agency scholars contend that by pitting stakeholders against each other, managers may in fact accrue private benefits in the guise of increasing general stakeholder welfare (Jensen, 2001).

Finally, research from a rent appropriation perspective has proposed another avenue through which a corporation's engagement in CSP may be unable to induce a positive spillover effect on its financial performance. It is well known that the prior performance of firms enables them to invest in improvements in future CSP (Waddock & Graves, 1997). However, when successful firms cater to powerful stakeholders such as buyers, suppliers, employees and the community at large, these stakeholders may accrue significant unobserved benefits generated by the firm (Coff, 1999). Such rent appropriation may in turn result in subsequently reduced observed levels of a firm's financial performance. A joint consideration of the above explanations reveals that it is likely that research examining the link between CSP and CFP may find either a modest positive or a non-significant relationship between the two constructs.

Although the normative stakeholder, agency and rent appropriation theoretical perspectives provide compelling reasons for why the link between CSP and CFP can

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either be positive, negative or inconclusive respectively, empirical results are far from confirmatory of any one theoretical perspective. Many researchers conclude that the heterogeneous results found in prior research are perhaps due to errors in measuring CSP and CFP, problems with the samples used, or omission of relevant variables from the models (Garcia-Castro, Ariño, & Canela, 2010; Margolis & Walsh, 2003; McWilliams & Siegel, 2000). In this dissertation I draw on past research and propose a model in which two other important considerations are added; the role of managers in controlling benefits arising out of CSP and the discretionary nature of social and environmental spending. The aim of introducing a possible moderating/mediating variable and an additional methodological consideration is to explore further the exact nature of the link between CSP and CFP. I demonstrate that a lack of association between the two variables in prior research does not mean that a relationship does not exist; rather it is confounded by either role of managers exercising their discretion or a methodological problem in model specification.

CSP and CFP – The role of managerial discretion. Increasingly, researchers are finding that the relationship between CSP and CFP is also possibly moderated by several exogenous variables (Margolis & Walsh, 2003; Russo & Fouts, 1997). The discretionary nature of CSP spending and the central role of managers in controlling CSP investments provides a compelling argument for including managerial discretion in a model in which managerial discretion contexts possibly moderate the cyclical relationship between CSP and CFP.

Research has long argued that even if managers pursue socially responsible initiatives, it is for their personal gain, not shareholder or stakeholder benefit. Quite

often, managers use social issue investments to further their own career goals at the expense of the firm and other stakeholders (Friedman, 1970). Pursuing social initiatives also enhances CEO's image in the eyes of their subordinates. CEO's are seen as visionary by their employees when they emphasize stakeholder values and autocratic when they emphasize economic values (Sully de Luque, Washburn, & Waldman, 2008). Thus, it is likely that benefits arising out of CSP are not fully appropriated by the firm but, are usurped by managers who gain utility at the expense of shareholders in creating a "warm glow" affect around the firm through excess CSP spending (Barnea & Rubin, 2010).

Managers also accrue private benefits from socially directed firm expenditures. For example, philanthropic giving by the firm provides an opportunity for managers to influence the image they present to important stakeholders, advancing their own interests while marginalizing the firm's social image (Haley, 1991). Managers ensure their firm's contributions are reflected as their personal achievement; managers of large corporations join relevant associations and socialize with other managers to achieve this purpose (Galaskiewicz & Burt, 1991). Therefore, it is possible for the firm's "good deeds" to be overshadowed by managers' personal image and missed by other stakeholders who hold the capacity to reward the firm for its better corporate social conduct.

Firms with satisfied stakeholders are able to extract better quality inputs from their suppliers, buyers and employees. Inputs from these motivates employees, committed buyers and loyal suppliers can help firm's improve their productivity and performance (Becchetti, Di Giacomo, & Pinnacchio, 2008). Yet, empirical evidence

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suggests that powerful internal stakeholders, such as managers, often appropriate the rewards from such firm efforts (Kim, Hoskisson, & Wan, 2004). CSP spending is also often used as a tool by managers to further entrench themselves in the firm. Inefficient managers are known to "play well" with social investors, environmental activists, and NGO's to get into their "good books" and use these vocal stakeholders against the threats of takeover by dissatisfied shareholders (Cespa & Cestone, 2007). In doing so, managers of inefficient firms protect themselves from being disciplined by the market for corporate control (Jensen & Ruback, 1983). Strong satisfied stakeholders who are accustomed to a generous treatment by collusive management make the firm an unattractive target for corporate raiders looking to discipline inefficient firms (Pagano & Volpin, 2005). Thus, managers are allowed a "free hand" to indulge in other value-destroying activities which may result in subsequent reductions in the financial performance of the firm (Surroca & Tribó, 2008). Because managerial discretion contexts accurately predict when managers can exercise a greater influence on firm strategies (Finkelstein & Hambrick, 1996), it follows that managerial discretion contexts will impact the relationship between CSP and CFP. More precisely, in contexts where discretion is high, the positive impact of CSP on CFP would be weakened. I capture the essence of the arguments made above in the following hypothesis:

H8: Managerial discretion contexts moderate the relationship between

CSP and CFP such that, higher the level of managerial discretion

contexts, weaker the CSP-CFP relationship..

CSP and CFP – Sample selection problems. Not all firms find it necessary to engage in investments that observers can categorize as socially and environmentally

responsible. Firms may choose to invest in CSP based on a variety of antecedents. For example, Chiu and Sharfman (2009) explain that firms' investments in CSP are a function of their visibility in the eyes of their stakeholders. Larger firms, or those firms which operate in particularly high-visibility industries, attract more stakeholder attention when they lack in their CSP commitment. They also found that higher slack resources are a strong predictor of whether a firm engages in CSP. Yet, all these CSP antecedents are also related to a firm's financial performance. For example, size, industry membership and slack resources are consistently reliable and strong predictors of financial performance of firms (Gooding & Wagner, 1985; Miles, Snow, & Sharfman, 1993; Singh, 1986). Thus, the choice of firms to invest in socially responsible activities is not independent of a cost-benefit analysis of engaging in CSP. In other words, to the extent that the factors that compel firms to engage in CSP are in turn associated with a firm's financial performance, the decision of the firm to invest in CSP may be endogenous. An omission of relevant antecedents to CSP in a model investigating the CSP-CFP link would introduce a sample selection bias in our estimates when only firms that choose to invest in CSP are included (Heckman, 1979). Results from such analyses would fail to generalize for all firms because empirical results would provide inconsistent estimates derived from analyses of non-random samples (Greene, 2008). Therefore, an examination of the CSP-CFP relationship should take into account all such factors that impact the firm's decision to invest in CSP and its financial performance.

An appropriate statistical methodology to resolve the endogeneity of the decision of firms to invest in CSP is to adopt the Heckman's (1979) two-step estimation

procedure. Specifically, in the first stage of this model, it can be tested whether the decision to invest in CSP is indeed endogenous. Subsequent to the results of the test, one can proceed to model the CSP-CFP relationship while controlling for the factors impacting the CSP investment decision. This procedure is a preferred statistical method for resolving sample-selection problems and has been used in management research to explain the inconsistent findings of empirical inquires into the corporate diversification and performance, and CEO duality and performance relationships (Campa & Kedia, 2002; Iyengar & Zampelli, 2009).

The specific application of the Heckman (1979) selection model to the sample-selection endogeneity problem of the CSP-CFP investigation is as follows:

$$CFP_{it} = \delta_0 + \delta_1 X_{it} + \delta_2 C_i + e_{it} \qquad (1)$$

Equation (1) shows the model used to investigate the financial performance of the firm where $\underline{X_{it}}$ represents firm characteristics such as size, slack, industry membership etc. which are known to affect the performance of the firm. The model includes the dichotomous term C_i to denote the decision of the firm i to invest in CSP. Under ordinary conditions, OLS estimation of equation (1) would yield unbiased and consistent results as long as C_i is exogenous. If however, the decision of firms to invest in CSP is not random but is spurred by factors that also affect a firm's performance, C_i will no longer be exogenous and OLS estimation would suffer from a selection bias if conducted on samples of only those firms for which CSP is observed. In other words, the sample selection hypothesis for CSP states that firms do not randomly decide to invest in CSP; rather they choose such investments based on observed or unobserved factors which may also affect firm performance.

Heckman (1979) shows that the sample selection bias is quite similar to a specification error where relevant antecedent variables are omitted in a model. Following Heckman's (1979) suggestions, and in order to resolve the selectivity bias, C_i^* is determined in a separate model as shown below:

$$Ci^* = \beta Z_{it} + u_{it}$$

$$C_i = 1 \text{ if } C_i^* > 0, \text{ otherwise } C_i = 0$$

(2)

In equation (2) the decision of firms to invest in CSP is represented by C_i^* which is determined by another set of firm characteristics in Z_{it} and u_{it} is the error term. In order to correctly identify equation (2) we require variables which impact a firm's decision to invest in CSP. As suggested by Chiu and Sharfman (2009), an important and often overlooked antecedent to CSP is the explicit stakeholder pressure placed on highly visible firms to increase their CSP. Visible firms are also more likely to be included in financial indices tracked by investors, and often end up being the only firms included in a sample in which the relationship between CSP and CFP is analyzed. The visibility of firms also affects the level of social pressure they receive (Pfeffer & Salancik, 1978). Research on stakeholder activism through proposal writing indicates that large and well-known firms persistently attract more stakeholder proposals than those firms that are relatively smaller and less visible (Proffitt & Spicer, 2006; Rehbein, Waddock, & Graves, 2004). Therefore, I explore stakeholder pressure exerted through stakeholder proposals as a relevant antecedent to CSP. I use this antecedent to control for the sample-selection bias of the CSP and CFP relationship. Accordingly, I propose the following hypotheses:

H9: Corporate social performance is positively associated with corporate financial performance once sample selection bias is removed.

In this chapter I provided a literature review of stakeholder activism and described how observing other outcomes can help us determine the true effectiveness of stakeholder activism. I developed hypotheses linking stakeholder pressure to stakeholder governance mechanisms within the firm. I introduced managerial discretion contexts as a possible moderator of the relationship between stakeholder pressure and stakeholder governance and stakeholder pressure and corporate social performance. Finally, I introduced the moderating role of managerial discretion in shaping the link between corporate social performance and corporate financial performance. I concluded this chapter by introducing a methodological correction to research methods utilized in past research to examine the CSP-CFP relationship. In the next chapter, I provide details on the data sources I utilized and the sample and variable construction strategies I used.

CHAPTER THREE

METHODS

In this chapter, I describe the various data sources that I used to construct the samples for testing the hypotheses. I have also provided details on the construction of variables and explain the different methods used to test the hypotheses. Most of the data used for this dissertation came from publicly available archival data sources. Below, I provide detailed descriptions of the data sources and my sample selection and variable construction methodology.

Data Sources

Stakeholder proposals. The Investor Responsibility Research Center (IRRC) compiles the shareholder proposal data, which includes all proposals, submitted each year to all S&P 1500 firms. IRRC makes the data available through Risk Metrics for the past 20 years (1997 through 2007). I used the Risk Metrics shareholder proposal database to acquire data on the governance and social responsibility proposals received by all firms for all years available in the database. Because the aim of this study is to investigate the impact of stakeholder proposals, I targeted only those proposals that raised social and environmental responsibility issues (SRI).

Financial data. I gathered firm-level financial data from the Standard & Poor's Compustat North America Database. The Compustat database is the world's leading database providing objective financial information on more than

13,000 US and international public firms serving almost the entire world's market.

Corporate social and environmental performance. The corporate social performance data was obtained for all firms covered in the Kinder Lydenberg and Domini Research & Analytics, Inc. (KLD) database. KLD is a social choice investment advisory firm specializing in evaluating publicly traded firms in the United States for their social and environmental performance. The use of KLD data to operationalize corporate social and environmental performance is pervasive in management research (e.g., Hillman & Keim, 2001; Johnson & Greening, 1999; McWilliams & Siegel, 2000; Sharfman & Fernando, 2008; Turban & Greening, 1997). CSP ratings from KLD have been assessed for their validity (Sharfman, 1996) and this database is considered to be one of the best sources available for social and environmental performance data (Graves & Waddock, 1994).

KLD employs independent analysts who conduct extensive research on companies to provide investment advice to socially conscious investors. KLD analysts use a variety of data sources to screen firms and compile a rating on corporations social and environment responsiveness (SR) or social issues/irresponsiveness (SI)[4]. Analysts gather indicators in five major areas of *community, diversity, employee relations, product, and environment* as shown in Table 1, to construct ratings on a scale of 0 to 30 for SR and -30 to 0 for SI.

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[4] The same CSR screening process also yields the Broad Market Social Index (BMSI) launched by KLD in 2001. BMSI is a subset of the Russell 3000 index and is comprised of nearly 3000 companies categorized in the SR category by KLD analysts.

Table 1: KLD Dimensions and Their Description

Strengths	Concerns
Product	
Benefits to the economically disadvantaged	Antitrust disputes
Quality	Marketing/Contracting controversies
R&D innovation	Product safety
Other strength	Other concern
Environment	
Beneficial products & services	Agricultural chemicals
Clean energy	Climate Change
Management Systems Strength	Hazardous waste
Pollution prevention	Regulatory problems
Recycling	Ozone depleting chemicals
Other strength	Substantial emissions
	Other concerns
Employee relations	
Cash profit sharing	Union relations concern
Employee involvement	Health and safety concern
Health and safety strength	Workforce reductions
Retirement benefits strength	Retirement benefit concerns
Union relations strength	Other concern
Other strength	
Community	
Charitable giving	Investment controversies
Innovative giving	Negative economic impact
Non-US charitable giving	Tax disputes
Support for housing	Other concerns
Support for education	
Volunteer programs strength	
Other strength	
Diversity	
CEO	Controversies
Board of Directors	Employee Discrimination
Promotion	Non-representation
Work/Life benefits	Other concerns
Family benefits	
Women & minority contracting	
Employment of the disabled	
Gay & Lesbian policies	
Other strength	

Stakeholder governance mechanisms. Data on overall stakeholder governance mechanism was obtained from the KLD database. KLD also compiles the concerns and strength of several stakeholder-oriented governance mechanisms in six related components. (1) Accounting strengths and concerns, (2) Strength and concern over limits on top management or board compensation, (3) Company ownership of other socially strong or weak companies (4) Quality of transparency in reporting on a wide range of social and environmental performance measures, (5) Involvement of the company in any noteworthy controversies, and (6) Other controversial issues. Table 2 displays the stakeholder governance measures and their description.

Table 2: KLD Stakeholder Governance Measures and Their Description

Strengths	Concerns
Company recently rewarded low annual pay to CEO (< $500,000) or outside directors (< $30,000)	Company recently rewarded high annual pay to CEO (> $10mil) or outside directors (>$100,000)
Company owns, or is owned by, another company KLD has rated as socially strong	Company owns, or is owned by, another company KLD rated as having social concerns.
Company reports on a wide range of social and environmental performance measures	Company is weak in reporting on social and environmental performance measures
Company has an exceptional record in maintaining transparency and accountability when dealing with state or federal level US or non-US politics.	Company is involved in noteworthy controversies surrounding its involvement in state or federal level US or non-US politics.
Company has a unique and positive corporate culture that promotes social performance	Company is involved in controversies surrounding its social and environmental performance
	Company is involved in accounting related controversies

Adapted from KLD Ratings Definitions

Data on committee structure and composition was obtained from the Capital IQ database which provides firm level data on the structure and composition of the board of directors, presence of CSR committees and the composition of CSR committees for firms that comprise a wide variety of stock market indexes.

