

## **GOVERNING FOR CORPORATE SOCIAL RESPONSIBILITY**

VANESSA STRIKE  
Richard Ivey School of Business  
The University of Western Ontario  
London, Ontario  
N6A 3K7  
Fax: (519) 661-3959  
Email: VStrike@ivey.uwo.ca

AND

PRATIMA BANSAL  
Richard Ivey School of Business  
The University of Western Ontario  
London, Ontario  
N6A 3K7  
Tel: (519) 661-3864  
Fax: (519) 850-2306  
Email: PBansal@ivey.uwo.ca

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### **ABSTRACT**

In this paper, we explain how governance structures are related to corporate social responsibility. In particular, we argue that the firm's proximity to critical stakeholders will influence its responsible actions. The construct of proximity is deconstructed into four constituent parts that explain why family owned businesses are more likely to be socially responsible than widely held business, and why they tend to less socially irresponsible.

Key Words: Proximity, Corporate Social Responsibility, Governance, Family Businesses

## **INTRODUCTION**

Corporations were formed as a means for owners to share risk and capital. Managers were required to govern in the best interests of shareholders. Their legal obligation, then, was to ensure that firms provided adequate returns to shareholders. However, many firms engage in socially responsible activities for which the costs are evident, but the benefits are not. For example, firms will often donate money to local charities, give employees time off to volunteer with non-profit agencies, or install environmental protection equipment that is not required or expected by the community. In this paper, we explain why.

In this paper, we investigate the relationship between corporate governance and corporate social responsibility. This relationship is best explained through the construct of proximity. We deconstruct proximity into four constituent parts: physical, psychological, social, and temporal. By exploring the micro mechanisms of the role of the proximity of firm activities, owners, and employees to its stakeholders, we argue that firms that are more proximate are more likely to be more socially responsible and less likely to be socially irresponsible. In this paper, we are able to deconstruct the role of proximity on different governance structures, focusing primarily on large widely held firms and family businesses.

## **CORPORATE SOCIAL RESPONSIBILITY**

Corporate social responsibility (CSR) is a multidimensional construct with numerous definitions (Carroll, 1998; 1979; Wood, 1991). Carroll (1999) offers an extensive history of the definition. One of the most well recognized definitions in the literature is Carroll's (1998; 1979) four faces of good corporate citizenship that is deconstructed into economic, legal, ethical, and discretionary responsibilities. Other authors have divided CSR into economic responsibility,

public responsibility, and social responsiveness (Wartick and Cochran, 1985) and principles, processes and outcomes (Wood, 1991). While the definitions may vary, researchers agree that CSR is a multidimensional construct that involves a responsibility not just to a firm's shareholders but also to society

We deconstruct CSR into three components: strategic CSR (for example, less toxic waste), altruistic CSR (for example, philanthropy), and corporate social irresponsibility or CSiR (for example, no pollution prevention or control efforts). Strategic CSR is where a firm engages only in legal activities and those that are expected to result in higher economic returns – the legal and economic pillars expounded by Carroll (1979). Strategic CSR is common among most firms. Firms need to be economically and legally responsible to survive and grow over time. Strategic CSR involves those activities, such as elimination of toxic emissions, where there are anticipated short-term or long-term benefits to the firm, and a direct expectation of financial outcomes. It may also involve risk management of the firm where the firm abides by all laws and will not engage in any activities that are visibly inappropriate.

Altruistic CSR and CSiR, however, are less common. Altruistic CSR refers to those activities in which there is no expectation of short term financial returns or reciprocity, such as philanthropy. CSiR is when decision makers are aware of harmful impacts of the firm's activities on its stakeholders. As strategic CSR is common to most firms, in this paper we focus on altruistic CSR and CSiR. By deconstructing CSR into strategic, altruistic, and CSiR components, our model provides a framework for analyzing differences in corporate governance.

## **CORPORATE SOCIAL RESPONSIBILITY AND GOVERNANCE**

Results in the governance and CSR literature are mixed. Furthermore, while there are multiple empirical studies, there is very little theory development in the area, which may account for much of the mixed results. Developing a theoretical base on governance and CSR may provide a basis for future empirical studies. The divergent results in the literature also highlight the importance of exploring typologies within groups, and not just between groups. The typologies within the institutional groups are just beginning to be explored (for example Johnson and Greening, 1999), but there is more room to deconstruct these further, as with insider ownership and other types of governance.

Empirical research has examined the relationship between institutional owners, stock owners, and CSR (Johnson and Greening, 1999; Galaskiewicz, 1997; Graves and Waddock, 1994; ; Zahra, Oviatt and Minyard, 1993; Coffey and Fryxell, 1991; Atkinson and Galaskiewicz, 1988) between boards of directors and CSR (Ibrahim, Howard and Angelidis, 2003; Coffey and Wang, 1998; Wang and Coffey, 1992) and between organizational types and CSR (Acar, Aupperle and Lowy, 2001; Litz and Stewart, 2000).

