CHAPTER II
LITERATURE REVIEW

A. Theoretical Framework
1. Stakeholders Theory

The introduction of the concept of environmental organizations growing company in line with the development of a systems approach to management, has changed the perspectives of the manager and the management theorists of the organization, particularly regarding on how a business organization can achieve its objectives effectively. A shift in the orientation of the business world from shareholders to stakeholders has been cited as a cause emergence of the issue of corporate social responsibility.

The definition of stakeholder has been defined in several ways. R. Edward Freeman, the father of Stakeholder Theory, define stakeholder plainly and simply as below:

“A stakeholder is any group or individual who can affect, or is affected by, the achievement of a corporation’s purpose.”

Every one of these “stakeholders” that may have an influence on the company’s goals has to be taken into account. Therefore, Freeman’s definition is regarded as a broad definition, for it leaves the notion of stake and the field of possible stakeholders unambiguously open to

include virtually anyone. Starik put forward that this definition has been broadened to include non-humans.\(^2\) A narrow definition is presented by the Stanford Research Institute “defining stakeholders as those groups” on which the organization is dependent for its continued survival.

Stakeholders are people or groups of people who can influence or be influenced by a variety of decisions, policies, and operations of the company. According to Jones in Solihin\(^3\) explains that the stakeholders are divided into two categories, namely:

a. Inside stakeholders: consists of people who have the interest and the demand for resources, and are within the company's organization. The parties that are included in the category inside the stakeholders are the stockholders, managers, and employees.

b. Outside stakeholders: consists of people and parties who are not the owners of the company, not the leaders of the company, nor the employees of the company, but has the benefit of the company and is influenced by the decisions and actions taken by the company. The parties included in the category of outside stakeholders are customers, suppliers, government, local communities and society in general.

In a more detailed explanation, Freeman wrote in his book that corporations have evolved from a rather simplistic view via a more complex one and finally to the stakeholder view. The first and simplest

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\(^3\) Ismail Solihin, *Corporate Social Responsibility: From Charity to Sustainability*, (Jakarta: Salemba empat, 2009)
view is what he refers to as the production view. At this stage, business was simply to buy raw materials and transform them into products which were then sold to customers. (see figure 2.1.)

![Figure 2.1. Production view of a company](image)

The figure above is mostly situation for small, entrepreneurial or family owned business. Even though those companies may have grown in size, but their perception of the task at hand has not changed. Outside of their own niche there is an environment with which they have very little interaction, thus the importance of this environment is minimal. Gradually new interest groups emerged and the view of the firm became somewhat more complex.

The second view, which Freeman refers to as the managerial view, includes owners and employees (incl. unions) along with suppliers and customers. The managerial view emerged because of the separation of ownership and control and the increasing influence of the workforce. Besides being more complex in the sense of more players the model also transforms the relationship between players into being reciprocal (see Figure 2.2.). Consequently, more interaction occurs among the different groups.
As the influence from the outside environment increases, Freeman’s view of the company develops further. This results in the emergence of the stakeholder view of business. In a modern business society, it is not enough to just look at the corporation from the managerial point of view; there are many other groups besides suppliers, customers, owners and employees that are of great importance to the company. As mentioned these stakeholders are those who can affect or are affected by the actions of the company. The increase in number of stakeholders materializes from increased pressure from, and dependence on, the outside environment. This results in a number of participants interacting bilaterally with the company (or at times multilaterally among each other and the company).

Donaldson & Preston point out that no priority of one set of interests prevails over another, i.e. the company’s interests are not more
important than an individual stakeholder group’s. Besides the four groups from the managerial view, many others including media, consumer advocates, competitors, environmentalists etc. are important (see Figure 2.3.).

Figure 2.3. Stakeholder view of a company

When studying the figure above, stakeholders are more important in the short term, whereas others may only matter in the long run and rarely affect the actions of a manager. Nevertheless, they must all be considered and cared for. Shareholder wealth maximization in its purest form fails to recognize the long term effects that the actions of e.g. special interest groups (SIG), local communities and environmentalists may have on a company. It thus merely regards such groups as obstacles to success. Freeman argues that by being responsive to the needs of all

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these groups a company will provide itself with a competitive advantage in the form of its good relationships. This advantage may not be obvious in the short run, but in the long term it may turn out to be crucial for the existence of the company. Freeman argues that companies ought to be attentive to the stakeholders because it is the right thing to do ethically, but he also holds that being responsive to the needs of the stakeholders may in fact benefit the company in many ways. This should provide the companies with an incentive to do so voluntarily, without the intervention of the legislative power.

From the views explained above, the concept of stakeholder indicates that it goes beyond the concept of the stockholder and searches for a broader concern for management. The concept was initially developed from a basis in strategic planning, but is now used in relation to systems theory and organization theory, as well.

Stakeholder theory is an instrument to identify critical stakeholders in the environment of the corporation in order to define developments for strategy. Moreover, in the contexts of business ethic and corporate social responsibility, stakeholder analysis has been used to identify important areas of concern.

In 1997, Mitchell, Agle, and Wood developed The Salience model to help managers identify and analyze project stakeholders needs. They

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5 J. D. Rendtorff, Responsibility, Ethics and Legitimacy of Corporations, (Denmark: Copenhagen Business School Press, 2009), p. 103
try to provide a very profound analysis of the problems of stakeholder theory. They argue that three views of salience are predominant in stakeholder theory:

1. the stakeholder’s **power** to influence the corporation: a stakeholder has power to the extent that it can use coercive (force/threat), utilitarian (material/ incentives), or normative (symbolic influence) power to “impose its will in the relationship”. While it is not identified nature’s “will” that the natural environment holds coercive and utilitarian power over business organizations as shown by countless examples of the natural environment’s significant influence on industrial activity. The impact of super-storms, hurricanes, and droughts on the agriculture industry shows that the natural environment holds coercive power over business organizations. The impact of the loss of financial resources in the fishing industry due to depletion of fish stocks shows that the natural environment has utilitarian power over business organizations. Similarly, real estate developers have been advised to address species habitat preservation, and most retailers to account for product and packaging disposal. As natural environments are increasingly seen as important business environments, identifying these, or components of them, as stakeholders becomes more likely.