Dependent Variables

Corporate social performance. Prior research argues against using a consolidated index of CSP and suggests that the strength and weakness ratings compiled by KLD conceptually represent distinct constructs (Mattingly & Berman, 2006). To construct a measure of social and environmental performance, I separately added the strengths and weaknesses scores for the community, diversity, employees, environment and product dimensions shown in Table 1. Two sub-variables named *CSP strength* and *CSP weakness* were created for each firm per year to represent its strengths and weaknesses in corporate social and environmental performance over time. *CSP strength* (Cronbach alpha = 0.82) is the sum of a firm's scores on all five strength dimensions shown in Table 1. *CSP weakness* (Cronbach alpha = 0.7) is the sum of the firm's scores on all five weakness dimensions. To compare my results with prior research which largely uses a combined measure of CSP, I created *CSP overall* (Cronbach alpha = 0.5) as the sum of *CSP strengths* and *CSP weakness.* Cronbach alpha values above 0.7 are generally considered acceptable by social scientists (Nunnally, 1978).

Corporate financial performance. I followed prior research and in most models used the return on assets (ROA) to proxy for firm performance. ROA was constructed as the ratio of net income to total assets. I also checked the robustness of the models with other operationalizations of performance as return on sales (ROS) constructed as the ratio of net income and sales and return on equity (ROE) computed as the ratio of net income and shareholder equity. Because these measures are highly correlated with each other, I used these variables interchangeably in most models.

I also used Tobin's Q as a more "forward-looking" performance measure which takes into account the growth opportunities available to firms (Lindenberg & Ross, 1981). The ratio is computed as the [market value of common stock + book value of preferred stock + book value of debt) / book value of total assets], where market value of common stock equals price at year-end times shares outstanding. In some models, I used an approximation of *Tobin's Q* presented by Chang and Pruitt (1994) computed as the ratio of market value (sum of market value of common equity, book value of preferred stock, and book value of debt) to book value of total assets. This approximation is highly correlated with Tobin's Q and has the benefit of requiring fewer variables thus improving sample size where observations for some variables are missing.

Independent Variables

Stakeholder pressure. Following prior research (David et al., 2007), I took a count of total social issue proposals submitted to the corporation in one

year. Construction of this variable in this fashion allows me to track longitudinally the trend of stakeholder-oriented proposals submitted to a firm.

Stakeholder governance. Because of the multidimensionality of this construct, I used separate strength, weakness, and overall measures of stakeholder governance in all models involving this variable. I added the strength and concern scores on all stakeholder governance dimensions shown in Table 2 separately to construct the *stakeholder governance strength* and *stakeholder governance weakness* variables. I then added these two variables to construct the *stakeholder governance overall* measure.

Presence of a CSR committee. This is a dichotomous variable that takes on the values of 1 when a company has a committee dedicated to social and environmental issues within its board of directors. The existence of such committees is indicated in most company texts by express labeling of committee names such as "public policy", "social responsibility" or "sustainability issues" committees etc. Table 3 provides details on all the CSP dimensions and sub dimensions, plus commonly found committee titles in the directors data obtained from Capital IQ. The last column of the table shows the keywords I employed to match committee names to CSP dimensions. I analyzed the contents of committee memberships of directors to match occurrences of the keywords. The variable takes on values of 1 for companies in which there was one such committee. For companies in which no directors were found to meet the criteria, the variable was set to zero.

Table 3: Construction of *Presence of a CSR Committee* Variable

CSP dimension	Sub-dimensions	Committee titles	Keywords used to construct variable
Community	Responsibility	Corporate responsibility Corporate social responsibility	*Respon* *Social*
	Ethics	Ethics Ethics and Conflict of Interest	*Ethic* *Conflict*
Environment	Environment	Environment health & safety Environmental & compliance Environmental policy	*Environment* *Waste* *Pollut* *Clean* *Climate* *Hazard* *Ozone* *Recycl* *Emission*
	Sustainability	Sustainability Sustainable Development Sustainability Community & Public Affairs	*Sustain*
Product	Quality Safety Innovation R&D	Safety & quality committee Safety health & environment Product innovation Research & development	*Quality* *Safety* *Innovation* *Research* *Prevention*
Employee relations and well-being	Employee health Retirement planning Pension Benefits Health	Employee health Retirement planning Pension Benefits Health Family Women Minority	*Employee* *Retire* *Pension* *Benefit* *Health*
Government	Public Regulation Relations	Public relations Regulation & oversight Government relations	*Public* *Regulat* *Relation*

Presence of a stakeholder sympathetic member in CSR committee. This variable was constructed as a dichotomous variable taking on values of 1 if a CSR committee member was deemed sympathetic to stakeholders. The determination of whether a director was "stakeholder-sympathetic" was made by following prior research (Kesner, 1988; Kosnik, 1990). I examined those directors who were a member of a CSR committee and whose current and past company affiliations, and occupations matched companies which are rated high in corporate social responsibility ratings. This variable was coded as 1 when a director within a CSR committee was found to be associated with another firm which was ranked in the top quartile of overall CSP scores in prior years. The variable was coded as 0 otherwise.

Strength of CSR committees. I used the proportion of stakeholder sympathetic directors on all CSR committees as a measure of the strength of the CSR committees. The proportion of stakeholder sympathetic directors is simply the ratio of the number of stakeholder-sympathetic directors on committees with the total number of directors in the CSR committees (Luoma & Goodstein, 1999). Determination of "stakeholder-oriented" directors followed the same guidelines as explained in the variable construction of the presence of sympathetic members in the committee above.

Managerial discretion. Hambrick and Abrahamson (1995) adopted a multi-method approach to validate certain organizational and environmental factors with assessments from a panel of business and academic experts. They confirmed that most of the organizational and environmental factors they tested

were indeed representative of contexts which impact managerial discretion. Given the sensitivity of my constructs of interest to both firm and industry factors; corporate social performance or stakeholder governance are likely to be influenced by both firm and industry level factors (Orlitzky, 2001), I will measure discretion at both levels of analysis.

Firm size has been used as both a positive and a negative indicator of managerial discretion. On one hand, because larger firms are slow to make dramatic changes (Aldrich, 1979), they may also engender strong bureaucratic structures which put limits on CEO discretion (Mintzberg, 1978). On the other hand, larger firms usually acquire greater market power and can have a controlling influence over their task environment allowing managers greater discretion (Reid, 1968). Prior research has however indicated that the effects of firm size on managerial discretion may be more negative than positive (Finkelstein & Hambrick, 1990). Similar to other recent research using size as an indicator of contexts of managerial discretion (Li & Tang, 2010), in this dissertation I operationalize firm size as the natural log of assets. As a validity check, I also used the natural log of sales to compute firm size.

Unabsorbed slack is a positive organizational indicator of managerial discretion contexts. Slack presents the organization with various options on which to act (Cyert & March, 1963), offering managers discretion to choose from any of those options (Hambrick & Finkelstein, 1987). I operationalize unabsorbed slack as both the current ratio - current assets divided by current liabilities and quick ratio - current assets - inventories / current liabilities

(Bourgeois, 1981). *Debt* is a negative organizational indicator of managerial discretion contexts because higher debt may constrain discretionary spending by managers (Jensen, 1986). I operationalized debt as the ratio of long term debt to total assets and also as the ratio of debt to shareholder's equity (Lang, Ofek, & Stulz, 1996). *R&D intensity* is another positive indicator of managerial discretion contexts. Prior literature informs that research and development is an exploratory activity (Cyert & March, 1963). Higher R&D expenses incurred by the firm are indicative of greater managerial control over both resource allocation and determination of organizational goals (Burgelman & Grove, 2007). Increased R&D expenditures may also increase the "information asymmetry" between providers of capital and CEO's increasing CEO's powers over decision making (Heeley, Matusik, & Jain, 2007). For all these reasons, higher R&D is considered a valid organizational indicator of managerial discretion contexts (Hambrick & Finkelstein, 1987). Following prior research, I will operationalize this variable by taking the ratio of R&D expenses and sales (Cohen & Levinthal, 1989) to minimize the impact of differences in firm sales on R&D expenditures. Because R&D expenses are not reported for a large number of companies, inclusion of this variable reduced samples sizes dramatically reducing the power to observe an effect (Cohen, 1992). I therefore filled the missing values of R&D by zeros. In order to ensure that this procedure did not introduce a bias in my results, I created a dummy variable *RDI* that took on values of 1 if R&D intensity was filled with zeroes and 0 otherwise. All

models using *R&D intensity* also used *RDI* as a control variable and the co-efficients were reported if statistically significant.

Market munificence is an environmental level indicator of high managerial discretion contexts. Munificent markets provide more opportunities and resources to firms. Hambrick and Finkelstein (1987) argue that in high-growth industries, firm-level decision making takes on an "entrepreneurial" mode (Mintzberg, 1973) allowing managers tremendous "strategic degrees of freedom" (Porter, 1980: 230). Lieberson and O'Connor (1972) found market growth to be an important determinant of managerial influence over firm profit margins. I followed prior research (Boyd, 1990; Keats & Hitt, 1988) and used past five year average growth in net sales as an indicator of munificence. Following the method outlined by Keats and Hitt (1988) and explained by McCleary and Hay (1980), I treated the natural log of industry sales over the past five years in a time series, where industry classification was based on the two-digit SIC code to which the firm belonged. The variable was computed by taking the anti-log of the regression co-efficient.

Market uncertainty was another environmental level indicator of managerial discretion. Competitively unstable markets put greater demands on CEOs who in turn use latitude in their decision-making in order to increase their role in designing and implementing firm strategies (Hambrick & Finkelstein, 1987). Following prior research, the volatility of net sales in the industry over the past five years was taken as a valid indicator of industry instability (Boyd, 1990; Keats & Hitt, 1988). The variable was constructed as the anti-log of

standard errors of the regression co-efficient obtained during the construction of the *market munificence* variable.

Market complexity was used as the third and final environmental indicator of managerial discretion contexts. Complex environments usually have higher competition and a prevalence of competitors. In highly competitive markets, CEO actions are less visible to observers (Zajac & Bazerman, 1991) and outcomes may be causally ambiguous. Hambrick and Finkelstein (1987) argue that although environment complexity is a valid indicator of managerial discretion contexts, the direction of affect on managers' discretion cannot be unequivocally predetermined. Therefore, I used environment complexity as an indicator without an a priori declaration of its direction of impact on managerial discretion. I based my computations on the number of competitors in the industry (Palmer & Wiseman, 1999). Industry concentration was measured by the Herfindahl-Hirschman index (HHI) which has been tested to be a very reliable indicator of industry structure (Bailey & Boyle, 1971). For each industry defined by the two-digit SIC code in COMPUSTAT, the index was computed as the sum of squared market share of sales of all firms in the industry.

Control variables. Firm size, debt, firm slack and R&D intensity were also used as control variables in most regressions to control for the effect of these variables on relevant dependent variables. For all models, industry and year effects were controlled. To control for industry effects, the average level of the dependent variable in the industry (defined at the two-digit SIC level) excluding the values for the focal firm was used. For cross-sectional and panel

random-effects models, year effects were introduced using dummy variables and remained in the regression if they were jointly significant. For fixed-effects panel models, year effects were introduced using two-way fixed-effects estimation methods (Baum, 2006). The inclusion of time control variables enhances the robustness of estimates to contemporaneous autocorrelation (Beck & Katz, 1995).

Analysis

All models use data on industrial firms only because accounting data on financial and non-industrial firms is incomparable with the accounting data on industrial firms. Data on firms was retained only if firm assets, sales and R&D expenses were positive. To analyze Hypothesis 2 and Hypothesis 3, I used cross-sectional logit regression analysis because the dependent variables *presence of a CSR committee* and *presence of stakeholder sympathetic member on CSR committee* both take on values of either 0 or 1. For analyzing Hypothesis 5, I used ordinary least squares (OLS) regression. I tested the residuals of OLS regressions for heteroskedasticity using a Breusch-Pagan / Cook-Weisberg (Breusch & Pagan, 1979; Cook & Weisberg, 1983) test and whenever the null hypothesis of constant variance was rejected, I used the he Huber-White (Huber, 1967; White, 1980) sandwich estimator which provides consistent standard errors in the presence of heteroskedasticity. I confirmed that using fixes to the White estimator suggested by Davidson and MacKinnon (1993) does not alter the findings.

For all the other hypotheses, I used panel data estimation because it offers increased degrees of freedom and improves the efficiency of estimates by reducing multi-collinearity (Hsiao, 2003). To reduce any remaining multi-collinearity between

variables and interaction terms, I followed prior research (Cohen, Cohen, West, & Aiken, 2003) and centered predictor variables around their means before creating interaction terms. After all regression estimations, I inspected variance inflation factors to ensure the average values were well under 2 and the condition number of the design matrix was well under 30 to suggest multi-collinearity did not pose a problem (Belsley, Kuh, & Welsch, 1980; Greene, 2008; Neter, Wasserman, & Kutner, 1996).

Using panel-data techniques also allowed me to model any firm-level time-invariant unobserved heterogeneity. Stable firm characteristics such as firm capabilities, or industry-related advantages could exert an influence over corporate social performance, stakeholder governance, and corporate financial performance. Omission of such unobserved effects from my models would cause an endogeneity bias in the estimates. Modeling unobserved time-constant variables as a "fixed-effect" avoids the bias and aids in correct inference of statistical results (Greene, 2008). However, whenever unobserved characteristics are uncorrelated with regressors, estimates obtained from a fixed-effects estimation are less efficient than those obtained from a random-effects estimation (Greene, 2008). Therefore, this conservative estimation technique was only deployed if time-invariant effects had a statistically significant effect within the model. A Hausman test (Hausman, 1978) helped me confirm the decision to use either fixed-effects or random-effects estimation. The null hypothesis of the test states that the variables omitted from the model are not related to the independent variables included in the model. Wherever I rejected the null hypothesis and problems of endogeneity were found, I used fixed-effects estimation to obtain consistent estimates of the impact of the independent variables on the dependent variables (Wooldridge, 2002).

Heteroskedasticity and serial correlation in the error term can bias the standard errors of regression co-efficients which may lead to incorrect inferences. I tested all fixed-effects panel-data regression models for group-wise heteroskedasticity by using a modified Wald test. The test was constructed by Greene (2008) and implemented in STATA by Baum (2001). I tested for autocorrelation using a method suggested by Wooldridge (2002: 282-283). This test is robust in the presence of conditional heteroskedasticity and has good size and power in reasonably large samples (Drukker, 2003). Wherever I found problems of heteroskedasticity and serial correlation, I used cluster-robust standard errors which are unbiased for clustered correlated panel data (Froot, 1989; Williams, 2000; Wooldridge, 2002).