Past research on institutional investors that grouped investors together as one entity found that institutional ownership was negatively associated with CSR (Zahra, Oviatt and Minyard, 1993) while yet others had mixed results (Graves and Waddock, 1994; Coffey and Fryxell, 1991). More recent research has deconstructed institutional investors into investor types such as pension funds, investment managers, and executive equity. Results show that longer-term investors, as in pension funds, have a positive direct relationship with CSR, while shorter-term investors have no direct relationship (Johnson and Greening, 1999). Research on management

equity and ownership has had mixed results depending on how CSR is deconstructed (Johnson and Greening, 1999).

Research on ownership by corporate insiders showed a positive association with CSR as increased insider ownership increases their long-term commitment to the firm and reduces self-serving actions (Zahra, Oviatt and Minyard, 1993). Coffey and Wang (1998) found similar results in their support for their managerial control thesis where the percentage of stock owned by insider directors was positively related to philanthropy. An earlier study showed similar findings (Wang and Coffey, 1992). In contrast, studies by Galaskiewicz (1997; 1985) and Atkinson & Galaskiewicz (1988) found that firms were less philanthropic if the CEO owned a significant percentage of the firm.

Research on boards and CSR that examined the ratio of insiders to outsiders and CSR has also had mixed findings. Some results show that the percentage of outside directors is positively associated with external CSR issues such as community involvement (Zahra, Oviatt and Minyard, 1993). Using the four levels of social responsibility – economic, legal, ethical, and discretionary, Ibrahim, Howard, and Angelidis (2003) found that outside directors exhibit a greater concern towards the discretionary component, also an element of external CSR. Contrary to these findings, in their study of the relationship between outside board representations and philanthropy, Coffey and Wang's (1998) findings suggest that as the number of inside board members increase, so does the philanthropic behavior of the firm; the authors use agency theory to explain their results. A previous study by Wang and Coffey showed similar results (1992).

There appear to be few empirical or theoretical studies that have explored the relationship between organizational types and CSR. Litz and Stewart (2000) examined whether family firms reported greater levels of community involvement than non-family firms; while their findings

were not significant, there was a notable pattern that family firms were more involved with the community. In one of the few studies including a classification of several organizational types, Acar, Aupperle, and Lowy (2001) explored 5 typologies and their orientation towards Carroll's (1998; 1997) four levels of social responsibilities: privately-held for profit, publicly-traded for profit, regulated for profit, revenue-generating not for profit, and non-revenue-generating not for profit. Findings show a significant difference between the types and their orientation towards economic, legal, ethical, and philanthropic responsibilities, suggesting that organizational typologies do matter.

What is needed is further theory development to help explain why such divergent results exist. We propose that it is not the different forms of governance themselves, but their degree of physical, psychological, social, and temporal proximity with their environment, and furthermore, that different types of governance may be more proximate than others. Assuming that all firms exhibit strategic CSR, different types of governance give rise to either altruistic CSR or CSiR depending on their proximity. This is developed further below.

### **THE ROLE OF PROXIMITY**

To explain the relationship between corporate governance and corporate social responsibility, we develop the notion of 'proximity'. Proximity refers to the closeness of the individual or the firm to its stakeholders. Closeness can refer to distance or sameness. We propose that proximity is comprised of physical, social, psychological, and temporal aspects. Each of these aspects will be described and its importance in explaining the corporate governance structures that will influence corporate social responsibility.

There is good precedence to believe that proximity is related to CSR. In his study of charitable contributions in the cities of Minneapolis-St. Paul, Galaskiewicz (1997) found that

philanthropic leaders were proximate in many of these ways; they were born or raised in the same city, had similar educations, were leaders of large businesses, were active in the same social clubs, and their parents were from large business families in that city. Therefore, the sharing of similar characteristics acquired through proximity can lead to collective socially responsible actions. Proximity builds social ties among firm members and with the firm and its stakeholders. The strength of these ties depends on the amount of time people spend together, the amount and quality of information they share, the trust they bestow, and the emotional intensity of their interactions (Granovetter, 1973). This builds a “sense of community” (Granovetter, 1973: 1373). Without a community, people have little motivation to act on issues where they have no connections. In order to act on information, it is important for personal ties to exist. Thus ties may facilitate organization and action. “The more local bridges in a community and the greater their degree, the more cohesive the community and the more capable of acting in concert” (Granovetter, 1973:1376).