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7 C. Driscoll and M. Starik, The Primordial Stakeholder: Advancing the Conceptual Consideration of Stakeholder Status for the Natural Environment, (2004), pg. 58
8 Starik (1995): pg. 210
2. **legitimacy** of the stakeholder’s relationship with the corporation: a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definition.⁹ One well-known stakeholder proponent¹⁰, for instance, has developed the moral legitimacy aspect of stakeholder management, in which those human individuals and organizations to whom an organization is morally obligated are included as stakeholders. If this ethical aspect of stakeholder management is credible, the development of environmental ethics implies that the natural environment also can be considered as one or more stakeholders of organizations.¹¹ The natural environment has attained legitimacy from the world's scientific community, which has reached consensus on the deteriorating state of the environment and the links to human activity.¹² For example, global climate change has been associated with human carbon emissions, including business use of fossil fuels, and the loss of biodiversity, again linked to habitat-destroying human economic activities such as fishing, forestry, and residential and commercial construction.¹³

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¹¹ Starik (1995): 211
¹³ Mitchell, Agle and Wood (1997): 867
3. **Urgency** of the stakeholder’s claim on the corporation: “the stakeholder’s claim for immediate attention based on the idea of time sensitivity” or the “degree to which stakeholder claims call for immediate attention.” During the environment crisis, the public quickly responded to the media's portrayal of oil-soaked, dying otters and birds. Human risks associated with critical and chronic long-term environmental problems are becoming increasingly tangible (e.g., increases in heat-related deaths in large cities, in skin cancer, and in super-storms and hurricanes) and more countries are acknowledging the association between human activity and slowly building environmental problems.¹⁴

According to the above, based on Mitchell, Agle and Wood (1997) stakeholder attributes of power, legitimacy and urgency, more and more corporations have regarded the natural environment as one of their stakeholders. That’s why it is important for a corporation to protect the environment. In their view, stakeholder theory is about which stakeholder should care for running the corporation in daily life. To this end, stakeholder salience is an important way to describe how to select between stakeholders.¹⁵

¹⁴ Driscoll and Starik (2004): p. 60
2. **Triple Bottom Line**

   The Triple Bottom Line is an accounting framework aimed at moving beyond traditional profit measures or reporting corporate performance to incorporate social and environmental measures. The major challenge is that while economic performance is easily measured in dollars, environmental and social performances are not easily quantifiable in these terms.

   John Elkington suggests reporting frameworks should be expanded to include the ‘The Triple Bottom Line’:

   Table 2.1. Triple Bottom Line Sustainability Issue

<table>
<thead>
<tr>
<th>Sustainability Issue</th>
<th>Broad considerations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ecological Sustainability</td>
<td>- Renewable vs non renewable energy sources</td>
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<tr>
<td>(Planet)</td>
<td>- Carbon and water footprints</td>
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<td></td>
<td>- Responsible exploitation of natural resources, replenishment of natural resources</td>
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<td></td>
<td>- Impact of man-made materials, pollution, long term well-being of the natural</td>
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<td></td>
<td>environment</td>
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<tr>
<td>Social Sustainability</td>
<td>- Social equity – community relationships and the well-being of individuals and the</td>
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<tr>
<td>(People)</td>
<td>community (local/ global)</td>
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<tr>
<td></td>
<td>- Ethics – ethical treatment of all stakeholders including channel members and supply</td>
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<td></td>
<td>chains</td>
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<tr>
<td>Financial Sustainability</td>
<td>- Long-term economic stability, sustainable and fair financial reward for all</td>
</tr>
<tr>
<td>(Profit)</td>
<td>stakeholders</td>
</tr>
</tbody>
</table>
1. Ecological Sustainability

The Triple Bottom Line approach to sustainability takes the view that the less impact of the business has on the environment and the fewer natural resources you consume, the longer and more successful the business will be. Controlling the Environmental bottom line means managing, monitoring, and reporting the consumption and waste and emissions. This is typically the work of the EHS department, though most sustainable business models also make waste reduction and green policies corporate-wide values across all levels of management. A sustainability committee is usually required to communicate the sustainability solution to all departments.

2. Social Sustainability

The Social bottom line measures the business’ profits in human capital, including the position within the local society. The social bottom line is increased by having fair and beneficial labor practices and through corporate community involvement. After all, if the business is not nurturing positive relationships with the community, the client base and employee pool shrinks accordingly. The social bottom line questions the belief that the less a business
pays its workforce the longer it can afford to operate. Instead, the social bottom line measures the long-term sustainability of business human capital, with the understanding that a business that is also a desirable workplace will always be able to operate. Essentially, corporate interests and labor interests are seen as interdependent.

3. Financial Sustainability

In the Triple Bottom Line approach, economic sustainability is not simply the traditional corporate capital in addition to you environmental and human capital. The economic capital must be measured in terms of how much of an impact the business has on its economic environment. The business that strengthens the economy it is part of is one that will continue to succeed in the future. Of course, a business needs to be aware of its traditional profits as well, and the Triple Bottom Line accounts for this as well.

By using the Triple Bottom Line method, the business can expand how it understands its position in the economy and its ability to survive in the future. Corporate sustainability measures the ability to be in business indefinitely, based on the impact on the environment, the relationship to the community, and contribution to the economy. Unlike the traditional method, the Triple Bottom Line allows them to see the business as a social and environmental entity and measure it long these parameters.
B. Conceptual Framework

a. Brief Review on Corporate Social Responsibility

1. The Concept of Corporate Social Responsibility

The concept of corporate social responsibility (CSR), calls for a lengthy discussion due to its varied history. In the past, there have been traces of evidence in the business community that showed their concerns for society in general. Although there are many definitions of CSR available, we center our attention on more recent concepts of CSR. According to Richardson, Welker and Hutchinson (1999), CSR behaviors can be defined as discretionary actions undertaken by companies that are intended to advance their social issues. Joyner, Payne & Raiborn (2002) noted that CSR are categories of economic, legal, ethical and discretionary activities of a business entity as adapted to the values and expectations from society. They also added that, CSR are the basic expectations of the company regarding initiatives that take the form of protection to public health, public safety, and the environment. In this concept, they explained that values and ethics influence the extent of a corporation's perceived social responsibility that is influenced by societal activities, norms or standard.

