

Ethical reforms initiated by multinationals after a crisis of governance: Case study*

ARNAUD CELKA **

Nach dem Skandal: ethische Reformen in multinationalen Konzernen

Vorstellung eines Dissertationsprojektes

1. Introduction

The past 20 years have been marked by a significant number of scandals involving questionable, abusive or criminal commercial practices. One of the most striking examples was the bankruptcy of Enron, which involved accounting fraud aimed at concealing financial losses from certain speculative transactions. Such scandals were not limited to fraudulent financial practices; they also involved the use of child labour (Nike, Reebok, etc.), mismanagement (Nortel, Vivendi, etc.) or environmental issues (Total, BP, etc.).

This type of behavior reflects the ‘wilding’ (Derber 2010) of certain commercial and financial practices resulting from the normative void caused by the State’s withdrawal from its regulatory role. The shift from government regulations to a market-driven regulatory process that started in the 1980s with the privatization, liberalization and deregulation processes created a normative void conducive to the development of such economic practices (Stiglitz 2003; Sales/Beschorner 2006). More recently, the international financial crisis demonstrated the wide-ranging, disastrous effects of capitalism whenever the market is the only regulatory force. These elements all demonstrate that taking ethics into consideration is not only a moral issue but also a condition for the sustainable operation of local, national and international commercial practices.

The private sector response to these excesses involved various measures to re-establish confidence among the stakeholders and vis-à-vis public opinion. The first response came in the form of codes of conduct put in place by individual companies. Standards organizations then appeared, still in the private sector, including various institutional actors such as representatives of civil society or NGOs, universities, companies and so forth. These private sector organizations that produced standards

* This PhD-project is part of a broader research project funded by the Social Sciences and Humanities Research Council (SSHRC) entitled *Role and impact of International Private Authorities in the Ethical Regulation of Corporate Activities* under the direction of Prof. Dr. Arnaud Sales and Prof. Dr. Thomas Beschorner.

** Arnaud Celka, Doctoral Candidate, Department of Sociology, University of Montreal, P.O. Box 6128, Downtown Station, H3S3J7 Montreal, QC/Canada, phone: +1 514 343-6111 ext.: 3702, e-mail: arnaud.celka@umontreal.ca, fields of expertise: economic sociology, corporate social responsibility.

were either sector-based, as in the case of the Fair Labor Association (FLA) in the textiles sector and Responsible Care in the chemicals industry, or intersectorial in the case of Social Accountability 8000 (SA 8000) and AccountAbility 1000 (AA 1000). These initiatives all had one thing in common: they promoted the use of ethical and responsible practices within multinational companies. Generally speaking, this shift involved an increase in private sector prerogatives (Cutler et al. 1999; Cutler 2003; Hall/Biersteker 2002). The development of these private sector standards organizations appeared in conjunction with the evolution of the concept of Corporate Social Responsibility (CSR) which companies incorporated into their value chain.

This thesis will examine this phenomenon by studying Multinational Companies (MNC) that were faced with fairly substantial governance issues, looking specifically at their response to these types of behaviors as well as the path they followed in relation to CSR. The focus of this research will be to answer the following general question:

How did companies that experienced a profound crisis in governance rebuild their organizations?

More specifically, I will analyze the mechanisms put in place by such companies to rebuild their organizations as well as the process they used to incorporate CSR into their value chain, where applicable. I will also study and analyze how the standards issued by private-sector standards organizations were incorporated into this process. In this regard, I will attempt to answer the following two sub-questions

- (1) What motivated companies to adopt one or more normative standards?
- (2) How were these standards incorporated into the organization?

The process employed by the companies to adopt and adapt, where applicable, these normative structures will also be investigated.