Before elaborating on the theory of proximity, it is important to discriminate it from similar constructs, in particular propinquity. Propinquity is most often associated with both geographic nearness and architecture in both the sociology and the urban planning literatures (Kono, Palmer, Friedland and Zafonte, 1998; Peach, 1974; Barnlund and Harland, 1963; Davie and Reeves, 1939). Quillian and Campbell (2003) extend this definition of propinquity to include those who share the same social situation, yet they also note that such propinquity results from the day-to-day contact of being within the same physical location. Propinquity is rooted in the theory of social networks that identifies the mechanisms by which social ties develop (McPherson, Smith-Lovin and Cook, 2001; Quillian and Campbell, 2003). Overall, the literature asserts that propinquity is important for the development of networks in that it enables the

breeding of trust through the sharing of information (DiMaggio, Hargittai, Neuman and Robinson, 2001). The urban planning literature also uses the term propinquity with respect to physical location, where Webber (1963) asserts that social networks are not limited by propinquity. We agree with Webber's assertion but extend it by identifying the non-physical elements that create ties through social and psychological proximity. Propinquity may be thought of as being akin to the physical aspect of proximity and is important in the development of social networks, but it does not encompass other elements of proximity we discuss such as psychological proximity.

### ***Physical Proximity***

Individuals or firms are physically proximate to one another if they are geographically close. This geographical distance may be within the same building or community, so that it is likely that the firm and its stakeholders will physically meet.

Prior research points to the importance of physical proximity in leading to the development of communities or macrocultures. For example, in the development of a theory on network governance, Jones, Hesterly & Borgatti (1997) argued that geographic proximity contributes to the formation of macrocultures. They assert that this development of macrocultures is due to the increased probability of interaction and the ease of interaction. Pfeffer and Langton (1993) argued for a similar phenomena in their study of college and university faculty and the effect of wage dispersion. Pfeffer and Langton found that research collaboration occurs more frequently within departments than across departments at universities because collaborators are located in the same department and building. Such proximity eases the frequency of interactions, and the sharing of both formal and informal research ideas and agendas, more timeliness when discussing research, which all lead to increased research

collaboration. Many research ideas are not developed simply because they are not shared and discussed with colleagues when the idea is first raised, and they may be shelved and soon forgotten.

There are a number of mechanisms by which physical proximity influences corporate social responsibility. Physical proximity facilitates the flow of information, so that more information is conveyed quickly. This is in part due to the fact that the firm can deliver more information and that the stakeholder is better able to receive it.

Information can be conveyed either through formal or informal communications (Greve and Taylor, 2000; Kulik and Ambrose, 1992). Formal communications occur when the firm carefully scripts the conversation. Such formal communications allow the firm to manage its impressions carefully. Informal communications are ad hoc and rely more heavily on non-verbal cues than do formal communications. Non-verbal cues can include dress, eye contact, and other body 'language'. For example, emotions are more easily conveyed through informal cues than through formal dialogue. Through these cues, the stakeholder can communicate quite effectively its distress over firm practices, such as through protests. Furthermore, the firm may communicate more information than what is communicated formally, communicate different information than what is being communicated formally, and communicate the information more efficiently.

Physical proximity also facilitates frequency of exchanges because unplanned encounters are more likely to occur. Furthermore, the costs of the exchange are lower because travel or telecommunications costs do not have to be incurred and because informal communications are efficient. A greater frequency of interactions will improve the quality and timeliness of communications. In a study on U.S. nursing homes, Baum and Usher (2000) found that firms

were more likely to acquire geographically proximate firms because of the high level of formal and informal communications, even when Baum and Usher controlled for other firm similarities.

Furthermore, closer geographic proximity permits stakeholders to experience the ill-effects of irresponsible firm actions or the positive effects of responsible actions. As well, managers of the firm can experience the impacts of the firm's production processes and products on the local community. As a result, both stakeholders and management are likely to be affected personally by the impact of the firm's activities. Morris and McDonald (1995) found empirical support for this view. In their study of moral intensity, they presented an environmental pollution scenario to respondents. In the scenario a plant considers dumping waste into a drain that runs off into a body of water. The study manipulated the proximity of the event by changing the location of the scenario. Respondents were asked to answer questions on moral judgment and moral intensity following each scenario where the obligation to act was based on these questions. The study found that the perceived proximity was a significant term in the model.

Not only are insights improved between the firm and its stakeholders, but insights are also improved among firms and among stakeholders. Firms are more likely to adopt socially responsible practices observed among their peers. In a study of employer involvement in work-family issues, Goodstein (1994) noted that when the adopters of institutional norms are within the same geographic region, mimetic isomorphism can be powerful. In their development of a model of ethical decision making for entrepreneurs, Solymossy and Masters (2002) asserted that networks can constrain socially irresponsible behavior, depending on the norms and codes of conduct, as individuals are more likely to observe the actions of others in their network. These physical observations are critical.

Summarizing the above discussion, the frequency, amount, type, and timeliness of information flows change as physical proximity increases. Having more information, insider information, and timely information will all influence the type of decisions made.