In today’s world, CSR can be defined as regards to all aspects of business behavior so that the impacts of these activities are incorporated in every corporate agenda (Orgrizek, 2001; Coldwell,
2001). So, with the literatures definition of CSR, it can be concluded that CSR is the continuing commitment taken by business organizations to strengthen their ethical concepts and social involvement in society, contribute to economic development, sponsor charitable programs, and improve the quality of the workforce and also the increment of services provided. However, on the other hand, Freeman & Liedtka (1991) argue that CSR can promote incompetence by leading the managers to get themselves involved in areas beyond their expertise, that is, trying to repair society’s ill.16

2. Definition of Corporate Social Responsibility

There are many available definitions for Corporate Social Responsibility. Here are a few definitions about Corporate Social Responsibility17:

1. Commission of the European Communities:

A concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.

2. World Business Council for Sustainable Development:

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Corporate Social Responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as the local community and society at large.

3. Woodward-Clyde:

CSR has been defined as a ‘contract’ between society and business wherein a community grants a company a license to operate and in return the matter meets certain obligations and behaves in an acceptable manner.

4. Ethics in Action Awards:

CSR is a term describing a company’s obligation to be accountable to all of its Social stakeholders in all its operations and Environmental activities. Socially responsible companies economic consider the full scope of their impact on communities and the environment when making decisions, balancing the needs of stakeholders with their need to make a profit.
3. Principles of Corporate Social Responsibility

There are three principles of Corporate Social Responsibility, which as follows:\[18\]:

1. Sustainability

This is concerned with the effect which action taken in the present has upon the options available in the future, and this is of particular concern if the resources are finite in quantity. Thus raw materials of an extractive nature, such as coal, iron or oil, are finite in quantity and once used are not available for future use. At some point in the future therefore alternatives will be needed to fulfil the functions currently provided by the resources. This may be at some point in the relatively distant future but of more immediate concern is the fact that as resources become depleted then the cost of acquiring the remaining resources tends to increase, and hence the operational costs of organizations tend to increase. Sustainability therefore implies that society must use no more of a resource than can be regenerated. This can be defined in terms of the carrying capacity of the ecosystem and described with input – output models of resource consumption. Thus the paper industry for example has a policy of replanting trees to replace

\[18\] A. B. Caroll, A three-dimensional conceptual model of corporate performance (Academy of management review Vol. 4 No. 4, 1979), p. 497-505
those harvested and this has the effect of retaining costs in the present rather than temporally externalizing them.

Viewing an organization as part of a wider social and economic system implies that these effects must be taken into account, not just for the measurement of costs and value created in the present but also for the future of the business itself. Measures of sustainability would consider the rate at which resources are consumed by the organization in the relation to the rate at which resources can be regenerated. Unsustainable operations can be accommodated for either by developing sustainable operations or by planning for a future lacking in resources currently required. In practice organizations mostly tend to aim towards less unsustainability by increasing efficiency in the way in which resources are utilized.

2. Accountability

This is concerned with an organization recognizing that its actions affect the external environment, and therefore assuming responsibility for the effects of its actions. This concept therefore implies a quantification of the effects of actions taken, both internal to the organization and externally. More specifically the concept implies a reporting of those quantification to all parties affected by those actions. This implies a reporting to external stakeholders of the effects of actions taken by the organization and how they are affecting those stakeholders.
This concept therefore implies a recognition that the organization is part of a wider societal network and has responsibilities to all of that network rather than just to the owners of the organization. Alongside this acceptance of responsibility therefore must be a recognition that those external stakeholders have the power to affect the way in which those actions of the organizations are taken and a role in deciding whether or not such actions can be justified, and if so at what cost to the organization and to other stakeholders.

Accountability therefore necessitates the development of appropriate measures of environmental performance and the reporting of the actions of the firm. This necessitates costs on the part of the organization in developing, recording and reporting such performance and to be of value the benefits must exceed the costs. Benefits must be determined by the usefulness of the measures selected to the decision-making process and by the way in which they facilitate resource allocation, both within the organization and between it and other stakeholders. Such reporting needs to be based upon the following characteristics:

1. Understandability to all parties concerned;
2. Relevance to the users of the information provided;
3. Reliability in terms of accuracy of measurement, representation of impact and freedom from bias;
4. Comparability, which implies consistency, both over time and between different organizations. Inevitably however such reporting will involve qualitative facts and judgments as well as quantifications. This qualitativeness will inhibit comparability over time and will tend to mean that such impacts are assessed different users of the information, reflecting their individual values and priorities.

A lack of precise understanding of effects, coupled with the necessarily judgmental nature of relative impacts, means that few standard measures exist. This in itself restricts the inter-organization comparison of such information. Although this limitation is problematic for the development of environmental accounting it is in fact useful to the managers of organizations as this limitation of comparability alleviates the need to demonstrate good performance as anything other than a semiotic.

3. Transparency

Transparency as a principle means that the external impact of the actions of the organization can be ascertained from that organization’s reporting and pertinent facts are not disguised within that reporting. Thus all the effects of the actions of the organization, including external impacts, should be apparent to all from using the information provided by the organization’s reporting mechanisms. Transparency is of the particular
importance to external users of such information as these users lack the background details and knowledge available to internal users of such information. Transparency therefore can be seen to follow from the other two principles and equally can be seen to be a part of the process of recognition of responsibility on the part of the organization for the external effects of its actions and equally party of the process of transferring power to external stakeholders.