I used the statistical package STATA 10.0 to run the analyses. The fixed-effects and random-effects panel data regressions were implemented using the *xtreg* command. A logit analysis for Hypotheses 2 and 3 was conducted using the *logit* command. OLS regression to test Hypothesis 5 was implemented using the *regress* command. Finally, the probit analysis required for Hypothesis 9 was conducted using the *probit* command.

CHAPTER FOUR

RESULTS

In order to test Hypothesis 1, I took all of the available data on stakeholder governance provided by KLD for the years 2005 to 2008 and merged it with stakeholder pressure data from Risk Metrics and firm level financial data from COMPUSTAT for the years 2004 to 2007 arriving at an initial sample of 1115 observations on 468 firms. Using prior years of data to construct the independent and control variables allows for stronger arguments in favor of the direction of potential causality from the independent variables to the dependent variable. In order for firm observations in a group to be meaningful, I restricted the panel to at least three years of consecutive observations per firm where data on all variables was available. I ended up with an final unbalanced panel of 659 observations on 175 firms over four years.

Table 4 presents the descriptive statistics of the relevant variables in the sample based on the year with the most observations (2007). Changing the years does not meaningfully alter the correlation results. The bi-variate correlations between the independent variable *stakeholder pressure* and the three dependent variables, *stakeholder governance strength, stakeholder governance weakness and stakeholder governance overall,* are statistically significant *(p<0.01).* The direction of the correlation co-efficient indicates that stakeholder pressure on organizations is positively associated with the strength of stakeholder governance mechanisms and negatively related to the weakness and overall stakeholder governance measures. I employed two-way fixed-effects panel data regression estimation after the null hypothesis of the

Table 4: Correlations, Means and Standard Deviations for All Variables Used to Test Hypothesis 1

	Means	s.d.	1	2	3	4	5	6
1. Stakeholder pressure	3.19	2.89						
2. Firm size	9.54	1.19	0.507***					
3. Performance	0.07	0.07	0.158*	0.00				
4. Debt	0.22	0.14	-0.121	-0.14	0.342***			
5. Stakeholder governance strength	2.62	2.83	0.313***	0.47***	0.152*	-0.234**		
6. Stakeholder governance weakness	-5.54	3.28	-0.490***	-0.44***	-0.192*	0.202**	-0.329***	
7. Stakeholder governance overall	-1.46	1.79	-0.202**	-0.03	-0.0557	-0.000117	0.493***	0.659***

N = 175 (for year 2007)
* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Hausman (1978) test was rejected ($\chi^2=19.23$, $p<0.05$). The null hypothesis of the Wald test suggesting no group-wise heteroskedasticity was also rejected ($\chi^2=76328.93$, $p<0.001$) indicating problems of heteroskedasticity. Similarly a test for serial correlation rejected the null of no first order serial correlation ($F=114.225$, $p<0.001$). I therefore report cluster robust standard errors. Table 5 presents the results of the panel data regression analysis run in three models, each with the three dimensions, strength, weakness and overall of the stakeholder governance dependent variable. All models show statistically significant model fit statistics.

Table 5: Fixed-Effects Regression Analysis Testing Hypothesis 1

Variables	Dependent variable: Stakeholder governance		
	Strength	**Weakness**	**Overall**
	Model 1	Model 2	Model 3
Stakeholder pressure	-0.0405	-0.155[**]	-0.0982[**]
	(0.0493)	(0.0589)	(0.0355)
Firm size	-0.0591	-0.169	-0.134
	(0.386)	(0.513)	(0.339)
Performance	0.558	-1.352	-0.390
	(0.979)	(1.228)	(0.814)
Debt	0.986	-0.625	0.227
	(1.374)	(1.951)	(1.244)
Mean industry stakeholder governance strength	0.305[**] (0.0976)		
Mean industry stakeholder governance weakness		0.204 (0.104)	
Mean industry stakeholder governance overall			0.203[*] (0.0875)
Constant	2.223	-2.107	0.361
	(3.712)	(4.831)	(3.155)
F	3.557[***]	15.62[***]	10.65[***]
R^2 (within)	0.0753	0.225	0.129

N= 659, 175 firms over 4 years – unbalanced panel
Heteroskedasticity and serial correlation robust clustered standard errors are in parentheses
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

In Table 5, The co-efficient of *stakeholder pressure* is negative and statistically significant *(p<0.01)* in Model 2 and Model 3 for both *stakeholder governance weakness* and *stakeholder governance overall* dependent variables respectively. The co-efficient of *stakeholder pressure* fails to achieve statistical significance for the stakeholder governance strength dependent variable in Model 1. The results suggest that although stakeholder pressure may be unable to strengthen stakeholder governance measures within the firm, it may be successful in improving the weaknesses in stakeholder governance mechanisms. The negative sign on stakeholder pressure in Model 3 suggests that perhaps the overall measure for stakeholder governance is more heavily influenced by the weakness scores than the strength scores; hence validating our use of strengths, weaknesses and overall measures as separate dependent variables.

Hypothesis 4 investigates the moderating role of managerial discretion on the stakeholder pressure and overall stakeholder governance relationship. To test hypothesis 4, I constructed the organizational and environmental discretion indicators from data corresponding to the time frame of stakeholder pressure (2004 to 2007) and merged it with the initial sample used to test Hypothesis 1. The resulting sample contained 1076 observations on 453 unique firms. Table 6 shows the means, standard deviations and correlations of the variables used to test Hypothesis 4 for the year 2007, chosen because it contained the largest number of observations. Using another year for generating the correlation table does not materially change the results. Bi-variate correlations show a strong association between the three dimensions of the *stakeholder governance* dependent variable and *stakeholder pressure.* Correlations between the regressors are however low and show no cause for concern. In order for observations on all firms to be

Table 6: Descriptive Statistics and Correlation of Variables Used to Test Hypothesis 4

	Means	s.d.	1	2	3	4	5	6	7	8	9	10	11	12	14	15
1.Stkhldr gov (s)	2.64	2.79	-													
2.Stkhldr gov (w)	-5.48	3.29	-0.34	-												
3.Stkhldr gov(o)	-1.42	1.77	0.48	0.67	-											
4.Industry avg (s)	-1.4	1.06	-0.03	0.16	0.13	-										
5.Industry avg (w)	-5.5	2.09	-0.15	0.28	0.15	0.75	-									
6.Indsutry avg (o)	-1.4	1.06	-0.03	0.16	0.13	1	0.75	-								
7.Performance	0.07	0.07	0.19	-0.22	-0.05	-0.15	-0.2	-0.15	-							
8.Stkhldr pressure	3.15	2.89	0.28	-0.49	-0.24	-0.1	-0.21	-0.1	0.19	-						
9.Firm size	9.53	1.19	0.45	-0.44	-0.06	-0.17	-0.25	-0.17	0.04	0.49	-					
10.Firm debt	0.21	0.14	-0.26	0.23	0.01	0.14	0.23	0.14	-0.33	-0.14	-0.16	-				
11.Firm slack	1.46	0.77	-0.08	-0.02	-0.08	0.02	-0.12	0.02	0.29	-0.11	-0.28	-0.27	-			
12.R&D intensity	0.03	0.09	0.05	-0.1	-0.05	0.09	-0.13	0.09	-0.2	0.02	-0.03	-0.13	0.49	-		
14.Market munificence	1.07	0.05	0.15	-0.03	0.1	0.15	-0.04	0.15	0.11	0.06	-0.02	-0.24	0.14	0.08	-	
15.Market uncertainty	1	0	-0.06	-0.09	-0.13	-0.22	-0.14	-0.22	0.22	0.1	0	0.08	0.02	-0.11	-0.32	-
16.Market complexity	0.07	0.08	-0.15	-0.14	-0.25	-0.4	-0.23	-0.4	0.15	0.11	-0.05	-0.05	0.04	-0.16	-0.05	0.53

N=166 for year 2007

Correlation co-efficients with a magnitude greater than |0.16| are statistically significant at $p<0.05$

meaningful, I limited the sample to those firms which had at least three years of consecutive data on all relevant variables. The final sample to test Hypothesis 4 comprised of 664 observations on 176 firms over four years. Year effects were used in all models initially, but dropped later because their joint effect was statistically insignificant; keeping the year effects in the regression does not alter the findings.

I failed to reject the null hypothesis of the Hausman test(χ^2=10.4, p=0.24) indicating that random-effects would deliver more efficient estimates than a fixed-effects estimation. I re-confirmed this decision by running the Sargan-Hansen (1982) test of overidentifying restrictions which is robust to conditional heteroskedasticity and within-group correlation (Hayashi, 2000). The test statistic failed to achieve statistical significance (p=.08) which indicated that the omitted fixed-effects would not cause an endogeneity problem in my estimates and I was correct in choosing a random-effects estimation over a fixed-effects one (Wooldridge, 2002). As a final check, I also ran a Breusch-Pagan (1980) LM test for random effects to make sure using a random effects estimation was preferred over using a pooled ordinary least square regression. The null hypothesis of no random effects was rejected (χ^2=293.06, p<0.001) and therefore I proceeded with a random-effects panel data estimation to test Hypothesis 4.

I ran three separate regressions with the three dimensions of stakeholder governance (strength, weakness, and overall) as dependent variables; results are presented in Table 7a, 7b and 7c respectively. Within each table, I ran several models, starting with the control variables only in Model 1. I then introduced the independent variable in Model 2, and then subsequently entered the organizational level discretion context variables in Model 3, followed by their interactions with stakeholder pressure in

Table 7a: Results of Random Effects Estimation of Hypothesis 4

	Dependent variable: Stakeholder governance strength					
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
Industry average stakeholder governance	0.38***	0.37***	0.31***	0.29***	0.35***	0.24***
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Performance	1.76	1.91	2.84*	2.63*	2.28*	2.74*
	(1.06)	(1.08)	(1.38)	(1.33)	(1.13)	(1.33)
Stakeholder pressure		0.04	-0.02	-0.03	0.04	-0.03
		(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Firm size			0.82***	0.82***		0.83***
			(0.13)	(0.14)		(0.13)
Firm debt			-0.48	-0.75		-1.05
			(0.89)	(0.91)		(0.90)
Firm slack			-0.26*	-0.10		-0.09
			(0.11)	(0.14)		(0.14)
R&D intensity			1.02	0.48		0.02
			(1.37)	(1.60)		(1.51)
R&D intensity missing indicator			-0.76*	-0.70*		-0.97**
			(0.35)	(0.35)		(0.36)
Stakeholder pressure x firm size				0.02		0.01
				(0.03)		(0.03)
Stakeholder pressure x firm debt				-0.40		-0.50
				(0.29)		(0.30)
Stakeholder pressure x firm slack				0.13*		0.14*
				(0.06)		(0.06)
Stakeholder pressure x R&D intensity				-0.26		-0.28
				(0.59)		(0.58)
Market munificence					-0.31	0.27
					(2.02)	(2.04)

Market uncertainty					1.60	67.51
					(56.83)	(57.72)
Market complexity					-5.20**	-6.84***
					(1.73)	(1.77)
Stakeholder pressure x market munificence					-0.45	-1.14*
					(0.56)	(0.56)
Stakeholder pressure x market uncertainty					-21.87	-23.23
					(12.42)	(12.15)
Stakeholder pressure x market complexity					0.71	0.56
					(0.45)	(0.42)
Constant	1.47***	1.41***	1.84***	1.86***	1.46***	2.10***
	(0.26)	(0.26)	(0.32)	(0.32)	(0.27)	(0.33)
N	640	624	624	624	624	624
R-sq within	0.06	0.05	0.06	0.07	0.07	0.09
Wald χ^2	35.20***	37.59***	91.13***	121.64***	54.11***	145.17***

166 firms over four years, (unbalanced panel)

Heteroskedasticity robust standard errors in parenthesis

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 7b: Random Effects Regression Testing Hypothesis 4

	Dependent variable: Stakeholder governance weakness					
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
Industry average stakeholder governance	0.52***	0.47***	0.40***	0.40***	0.47***	0.40***
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Performance	-3.51**	-3.49**	-4.38**	-4.44**	-3.71**	-4.47**
	(1.33)	(1.29)	(1.47)	(1.52)	(1.32)	(1.55)
Stakeholder pressure		-0.29***	-0.22***	-0.17**	-0.27***	-0.16**
		(0.05)	(0.05)	(0.05)	(0.05)	(0.05)
Firm size			-0.75***	-0.81***		-0.78***
			(0.15)	(0.16)		(0.16)
Firm debt			-0.31	-0.64		-0.61
			(1.05)	(1.10)		(1.11)
Firm slack			0.01	-0.06		-0.07
			(0.17)	(0.19)		(0.19)
R&D intensity			-2.22	-2.00		-2.51
			(1.26)	(1.38)		(1.31)
R&D intensity missing indicator			0.80*	0.77*		0.73
			(0.37)	(0.38)		(0.39)
Stakeholder pressure x firm size				-0.07*		-0.05
				(0.04)		(0.04)
Stakeholder pressure x firm debt				-0.45		-0.23
				(0.41)		(0.41)
Stakeholder pressure x firm slack				-0.07		-0.09
				(0.08)		(0.08)
Stakeholder pressure x R&D intensity				0.15		-0.27
				(0.55)		(0.53)
Market munificence					-1.98	-2.55
					(2.30)	(2.34)

Market uncertainty					32.31	-15.09
					(92.58)	(92.05)
Market complexity					-0.52	-0.50
					(3.04)	(3.13)
Stakeholder pressure x market munificence					1.02	1.45[*]
					(0.64)	(0.66)
Stakeholder pressure x market uncertainty					-1.42	1.34
					(18.27)	(18.44)
Stakeholder pressure x market complexity					-1.34[*]	-1.19
					(0.62)	(0.62)
Constant	-2.36[***]	-2.68[***]	-3.29[***]	-3.19[***]	-2.63[***]	-3.20[***]
	(0.41)	(0.41)	(0.47)	(0.47)	(0.42)	(0.49)
N	640	624	624	624	624	624
R-sq within	0.14	0.14	0.16	0.17	0.17	0.19
Wald χ^2	72.66[***]	110.59[***]	150.96[***]	175.85[***]	130.95[***]	208.55[***]

166 firms over four years, (unbalanced panel)
Heteroskedasticity robust standard errors in parenthesis
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

Table 7c: Random Effects Regression Testing Hypothesis 4

	Dependent variable: Stakeholder governance overall					
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
Industry average stakeholder governance	0.38***	0.35***	0.36***	0.35***	0.32***	0.32***
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Performance	-1.00	-0.80	-0.70	-0.87	-0.76	-0.91
	(0.82)	(0.83)	(0.96)	(0.97)	(0.82)	(0.98)
Stakeholder pressure		-0.11***	-0.11***	-0.09**	-0.10***	-0.08*
		(0.03)	(0.03)	(0.03)	(0.03)	(0.03)
Firm size			0.02	-0.02		-0.01
			(0.10)	(0.10)		(0.10)
Firm debt			-0.44	-0.74		-0.85
			(0.67)	(0.70)		(0.71)
Firm slack			-0.15	-0.09		-0.09
			(0.11)	(0.12)		(0.12)
R&D intensity			-0.53	-0.68		-1.29
			(0.88)	(1.01)		(0.94)
R&D intensity missing indicator			0.08	0.09		-0.05
			(0.25)	(0.25)		(0.26)
Stakeholder pressure x firm size				-0.03		-0.03
				(0.02)		(0.02)
Stakeholder pressure x firm debt				-0.39		-0.33
				(0.25)		(0.25)
Stakeholder pressure x firm slack				0.03		0.03
				(0.05)		(0.05)
Stakeholder pressure x R&D intensity				-0.04		-0.29
				(0.39)		(0.37)
Market munificence					-1.29	-1.31
					(1.50)	(1.52)

Market uncertainty					11.60	22.72
					(50.74)	(51.28)
Market complexity					-3.26	-3.56*
					(1.69)	(1.77)
Stakeholder pressure x market munificence					0.40	0.21
					(0.44)	(0.45)
Stakeholder pressure x market uncertainty					-12.00	-11.74
					(11.80)	(11.53)
Stakeholder pressure x market complexity					-0.34	-0.30
					(0.41)	(0.40)
Constant	-0.83***	-0.91***	-0.94***	-0.89***	-0.96***	-0.89***
	(0.17)	(0.17)	(0.22)	(0.22)	(0.17)	(0.22)
N	640	624	624	624	624	624
R-sq within	0.07	0.08	0.08	0.09	0.10	0.10
Wald χ^2	34.60***	48.34***	52.54***	57.79***	63.03***	79.11***

166 firms over four years, (unbalanced panel)
Heteroskedasticity robust standard errors in parenthesis
* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Model 4. Environment level discretion context variables and their interaction with stakeholder pressure were entered in Model 5. Finally, Model 6 within each table presents the results of the full model and is used to report the results. The co-efficient of stakeholder pressure and its interaction with the organizational or environmental discretion context variables is only statistically significant in Table 7b where stakeholder governance weakness was used as a dependent variable. The sign on the interaction of stakeholder pressure and market munificence is positive. This indicates that while the direct effect of stakeholder pressure is to alleviate weaknesses in stakeholder governance mechanisms, in munificent environmental contexts where managers may exercise more discretion, stakeholder pressure is less effective in improving the weaknesses in stakeholder governance mechanisms within the firm. Therefore, Hypothesis 4 was confirmed using stakeholder governance mechanisms weakness indicators and market munificence denoting managerial discretion contexts.