### ***Psychological Proximity***

Firms and their stakeholders are psychologically proximate if they relate cognitively to another. This often occurs if the two parties have similar ascribed, achieved, or internal psychological characteristics, otherwise known as homophily (Ruef, Aldrich and Carter, 2003). The ascribed characteristics on which we focus in this paper are endogenous to the person, such as gender, age, ethnicity, and appearance. Achieved characteristics are naturalized and include values, attitudes, and beliefs (McPherson, Smith-Lovin and Cook, 2001). While achieved characteristics often form through social interactions, individuals and organizations can share achieved characteristics, and yet not have socially interacted with them. For example, cultural groups are linked by similar backgrounds, beliefs, values, and a sharing of traditions. They may belong to the same ethnic club, religious organization, celebrate the same holidays, share the same native language, eat the same foods, and dress in a similar fashion. Internal psychological characteristics include those of intelligence, emotions, attitudes, and aspirations.

Psychological proximity leads to greater interaction among others who share the same characteristics. People will seek others who are similar to them. Huston and Levinger's (1978) extensive review of the social psychology literature establishes that similarities in attitudes, beliefs, and values lead to interaction. In their study of homophily, based on gender, nationality and appearance, and strong ties amongst U.S. entrepreneurs, Ruef, Aldrich, and Carter (2003) found that homophily leads to group formation based on the similarity of the members characteristics. These innate characteristics promote the formation of strong ties. Granovetter

(1973) asserted that the strength of a tie depends on how much time people spend together, how closely they confide in one another, and the emotional intensity of their interactions. He also asserted that similar individuals share strong ties. While people share acquired characteristics through social proximity, innate psychological attributes allow the connection to develop to a deeper level, creating strong ties. Strong ties are then concentrated and unfaltering.

Further, those who share psychological proximity will have common interests and worldviews which leads to the formation of expressive ties (Ibarra, 1992). As a result, people with such ties will be more emotionally involved and have an internal vested interest. These firms and stakeholders hold common identities. In a study on the effects of community outreach on identity, Bartel (2001) found that firms involved in boundary-spanning activities are able to link with important stakeholders in their external environment. Such activities that are often socially responsible in nature build ties with the community and allow the firm to identify with the community. For example, people who have their own children are more likely to be affected by the use of child labor, even if their children are not working, than people who do not have children.

Psychological proximity appears to heighten the moral intensity experienced by the firm to its stakeholders. In his study of webmasters' attitudes, Shaw (2003) measured the organizational proximity of the webmasters using a measure of psychological and emotional proximity. This closeness was defined as feeling a sense of belonging and having common identities and values. Those who were psychologically and emotionally proximate were more concerned about both co-workers and the organization. The study found that organizational proximity was the most theoretically significant finding in their study. For webmasters with a high level of organizational proximity, there is a strong relationship with organizational

consensus and moral attitudes. As a result they think more like their co-workers and put more value on the attitudes of their organization.

The norms of the institution may then be affected by proximity. When individuals identify themselves as being close to the institution, norms and outcomes of social responsiveness may be relevant in forming the moral attitude towards an issue; this proximity is psychological in nature (Shaw, 2003). Those who are highly psychologically proximate to the institution will place more value on the attitudes of the institution and are more likely to conform to the norms (Shaw, 2003).

Empirical studies have shown that people are more likely to help those who are similar to themselves (Ehlert, Ehlert, and Merrens, 1973). In a cross-cultural comparison on ethical decision making, Davis, Johnson, and Ohmer (1998) noted that as proximity leads to strong personal attachments, people who are more proximate are more likely to help one another and immoral behavior will be deterred. The study found that social consensus has a critical effect on issues of moral concern.

Psychological proximity leads to feelings of greater social responsibility and decreases the likelihood of unethical behavior (Brass, Butterfield and Skaggs, 1998). In their theoretical development on relationships and unethical behavior, Brass, Butterfield, and Skaggs (1998) asserted that people with strong ties will be similar in attitudes and values. In their study on ethics and moral decision making, Sama and Shoaf (2002) noted that moral proximity relates to how close the decision-maker feels they are to the recipient of the unethical decision. In their study on moral intensity in ethicality judgments, Singer, Mitchell and Turner (1998) showed that empathy and moral intensity is moderated by proximity. Those who are more physically and psychologically proximate regard the ethical situation as being more morally intense and more

unethical and as a result feel greater empathy. (Singer, Mitchell and Turner, 1998). As a result, we expect that those who are psychologically proximate would exhibit more socially responsible behavior.

### ***Social Proximity***

Firms and their stakeholders are socially proximate through social interactions. While interactions are likely to occur in physically proximate environments with psychologically proximate people, such as on the golf course or at the local pub, they can also occur in distant environments and with distinctly different people.