4. Factors influencing involvement in Corporate Social Responsibility

The following are the factors that influence the involvement of Corporate Social Responsibility:\[19\]:

1. Sustainable development:

United Nations’ (UN) studies and many others have underlined the fact that humankind is using natural resources at a faster rate than they are being replaced. If this continues, future generations will not have the resources they need for their development. In this sense, much of current development is unsustainable—it can’t be continued for both practical and moral reasons. Related issues include the need for greater attention to poverty alleviation and respect for human rights. *CSR is an entry point*
for understanding sustainable development issues and responding to them in a firm’s business strategy.

2. Globalization:

With its attendant focus on cross-border trade, multinational enterprises and global supply chains—economic globalization is increasingly raising CSR concerns related to human resource management practices, environmental protection, and health and safety, among other things. CSR can play a vital role in detecting how business impacts labor conditions, local communities and economies, and what steps can be taken to ensure business helps to maintain and build the public good. This can be especially important for export-oriented firms in emerging economies.

3. Governance

Governments and intergovernmental bodies, such as the UN, the Organization for Economic Co-operation and Development (OECD) and the International Labor Organization (ILO) have developed various compacts, declarations, guidelines, principles and other instruments that outline norms for what they consider to be acceptable business conduct. CSR instruments often reflect internationally-agreed goals and laws regarding human rights, the environment and anti-corruption.

4. Corporate sector impact:

The sheer size and number of corporations, and their potential to impact political, social and environmental systems relative to
governments and civil society, raise questions about influence and accountability. Even small and medium size enterprises (SMEs), which collectively represent the largest single employer, have a significant impact. Companies are global ambassadors of change and values. How they behave is becoming a matter of increasing interest and importance.

5. Communications:
Advances in communications technology, such as the Internet and mobile phones, are making it easier to track and discuss corporate activities. Internally, this can facilitate management, reporting and change. Externally, NGOs, the media and others can quickly assess and profile business practices they view as either problematic or exemplary. In the CSR context, modern communications technology offers opportunities to improve dialogue and partnerships.

6. Finance:
Consumers and investors are showing increasing interest in supporting responsible business practices and are demanding more information on how companies are addressing risks and opportunities related to social and environmental issues. A sound CSR approach can help build share value, lower the cost of capital, and ensure better responsiveness to markets.

7. Ethics:
A number of serious and high-profile breaches of corporate ethics resulting in damage to employees, shareholders, communities or the environment—as well as share price—have contributed to elevated public mistrust of corporations. A CSR approach can help improve corporate governance, transparency, accountability and ethical standards.

8. Consistency and Community:
Citizens in many countries are making it clear that corporations should meet the same high standards of social and environmental care, no matter where they operate. In the CSR context, firms can help build a sense of community and shared approach to common problems.

9. Leadership:
At the same time, there is increasing awareness of the limits of government legislative and regulatory initiatives to effectively capture all the issues that CSR address. CSR can offer the flexibility and incentive for firms to act in advance of regulations, or in areas where regulations seem unlikely.

10. Business Tool:
Businesses are recognizing that adopting an effective approach to CSR can reduce the risk of business disruptions, open up new opportunities, drive innovation, enhance brand and company reputation and even improve efficiency.
5. Pyramid of Corporate Social Responsibility

CSR can be distinguished between economic, legal, ethical, philanthropic, or discretionary responsibility. Carroll’s Pyramid of Corporate Social Responsibility\(^{20}\) (see figure 2.4), shows that all of these kinds of responsibilities have always existed to some extent, but it has only been in recent years that ethical and philanthropic functions have taken a significant place.

![Pyramid of Corporate Social Responsibility](image)

**Figure 2.4. Pyramid of Corporate Social Responsibility\(^{21}\)**

1. Economic Responsibility

The economic responsibility shall be looked upon as the core responsibility and are therefore placed in the bottom of the pyramid symbolizing the bedrock.


\(^{21}\) Caroll, loc.cit
Profit making and maximizing a company’s earnings can be looked upon as one of the major responsibilities. This to be able to give a strong return to investors as well as other stakeholders, create jobs, produce goods and services demanded in order to make a profit.\(^{23}\)

2. **Legal Responsibility**

A company needs to and is expected to perform its economical performance by following certain laws and regulations stated by federal, state and local government\(^{24}\). If a company operates in more than one country foreign laws and regulations also has to be followed. Operating under certain laws and regulations can help a company to increase its relationship towards its stakeholders. Carroll further describes that companies sometimes see regulations in the opposite way, whereas laws and regulations often hinder rather than help their economical performance.\(^{25}\)

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\(^{24}\) Carroll (1979; 1991)

3. **Ethical Responsibility**

Ethical responsibility has a major impact on a company and its reputation, such as following unwritten norms, standards and expectations from its stakeholders\(^{26}\). Ethical responsibility can, according to Carroll (2004) be hard to define, especially in developing countries where ethical standards and norms are hard to identify. A company has to operate in such manner that the company follows its moral as well as ethical believes and be aware that ethical behavior can affect the company as much or even more than legal responsibility. Sometimes ethical norms and values can be the underlying force behind new upcoming laws and regulations\(^{27}\).

4. **Philanthropic Responsibility**

According to Carroll, the difference between ethical responsibility and philanthropic responsibility is that philanthropic responsibility is not expected in an ethical nor legal point of view. It is more considered as desired from its stakeholders. Philanthropic expectations can

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\(^{26}\) Carroll (1979; 1991; 2004)  
\(^{27}\) Carroll (1991)
differ regarding in what region or country a company is located and performing its activities. Philanthropic responsibility can include providing daycare centers for employees, voluntary programs to promote human welfare, charity and building schools.

Carroll\(^{28}\) compare philanthropic behavior with acting like a good corporate citizen and that “some firms feel they are being socially responsible if they are just good citizens in the community”. The author points out that philanthropic responsibility is important for a company though less important than the other steps in the pyramid and that a company shall focus on the whole pyramid, especially if a company aims to satisfy several stakeholders which can be of essence for its well being.