For testing Hypothesis 2 and 3, I used the most recently available data (2010) on director committee memberships. For the independent variable, I used the most recently available data on stakeholder pressure (2007)[5]. The two-year separation between the independent and dependent variable serves two purposes. First, the lagged structure of our model would allow stronger causal arguments to be made in favor of the direction of impact of the independent variable on the dependent variable. Second, changes in organization structure due to institutional pressures are likely to meet organizational resistance (Oliver, 1991) and hence take some time to manifest themselves; a period of

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[5] At the time of writing the results of the analyses, Risk Metrics released shareholder proposal data for 2008 and 2009. Supplemental analyses using the data from the latest available year (2009) are included in the third column in Table 9 and Table 10.

three years would appear to be sufficient separation between stakeholder pressure and subsequent changes within organizational stakeholder governance structures. Control variables were constructed using data for the same year as the independent variables. The initial sample for testing Hypotheses 2, 3 and 5 was constructed by merging director committee membership data for 1055 firms with stakeholder pressure data on 212 (385 for the year 2009) firms resulting in a final merged sample of data on 78 (136 for the year 2009) firms.

In order to account for the effect of firm size on the existence of a CSR committee I took the natural log of total directors in the company. Debt and performance were also used as control variables to remove organizational influences on the dependent variables. To remove the effect of industry, I computed the average number of directors in the industry excluding the number of directors in the focal firm. Table 8 presents the descriptive statistics for the variables used to test Hypothesis 2 and Hypothesis 3. Bi-variate correlations between both dependent variables: *presence of a CSR committee* and *presence of a stakeholder sympathetic member on the CSR committee*, with *stakeholder pressure, firm size* and *industry effects* are positive and statistically significant.

Table 9 presents the results of the logit analysis with the *presence of a CSR committee* as a dependent variable. Results are presented for *stakeholder pressure* and control variables constructed from both 2007 and 2009 in separate columns labeled respectively. Because logit estimation is quite sensitive to heteroskedasticity (Davidson & MacKinnon, 1993) I have reported robust standard errors for statistical inference. I have reported the *pseudo-R^2* which is a recommended goodness-of-fit measure of logit

Table 8: Descriptive Statistics of Variables Used to Test Hypothesis 2, 3 and 5

Variables	Means	s.d.	1	2	3	4	5	6	7
1.Presence of a CSR committee	.45	.50	-						
2. Presence of a stakeholder sympathetic member on the CSR committee	0.40	0.50	0.90^{***}	-					
3. Strength of CSR committee	0.18	0.22	0.89^{***}	0.81^{***}	-				
4.Stakeholder pressure	1.92	1.76	0.38^{***}	0.35^{**}	0.25^{*}	-			
5. Firm size	2.44	.38	0.30^{**}	0.32^{**}	0.20	0.30^{**}	-		
6. Industry effects	12.06	1.50	0.39^{***}	0.39^{***}	0.32^{**}	0.39^{***}	0.26^{*}	-	
7. Debt	.19	.13	-0.20	-0.20	-0.20	-0.18	-0.12	-0.02	-
8. Performance	.08	.07	0.09	0.04	0.09	0.19	0.09	0.15	-0.29^{*}

N=78
$^{*}p < 0.05,$ $^{**}p < 0.01,$ $^{***}p < 0.001$

Table 9: Result of Logistic Regression Testing Hypotheses 2

Independent variables	Dependent Variable: Presence of a CSR committee on the board of directors, 1 = Yes, 0 = No	
	Past pressure (2007)	**Recent pressure (2009)**
Stakeholder pressure	0.493[*]	0.196
	(0.258)	(0.140)
Firm size	1.038	2.572[**]
	(0.791)	(0.858)
Industry effects	0.509[*]	0.0670
	(0.251)	(0.206)
Debt	-3.219	0.320
	(2.250)	(1.506)
Performance	-2.241	0.649
	(3.786)	(2.732)
Constant	-8.991[*]	-7.453[**]
	(3.590)	(2.811)
N	78	136
Wald χ^2	15.54[***]	12.00[*]
Pseudo R^2	0.224	0.0927

Heteroskedasticity-robust standard errors in parentheses
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

Table 10: Result of Logistic Regression Testing Hypotheses 3

Independent variables	Dependent variable: Presence of stakeholder sympathetic member, 1=Yes, 0 = No	
	Past pressure (2007)	**Recent pressure (2009)**
Stakeholder pressure	0.248	0.148
	(0.233)	(0.133)
Firm size	1.588	3.180[***]
	(1.312)	(0.923)
Industry average directors	0.593[*]	-0.0836
	(0.298)	(0.196)
Debt	-3.963	-0.781
	(2.516)	(1.596)
Performance	-4.237	0.621
	(3.408)	(2.795)
Constant	-10.97[*]	-7.140[**]
	(4.915)	(2.702)
N	78	136
Wald χ^2	16.74[**]	14.30[*]
Pseudo-R^2	0.229	0.101

Heteroskedasticity-robust standard errors in parentheses
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

models because of its similarity with the R^2 of OLS regressions (Veall & Zimmermann, 1996). Based on these results, Hypothesis 2 was confirmed; stakeholder pressure is positively associated with the presence of a CSR committee in the firm. Note that the estimates from the analysis using stakeholder pressure and control variable data from 2009 has a similar positive sign but is not statistically significant. These results may lend support to my choice of using a two year lag as a reasonable estimate of the strategy implementation horizon of these organizations.

Hypothesis 3 changes the dependent variable to the presence of a stakeholder sympathetic member on the CSR committee. Table 10 presents the results of the logit regression testing Hypothesis 3. The results indicate that stakeholder pressure has a positive impact on the presence of a stakeholder sympathetic member on the CSR committee. Using stakeholder pressure data from 2009 does not change the direction of this positive effect. However, the co-efficients of regression estimates are not statistically significant and hence, Hypothesis 3 was not confirmed. In order to confirm whether I lacked the statistical power to detect an effect (Cohen, 1992), I ran a power analysis tailored for logistic regressions (Friendly, 2001). The test results indicate that with high probabilities of the presence of stakeholder sympathetic member in the committee at both the mean and mean plus one standard deviation values of stakeholder pressure, I needed at least 300 observations to detect an effect.

Hypothesis 5 proposes that the organizational and environmental discretion variables will moderate the relationship between stakeholder pressure and the strength of CSR committees. I used data from 2008 to construct the organizational and environmental discretion variables. Table 11 presents the results of the OLS regression

Table 11: Result of OLS Regression Testing Hypothesis 5

	Dependent variable: Strength of CSR committee		
	Model 1	**Model 2**	**Model 3**
Stakeholder pressure	0.02	0.00	0.02
	(0.01)	(0.03)	(0.03)
Firm size	0.06	0.06	0.06
	(0.04)	(0.05)	(0.05)
Industry effect	0.04[*]	0.02	0.03
	(0.02)	(0.02)	(0.02)
Performance	0.09	-0.17	0.02
	(0.30)	(0.37)	(0.29)
Organizational			
Size		0.05	
		(0.03)	
Debt		-0.22	
		(0.19)	
Slack		-0.00	
		(0.04)	
Environmental			
Market munificence			-0.06
			(0.78)
Market uncertainty			-14.92
			(22.73)
Market complexity			0.28
			(0.96)
Stakeholder pressure x size		0.00	
		(0.01)	
Stakeholder pressure x debt		0.11	
		(0.16)	
Stakeholder pressure x slack		0.00	
		(0.04)	
Stakeholder pressure x market munificence			-0.16
			(0.25)
Stakeholder pressure x market uncertainty			4.44
			(22.11)
Stakeholder pressure x market complexity			0.18
			(1.10)
Constant	-0.41	-0.21	-0.38
	(0.21)	(0.22)	(0.27)
N	78	75	78
R^2	0.13	0.23	0.16
F	4.73[**]	4.69[***]	5.73[***]

Heteroskedasticity robust standard errors in parentheses
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

testing Hypothesis 5. None of the main effects or interaction terms with either the organizational or the environmental variables are significant. Therefore Hypothesis 5 was not supported.

In Hypothesis 6, I am interested in finding out whether stakeholder governance mechanisms carry over the influence of stakeholder pressure to CSP. To construct the sample, I merged the stakeholder pressure data from 2004 to 2007 with the KLD data on stakeholder governance and CSP from 2005 to 2008 in order for the direction of potential causality to remain from the independent variable to the dependent variable. The resulting merged sample contained 1115 observations on 468 unique firms. The sample was further reduced to 660 observations on 175 firms upon imposing the requirement of at least three consecutive observations for each firm for inclusion in the sample. I confined the data to at least three consecutive observations per firm because I planned to use a lagged dependent variable in the model. Past CSP is an extremely strong predictor of current CSP and omission of this variable would seriously bias the results. To confirm the inclusion of this variable, I conducted a Ramsey (1969) regression specification error test without the first lag of CSP. I rejected the null hypothesis *(p<0.05)* which states that there are no omitted variables in the regression. Once the first lag of CSP was included, I failed to reject the null *(p=0.18)*. I included all other previously identified control variables to account for the impact of firm size, debt, performance, firm slack and R&D intensity on the CSP of a firm. Year effects were included but were found to be jointly insignificant and were hence removed from the model. I ran a Breusch-Pagan (1979) test and rejected the null hypothesis of homoskedasticity $(\chi^2=14.91, p<0.001)$; hence heteroskedasticity-robust standard errors

Table 12: Descriptive Statistics and Correlation of Variables Used to Test Hypothesis 6

	Means	s.d.	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
CSP strength	5.18	2.85	-														
CSP weakness	-5.71	3	-0.24	-													
CSP overall	-0.27	1.8	0.59	0.64	-												
Stakeholder pressure	3.16	2.91	0.32	-0.55	-0.2	-											
Stakeholder governance strength	2.63	2.8	0.66	-0.3	0.27	0.28	-										
Stakeholder governance weakness	-5.5	3.3	-0.38	0.37	0.01	-0.49	-0.33	-									
Stakeholder governance overall	-1.43	1.77	0.17	0.11	0.22	-0.24	0.48	0.67	-								
Mean industry CSP strength	5.18	1.75	0.41	0.04	0.36	0.17	0.18	-0.18	-0.02	-							
Mean industry CSP weakness	-5.71	1.78	0.04	0.29	0.28	-0.28	-0.02	0.08	0.06	-0.09	-						
Mean industry CSP overall	-0.27	1.19	0.33	0.25	0.47	-0.09	0.12	-0.07	0.03	0.67	0.68	-					
Firm size	9.54	1.2	0.5	-0.64	-0.13	0.49	0.45	-0.44	-0.06	0.15	-0.31	-0.12	-				
Performance	0.07	0.07	0.24	0.05	0.23	0.19	0.19	-0.22	-0.05	0.17	0.05	0.16	0.04	-			
Debt	0.21	0.14	-0.34	-0.15	-0.39	-0.14	-0.26	0.22	0	-0.22	-0.09	-0.23	-0.15	-0.33	-		
Firm slack	1.45	0.77	-0.03	0.28	0.21	-0.11	-0.09	-0.02	-0.08	0.29	0.28	0.42	-0.28	0.29	-0.27	-	
R&D intensity	0.03	0.09	0.16	0.17	0.27	0.02	0.05	-0.1	-0.05	0.41	0.05	0.34	-0.04	-0.2	-0.12	0.48	-
R&D missing	0.38	0.49	-0.26	-0.16	-0.34	-0.11	-0.13	0.22	0.1	-0.34	-0.21	-0.41	0.09	-0.18	0.31	-0.35	-0.29

N=164, for year 2007.
Correlation co-efficients with a magnitude greater than |0.08| are statistically significant at $p<0.05$

were used and are reported. After the estimation, I conducted the Arellano-Bond (1991) test of autocorrelation and failed to reject the null hypothesis for both first ($p=0.25)$ and second ($p=0.65$) order auto-correlated disturbances. The results of this test suggest that serial correlation was not a problem and it alleviated concerns of using the lag of the dependent variable as an independent variable in the regression (Keele & Kelly, 2006).

As before, I ran three separate tests with CSP strengths, weakness and overall as dependent variable, stakeholder governance strength weakness and overall measures as the mediating variable respectively and stakeholder pressure as the independent variable in all models. Table 12 provides the descriptive statistics and correlations for the variables used to test Hypothesis 6. The year 2007 was chosen because it had the largest number of observations; choosing another year for running the correlation analysis does not change the findings. Because lagged CSP variables are highly correlated with CSP by construction, they have been omitted from the table. All other variables exhibit correlations within acceptable limits. I ran collinearity diagnostics after the regression analysis. Because the mean VIF was 1.5 and all the individual VIF values were under 2, I found no concern for issues stemming from multicollinearity.