2. Institutional pressure

Organizations in general and MNCs in particular cannot be examined in isolation and independently from one another. MNCs function alongside other MNCs as well as other types of organizations including NGOs, standards organizations, public organizations, unions, universities, think tanks, and so forth. These actors interact both formally and informally, directly and indirectly, visibly and invisibly. The impact of the environment and more specifically the actors functioning within the environment, are key to analyzing an organization's actions, and in the context of this thesis, the actions of MNCs. Neo-institutional theories (Zucker 1977/1983/1987; Meyer/Rowan 1977; Scott 1987/1994/1995; Powell/DiMaggio 1991) and more specifically the theorization of institutional pressure within *organizational fields* developed by Powell and DiMaggio (1991) are key theoretical elements I will use to determine the weight and role of actors involved in the CSR process undertaken by certain MNCs. The authors define an *organizational field* as follows: "By organizational field I mean those organizations that, in the aggregate, constitute a recognized area of institutional life: key suppliers, resource and product consumers, regulatory agencies, and other organizations that produce similar services or products. The virtue of this unit of analysis is that it directs our attention not simply to competing firms, [...] but to the totality of relevant actors." (DiMaggio/Powell 1983: 148). According to DiMaggio and Powell, the *organizational fields* in which organizations function tend to become homogenized through the process of institutionalization. In that regard, the authors distinguish three types of

mechanisms, derived from the environment, organizations and institutional change vectors: *coercive isomorphism*, *mimetic isomorphism* and *normative isomorphism* (DiMaggio/Powell 1983/1997; Powell/DiMaggio 1991). *Coercive isomorphism* results from both formal and informal pressures exerted on organizations by other organizations upon which they are dependent and by cultural expectations in the society within which organizations function (DiMaggio/Powell 1983: 150). In our case, this may involve pressure exerted by public or private actors, focused on incorporating a specific ethical dimension into the company. *Mimetic processes* emerge as a response to uncertainty that encourages companies to imitate one another (DiMaggio/Powell 1983: 151). Some companies will be inspired by what others have done, for example, by adopting the same responsible governance structures. Finally, *normative processes* stem from professionalization and the development of the conditions and methods associated with a specific occupation (DiMaggio/Powell 1983: 152). It would be the sector itself through its training structures or professional organizations that would encourage change in certain production practices.

These various forms of institutional constraints seem a priori to be essential to define the three key research elements in the analysis: First, the underlying reasons the company initiated the reforms; second, the form such reforms took; and third, the roles played by the various organizational actors in the company's development.

3. Organizational Learning

To examine the way in which the reforms were initiated and undertaken within companies and to eventually answer both the general question 'How did companies that had experienced a profound crisis in governance rebuild their organizations?' and the second sub-question 'How were these voluntary standards incorporated into the organization?' I will apply the organizational learning concept developed by Argyris & Schön (Argyris/Schön 2002; Argyris 2003). Their theorization seems relevant in that it will enable to determine the type and scope of the reforms undertaken by the companies under study.

Argyris and Schön defined two types or levels of learning (2002). The first level called *single-loop learning* entails practical, ad hoc answers to specified problems, without questioning the underlying values that led to the problems. The second level, or *double-loop learning*, involves dealing with problems in ways that surpass the simple behavioral adjustments performed in *single-loop learning*. In *double-loop learning*, the values underlying the problem are called into question and are adjusted. Chris Argyris developed the idea that a number of entrenched "defensive routines" (1986/2003: 66-84) prevent organizations from questioning the values underlying the actions they take. Defensive routines defined by the author as "[...] any action or policy designed to avoid surprise, embarrassment, or threat" (Argyris 1986: 75) limit learning which is a characteristic of *single-loop learning*. For an organization to promote learning, the author maintains that it is essential to change these defensive routines at the individual and organizational levels by explaining and critiquing the ideas that underlie the actions. Constructive reasoning should be encouraged as opposed to defensive reasoning (Argyris 2003: 73f.). It is imperative to publicize this way of thinking throughout the organization and ensure it becomes part of the corporate culture.

This theoretical framework, in connection with organizational learning, will allow to track a MNC's post-crisis CSR process in light of the analysis of the type of reforms implemented within the organization.

4. Methodology

I will apply a case study approach in this research, and will select two companies, with different issues and from different sectors, so as to enhance opportunities for comparison.

This study will combine a literature search relative to the target companies as well as the standards they have adopted and semi-directive interviews conducted within the companies. The goal is to interview key actors in the ethics-related reform process, namely the management team and those in charge of the CSR process, where applicable. The information gathering will be focused on the following six points or themes: the companies' history and structure; the governance issue or issues the companies experienced; the reforms undertaken; the standard or standards selected as well as the registration process; proposed audit or sanction mechanisms; and finally the relationships with relevant organizational actors such as other MNCs, stakeholders, standards organizations, public organizations and so forth. The information required to answer the main research question 'How did companies that experienced a profound crisis in governance rebuild their organizations?' and for the second part of the inquiry into how the private standard or standards are applied by the companies will be derived from these sources. In relation to the conditions leading to the application of the standards I hope to answer the following main questions: What reforms were implemented? Where did the voluntary standards fit in chronologically and structurally? How were the reforms and standards selected?