“The CSR firm should strive to make profit, obey the law, be ethical and be a good corporate citizen”.\(^{29}\)

Earlier research performed by Carroll and Hatfield\(^{30}\) showed that managers in corporations when ranking their responsibility to-ward stakeholders had prioritized economic responsibility first, secondly legal followed by ethical and finally philanthropic.

\(^{28}\) Caroll (1991), pg. 42  
\(^{29}\) ibid, pg. 43  
\(^{30}\) Caroll (2004)
According to Carroll (1991) there is a natural connection between CSR and a company’s stakeholders. A company will develop its CSR performance depending on the stakeholder and different stakeholders have different claims towards the company. To be able to identify the importance of a stakeholder, Carroll has chosen to use two criteria’s; the stakeholders’ legitimacy and its power. The stakeholder perspective on CSR can facilitate for a company in a strategically point of view, due to a more personalized approach.

Critics toward the CSR pyramid question the possibilities for a company to be able to satisfy all four groups at the same time. The focus should mainly be towards the economical responsibility without any of the other three groups stealing attention and resources. The use and implementation of the different responsibilities will also vary depending of the size of the firm, field of industry and economical conditions.31

b. Definition of Mandatory

According to US Legal dictionary, Mandatory refers to something that is required, and not optional or subject to discretion. In legal

construction of statutes, mandatory requirements of law are typically found by the use of words such as "must", "will" and "shall". For example, if a statute provides that after a person files a petition, "a hearing shall be held", then a hearing on the petition must be held.

According to Kamus Besar Bahasa Indonesia, Mandatory or ‘wajib’ means harus dilakukan; tidak boleh tidak dilakukan. In English it means should be done.

In the ‘Lectric Law Library, the definition of mandatory is not available, however writer found the word ‘mandate’ which means as follows:

A judicial command or precept issued by a court or magistrate, directing the proper officer to enforce a judgment, sentence or decree. Mandatum or commission, contracts. Some define a mandate to be a bailment of goods without reward, to be carried from place to place, or to have some act performed about them. This seems more properly an enumeration of the various sorts of mandates than a definition of the contract. According to Mr. Justice Story, it is a bailment of personal property, in regard to which the bailee engages to do some act without reward. Others define it to be when one undertakes, without recompense, to do some act for the other in respect to the thing bailed.

From the very term of the definition, three things are necessary to create a mandate. First, that there should exist something which should be the

matter of the contract; secondly, that it should be done gratuitously; and thirdly, that the parties, should voluntarily intend to enter into the contract. There is no particular form or manner of entering into the contract of mandate, prescribed either by the common law, or by the civil law, in order to give it validity. It may be verbal or in writing; it may be express or implied it may be in solemn form or in any other manner. The contract may be varied at the pleasure of the parties. It may be absolute or conditional, general or special, temporary or permanent.

The contract of mandate may be dissolved in various ways:

1. It may be dissolved by the mandatary at any time before he has entered upon its execution; but in this case, as indeed in all others, where the contract is dissolved before the act is done which the parties intended, the property bailed is to be restored to the mandator. It may be dissolved by the death of the mandatory; for, being founded in personal confidence, it is not presumed to pass to his representatives, unless there is some special stipulation to that effect. But this principally applies to cases where the mandate remains wholly unexecuted; for if it be in part executed, there may in some cases, arise a personal obligation on the part of the representatives to complete it. Whenever the trust is of a nature which requires united, advice, confidence and skill of all, and is deemed a joint personal trust to all, the death of one joint mandatary dissolves the contract as to all. The
death of the mandator, in like manner, puts an end to the contract. But although an unexecuted mandate ceases with the death of the mandator, yet, if it be executed in part at that time, it is binding to that extent, and his representatives must indemnify the mandator. The contract of mandate may be dissolved by a change in the state of the parties; as if either party becomes insane, or, being a woman, marries before the execution of the mandate. It may be dissolved by a revocation of the authority, either by operation of law, or by the act of the mandator. It ceases by operation of law when the power of the mandator ceases over the subject-matter; as, if he be a guardian, it ceases, as to his ward's property, by the termination of the guardianship. So, if the mandator sells the property, it ceases upon the sale, if it be made known to the mandatory. By the civil law the contract of mandate ceases by the revocation of the authority. At common law, the party giving an authority is generally entitled to revoke it. But, if it be given as a part of a security, as if a letter of attorney be given to collect a debt, as a security for money advanced, it is irrevocable by the party, although revoked by death. Roman law. Mandates were the instructions which the emperor addressed to public functionaries, which were to serve as rules for their conduct.
2. These mandates resembled those of the pro-consuls, the mandata jurisdiction, and were ordinarily binding on the legates or lieutenants of the emperor of the imperial provinces, and, there they had the authority of the principal edicts.  


c. Definition of Voluntary

According to The ‘Lectric Law Dictionary, voluntary means willingly; done with one's consent; negligently. To render an act criminal or tortious it must be voluntary. If a man, therefore, kill another without a will on his part, while engaged in the performance of a lawful act, and having taken proper care to prevent it, he is not guilty of any crime. And if he commits an injury to the person or property of another, he is not liable for damages, unless the act has been voluntary or through negligence, as when a collision takes place between two ships without any fault in either.  

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d. Overview of Corporate Social Responsibility in Indonesia

Indonesia has an extensive history, but from the beginning of the 17th century until becoming a fully independent Republic of Indonesia in 1949, the archipelago was under the colonial rule of Holland and
known as Dutch East India. During this time, capitalism ruled, and thus capitalism was linked to colonialism. This association, along with the oppressive treatment of the Dutch colonizers, led to a “positively hostile” environment for foreign investors in Indonesia under the regime of the first president, Soekarno, especially from 1958 to 1965. However, Indonesia opened up to Foreign Direct Investment (FDI) when the second president, Suharto, took power. Most of Indonesia’s FDI came from countries lacking CSR, establishing a trend to ignore CSR practices within Indonesia. From 1968 to 1986, Indonesia experienced great economic growth due to the international oil boom which saw more than 60% of foreign exchange revenues. On the surface, Indonesia appeared to flourish under Suharto, but corruption was rampant. Much of the profit from this growth was kept by Suharto, his family, and his political cronies, which can be seen as a reflection of the rational choice theory.