In Hypothesis 6, I proposed that stakeholder governance mechanisms will mediate the relationship between stakeholder pressure and CSP. Researchers define a mediator as a variable that accounts for all or part of the direct relationship between an independent variable and a dependent variable (Baron & Kenny, 1986). To assess the effect of mediation, I followed the recommendations of Judd and Kenny (1981) and as a first step regressed CSP on stakeholder pressure. In the second step I regressed CSP on

Table 13: Results of OLS Regression Testing Hypothesis 6

	CSP strength			CSP weakness			CSP overall		
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**	**Model 7**	**Model 8**	**Model 9**
First lag of CSP	0.92^{***}	0.92^{***}	0.88^{***}	0.89^{***}	0.86^{***}	0.86^{***}	0.91^{***}	0.90^{***}	0.88^{***}
	(0.02)	(0.02)	(0.02)	(0.03)	(0.04)	(0.04)	(0.03)	(0.03)	(0.03)
Mean industry CSP	0.06^{*}	0.06^{*}	0.07^{**}	-0.03	-0.04	-0.04	0.04	0.04	0.04
	(0.03)	(0.03)	(0.03)	(0.03)	(0.03)	(0.03)	(0.04)	(0.03)	(0.03)
Firm size	0.05	0.09	0.06	-0.23^{***}	-0.21^{**}	-0.18^{**}	-0.05	-0.01	-0.01
	(0.04)	(0.05)	(0.05)	(0.07)	(0.07)	(0.07)	(0.03)	(0.03)	(0.03)
Performance	1.42^{*}	1.62^{**}	1.32^{*}	-0.06	0.34	0.66	0.85^{*}	1.14^{*}	1.22^{**}
	(0.58)	(0.59)	(0.58)	(0.68)	(0.70)	(0.74)	(0.43)	(0.44)	(0.45)
Debt	-0.52	-0.52	-0.47	-0.42	-0.56	-0.57	-0.38	-0.43	-0.43
	(0.27)	(0.27)	(0.27)	(0.34)	(0.36)	(0.36)	(0.23)	(0.23)	(0.24)
Firm slack	-0.14^{*}	-0.15^{*}	-0.14^{*}	-0.13	-0.15	-0.16	-0.15^{**}	-0.17^{**}	-0.16^{**}
	(0.07)	(0.07)	(0.07)	(0.09)	(0.09)	(0.09)	(0.05)	(0.05)	(0.05)
R&D intensity	0.82	0.90	0.72	2.46^{**}	2.71^{**}	2.83^{**}	1.78^{***}	1.97^{***}	1.97^{***}
	(0.78)	(0.78)	(0.79)	(0.91)	(0.94)	(0.93)	(0.35)	(0.36)	(0.35)
R&D missing	0.08	0.05	0.05	-0.22	-0.26^{*}	-0.30^{*}	-0.06	-0.10	-0.12
	(0.09)	(0.09)	(0.09)	(0.12)	(0.12)	(0.13)	(0.07)	(0.08)	(0.08)
Stakeholder pressure		-0.03^{*}	-0.03		-0.06^{*}	-0.05		-0.03^{*}	-0.03^{*}
		(0.01)	(0.01)		(0.03)	(0.02)		(0.01)	(0.01)
Stakeholder governance			0.08^{***}			0.04			0.05^{**}
			(0.02)			(0.02)			(0.02)
R^2	0.908	0.909	0.913	0.878	0.880	0.881	0.859	0.862	0.864
F	556.50^{***}	514.17^{***}	488.59^{***}	377.23^{***}	352.30^{***}	332.13^{***}	331.67^{***}	310.46^{***}	277.47^{***}

N = 452, 162 firms over three years

Robust standard errors in parentheses. Year effects were jointly insignificant. A constant was used but co-efficients are not reported.

$^{*} p < 0.05$, $^{**} p < 0.01$, $^{***} p < 0.001$

both stakeholder pressure and stakeholder governance. This two-step procedure is quantitatively similar to the method recommended by Baron and Kenny (1986) in which an addition step is included after the first step involving a regression of the dependent variable on the mediating variable. The two methods "yield identical estimates of mediation when the dependent variable is continuous and ordinary regression is used" (MacKinnon, Warsi, & Dwyer, 1995: 45), as is the case in this analysis.

I present the results of the OLS regression I ran to test Hypothesis 6 in Table 13; I ran three separate models for each dimension of the dependent variable. Model 1, Model 2 and Model 3 present the results with CSP strength as the dependent variable, Model 4, Model 5 and Model 6 present the results with CSP weakness as the dependent variable. Finally, Model 7, Model 8 and Model 9 present the results with CSP overall as the dependent variable. In the first model of each set (Model 1, Model 4 and Model 7), I entered all the control variables identified in prior research. In the second model (Model 2, Model 5 and Model 8), I entered the stakeholder pressure variable to determine if it could incrementally explain changes in CSP. Finally, in the third model of each set (Model 3, Model 6 and Model 9), I included the mediating variable stakeholder governance mechanisms. In Table 13, results indicate that the effect of stakeholder pressure on CSP is indeed mediated by strengths and weaknesses in stakeholder governance mechanisms.

While the methods outlined by Judd and Kenny (1981) and Baron and Kenny (1986) allow researchers to test meditational hypotheses, the Sobel-Goodman mediation tests allows researchers to assess the statistical significance of the mediation effect. (Baron & Kenny, 1986; Goodman, 1960; MacKinnon et al., 1995; Sobel, 1982). I

employed a Sobel-Goodman mediation test to ascertain whether stakeholder governance carried the impact of stakeholder pressure to CSP. In Table 14, I have presented the results of three mediation significance tests, run on all three dependent variables separately. In all tests, co-variates shown in Table 13 were also included. The co-efficients of the three tests are statistically significant ($p<0.05$) for CSP overall; 16% of the total effect of stakeholder pressure on CSP overall is mediated by overall stakeholder governance. In other words, stakeholder governance partially mediates the relationship between stakeholder pressure and CSP.

Table 14: Results of Sobel-Goodman Tests

	Dependent variable: CSP		
	Strength	*Weakness*	*Overall*
Sobel	-0.84	-1.91	-2.15[*]
Goodman-1	-0.83	-1.88	-2.09[*]
Goodman-2	-0.86	-1.94[*]	-2.20[*]
Proportion of total effect mediated	0.10	0.19	0.16

N=452
[*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

In Hypothesis 7, I proposed that managerial discretion contexts moderate the relationship between stakeholder pressure and CSP. In order to test the Hypothesis, I merged data on managerial discretion context variables taken from 2004 to 2007 to correspond with data on stakeholder proposals from 2004 to 2007. I matched this data to CSP data for the years 2005 to 2008 to maintain temporal separation between the independent and the dependent variables. The resulting sample consisted of 1115 observations on 468 firms. As before, I ensured that each firm had at least three years of data on all variables. The final merged sample used to run the analysis consisted of 664 observations on 176 firms over four years in an unbalanced panel. Table 15 displays the

descriptive statistics and correlations between variables for the year 2007, chosen because it had the largest number of observations. Correlations based on other years do not differ significantly from those presented in Table 15. I also ran collinearity diagnostics and determined that the condition index of the design matrix was 21, a value much lower than the recommended threshold of 30 indicating there were likely no problems of multicollinearity (Belsley et al., 1980). I tested for endogeneity due to omitted variables and rejected the null of the Hausman test $(\chi^2=242.20, p<0.001)$. Because year effects were also jointly significant I proceeded with the conservative two-way fixed-effects panel data estimation method. All models were tested for heteroskedasticity and serial correlation. I rejected the null hypothesis of homoskedasticity specified by the Wald test $(\chi^2=612.58, p<0.001)$. The null hypothesis of no serial correlation using Wooldridge's (2002) test was also rejected $(F=43.54, p<0.001)$. Therefore, I used and have reported cluster-robust standard errors. Results of the estimation with the three dependent variables, CSP strength, CSP weakness and CSP overall are presented in Table 16a, 15b and 15c respectively.

For each dependent variable, I ran the regression first with only the control variables and present those results in Model 1 of the respective table. In Model 2, I have shown the results of adding the independent variable stakeholder pressure into the regression. Model 3 in each table shows the results of including the main and interaction effects of organizational discretion variables and stakeholder pressure. Model 4 shows the main and interaction effects of environmental discretion variables with stakeholder pressure. Finally Model 5 in each table shows the results of running

Table 15: Descriptive Statistics and Correlation of Variables Used to Test Hypothesis 7

	Means	s.d.	1	2	3	4	5	6	7	8	9	10	11	12	13	14
1.CSP strength	5.19	2.84	-													
2.CSP weakness	-5.74	3.01	-0.24	-												
3.CSP overall	-0.28	1.8	0.59	0.65	-											
4.Mean industry CSPs	5.19	1.75	0.41	0.05	0.36	-										
5.Mean industry CSPw	-5.74	1.79	0.05	0.28	0.27	-0.09	-									
6.Mean industry CSP	-0.28	1.19	0.33	0.24	0.47	0.67	0.69	-								
7.Stakeholder pressure	3.16	2.9	0.32	-0.55	-0.21	0.17	-0.27	-0.08	-							
8.Firm size	9.54	1.19	0.5	-0.63	-0.13	0.15	-0.31	-0.12	0.48	-						
9.Debt	0.21	0.14	-0.34	-0.14	-0.38	-0.22	-0.08	-0.22	-0.14	-0.15	-					
10.Performance	0.07	0.07	0.24	0.06	0.23	0.19	0.02	0.15	0.19	0.04	-0.33	-				
11.Firm slack	1.46	0.77	-0.02	0.27	0.2	0.29	0.28	0.42	-0.1	-0.28	-0.27	0.29	-			
12.R&D intensity	0.04	0.09	0.17	0.16	0.26	0.4	0.06	0.34	0.02	-0.04	-0.12	-0.2	0.49	-		
13.Market munificence	1.07	0.05	-0.04	-0.02	-0.05	-0.06	-0.04	-0.07	0.05	-0.02	-0.24	0.11	0.14	0.08	-	
14.Market uncertainty	1	0	-0.07	-0.13	-0.17	-0.12	-0.23	-0.26	0.11	0.01	0.08	0.22	0.02	-0.11	-0.32	-
15.Market complexity	0.07	0.08	-0.13	-0.1	-0.18	-0.21	-0.16	-0.28	0.12	-0.05	-0.07	0.15	0.04	-0.15	-0.05	0.53

N=165, for year 2007
Correlation co-efficients at and above |0.16| are statistically significant at $p<0.05$

Table 16a: Fixed-Effects Panel Data Regression Results Testing Hypothesis 7

	Dependent variable: CSP strength				
	Model 1a	**Model 2a**	**Model 3a**	**Model 4a**	**Model 5a**
Lag of CSP strength	0.13	0.13	0.13[*]	0.11	0.11
	(0.06)	(0.06)	(0.06)	(0.06)	(0.06)
Mean industry CSP strength	0.17[*]	0.17[*]	0.18[*]	0.09	0.10
	(0.08)	(0.08)	(0.08)	(0.09)	(0.09)
Performance	0.60	0.59	0.82	0.58	0.78
	(0.70)	(0.70)	(0.99)	(0.69)	(0.97)
Stakeholder pressure		-0.00	-0.01	-0.01	-0.01
		(0.03)	(0.03)	(0.03)	(0.03)
Firm size			0.27		0.23
			(0.20)		(0.17)
Debt			-0.40		-0.27
			(0.91)		(0.96)
Firm slack			-0.04		-0.09
			(0.14)		(0.15)
R&D intensity			1.22		1.07
			(1.35)		(1.38)
R&D missing			-0.08		-0.16
			(0.21)		(0.22)
Market munificence				0.67	1.11
				(2.21)	(2.37)
Market uncertainty				87.96	93.79
				(52.00)	(51.89)
Market complexity				7.89	7.41
				(4.21)	(4.21)
Stakeholder pressure x firm size			0.01		0.01
			(0.02)		(0.02)

Stakeholder pressure x debt				0.09	0.10
				(0.20)	(0.23)
Stakeholder pressure x firm slack				-0.03	-0.02
				(0.04)	(0.04)
Stakeholder pressure x R&D intensity				0.33	0.34
				(0.52)	(0.53)
Stakeholder pressure x market munificence				-0.13	-0.14
				(0.41)	(0.46)
Stakeholder pressure x market uncertainty				-13.88*	-14.68**
				(5.44)	(5.61)
Stakeholder pressure x market complexity				0.37	0.37
				(0.22)	(0.23)
Constant	3.64***	3.64***	3.59***	4.08***	4.09***
	(0.49)	(0.49)	(0.53)	(0.54)	(0.59)
R^2 (within)	0.234	0.235	0.244	0.274	0.283
F	17.36***	14.74***	8.228***	8.513***	6.030***

N=455, 165 firms over three years, unbalanced panel.

Heteroskedasticity and serial correlation robust standard errors in parentheses

Two-way fixed effects were used, year effects were jointly significant in all models, co-efficients not reported.

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 16b. Fixed-Effects Panel Data Regression Results Testing Hypothesis 7

	Dependent variable: CSP weakness				
	Model 1b	**Model 2b**	**Model 3b**	**Model 4b**	**Model 5b**
Lag of CSP weakness	0.19**	0.19**	0.18*	0.19**	0.17*
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Mean industry CSP weakness	0.00	0.00	-0.01	-0.04	-0.05
	(0.10)	(0.10)	(0.10)	(0.09)	(0.09)
Performance	0.81	0.84	0.48	0.82	0.36
	(0.97)	(0.96)	(1.35)	(0.99)	(1.45)
Stakeholder pressure		0.03	0.04	0.03	0.04
		(0.04)	(0.04)	(0.04)	(0.04)
Firm size			-0.18		-0.25
			(0.48)		(0.52)
Debt			-3.63**		-3.76**
			(1.37)		(1.38)
Firm slack			-0.19		-0.12
			(0.22)		(0.23)
R&D intensity			3.36		3.57
			(2.37)		(2.35)
R&D missing			-0.60		-0.66
			(0.62)		(0.61)
Market munificence				-5.27*	-6.61*
				(2.43)	(2.73)
Market uncertainty				-10.21	-22.42
				(69.14)	(75.14)
Market complexity				-3.14	-2.64
				(3.41)	(3.14)
Stakeholder pressure x firm size			0.02		0.01
			(0.04)		(0.03)

Stakeholder pressure x debt			0.24		0.33
			(0.27)		(0.27)
Stakeholder pressure x firm slack			-0.06		-0.06
			(0.07)		(0.07)
Stakeholder pressure x R&D intensity			0.80		0.89
			(0.75)		(0.73)
Stakeholder pressure x market munificence				-0.82	-0.60
				(0.62)	(0.72)
Stakeholder pressure x market uncertainty				3.19	0.47
				(8.00)	(8.73)
Stakeholder pressure x market complexity				-0.27	-0.12
				(0.39)	(0.45)
Constant	-4.83***	-4.81***	-4.81***	-5.04***	-5.07***
	(0.69)	(0.69)	(0.72)	(0.65)	(0.70)
R^2 (within)	0.176	0.178	0.223	0.205	0.251
F	9.068***	7.600***	5.004***	6.218***	5.687***

N=455, 165 firms over three years, unbalanced panel.

Heteroskedasticity and serial correlation robust standard errors in parentheses

Two-way fixed effects were used, year effects were jointly significant in all models, co-efficients not reported.