Intuitively, having an increased understanding of the issues or actions in question should result in more efficient and effective results. It is during the sharing of these activities that interactions and social cohesion takes place. Sharing a vocation may also result in increased social proximity. This may occur at an individual level, a firm level, or an industry level. For example, chocolatiers may be linked to one another through their knowledge of the art and science of making chocolate; they may also be linked together through the global confectionary industry. In their field study of the difference in work groups Jehn, Northcraft, & Neale (1999) note that natural groups form because members share similarity, familiarity, and proximity. Those within the same social networks share knowledge, experiences, norms, and perspectives (Burns and Wholey, 1993; Jehn, Northcraft and Neale, 1999). With greater shared understandings of each others' perspective, the organization and its stakeholders will build greater trust (Sheppard and Sherman, 1998). As a result, the firm is more likely to respond to the desires of stakeholders, and stakeholders will be more accommodating of firm constraints.

Social interaction leads to increased information, an increased awareness of issues and the moral nature of those issues, and the development of weak ties. In their theoretical

development on relationships and unethical behavior, Brass, Butterfield, and Skaggs (1998) suggested that increased moral awareness leads to more ethical behaviour, especially towards those with whom one is close. People become close through the development of weak ties. In his theory on network governance, Jones (1997) supported this view, noting that the more connected people are, the more they share values, assumptions, and understandings.

Through the creation of weak ties social proximity promotes the formation of networks. Networks can change the flow of resources that can change the dynamics of populations (Hannan & Freeman, 1989). Where populations were once distinct, they may become joined together. By joining together and creating networks, people and firms come to share characteristics such as underlying attitudes, values, and beliefs. This sharing results in a closeness with others and an awareness of both the actions and consequences that these actions may have on the other.

In his discussion of moral and ethical distance and moral responsibility Mellema (2003) asserts it is the nature of one's involvement and the relationship to those involved that determine moral distance. The more morally distant people are from the social issue, the less they will feel morally responsible. Thus, where subtle ties are present, people will feel more socially responsible. For example, when a war or natural disaster takes place in a person's home country to which they are socially proximate, they are more likely to provide forms of relief support and direct resources to the disaster area, even if they are not physically proximate. Whereas individuals who merely happen to be in the area when the tragedy takes place and who have no weak ties, may not show the same social responsiveness.

### ***Temporal Proximity***

Temporal proximity refers to the degree that an individual's or a firm's orientation to time is similar to one another. More specifically, do they share the same time-perspective?

Time may be viewed from a short-term or a long-term perspective and can have various meanings depending on both the importance of the issue and how it impacts others. Thus for people to be temporally proximate to one another they must share a similar time-perspective.

In his theoretical paper on ethical decision making Jones (1991) uses the term temporal immediacy. Temporal immediacy is an important part of temporal proximity as it refers to the temporal distance between when an event occurs and when the effects are felt; if the temporal distance is great, then those involved in the initial event will likely assume little responsibility. Temporal proximity then refers to the sharing of the same orientation towards that temporal distance *and* its relative importance.

How do people achieve the same time-perspective? In his development of a model of trust Sheppard and Sherman (1998) assert that time is the essential construct that leads to the evolution of similar views, beliefs, and values. Similar time-perspectives are then often only achieved over time

There is little in the literature on temporal proximity yet it has an important influence on CSR. Individuals and firms devote more resources to issues that have an immediate effect on their own lives (Chia and Mee, 2000). If a socially responsible activity were to affect an individual or a firm immediately, they would be inclined to dedicate time and energy to that issue. We extend this thinking by proposing that people will be socially responsible if they believe the activity impacts them according to their time-perspective. For example, a logging company that comes into a community surrounded by forests, and then clear cuts the area without planting trees, has a very different time-perspective than that of the residents of the area who live and raise their families in that same community. In this scenario the logging company is concerned about the initial return that they will receive for their labor, and not the long-term

effects their actions will have on the community. The residents of the community are concerned about the ecological effects that clear cutting will have, such as protection from storms, protection from water run-offs, the provision of a home to animals, as well as the overall aesthetic effect.

## **PROPOSITIONS**

We apply Hambrick and Finkelstein's (1987) upper echelon theory in this paper where they assume that the top management team governs the firm. As a result, top management team demographics and ownership are important in this paper. Chief executives govern the firm based on how much discretion or "latitude of action" they possess; in addition, managers have more discretion in some organizations than in others and more at some times than at others (Hambrick and Finkelstein, 1987:369). We propose that proximity is a significant influence of the executives' discretion and that the presence of physical, psychological, social, and temporal proximity are critical mechanisms in determining how much discretion is present and when. Furthermore, we propose that organizational structures differ in their approaches to CSR due to differences in proximity.

The governance and CSR literatures have primarily focused on different institutional ownership types such as public pension funds, investment funds, inside and outside directors, and top management team equity (Hoskisson, Hitt, Johnson and Grossman, 2002; Johnson and Greening, 1999; Tihanyi, Johnson, Hokisson and Hitt, 2003; David, Kochhar and Levitas, 1998). There have also been studies which compare the differences in social responsibility across a spectrum of organizational types ranging from non-profit to government to for-profit firms (Acar, Aupperle and Lowy, 2001).