The Indonesian miracle boom did not last forever, and shortly after the start of the Asian economic crisis of 1997 emerging from

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37 Melody Kemp, Corporate Social Responsibility in Indonesia: Quixotic Dream or Confident Expectation?, UNRISD, 2001
38 Ibid
39 Ibid, 3
40 Ibid
42 Kemp, 5
43 Ibid, 2
Thailand\textsuperscript{44}, Indonesia had a drastic economic downturn in 1998, with a GNP growth rate of minus 15\%\textsuperscript{45}. This led to the end of the Suharto reign and his so-called “New Order”\textsuperscript{46}. However, through this financial struggle, the economy has managed to partially recover, and even with the current instability, Indonesia still sees 3 to 5\% growth per annum\textsuperscript{47}.

The trend toward CSR in Indonesia started in the early to mid-2000s with the fall of Suharto\textsuperscript{48}. In the Suharto government, businesses previously had political protections from community needs which led to the marginalization and impoverishment of community members\textsuperscript{49}. And after the several decades of corporate exploitation under the Suharto administration, the public wanted more openness from corporations\textsuperscript{50}, paving the way for CSR policies.

That being said, the corruption that was extensive under Suharto continues even today, and this endemic corruption negatively impacts CSR practices within Indonesia. Overall, workers seem more concerned with earning a wage than getting fair treatment\textsuperscript{51}. Also, labor conditions are not viewed by Indonesian companies as part of CSR projects.

\textsuperscript{45} Sasongko, p. 37
\textsuperscript{46} Ibid.
\textsuperscript{47} Kemp, pg. 10
\textsuperscript{49} Ibid, 300-301
\textsuperscript{50} Ibid, 301
\textsuperscript{51} Kemp, pg. 8
performance and reporting\textsuperscript{52}. However, the growing influence of Muslim law, Sharia, which explicitly bans bribery, looting, or deception for the acquisition of land, may lead to a change in CSR perspectives, and create an environment more conducive to CSR practices\textsuperscript{53}. Additionally, the government has begun to put pressure on government companies to disclose CSR practices, showing that the government is trying to deal with CSR\textsuperscript{54}. Also, the recently elected president, Joko Widodo, has vowed to crack down on corruption\textsuperscript{55}. Ultimately, it is necessary for Indonesia to keep up with international companies concerning CSR in order to survive in what is becoming a global market\textsuperscript{56}.

In Indonesia, the meaning of Corporate Social Responsibility is written in the Article 1 (3) Limited Liability Company Law (Law No. 40/2007) which is as follow:

\textit{“Tanggung jawab sosial dan lingkungan adalah komitmen Perseroan untuk berperan serta dalam pembangunan ekonomi berkelanjutan guna meningkatkan kualitas kehidupan dan lingkungan yang bermanfaat, baik bagi Perseroan sendiri, komunitas setempat, maupun masyarakat pada umumnya.”}

\textit{Which if writer translate in English would be:}

\textsuperscript{52} Fitra Roman Cahaya, et al., \textit{Indonesia’s low concern for labor issues}, (Social Responsibility Journal 8, no. 1, 2012), p. 123

\textsuperscript{53} Kemp, pg. 9

\textsuperscript{54} Cahaya, et. al., Op. Cit.


\textsuperscript{56} Cahaya, et. al., Op. Cit., 124
“Corporate Social Responsibility is a commitment of a company to participate in the sustainable economic development in order to increase the quality of life and useful environment, be it for the company itself, the local community, as well as the society in general.”

e. Overview of Corporate Social Responsibility in Malaysia

Way back in 1980s, CSR in Malaysia has started to show its appearance in terms of awareness and implementation. However, only in this past decade has CSR truly made headway. It sprouted from a combination of traditionally wholesome values, western business influence and pressure on Malaysia’s big international companies from first-world business partners.

Much to credit of the policies and initiatives of the federal government and its agencies. Of these, there are two major milestones in particular. The first is the launch of the “Silver Book” in May 2005 – a set of CSR principles and guidelines for Government-linked companies (GLCs) in Malaysia (Putrajaya Committee on GLC High Performance [PCG], 2005). Its objective is to assist GLCs in incorporating CSR into their business agenda.

The other key milestone, was when Bursa Malaysia – the Malaysian Stock Exchange – in late 2006, The Bursa Malaysia has launched a CSR framework for the public-listed companies (PLCs). This CSR


58 B. Sharma, Contextualizing CSR in Asia: Corporate social responsibility in Asian economies. (Singapore: Lien Centre for Social Innovation, 2013)
framework is a set of guidelines for Malaysian PLCs to help them in developing meaningful CSR agendas, policies and initiatives. Also, from 2006 onwards, Bursa Malaysia made it mandatory for all public listed companies (PLCs) in Malaysia to disclose their CSR initiatives in their annual financial reports. As such, it will encourage PLCs to look seriously into engaging into CSR activities. In June 2009, Bursa Malaysia also launched another guide intended for directors of listed companies to gain a clear and constructive direction on corporate governance best practices called the “Corporate Governance Guide: Towards Boardroom Excellence”. This guide focuses on bringing clarity to the roles and requirements needed to enhance corporate governance practices among their boards and committees.  

All this has led to a present day Malaysia where CSR is driven by government incentives, big business, Bursa Malaysia’s reporting requirements and government or NGO collectives focused on spreading CSR. This trend in CSR has been indeed confirmed by several empirical studies. Both Ahmad’s (2003) and Rashid’s (2002) studies have indeed shown the evidence of increased level of CSR awareness in Malaysia over the past decade. Therefore, it is believed that the level of CSR awareness of Malaysia will improve. Ahmad’s (2003) research has indicated that 93.1% of managers in their sample are relatively aware

of CSR. However, the study also concludes that the managers do not fully comprehend the importance of CSR.