$^{*}p < 0.05$, $^{**}p < 0.01$, $^{***}p < 0.001$

Table 16c. Fixed-Effects Panel Data Regression Results Testing Hypothesis 7

	Dependent variable: CSP overall				
	Model 1c	**Model 2c**	**Model 3c**	**Model 4c**	**Model 5c**
Lag of CSP overall	0.16**	0.16**	0.16*	0.17**	0.16*
	(0.06)	(0.06)	(0.06)	(0.06)	(0.06)
Mean industry CSP overall	0.04	0.04	0.02	-0.02	-0.03
	(0.12)	(0.12)	(0.12)	(0.12)	(0.12)
Performance	0.74	0.76	0.72	0.74	0.64
	(0.52)	(0.52)	(0.77)	(0.52)	(0.77)
Stakeholder pressure		0.02	0.02	0.01	0.02
		(0.02)	(0.02)	(0.02)	(0.02)
Firm size			0.03		-0.02
			(0.24)		(0.25)
Debt			-2.00**		-1.97**
			(0.74)		(0.74)
Firm slack			-0.12		-0.11
			(0.12)		(0.12)
R&D intensity			2.30**		2.31**
			(0.75)		(0.73)
R&D missing			-0.33		-0.39
			(0.39)		(0.40)
Market munificence				-2.26	-2.69
				(1.53)	(1.61)
Market uncertainty				39.85	37.48
				(35.40)	(38.08)
Market complexity				2.77	2.91
				(2.57)	(2.55)
Stakeholder pressure x firm size			0.01		0.01
			(0.02)		(0.02)

Stakeholder pressure x debt			0.15		0.21
			(0.14)		(0.15)
Stakeholder pressure x firm slack			-0.04		-0.04
			(0.03)		(0.03)
Stakeholder pressure x R&D intensity			0.55*		0.59*
			(0.25)		(0.25)
Stakeholder pressure x market munificence				-0.52	-0.42
				(0.31)	(0.34)
Stakeholder pressure x market uncertainty				-5.31	-6.77
				(4.37)	(4.82)
Stakeholder pressure x market complexity				0.02	0.10
				(0.21)	(0.24)
Constant	-0.32***	-0.32***	-0.24	-0.34***	-0.22
	(0.05)	(0.05)	(0.15)	(0.05)	(0.15)
R^2 (within)	0.0481	0.0500	0.101	0.0657	0.117
F	3.546***	3.017***	3.171***	2.478***	3.010***

N=455, 165 firms over three years, unbalanced panel.

Heteroskedasticity and serial correlation robust standard errors in parentheses

Two-way fixed effects were used, year effects were jointly significant in all models, co-efficients not reported.

$^* p < 0.05$, $^{**} p < 0.01$, $^{***} p < 0.001$

the regression on the full model with all the variables included and was used to report the findings. Based on the results of the regression, the interaction of stakeholder pressure with one organizational discretion variable (*R&D intensity* in Table 16c) and one environmental discretion context variable (*market uncertainty* in Table 16a) is statistically significant at *p<0.05*. However because the main effect of stakeholder pressure on CSP in those models is not statistically significant, I will not attempt to interpret the moderation effects; Hypothesis 7 was therefore not confirmed.

In Hypothesis 8, I proposed that managerial discretion contexts moderate the relationship between corporate social performance (CSP) and corporate financial performance (CFP). In order to test the hypothesis, I merged CSP data on all available years (2005 to 2008) with firm financial performance data from 2006 to 2009. The temporal separation would allow me to make a causal argument in favor of CSP impacting CFP and not the other way around. The organizational and environmental discretion variables were gathered for years corresponding to years for which CSP data was available (2005 to 2008). The initial merged sample consisted of 6109 observations on 1970 firms over four years. As before, in order to ensure there are no gaps in the time series, each firm was required to have at least three consecutive years of data to be included in the sample. I dropped extreme values for the dependent variable and some independent variables to ensure that no single observation or set of observations influences the regression estimates. The final sample contained 3423 observations on 1144 firms. The use of a lagged dependent variable as an explanatory variable reduced the size of the final regression sample to 3107 (3620 for Tobin's Q) observations on

Table 17: Descriptive Statistics And Correlations For Variables Used To Test Hypothesis 8

	Means	s.d.	1	2	3	4	5	6	7	8	9	10	11	12
1.ROA	0	0.17	-											
2.Mean industry ROA	0	0.04	0.13	-										
3.CSP strength	2.1	2.22	0.14	0.07	-									
4.CSP weakness	-2.36	1.99	-0.07	-0.13	-0.46	-								
5.CSP overall	-0.13	1.1	0.07	-0.05	0.59	0.44	-							
6.Firm size	7.37	1.6	0.22	0.14	0.61	-0.63	0.05	-						
7.Debt	0.4	0.18	0	-0.05	0.13	-0.18	-0.03	0.32	-					
8.Firm slack	2.43	1.93	-0.01	-0.05	-0.23	0.3	0.04	-0.48	-0.49	-				
9.R&D intensity	0.06	0.23	-0.26	-0.03	-0.05	0.14	0.07	-0.34	-0.11	0.31	-			
10.R&D missing	0.38	0.49	-0.03	-0.07	-0.09	-0.14	-0.21	0.1	0.14	-0.26	-0.22	-		
11.Market munificence	1.07	0.04	-0.01	-0.03	-0.08	0.02	-0.07	-0.05	-0.11	0.05	0.03	0.04	-	
12.Market uncertainty	1	0	0.06	0.23	-0.01	-0.05	-0.06	0.07	0.03	-0.05	-0.11	0.06	-0.32	-
13.Market complexity	0.06	0.06	0.05	0.21	-0.01	-0.04	-0.04	0.15	0.05	-0.05	-0.14	-0.05	-0.17	0.55

N=1056 for year 2008
Correlation co-efficients above |0.7 | are statistically significant at $p<0.05$

Table 18a: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Return on assets				
	Model 1a	Model 2a	Model 3a	Model 4a	Model 5a
First lag of ROA	-0.25***	-0.25***	-0.25***	-0.25***	-0.25***
	(0.04)	(0.04)	(0.05)	(0.04)	(0.05)
Mean industry ROA	0.57***	0.58***	0.60***	0.57***	0.59***
	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)
CSP strength		0.00	0.00	0.00	0.00
		(0.00)	(0.00)	(0.00)	(0.00)
Firm size			0.05*		0.05*
			(0.02)		(0.02)
Debt			0.09*		0.09*
			(0.04)		(0.04)
Firm slack			0.00		0.00
			(0.00)		(0.00)
R&D intensity			-0.09*		-0.09*
			(0.04)		(0.04)
R&D missing			-0.00		-0.00
			(0.03)		(0.03)
Market munificence				-0.01	-0.07
				(0.10)	(0.10)
Market uncertainty				-0.84	-0.63
				(2.46)	(2.47)
Market complexity				-0.19	-0.16
				(0.17)	(0.18)
CSP strength x firm size			0.00		0.00
			(0.00)		(0.00)
CSP strength x firm debt			0.02		0.02
			(0.02)		(0.02)
CSP strength x firm slack			0.00		0.00
			(0.00)		(0.00)
CSP strength x R&D intensity			-0.03		-0.03

	(1)	(2)	(3)	(4)	(5)
			(0.03)		(0.03)
CSP strength x market munificence				0.03	0.03
				(0.04)	(0.04)
CSP strength x market uncertainty				1.22	1.28
				(0.83)	(0.83)
CSP strength x market complexity				0.01	-0.01
				(0.03)	(0.03)
Constant	0.02^{***}	0.02^{***}	0.02	0.02^{***}	0.02
	(0.00)	(0.00)	(0.01)	(0.00)	(0.01)
R^2	0.146	0.146	0.163	0.147	0.164
F	44.80^{***}	38.42^{***}	16.96^{***}	18.01^{***}	12.11^{***}

N = 3107 observations – 1056 firms over four years (unbalanced panel)
Heteroskedasticity and serial correlation robust standard errors in parentheses
* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 18b: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Return on assets				
	Model 1b	Model 2b	Model 3b	Model 4b	Model 5b
First lag of ROA	-0.25***	-0.25***	-0.25***	-0.25***	-0.25***
	(0.04)	(0.04)	(0.05)	(0.04)	(0.05)
Mean industry ROA	0.57***	0.57***	0.60***	0.57***	0.60***
	(0.08)	(0.08)	(0.08)	(0.08)	(0.09)
CSP weakness		-0.01	-0.01	-0.01*	-0.01
		(0.00)	(0.00)	(0.00)	(0.00)
Firm size			0.05*		0.05*
			(0.02)		(0.02)
Debt			0.10*		0.10*
			(0.04)		(0.04)
Firm slack			0.00		0.00
			(0.00)		(0.00)
R&D intensity			-0.06		-0.06
			(0.05)		(0.05)
R&D missing			-0.00		-0.00
			(0.03)		(0.03)
Market munificence				-0.00	-0.06
				(0.10)	(0.10)
Market uncertainty				-1.12	-0.80
				(2.41)	(2.47)
Market complexity				-0.21	-0.15
				(0.19)	(0.19)
CSP weakness x firm size			0.00		0.00
			(0.00)		(0.00)
CSP weakness x firm debt			-0.03*		-0.03
			(0.01)		(0.01)
CSP weakness x firm slack			-0.00		-0.00
			(0.00)		(0.00)
CSP weakness x R&D intensity			-0.01		-0.01
			(0.01)		(0.01)

CSP weakness x market munificence				0.02	0.02
				(0.03)	(0.03)
CSP weakness x market uncertainty				0.79	0.56
				(0.74)	(0.74)
CSP weakness x market complexity				-0.00	0.01
				(0.02)	(0.02)
Constant	0.02***	0.02***	0.02	0.02***	0.02
	(0.00)	(0.00)	(0.01)	(0.00)	(0.01)
R^2	0.146	0.147	0.164	0.147	0.164
F	44.80***	35.86***	15.24***	16.68***	10.92***

N = 3107 observations – 1056 firms over four years (unbalanced panel)

Heteroskedasticity and serial correlation robust standard errors in parentheses

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 18c: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Return on assets				
	Model 1c	**Model 2c**	**Model 3c**	**Model 4c**	**Model 5c**
First lag of ROA	-0.25***	-0.25***	-0.25***	-0.25***	-0.25***
	(0.04)	(0.04)	(0.05)	(0.04)	(0.05)
Mean industry ROA	0.57***	0.57***	0.60***	0.58***	0.60***
	(0.08)	(0.08)	(0.08)	(0.08)	(0.09)
CSP overall		-0.00	-0.01	-0.00	-0.01
		(0.00)	(0.01)	(0.00)	(0.01)
Firm size			0.05*		0.05*
			(0.02)		(0.02)
Debt			0.08*		0.08*
			(0.04)		(0.04)
Firm slack			0.00		0.00
			(0.00)		(0.00)
R&D intensity			-0.06		-0.07
			(0.05)		(0.05)
R&D missing			0.00		-0.00
			(0.03)		(0.03)
Market munificence				0.00	-0.06
				(0.10)	(0.10)
Market uncertainty				-0.92	-0.86
				(2.46)	(2.46)
Market complexity				-0.20	-0.15
				(0.18)	(0.18)
CSP overall x firm size			0.00		0.00
			(0.00)		(0.00)
CSP overall x firm debt			0.00		0.00
			(0.03)		(0.03)
CSP overall x firm slack			0.00		0.00

	(1)	(2)	(3)	(4)	(5)
				(0.00)	(0.00)
CSP overall x R&D intensity				-0.02	-0.02
				(0.02)	(0.02)
CSP overall x market munificence				0.07	0.08
				(0.06)	(0.06)
CSP overall x market uncertainty				4.19*	3.76
				(2.08)	(2.09)
CSP overall x market complexity				-0.01	-0.00
				(0.05)	(0.05)
Constant	0.02***	0.02***	0.02	0.02***	0.02*
	(0.00)	(0.00)	(0.01)	(0.00)	(0.01)
R^2	0.146	0.146	0.162	0.147	0.163
F	44.80***	37.33***	16.07***	17.39***	11.49***

N = 3107 observations – 1056 firms over four years (unbalanced panel)
Heteroskedasticity and serial correlation robust standard errors in parentheses
* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 18d: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Tobin's Q				
	Model 1d	Model 2d	Model 3d	Model 4d	Model 5d
First lag of Tobin's Q	-0.04	-0.04	-0.08*	-0.04	-0.09*
	(0.03)	(0.03)	(0.03)	(0.03)	(0.03)
Mean industry Tobin's Q	0.62***	0.62***	0.54***	0.62***	0.55***
	(0.07)	(0.07)	(0.06)	(0.07)	(0.06)
CSP strength		-0.03	-0.02	-0.03	-0.02
		(0.02)	(0.02)	(0.02)	(0.02)
Firm size			-0.51***		-0.52***
			(0.06)		(0.06)
Debt			0.23		0.22
			(0.15)		(0.15)
Firm slack			-0.02		-0.02
			(0.02)		(0.02)
R&D intensity			0.44		0.45
			(0.34)		(0.34)
R&D missing			-0.00		-0.02
			(0.12)		(0.12)
Market munificence				0.26	0.45
				(0.39)	(0.38)
Market uncertainty				1.55	2.19
				(9.82)	(10.46)
Market complexity				-0.54	-0.75
				(0.78)	(0.75)
CSP strength x firm size			0.03*		0.03*
			(0.01)		(0.01)
CSP strength x firm debt			-0.05		-0.04
			(0.06)		(0.06)
CSP strength x firm slack			-0.00		-0.00

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	(1)	(2)	(3)	(4)	(5)
				(0.01)	(0.01)
CSP strength x R&D intensity				0.29	0.30
				(0.22)	(0.22)
CSP strength x market munificence				0.23	$0.30^{\dagger}$
				(0.15)	(0.16)
CSP strength x market uncertainty				3.75	3.42
				(5.00)	(5.17)
CSP strength x market complexity				0.30	0.31
				(0.19)	(0.22)
Constant	0.49^{***}	0.49^{***}	0.57^{***}	0.49^{***}	0.58^{***}
	(0.09)	(0.09)	(0.10)	(0.09)	(0.10)
R^2		0.287	0.287	0.332	0.288	0.334
F		176.8	141.4	56.62	65.59	40.26

N = 3620 observations – 1259 firms over four years (unbalanced panel)
Heteroskedasticity and serial correlation robust standard errors in parentheses
$^{\dagger} p < 0.10$, $^{*} p < 0.05$, $^{**} p < 0.01$, $^{***} p < 0.001$

Table 18e: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Tobin's Q				
	Model 1e	**Model 2e**	**Model 3e**	**Model 4e**	**Model 5e**
First lag of Tobin's Q	-0.04	-0.04	-0.08[*]	-0.04	-0.08[*]
	(0.03)	(0.03)	(0.04)	(0.03)	(0.04)
Mean industry Tobin's Q	0.62[***]	0.61[***]	0.55[***]	0.60[***]	0.54[***]
	(0.07)	(0.07)	(0.06)	(0.07)	(0.06)
CSP weakness		-0.03	-0.04	-0.03	-0.04[†]
		(0.02)	(0.02)	(0.02)	(0.02)
Firm size			-0.53[***]		-0.54[***]
			(0.06)		(0.06)
Debt			0.22		0.21
			(0.15)		(0.15)
Firm slack			-0.02		-0.03
			(0.02)		(0.02)
R&D intensity			-0.05		-0.05
			(0.18)		(0.18)
R&D missing			-0.01		-0.01
			(0.13)		(0.12)
Market munificence				0.26	0.55
				(0.40)	(0.39)
Market uncertainty				-0.16	1.08
				(9.92)	(10.51)
Market complexity				-0.75	-0.96
				(0.79)	(0.77)
CSP strength x firm size			0.01		0.01
			(0.01)		(0.01)
CSP strength x firm debt			0.08		0.06
			(0.07)		(0.07)
CSP strength x firm slack			0.01		0.01