Results overall show that the nature of the ownership structure is important in a firm's strategic planning and decision making and that different ownership constituencies prefer different strategic actions. As agency theory tells us, owners and managers seek to maximize their different utility functions, as a result ownership structures should also differ. Further, CSR researchers argue that not all firms are similar in their concern for CSR issues; though there have been little empirical studies, it is believed that organizational types do matter (Acar, Aupperle and Lowy, 2001). Yet there appears to be little research on ownership structures outside of institutional investor ownership. In this paper, to illustrate the mechanism of proximity, we contrast two distinct types of governance that differ in their preferences and approaches to CSR based on their physical, psychological, social, and temporal proximity: the widely-held firm and the family business.

We define the widely-held firm as one where ownership is shared among multiple shareholders without any one shareholder having a controlling interest. Multinational enterprises (MNEs) and their subsidiaries are included in our definition.

There is no widely agreed upon definition of the family firm and different studies use various definitions (Astrachan, Klein and Smyrniotis, 2002; Littunen and Hyrsky, 2000). We define the family firm as follows:

- one or more members of the same family have a controlling interest in the firm;
- more than one family member is involved in the management of the firm or providing advice to the firm; and
- an intention to pass the firm on to the next generation.

Widely-held firms are limited by bureaucracy (Holmstrom, 1989). As a result, executives in such organizations, often without a locus of control, are constrained by the preferences of

multiple shareholders. In addition, research shows that when the locus of control/decision makers is external they are less likely to observe unethical actions (McCuddy and Peery, 1996; Zahra, 1989). We anticipate this is due not to an unethical orientation, but to not being in the same geographic location; as a result they do not have the same flow of information as one who is physically proximate. The flow of information made possible by physical proximity is important; in order for an option to be part of a discretionary set that a firm may act upon, the firm must be aware of the option. In fact, managerial excellence is made possible by being aware of options (Hambrick and Finkelstein, 1987).

By accounting for physical proximity, we can draw a relationship between corporate governance and corporate social responsibility. Widely-held firms are not necessarily physically proximate to the community in which they do business. Often, especially in the case of subsidiaries and MNEs, top management and owners of the firm live elsewhere and the many shareholders are scattered around the country or around the globe. By not being physically proximate to the community where the firm or its subsidiaries operate, there is less interaction, less informal communication, increased costs of communication, reduced quality of information, and less timeliness of information. As a result, the widely-held firm, without the strength of information flows that physical proximity promotes, may not even be aware of some of the ill-effects of its actions. In addition, by not being physically proximate, it may not personally experience the effects of these actions. For these reasons we predict that:

*Proposition 1: A firm that is widely-held and not proximate to its stakeholders will be positively associated with corporate social irresponsibility.*

Research suggests that one of the crucial success factors to a family firm is sensitivity to the region in which it resides (Astrachan, 1988). In fact, the commitment to community is often

taken into consideration when making strategic business decisions and may sometimes even rank above the firm's profitability (Strike, 2004). A firm's relationship with the environment that lies within its domain may also affect the level of discretion (Hambrick and Finkelstein, 1987). Family businesses firms see their business as a source of pride in the community and assist the community by providing employment (Deloitte&Touche, 1999). They see the firm as an integral part of the community and the community as an important part of the firm. For example, research has shown that small business owners are more sensitive to the expectations of society (Humphreys, Robin, Reidenbach and Moak, 1993). We anticipate they therefore have a vested interest in ensuring the community remains healthy.

The firm's owners who live in the local community also have more information about the impact of their firm's operations than owners, managers, and directors who do not live locally. By sharing the same golf clubs, children's schools, and grocery stores, significant informal interactions with the local community facilitate greater empathy and information transfer. This is particularly the case when stakeholders know who own the organization. Having more information, insider information, and timely information will all influence the decision about where to make a contribution. The frequency, amount, type, and the timeliness of information flows change as physical proximity increases.

Intuitively, owners that reside in the same community have more of a concern for the well-being of that community as they have a vested interest by virtue of being a resident. Thus, they may also influence a firm to be socially responsible to the community. In addition, they would have more information about the social issues within the community that require attention. In fact, not only would they have more information, they would also have more timely information about the issues in the community than those who reside outside the community.