According to Dr. Geoffrey Williams in the New Straits Time, “Malaysia is one of the leading countries in CSR, certainly among developing countries and in Southeast Asia, ... because CSR is part of the National Integrity Plan and the government-linked companies’ transformation program.” However, other researchers (Ahmad and Rahim, 2003; Ramasamy and Ting, 2004; Rashid and Ibrahim, 2002) hold different views and suggested that CSR is still considered to be at its infancy stage in Malaysia.

One of the core challenges that the government is facing is to understand the concept of CSR, comprehend the understanding of CSR by wider public, the types of CSR activities practiced in Malaysia and the types of assistance the government can offer to motivate the industries to adopt CSR (Rashid and Ibrahim, 2002).

Ramasamy (2003) attempts to determine the CSR awareness level from the employee’s perspective (one set of stakeholders) in both Malaysia and Singapore. As expected, Singaporean companies tend to exhibit a relatively higher level of awareness, although both countries showed a low level of awareness.

Rashid’s (2002) study has shown that family upbringing, traditional beliefs and customs have had much influence in the improvement of the level of CSR awareness among the Malaysian executives and managers. The studies are also unanimous that the education is the key for success
in the future. Ramasamy (2004), Ahmad (2003) and Rashid (2002) furthermore asserted that the CSR education in Malaysia will be especially needed in terms of assisting organization’s success in a long run.60

C. Legal Framework

a. Overview of Law concerning with Corporate Social Responsibility in Indonesia

Ever since Indonesia entered its reformed era in 1998, the House of Representatives (Dewan Perwakilan Rakyat-DPR) has often suggested that Corporate Social Responsibility shall become a mandatory requirement in legislation in the field of economic, social and environmental matters. The notion of Corporate Social Responsibility was introduced in three particular Indonesian laws: The Investment Law (Law No. 25/2007), the Limited Liability Company law (Law No. 40/2007) and the State-Owned Enterprises Law (Law No. 19/2003). Although the three basic laws have the same goal, i.e. to institutionalize the Corporate Social Responsibility obligation in the Indonesian legal system, each one has its own characteristics. For example, the implementation of Corporate Social Responsibility according to the Investment Law concerns all the operating investors on Indonesian territory, either domestic or foreign. The Limited Liability Company Law requires the implementation of Corporate Social Responsibility

60 Loc.cit.
only from companies doing business in the field of the natural resources sector. Furthermore, the Company Law uses the term ‘environmental and social responsibility’ instead of ‘corporate’, with the intention being to emphasize the environmental obligation of natural resources companies. The existing Corporate Social Responsibility obligation in the State-Owned Enterprises Law is only applicable to state-owned enterprises (SOEs).

The table below is to describe the types of companies and which Corporate Social Responsibility law applies to each company type.

Table 2.2. Types of companies and which CSR law applies to each type.

<table>
<thead>
<tr>
<th>No.</th>
<th>Type of Company</th>
<th>Law dealing with CSR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Domestic Investors:</td>
<td>Investment Law (Law No. 25/2007)</td>
</tr>
<tr>
<td></td>
<td>- Limited liability companies performing investment activities in the field of and/or related to natural resources:</td>
<td>Limited liability Company Law (Law No. 40/2007); GovR No. 47/2012 about ESR; Investment Law (Law No. 25/2007)</td>
</tr>
<tr>
<td></td>
<td>Foreign Investors:</td>
<td>Investment Law (Law No. 25/2007)</td>
</tr>
<tr>
<td>2.</td>
<td>Foreign/ Domestic Investors Limited Liability Companies performing investment activities not in the field of and/or related to natural resources</td>
<td>Investment Law (Law No. 25/2007)</td>
</tr>
</tbody>
</table>
### Overview of Law concerning with Corporate Social Responsibility in Malaysia

Recently, there is rapid development of CSR in Malaysia and Malaysia has become one of the most active emerging economies that involve in corporate social responsibility. Since 1974, development of CSR was started in Malaysia where several issues and act was raised by various parties. Government was introduced the Environmental Quality Act to legislate issue on environmental safety and pollution and

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**Source:** “Corporate Social Responsibility in Indonesia, Legislative Developments and Case” by Tineke Elisabeth Lambooy, 2013, p. 65

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**Table:**

<table>
<thead>
<tr>
<th>Business Category</th>
<th>Law</th>
</tr>
</thead>
<tbody>
<tr>
<td>3. Limited Liability Companies (Natural Resources)</td>
<td>Limited liability Company Law (Law No. 40/2007); GovR No. 47/2012 about ESR</td>
</tr>
<tr>
<td>4. Limited Liability Companies (Not in Natural Resources)</td>
<td>N.A.</td>
</tr>
<tr>
<td>5. SOEs (Natural Resources)</td>
<td>Limited liability Company Law (Law No. 40/2007) (Only for State-Owned; Persero); GovR No. 47/2012 about ESR State-Owned Enterprises Law (Law No. 19/2003)</td>
</tr>
<tr>
<td>6. SOEs (Not in Natural Resources)</td>
<td>State-Owned Enterprises Law (Law No. 19/2003)</td>
</tr>
</tbody>
</table>

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instruct construction companies to comply with the Environmental Impact Assessment (EIA) before developing new housing areas or any projects. Besides, several non-governmental organizations (NGO) and the media have also raised issues on health hazards products, product safety, environmental pollution and discrimination against the handicapped people. In 2004 Malaysian Institute of Integrity (IIM) was established under National Integrity Plan to promote CSR practices in both public and private companies. IIM is responsible to promote the practice of ethical principles, good values and integrity.

Most of the CSR studies in Malaysia focused widely on the disclosure. Within the disclosure context, several issues on CSR disclosure were examined. Among the issues examined are level of disclosure, quantity of information disclosed, types of disclosure and companies’ characteristics. Among these issues, disclosure level is the most popular theme being examined where most studies examined the level of disclosure and motivating factors influencing disclosure level.