				(0.01)	(0.01)
CSP strength x R&D intensity				0.15	0.15
				(0.12)	(0.12)
CSP strength x market munificence				-0.23	-0.34[†]
				(0.17)	(0.18)
CSP strength x market uncertainty				5.16	7.48[*]
				(3.57)	(3.31)
CSP strength x market complexity				-0.21	-0.25
				(0.18)	(0.21)
Constant	0.49[***]	0.50[***]	0.62[***]	0.50[***]	0.64[***]
	(0.09)	(0.09)	(0.10)	(0.09)	(0.10)
R^2	0.287	0.287	0.333	0.289	0.335
F	176.8	144.0	56.61	67.33	41.51

N = 3620 observations – 1259 firms over four years (unbalanced panel)
Heteroskedasticity and serial correlation robust standard errors in parentheses
[†] $p < 0.10$, [*] $p < 0.05$, [**] $p < 0.01$, [***] $p < 0.001$

Table 18f: Fixed-Effects Regression Results Testing Hypothesis 8

Variables	Dependent variable: Tobin's Q				
	Model 1f	Model 2f	Model 3f	Model 4f	Model 5f
First lag of Tobin's Q	-0.04	-0.04	-0.08*	-0.04	-0.08*
	(0.03)	(0.03)	(0.03)	(0.03)	(0.04)
Mean industry Tobin's Q	0.62***	0.61***	0.55***	0.60***	0.53***
	(0.07)	(0.07)	(0.06)	(0.07)	(0.06)
CSP overall		-0.06*	-0.07*	-0.06*	-0.07*
		(0.03)	(0.03)	(0.03)	(0.03)
Firm size			-0.51***		-0.52***
			(0.06)		(0.06)
Debt			0.25		0.24
			(0.15)		(0.15)
Firm slack			-0.02		-0.02
			(0.02)		(0.02)
R&D intensity			0.13		0.13
			(0.24)		(0.24)
R&D missing			-0.00		-0.00
			(0.13)		(0.12)
Market munificence				0.21	0.46
				(0.39)	(0.38)
Market uncertainty				3.20	6.04
				(10.43)	(11.32)
Market complexity				-0.59	-0.72
				(0.81)	(0.83)
CSP strength x firm size			0.03†		0.03†
			(0.02)		(0.02)
CSP strength x firm debt			0.00		0.00
			(0.10)		(0.10)
CSP strength x firm slack			0.00		0.00

	(1)	(2)	(3)	(4)	(5)
			(0.02)		(0.02)
CSP strength x R&D intensity			$0.30^{\dagger}$		$0.30^{\dagger}$
			(0.18)		(0.18)
CSP strength x market munificence				-0.12	-0.22
				(0.31)	(0.34)
CSP strength x market uncertainty				18.66	$23.18^{\dagger}$
				(12.76)	(12.62)
CSP strength x market complexity				-0.12	-0.17
				(0.29)	(0.28)
Constant	0.49^{***}	0.49^{***}	0.61^{***}	0.51^{***}	0.63^{***}
	(0.09)	(0.09)	(0.10)	(0.09)	(0.10)
R^2	0.287	0.288	0.334	0.289	0.336
F	176.8	143.9	56.21	67.00	40.63

N = 3620 observations – 1259 firms over four years (unbalanced panel)

Heteroskedasticity and serial correlation robust standard errors in parentheses

$^{\dagger}\,p < 0.10$, $^{*}\,p < 0.05$, $^{**}\,p < 0.01$, $^{***}\,p < 0.001$

1056 (1259 for Tobin's Q) firms. Descriptive statistics and correlations for the year 2008 (with the largest number of observations) are presented in Table 17. Changing the. year for which correlations are tested does not change the findings. Overall, all variables have reasonable correlations amongst each other. Collinearity diagnostics reveal that the condition number for the design matrix is well under 30. I ran tests of endogeneity, heteroskedasticity plus serial correlation and rejected the null for all of them. I therefore proceeded with two-way fixed-effects estimation with cluster-robust standard errors.

For each dimension of CSP strength, weakness, and overall a separate set of models was analyzed and the results are presented in Table 18a, 18b and 18c respectively. In each table, Model 1 only included the control variables. Model 2 introduced the effect of the independent variable. Model 3 introduced the organization discretion indicators and their interactions with CSP, Model 4 repeated the same with environment discretion variables. Finally, Model 5 presents the results of the full model including all variables. Based on the results of the analysis, none of the organizational or the environmental discretion indicators moderate the relationship between CSP and Performance. These results indicate that when all other relevant factors such as specification errors and assumption violations are controlled, the relationship between CSP and CFP is reduced to statistical insignificance. Therefore Hypothesis 8 could not be confirmed using ROA as an operationalization for firm performance.

I conducted a power test using the *powerreg* command in STATA 10.0. The results indicated that I had sufficient statistical power to detect an effect in a regression of five variables focused on the relative effect of adding one predictor variable. I re-ran

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all models using ROS and ROE as dependent variables but the results were not materially different and hence are not reported. I then used Tobin's Q as a dependent variable in the same regressions. The results are presented again in three separate tables, Table 18d, 18e and 18f, each testing CSP strength, CSP weakness and CSP overall as the key independent variable and organizational and environmental discretion indicators as potential moderators of the relationship between CSP and performance. Based on the results in Table 18c, while overall CSP emerged as a statistically significant predictor of performance ($p<0.05$) none of the interactions with either the organization or the environmental discretion variables turned out to be statistically significant. Therefore Hypothesis 8 is rejected using all generally accepted operationalizations of firm performance.

Finally, in Hypothesis 9, I test whether the relationship between CSP and CFP suffers from a sample selection problem. In order to test this hypothesis, I followed prior research (Campa & Kedia, 2002; Heckman, 1979) and adopted a three-step approach. In the first step I estimated the CSP-CFP relationship in a sample with all industrial firms that report financial performance regardless of their selection into KLD CSP rankings. In the second step, I took the probability of a firm's CSP being rated by KLD as a proxy for a firm's decision to engage in CSP, and determined the antecedents of this decision. In particular, as hypothesized, I use stakeholder pressure as a likely factor impacting a firm's decision to engage in CSP. I saved the predicted results and after applying statistical transformations, used the transformed variable in a regression predicting the relationship between CSP and CFP. The final step is carried out in a sample restricted to only those firms whose CSP is ranked by KLD. Using this method,

I effectively replicated prior work which has used only those firms whose CSP ratings are ranked by KLD to investigate the CSP-CFP relationship. However, the results of my estimation would include the statistical correction I have applied by accounting for the endogenous decision of firms to engage in CSP. Thus the results from this regression would provide the unbiased estimates and correct inferences of the direction of relationship between CSP and CFP having accounted for the endogeneity problem of self selection (Heckman, 1979).

I began by merging all the available CSP data (2005-2008) from KLD with all the available financial data on industrial firms from COMPUSTAT for the years 2006 to 2009 in order to keep the direction of potential causality from CSP to CFP. The initial merged sample contained I then merged data on stakeholder resolutions from Risk Metrics for the years 2004 to 2007 in order to retain the direction of potential causality from stakeholder pressure to CSP. I also merged control variable for various steps of the estimation process. In order to estimate the CSP-CFP relationship, organizational level control variables were constructed to coincide with the duration of the independent variable CSP (2005 to 2008). When estimating the stakeholder pressure and CSP regressions, I used organizational control variables contemporaneous to stakeholder pressure for the years 2004 to 2007.

The merging of CSP data with CFP data resulted in 9909 observations. As before, I limited the sample to at least three consecutive years of data on all variables for each firm. I used Tobin's Q to denote market-based financial performance of the firm. I also included the lagged values of the dependent variable plus past accounting financial performance as relevant predictors of the current Tobin's Q of the firm.

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Because I found problems of endogeneity due to omitted variables, group-wise heteroskedasticity and serial correlation, I used the two-way fixed-effects estimation method and have reported cluster-robust standard errors. The final sample used to run the first stage of the regressions consisted of 9754 observations on 2591 firms over four years (actual date ranges from year 2004 to 2009 for different variables).

As a first step, I created a dichotomous variable *decision to engage in CSP* which took on values of 1 if the CSP ratings were available and reported by KLD; the variable was coded zero otherwise. In Table 19, I have reported the results of the regression using the decision to engage in CSP as a predictor of firm performance. In Model 1, I only entered the primary control variables. In Model 2, I added the predictor variable and it was statistically significant *(p<0.05)* indicating the main effect of CSP on CFP. I then tested the robustness of my specification by introducing the lagged values of performance in Model 3 and the first lag of the dependent variable in Model 4 respectively. I then ensured that the predictor remains a significant variable if added after these control variables were included in the model. Model 5 shows the results of the regression run with the addition of predictor variables and Model 6 shows the full model when the predictor is entered as the final variable in the regression. These results appear to indicate that there is a statistically significant negative relationship between a firm's decision to engage in CSP and financial performance *(p<0.05)*.

In the second step, I used the *decision to engage in CSP* variable as a dependent variable and used several possible predictor variables identified in prior research in a probit model. A probit model is recommended in the second step (Heckman, 1979) because the variable *decision to engage in CSP* takes on values of 0 and 1. The purpose

Table 19: Fixed-Effects Regression Results Testing Hypothesis 9

Variables	Dependent variable: Tobin's Q					
	Model 1	**Model 2**	**Model 3**	**Model 4**	**Model 5**	**Model 6**
Firm size	-0.185***	-0.182***	-0.202***	-0.193***	-0.211***	-0.207***
	(0.0330)	(0.0330)	(0.0293)	(0.0285)	(0.0290)	(0.0290)
Firm slack	-0.000201	-0.000199	-0.000127	-0.000192	-0.000271	-0.000268
	(0.000532)	(0.000529)	(0.000510)	(0.000524)	(0.000572)	(0.000567)
Firm leverage	0.192***	0.192***	0.195***	0.252***	0.261***	0.261***
	(0.0548)	(0.0548)	(0.0546)	(0.0544)	(0.0542)	(0.0542)
Mean industry Tobin's Q	0.698***	0.700***	0.702***	0.670***	0.676***	0.677***
	(0.0516)	(0.0515)	(0.0515)	(0.0499)	(0.0505)	(0.0504)
Decision to engage in CSP		-0.0616*	-0.0593*	-0.0700*		-0.0694*
		(0.0300)	(0.0299)	(0.0295)		(0.0297)
Past performance			0.00362***	0.00364**	0.00212*	0.00210*
			(0.00107)	(0.00117)	(0.00103)	(0.00102)
Lag of Tobin's Q (1yr)				0.104***	0.112***	0.113***
				(0.0172)	(0.0172)	(0.0172)
Constant	1.464***	1.477***	1.588***	1.392***	1.449***	1.458***
	(0.208)	(0.207)	(0.187)	(0.185)	(0.188)	(0.187)
R^2 (within)	0.312	0.313	0.316	0.326	0.328	0.329
F	336.0***	296.7***	265.8***	246.6***	265.5***	241.6***

N=9754, 2591 firms over four years, unbalanced panel

Heteroskedasticity and serial correlation robust cluster standard errors in parentheses.

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 20: Heckman Selection Model Testing Hypothesis 9

	Tobin's Q Model 1	Decision to engage in CSP Model 2	Model 3	Tobin's Q Model 4
Lag of Tobin's Q (1yr)	0.113***			0.0874***
	(0.0172)			(0.0215)
Mean industry Tobin's Q	0.677***			0.819***
	(0.0504)			(0.0309)
Past performance	0.00210*			-0.0326*
	(0.00102)			(0.0153)
Firm size	-0.207***			-0.285***
	(0.0290)			(0.0570)
Debt	0.261***			0.313***
	(0.0542)			(0.0849)
Firm slack	-0.000268			-0.0138
	(0.000567)			(0.0124)
Decision to engage in CSP	-0.0694*			
	(0.0297)			
Lambda				0.255*
				(0.120)
Stakeholder pressure			1.721***	
			(0.242)	
Firm size		0.472***	0.455***	
		(0.0116)	(0.0118)	
Performance		0.175	0.197	
		(0.151)	(0.149)	
Debt		-1.007***	-0.988***	
		(0.0962)	(0.0963)	
Firm slack		0.00168**	0.00160**	
		(0.000533)	(0.000520)	
Constant	1.458***	-3.948***	-3.985***	2.069***
	(0.187)	(0.160)	(0.175)	(0.442)
N	9754	9711	9711	4548
Pseudo R^2		0.297	0.306	
χ^2		2080.3	1944.8	
R^2 (within)	0.329			0.360
F	241.6***			156.1***

Heteroskedasticity robust errors are shown in parentheses
Year effects were used in all regressions, co-efficients are not displayed
$^\dagger p < 0.10$, $^* p < 0.05$, $^{**} p < 0.01$, $^{***} p < 0.001$

of this step is to account for possible explanations for a firm's decision to engage in CSP. I limited the sample to those observations over which I had earlier investigated the models in Table 19, in order to reduce other differences between samples. Thus Model 1 in Table 20 is run on the full sample of 9754 observations. Model 2 and Model 3 use stakeholder pressure and therefore the total number of observations is reduced to 9711. Finally, in Model 4, the sample comprises only those observations for which the variable *decision to engage in CSP* takes on values of 1.

To test Hypothesis 9, I also introduced the role of stakeholder pressure on firms as a relevant predictor of the decision of a firm to engage in CSP. The results of this analysis are presented in Table 20. In Model 1 of Table 20, I repeated the regression analysis presented in Table 19 as a starting point to establish sample parameters over which further investigation will proceed. In this model, Tobin's Q serves as the dependent variable. As displayed, the co-efficient of the *decision to engage in CSP* variable is negative and statistically significant *(p<0.05)*. This result replicates the main results shown in Table 19. In Model 2, I ran a probit estimation with the *decision to engage in CSP* as the dependent variable and entered accepted and established predictors of a firm's decision to engage in CSP as control variables. In Model 3, I introduced the role of stakeholder pressure as a relevant predictor of firm's decision to engage in CSP. As shown, the co-efficient of stakeholder pressure variable is positive and statistically significant *(p<0.05)*. This indicates that the pressure on firm's to engage in CSP is indeed a factor in firms' decision to pursue social performance. Finally, In Model 4, I use the statistically corrected variable *lambda*, which accounts for the endogeneity of a firm's decision to engage in CSP and estimates the correct

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relationship between CSP and CFP. This regression is estimated over only those observations for which CSP data is available from KLD, i.e. observations for which *decision to engage in CSP* takes on values of 1. The results of this regression show that the co-efficient of *lambda* is positive and statistically significant *(p<0.05)*. This means that the relationship between CSP and CFP is indeed a positive one after sample-selection error is removed. Thus, Hypothesis 9 was supported using Tobin's Q as a measure of financial performance.