Such enhanced information flows may therefore result in increased CSR behavior. For these reasons, we propose that:

*Proposition 2: Firms with owners living locally will be positively associated with altruistic corporate social responsibility.*

Not only does this argument apply to firm ownership, but also firm management, primarily firms that are managed. This is even more the case when the owners are also the managers of the firm, as in the case of family owned businesses. Such managers will be more likely to respond to issues raised by the local community because it is also ‘their’ community than managers that are either living in the local community because of a short term assignment or if the firm is being managed by a headquarters office located elsewhere. Hence, local managers and owners will facilitate greater corporate social responsibility. Consequently, we propose the following:

*Proposition 3: Firms whose owners, directors, and managers live in the local community are more likely to have a positive association with altruistic corporate social responsibility than firms whose owners, directors, and managers live in a different community.*

Ownership is a key determinant in the strategy of a firm. The distribution of ownership has a major impact as powerful owners can consider controversial options that could not be considered by others (Hambrick and Finkelstein, 1987). An owner’s values are critical in making socially responsible business decisions. In their study on the ethical perceptions of 282 small business owners, Hornsby, Kuratko, Naffziger, LaFollette and Hodgetts (1994) suggest that a small business owner’s ethics contains concepts that exceed adherence to simply legal responsibilities and that the owner’s values play a critical role. While the authors focus on small

business, we expect this same tendency to be present in larger family firms. Thus, we propose that it is not necessarily the size of the firm that plays a role, but it is the ownership structure. If the firm grows, and if it remains an owner-operated firm, these same values should remain. What often happens is the firm is bought out by a larger firm or the owner dies and the firm is sold or closes up, it may then appear that it is firm size and not ownership structure which is the main factor.

In a survey of 2,290 nationwide firms, Longenecker, McKinney, and Moore (1989) also found there were significant differences in the way small businesses owners perceived ethical issues compared to managers at large firms. Vyakarnam, Bailey, Myers, and Burnett (1997) further suggested that owners may differ in the issues that they identify and not just that they may judge situations differently. Those who share similar values, and who perceive ethical issues in a similar manner are more psychologically proximate to one another. In their study on moral intensity in ethicality judgments, Singer, Mitchell and Turner (1998) showed that empathy and moral intensity is moderated by proximity. Those who are more physically and psychologically proximate regard the ethical situation as being more morally intense and more unethical and as a result feel greater empathy. (Singer, Mitchell and Turner, 1998). As a result, we expect that those who are psychologically proximate would exhibit more socially responsible behavior.

In a research study using focus groups to assess the ethical perspectives of small business owners Vyakarnam et al. (1997) found that different factors influence small business owners' judgments with respect to ethical dilemmas (Vyakarnam et al., 1997). The authors suggest that not only does the consequence of the action matter, but also the current and potential future quality of the relationship with the recipient of the consequence.

Relationships are important to family owners especially for the on-going success of their business. Small business owners find it challenging to make purely impersonal business decisions (Hornsby et al., 1994). We expect this is due not only to the relationships that develop, but also that family businesses view the firm as an extension of themselves that they will pass to future generations. As a result, we propose that:

*Proposition 4: The closer the proximity of a firm to its stakeholders, the greater the likelihood that the firm will exhibit altruistic corporate social responsibility to those stakeholders.*

Social proximity promotes the formation of networks. Family businesses are based on a sense of trust, on embedded networks, and less on contracts (Belardinelli, 2002). Network theory and embeddedness theory assert that embeddedness shifts motivations away from pursuing economic gains towards relationships based on trust and reciprocity (Uzzi, 1996). In an ethnographic study of apparel firms, Uzzi (1996) found that trust assists in reducing transactional uncertainty; instead, trust creates opportunities for business activities that are difficult to enforce by legal contract. As well, he found that with embedded ties firms do not selfishly pursue immediate gain, but instead focus on the long-term.

*Proposition 5: Firms with managers, directors, and owners drawn from socially responsible regions are more likely to have a positive association with altruistic corporate social responsibility.*

Research shows that non-owners are more likely to take short-term actions to increase personal wealth (Malatesta and Walkling, 1988). Executives of widely-held firms are primarily compensated on short-term results and as a consequence do not manage for the long-term (Johnson and Greening, 1999). Such executives focus their efforts on shorter-term goals that

maximize shareholder value. Given these pressures, decisions will have a short-term focus to ensure there is healthy current profit maximization to satisfy the shareholders. Long term incentive plans, such as stock options, have become more common in an attempt to increase the executive's long-term vested interest that comes with ownership. Yet there is so much money vested in the share performance of the firm that managers are still forced to act as short-term investors. These pressures to maximize shareholder value and short-term profitability result in preferences for strategies that have a short-term pay-off (Johnson and Greening, 1999). This view is supported in Mahapatra's (1984) study of six U.S. industries where he notes that institutional investors with a long-term focus may interpret the costs of being more socially responsible as minimal when contrasted with the long-term benefits. He found that investors viewed expenditures on pollution control as a drain that could have been invested profitably. (Mahapatra, 1984). Thus, we assert that executives will invest in those activities that have a more direct effect on the firm's profits and which will maximize shareholder value.