Furthermore, below are the regulations, legal provisions law concerning with CSR in Malaysia:

1. Companies Act 1965 that will be replaced with the new Companies Act 2016 (Act 777) (“new act”). The new Act was gazette on 15

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September 2016 and is expected to be implemented in stages starting in 2017\textsuperscript{64}.

1. In section 252 of Act 777, it is mentioned that Directors shall prepare directors’ report, in which the report may contain information about environmental matters. Below is the part of the section that mentioned concerning CSR with its explanation is as follows:

\textquotedblleft Directors shall prepare directors’ report

252. (1) The directors of a company shall prepare for each financial year a report and such report shall be attached to the financial statements prepared under section 248.

(2) A directors’ report –

(a) shall be approved by the Board; and

(b) shall be signed on the directors’ behalf by at least two directors, or in the case of a single director, that director.

(3) Every copy of directors’ report laid before a company in an annual general meeting under section 340, or sent to a member under section 257 or otherwise circulated, published or issued by the company shall state the name of the person who signed the report on the directors’ behalf.

(4) Any director who fails to take all reasonable steps to secure compliance under subsection (1) commits an offence and shall, on conviction, be liable to a fine not exceeding five hundred thousand ringgit or imprisonment not exceeding one year or to both.

(5) The company and every officer who contravene subsection (2) commit an offence and shall, on conviction, be liable to a fine not exceeding twenty thousand ringgit.65

The explanation of the section is as follows:

1. Each report prepared under section 252 may include a business review.

2. The business review may, to the extent necessary for an understanding of the development, performance or position of the company’s business, contain—

   a. A fair review of the company’s business;

   b. A description of the principal risks uncertainties facing the company;

   c. A balanced and comprehensive analysis of—

      i. The development and performance of the company’s business during the financial year;

ii. The position of the company’s business at the end of that year, consistent with the size and complexity of the business; and

iii. The key performance indicators of the company;

d. Information about –

i. Environmental matters, including the impact of the company’s business on the environment;

ii. The company’s employees; and

iii. Social and community issues, including information about any policies of the company in relation to those matters and the effectiveness of those policies; and

e. Subject to paragraph 7 of this part, information about persons with whom the company has contractual or other arrangements which are essential to the business of the company

3. If the review does not contain any of the information mentioned in subparagraphs 2(a), (b), (c) and (d), its shall state which of the information it does not contain.

4. The review may, where appropriate, include reference to, and additional explanations of, amounts included in the company's financial statements.
5. In relation to a group directors’ report, this Part has effect as if the references to the company include references to its subsidiary included in the consolidation.

6. Nothing in this part requires the disclosure of information about impending developments or matters in the course of negotiation if the disclosure would, in the opinion of the directors, be prejudicial to the interests of the company.

7. Nothing in subparagraph 2(e) requires the disclosure of information about a person if the disclosure would, in the opinion of the directors, be prejudicial to that person and contrary to the public interest.

8. For the purposes of this part, “key performance indicators” means factors by the reference to which the development, performance or position of the company’s business can be measured effectively.66

3. Act 177 Industrial Relations Act 1967
4. Act A1478 of Companies commission of Malaysia (Amendment) Act 2015:

1. Formerly in section 17(d) of Act 614 Companies Commission of Malaysia 2001, it states as follows: “(d) to encourage and promote proper conduct amongst directors, secretaries, managers and other officers of a

66 ibid, pg. 564
corporation, and self-regulation by corporations, companies, businesses, industry groups and professional bodies in the corporate sector in order to ensure that all corporate and business activities are conducted in accordance with established norms of good corporate governance;”

Which then amended as below:

Amendment of section 17:

Paragraph 17(d) of the principal Act is amended by inserting after the words “good corporate governance the words “and to encourage and to promote corporate responsibility and business sustainability;”.

These are the list of Practices and Guidance for Corporate Social Responsibility in Malaysia68:

1. 2006 : ISO 26000

The Securities Commission is a member of the ISO Mirror Committee which is involved in developing ISO 26000 which is a voluntary guidance standard for the implementation of Social Responsibility (SR) related practices. This Guidance will be in line with the International Standard which serves to provide guidance to organizations on:


2. Principles, practices and issues relating to social responsibility
3. Integrating and implementing social responsibility throughout an organization and its sphere of influence, including its supply chain
4. Identifying and engaging with stakeholders
5. Communicating commitments and performance related to social responsibility
6. Contribution of an organization to sustainable development.

It promotes common understanding in the field of social responsibility and seeks to clarify the relationship between social responsibility principles and organization governance frameworks. This guidance will be applicable to all types of organizations. The drafting of the guidance standard is still ongoing.

2. September 2006: Bursa Malaysia’s CSR Framework

The Bursa Malaysia CSR Framework for public-listed companies was launched on 5 Sept 2006. The CSR Framework provides a guide to Malaysian companies to develop CSR strategies as well as to communicate them effectively to stakeholders. The CSR Framework looks at 4 main focal areas for CSR practice namely, environment, workplace, community and the marketplace. The framework supports the new rules
incorporated in Bursa Malaysia Listing Requirements that require reporting of CSR activities by public-listed companies in their annual report.

The Silver Book is the fourth in a series under the GLC Transformation Programme. The Silver Book has three key objectives i.e to clarify expectations on GLCs’ contribution to society, to guide GLCs in evaluating their starting position in contributing to society and to provide the GLCs with a comprehensive set of tools, methodologies and processes to proactively contribute to society in a responsible manner while still creating value for their shareholders.

4. December 2006: CSR Reporting
To inculcate the culture of CSR, the Prime Minister had announced in his 2007 budget speech, that public-listed companies are required to disclose their CSR activities. The Listing Requirements were subsequently amended to impose a new obligation on listed issuers to disclose their CSR activities in their annual reports. The new provisions require the disclosure of the CSR activities or practices undertaken by the listed issuer and its subsidiaries or if no such activities or practices are undertaken, a statement to that effect is to be made in the annual report.