I attempted to replicate these results with other indicators of performance but the results with Tobin's Q as an indicator of financial performance present the clearest picture of the dynamics of a sample selection problem in the investigation of the CSP-CFP relationship. In the next chapter, I discuss the results of my analysis and how these results relate to my theory and the broader investigation into the relationship between CSP, stakeholder governance mechanisms and CFP.

CHAPTER FIVE

DISCUSSION

In this dissertation, I looked deeper into the relationship between stakeholder pressure and CSP. I argued that one possible reason there is an ambiguity surrounding this relationship could be the presence of intervening factors. Prior research questions whether activism by shareholders directed at improving an organization's social and environmental performance meets its goals, i.e., improves the CSP of firms (Sjöström, 2008) . Results of such investigations are mixed and researchers acknowledge that it is difficult to observe direct changes in organizational behavior in response to stakeholder activism, and compliance may take other forms (Lee, 2008). To better understand the outcomes of stakeholder pressure, I focused specifically on the role of stakeholder governance mechanisms. Departing from the various theoretical approaches used in prior literature, I used an agency theory framework (Davis & Thompson, 1994; Jensen & Meckling, 1976) to hypothesize that pressure on firms to increase their social and environmental performance is at least successful in achieving structural changes within the firm concerning stakeholder governance mechanisms, if not achieving the ultimate goal of improving CSP. To the best of my knowledge, this is the first empirical study in a US setting to investigate explicitly stakeholder governance related outcomes of stakeholder pressure, and to establish boundary conditions of this relationship.

The results demonstrate that stakeholder pressure is associated with the quality of overall stakeholder governance within the firm. In particular, pressure exerted by stakeholders can be successful in pressuring the board of directors to create specialist

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committees to address the concerns of stakeholders. Strategic choice scholars have long acknowledged the power held by external constituents to influence structural changes within the organization (Child, 1997). Institutional theorists too have suggested the possibility of organizations strategically complying with stakeholders' demands without sacrificing precious resources (Oliver, 1991). The findings in this study are consistent with these arguments. I find that pressure from stakeholders is successful in changing the structure of stakeholder governance mechanisms. From an organizational point of view, response to stakeholder pressure comes in the form of altered internal structures that may be relatively less costly to change than improving CSP which requires discretionary spending and in turn raises costs (Friedman, 1970).

The results of the stakeholder pressure and overall stakeholder governance relationship tests also reveal that stakeholder pressure is only successful in improving weaknesses in stakeholder governance mechanisms, not in augmenting governance strengths. Stakeholder pressure had a positive impact on stakeholder governance weaknesses, but there was no association between stakeholder pressure and stakeholder governance strengths. This implies that firms react to stakeholder pressure by focusing only on areas of concerns within their stakeholder governance mechanisms. These results mirror the findings of the shareholder activism literature in which researchers found that stakeholder pressure was most successful in removing weaknesses in corporate governance mechanisms such as the existence of poison pills (Gillan & Starks, 2007). Evidence from recent stakeholder proposal activity also indicates that firms are increasingly improving their environmental disclosure practices to pacify concerned stakeholders (Kropp, 2011). Such acquiescence and promises of

improvements signals compliance to stakeholders who subsequently agree to withdraw resolutions. Thus, while these results confirm the utility and success of stakeholder activism in bringing about organizational changes, they also highlight the reality that overall, stakeholder pressure may not induce more positive organization behavior but rather a less negative one.

The tests of mediation concerning the stakeholder pressure and CSP also confirm the theory presented in this dissertation. Stakeholder governance mechanisms do at least partially mediate the stakeholder pressure and CSP relationship and the relative magnitude of the total effect that is mediated could be as high as 20%. To recast, while changes in stakeholder governance mechanisms may not account for all the impact of stakeholder pressure on CSP, they at least channel some of that effect. In light of these results, it may be useful to explore organizational structures related to social issue handling when researching processes that lead to changes in an organization's CSP. Much of the research on CSP antecedents is centered around organizational variables such as firm size, need for legitimacy and slack resources (Chiu & Sharfman, 2009). Inclusion of stakeholder governance mechanisms could possibly provide additional explanations for why firms engage in CSP.

In this study, I contributed to both stakeholder theory and corporate governance literatures. Corporate governance is more commonly referred to as the "structures and processes by which an organization's assets and activities are overseen" (Hambrick, Werder, & Zajac, 2008). The oversight of managerial activities is grounded in economic assumptions that shareholders' invested wealth needs to be protected and maximized because they are separated from the control of the corporation (Berle & Means, 1932;

Shleifer & Vishny, 1997). Departing from traditional agency theory arguments and assumptions, I ascribe more importance to social issue shareholders and the protection and maximization of the "social wealth" generated within the firm. Existing research building on stakeholder theory has attempted to impact corporate governance mechanisms in order to harmonize them with the needs of social-issue shareholders. The results of this study confirm that stakeholder activism yields changes within the stakeholder governance mechanisms within the firm which are distinct from traditional corporate governance mechanisms. This implies that in order to achieve stakeholder-centric goals, corporate governance could even be supplanted with stakeholder-centric governance mechanisms.

In this dissertation, I also introduced the role of managers as the key decision-makers of the strategy involving CSP. Past research has surprisingly often assumed away this important stakeholder within the organization when investigating CSP as an outcome. Drawing upon managerial discretion theory (Hambrick & Finkelstein, 1987) I argued that the impact of managers on strategic decisions impacting CSP is stronger in certain organizational and environmental contexts. To test these hypotheses, I introduced contexts identified in prior research in which managers are known to exercise more discretion, as moderators of relationships between stakeholder pressure and stakeholder governance mechanisms. The results indicate that not only do managers matter, but also they counteract the pressures exerted by stakeholders. In munificence markets, managers possess greater managerial discretion and counter stakeholder pressure by thwarting improvements in weak stakeholder governance mechanisms.

Social-issue proponents need to remain alert to the reality that a stronger management may often not subscribe to the stakeholder point of view and may even "push back".

The results of this study also inform empirical research on the CSP-CFP relationship. As explained in the dissertation, researchers have exhibited substantial interest in examining the CSP-CFP relationship and for the last 20 years there seems to have been a series of studies aimed at determining the exact nature of this relationship. Based on empirical research on the topic, the dominant view has gravitated towards the acceptance of a mild positive relationship between CSP and CFP (Orlitzky et al., 2003). Concurrently, researchers have noted that the results derived from most empirical investigations may be suspect because researchers often used invalid or unreliable measures of CSP and CFP (Van Beurden & Gössling, 2008), failed to control for relevant variables (McWilliams & Siegel, 2000), and made weak arguments of causality leading to statistically incorrect estimates plus possibly flawed inferences (Margolis & Walsh, 2003; Post, Preston, & Sachs, 2002). To ensure that my analysis did not suffer from such problems I included all identified variables in econometric models to avoid endogeneity issues, maintained temporal separation between predictor and dependent variables to avoid potential problems of reverse causality, and ruled out alternate explanations by using rigorous analytical techniques. Despite having sufficient empirical power to detect and effect, the results of my investigation yielded a statistically insignificant main effect of CSP on CFP. The results do not change when I use alternate measures of financial performance. In recent research, other scholars have arrived at a similar conclusion. When subjected to a rigorous methodological scrutiny,

the CSP-CFP relationship turns out to be a statistically insignificant one and not a mild positive one (Garcia-Castro et al., 2010; Surroca, Tribó, & Waddock, 2010).

However, even recent research did not consider the possibility of the results being impacted by a sample selection problem. In this study, I corrected the endogeneity problem arising due to sample selection which is inherent in studies which use only those firms whose ratings are reported by KLD to investigate the CSP-CFP relationship. The results in my dissertation indicate that the relationship between CSP and market based financial performance is indeed positive and statistically significant once sample selection bias is removed. To the best of my knowledge, this study is the first to draw researchers' attention towards a possible sample selection bias that exists in estimating the CSP-CFP relationship and the problem of generalizing conclusions based on studies of only those firms which are selected by KLD to report CSP rankings. Future research would benefit from ensuring that samples are not biased before proceeding with an estimation of the CSP-CFP relationship.

Implications for Stakeholders

Stakeholders' demands expressed through shareholder proposals comprise a wide gamut but surprisingly, demands for the design and implementation of governance mechanisms that align managers' interests with those of social-issue stakeholders is almost non-existent (Sjöström, 2008). The results of this study indicate that corporate compliance takes many forms, one of which is the creation of stakeholder-centric governance mechanisms within the firm. In the absence of concrete evidence linking stakeholder pressure with CSP, stakeholders desirous of achieving progress on social and environmental issues would perhaps be better served by targeting the creation and

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change of governance structures within the firm to bring them in line with the interests of stakeholders. Such stakeholder governance structures can in turn help managers navigate the conflicting pressures of wealth maximizing shareholders and social-issue stakeholders.

Recent rule changes by the SEC allow stakeholders an unprecedented influence over who to appoint to the board of directors of public corporations (Holzer & Berman, 2010). Stakeholders should find themselves even more empowered to bring about social change by advocating the appointment of stakeholder sympathetic members with related qualifications to the board of directors. Such directors can in turn influence organizational policy for the betterment of stakeholders by monitoring managerial actions and ensuring that managerial motives are aligned with those of stakeholders.

Implications for Managers

The results of this dissertation also has implications for managers. Stakeholders are key to the success of any organization (Greening & Turban, 2000). Granted, the modern corporation has come to ascribe an inordinate importance to wealth-maximization objectives, managers need to stay cognizant of the needs of social-issue stakeholders. Eliciting positive inputs from important stakeholders requires addressing those issues which are salient to stakeholders. Therefore, executives may need to check the impulsive reaction of working against the will of stakeholders in an effort to retain their own discretion (David et al., 2007) and allow structural changes within the organization that may facilitate stakeholder welfare.

Another implication for managers is that social and environmental issues have gained widespread importance in the eyes of stakeholders and increasingly the board of

directors is taking it upon themselves to oversee the organization's performance in these areas. Many large US corporations have begun to institute governance mechanisms which are intended to safeguard stakeholder interests within the firm. According to a recent report, formal board oversight of CSP exists at 65% of the S&P 100 and about a fifth of the Russell 1000 member companies (Freeman & Bennette, 2010). Experts are increasingly advising organizations to drop a reactive stance and adopt a more integrated approach to CSP by including social-issue considerations in strategic decision-making at the top of the organization (Spitzeck, 2010). Amidst societal pressures, the board of directors could be compelled to couple CEO incentives or even pay to not only the attainment of a financial competitive advantage but also the achievement of social performance. Managers are therefore well-advised to adopt a proactive stance to handling social and environmental issues within their own sphere of influence.

Limitations and Directions for Future Research

In this study, I have used social-issue proposals to proxy for stakeholder pressure though admittedly, stakeholders adopt a wide variety of pressures mechanisms. Recent events lend credence to the notion that disenfranchised stakeholders adopt activism through proposals as a means of voicing their opinions. Fishermen from the Gulf of Mexico affected by BP's oil spill purchased shares in the corporation to be eligible to participate in the annual shareholder meeting (Webb & McVeigh, 2011). Focusing only on stakeholder proposals therefore provides theoretical and empirical clarity to the arguments raised within this dissertation and the results obtained from the analysis respectively. However, generalization to outcomes of other informal means of

stakeholder pressure should be treated with caution. Future research could benefit by replicating this line of inquiry using the oft-researched informal means of stakeholder pressure, such as boycotts, petitions and other social movements (Davis et al., 2005).

While I did find evidence of structural changes in the form of existence of committees and overall quality of stakeholder governance measures, there were no statistically significant evidence of stakeholder pressure succeeding in appointing more stakeholder sympathetic members to stakeholder committees. A possible explanation could be the lack of statistical power to detect the effect. Because logistic regression uses maximum-likelihood estimates, many researchers believe that such estimation requires fairly large samples (Long, 1997). Future research could benefit from collecting more data and defining the stakeholder sympathetic members more narrowly to achieve more variance in the dependent variable. Another possibility would be to collect data at intervals so a more longitudinal sample can be constructed. A compilation of committee composition over time would enable researchers to model any effects of time trends on board composition. Recent rules changes by the SEC allowing stakeholders to directly appoint directors to the board may be another institutional change that may affect the phenomena.

I adopted the traditional agency-theoretic view of managers having divergent predilections than the shareholders of the firm. The creation of stakeholder-centric committees indicates at least some acceptance on the part of managers to stakeholder demands. Prior research indicates that managerial actions in the domain of corporate governance mechanisms may be only "window-dressing" to placate stockholders (Westphal & Zajac, 1998). Even in the face of shareholder activism, managerial

response is "symbolic rather than substantive" (David et al., 2007: 98). Future research could undertake an inquiry along similar lines based on the results of this dissertation. For example, researchers could look in a more fine-grained way into managerial actions of shaping stakeholder-centric governance structures in response to stakeholder activism. Research could explore whether such changes indeed yield substantive improvements in corporate social performance or they are still symbolic actions by managers intended to deflect stakeholder demands.

Another limitation of this study is that the data used for analysis is comprised of only US firms. Future research could enhance the generalizability of the theory presented in this dissertation by replicating it in other countries with different institutional settings. A promising area of future research could be the test of the theory presented in this dissertation in countries which espouse relatively more stakeholder-protective views and where managers exercise limited discretion. Because of the existing corporate laws, rules and regulations, stakeholder issues and demands are different in the US than in other countries. Similarly, corporate governance mechanisms vary according to the constraints imposed due to country-level institutions (Aguilera & Jackson, 2003). Crossland and Hambrick (2007) find that managerial discretion too varies across institutional contexts. For example, they find that in a country such as China which is known to espouse collectivist values (Redding, 1993), managers exercise less discretion. If the results of replicated studies vary across different discretion-limiting contexts, one could argue that there are multiple boundary conditions of the theory presented in this dissertation. Findings of such studies could

provide more insights into the success of activism on social issues in emerging market contexts.

Conclusion

Past research has largely focused on improvements in CSP as an outcome of stakeholder activism. Because of mixed findings, researchers have implicitly assumed that stakeholder activism is unsuccessful in bringing about changes within the organization. In this dissertation I focused on changes in stakeholder governance mechanisms within the firm as a possible outcome of stakeholder pressure. I confirmed that stakeholder pressure exerted through social-issue proposals directed at corporations results is associated with the existence of stakeholder-centric committees within the board of directors, and improvements in weaknesses of stakeholder governance mechanisms. I also introduced the role of managers exercising discretion of design and change in stakeholder governance mechanisms. Managers exercise their discretion in uncertain environments by blocking improvements in stakeholder governance mechanisms. Stakeholder governance mechanisms partially mediate the relationship between stakeholder pressure and CSP such that at least 20% of the effect is mediated. In a re-investigation of the relationship between CSP and financial performance, I found that once all methodological corrections are employed the CSP and financial performance relationship is statistically insignificant. However I was able to confirm that the relationship between CSP and market-based financial performance suffers from a sample-selection bias. Upon removal of this bias from estimates, the relationship between CSP and market based financial performance turned out to be positive.

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