Investments in CSR are a long-term commitment to the firm and there needs to be compatibility between the owners' or executives' time horizon with the time required to realize the benefits of investing resources in CSR (Johnson and Greening, 1999; Graves and Waddock, 1994; Mahapatra, 1984). Altruistic philanthropic activities for example, often do not have a direct short-term benefit on the firm. These investments in CSR will likely not provide a return to the firm for many years, and they are nebulous and difficult to quantify. Given their shorter-term economic focus, we do not expect widely-held firms to invest as much in such activities as other ownership structures. For these reasons we predict that:

*Proposition 6: A widely-held firm that has a short-term focus will invest less in altruistic corporate social responsibly activities than firms that have a long-term focus.*

Family businesses also have a longer time horizon (Daily and Dollinger, 1993), thus they do not feel the pressure for immediate returns. They exhibit long-term strategies as opposed to focusing on short-term term results; as a result they more efficiently allocate resources. Family businesses often view the firm as a life-long entity; they may also foresee passing the firm through multiple family generations. Other research has shown that those that have a long-term outlook are more concerned with a firm's social responsibility as they believe such investments will impact a firm's financial performance over time (Johnson and Greening, 1999). Hill and Snell (1989; 1988) suggested that insider ownership increases long-term commitment and that this increase may be associated with increased social responsibility, and Litz & Stewart (2000) proposed that family firms are more socially responsible towards their community as the firm is more than just an economic entity. Ethical actions, which encourage trust, can make an important contribution to the success of long-term planning and the long term advantage of staying in business (Vyakarnam et al., 1997). Given that the family firm has such a long-term focus, we expect they will have a long term commitment to their stakeholders.

Johnson & Greening (1999) assert that concerns for the longer term help firms to develop a constructive reputation that results from investing in positive environmental policies and acting environmentally responsible. Furthermore, Zahra, Oviatt & Minyard (1993) found that as inside ownership increased, there was a strong positive association with CSR. By extension, insiders have a longer-term perspective towards the firm and those with a longer-term perspective are found to be more attuned to CSR. Family business owners and corporate insiders with significant ownership would share similar perspectives with one another based on their ownership. As a result, we propose that family businesses that have a long-term perspective are more socially responsible than widely-held firms and invest more in long-term CSR initiatives.

*Proposition 7: Family businesses will invest more in altruistic corporate social responsible activities that may provide long-term benefits to the firm and their stakeholders.*

Research in the family business literature has found that family businesses are distinct from other types of ownership structures in a variety of other ways. Family businesses have an uncommon commitment to their business (Brokaw, 1992). They are preferred by consumers, they respond to customers differently (Gudmundson, Tower and Hartman, 2003), they are more involved with customer service, offer greater opportunities for women, have a respect for tradition, and take care of their employees (Longenecker, Moore and Schoen, 1989). In a comparison of family business and non-family businesses Koiranen (2002) found that core values are more important to a family business than to a non-family business because the two realms of business and family can have so many conflicting interests. Values take time to become ingrained; it is only over time that people gradually internalize beliefs and values (Koiranen, 2002). Family businesses are also more innovative; innovation is positively related to level of support for employees and degree of empowerment given to employees (Gudmundson, Tower and Hartman, 2003). We assert that these distinctive characteristics are due to the physical, psychological, social, and temporal proximity that family firms have to their stakeholders. For these reasons we propose:

*Proposition 8: Family firms are more likely to have a positive association with altruistic corporate social responsibility than widely held firms.*

## **CONCLUSION**

In this paper we have sought to explain the relationship between CSR and governance by leveraging the construct of proximity. We defined CSR as consisting of three components:

strategic CSR, altruistic CSR, and CSiR. By deconstructing the construct of proximity into its physical, psychological, social, and temporal components, we are able to explore the relationship between governance structures and altruistic CSR and CSiR. We used two examples of governance structures, the widely-held firm and the family business, to explain and contrast the relationship between corporate governance and corporate social responsibility through the construct of proximity.

This paper makes several contributions. First, it argues that family owned businesses are more likely to engage in altruistic activities than widely held businesses. By default, then, it suggests that widely held businesses tend to be more strategic in their orientation to CSR. The implications, then, is to consider from a social policy perspective if gaps are likely to arise in the execution of CSR. If so, it may be possible for governments to consider different policy measures to increase the proximity of widely held firms. Such measures could include the requirement of greater transparency of the firm's activities, which will increase the psychological proximity of the firm to its stakeholders. These propositions are testable and it is worthwhile for future researchers to assess if family owned businesses engage in different types of CSR activities than widely held firms.

Second, this paper develops the construct of proximity. Its four components offer a rich avenue for future research and additional applications. For example, it is likely that proximity is relevant to the area of social embeddedness. By further exploring the role of the mechanisms of proximity on a variety of research levels, it is possible to better understand their impact on relationships other than governance structures and CSR, and their implications.

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