The next step will entail gathering information on the standards selected by the companies. The focus here will be on three main themes: a) the organizations' origins and their objectives; b) institutional data such as their organizational structure and governance methods; and c) the presence and type of control mechanisms and sanctions.

These various sources of information whether from internal and external documents combined with the interviews will allow for the triangulation of the units of analysis. My analysis will focus on evaluating the content of the material gathered from the various sources, namely the themes referred to above. The triangulation of the company-related units of analysis gathered from the various sources will allow to examine the reforms the company initiated following the crisis in governance. Using these elements, I will

- (1) compile and analyze the reforms undertaken;
- (2) analyze on the basis of Argyris' organizational learning theory the type of learning (single-loop or double-loop) embraced in the change process;
- (3) define the voluntary standards adopted chronologically and structurally as part of the rebuilding process;
- (4) update the reasons that motivated the company to adopt the standard or standards; and
- (5) study the institutional pressures that impacted the type of reforms embraced in general and the type of standards adopted in particular.

I will then compare the elements associated with the standard or standards adopted by the companies with the previous elements of information gathered from within the companies to determine whether a process to adapt the standards existed within these MNCs. These elements will allow to examine both the reform process initiated by a company while trying to rebuild itself in the aftermath of an ethics issue and the role and impact of the voluntary standards deployed.

References

- Argyris, C.* (1986): Skilled Incompetence, in: Harvard Business Review, Vol. 64/No. 5, 74-79.
- Argyris, C.* (2003): Savoir pour agir, Surmonter les obstacles de l'apprentissage organisationnel, Paris: Dunod.
- Argyris, C./ Schön, D.* (2002): Apprentissage organisationnel, théorie, méthode, pratique, translation of the first U.S. edition, Paris, Bruxelles: De Boeck.
- Boiral, O.* (2003): La norme ISO 14001: Vers une uniformisation des pratiques?, in: Corinne Gendron and Jean-Guy Vaillancourt (Eds.): Développement durable et participation publique. De la contestation écologique aux défis de la gouvernance, Montréal: Les Presses de l'Université de Montréal, 91-108.
- Cragg, W.* (2005): Ethics Codes, Corporations and the Challenge of Globalization, Cheltenham, U.K., Northampton, MA: Edward Elgar.
- Cutler, A. C.* (2003): Private Power and Global Authority: Transnational Merchant Law in: The Global Political Economy, Cambridge, U.K., New York: Cambridge University Press.
- Cutler, A. C./ Haufler, V./ Porter, T.* (1999): Private Authority and International Affairs, Albany: State University of New York Press.
- Derber, C.* (2010): The Wilding of America: Money, Mayhem, and the New American Dream New York: Worth Publishers.
- Dicken, P.* (1998): Global Shift: the Internationalization of Economic Activity, Third edition, London: The Guildford Press.
- DiMaggio, P. J./ Powell, W. W.* (1983): The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields, in: American Sociological Review, Vol. 48/No. 2, 147-160.
- DiMaggio, P. J./ Powell, W. W.* (1997): Le néo-institutionnalisme dans l'analyse des organisations, in: Politix, No. 40, 113-154.
- Gereffi, G.* (1999): International Trade and Industrial Upgrading in the Apparel Commodity Chain, in: Journal of International Economics, Vol. 48/No. 1, 37-70.
- Gereffi, G.* (2001): Beyond the Producer-driven/Buyer-driven Dichotomy: The Evolution of Global Value Chains in the Internet Era, in: IDS Bulletin, Vol. 32/No. 3, 30-40.
- Gereffi, G./ Korzeniewicz, M.* (1994): Commodity Chains and Global Capitalism, Westport, Conn.: Praeger.
- Grove, H./ Basilico, E.* (2008): Fraudulent Financial Reporting Detection: Key Ratios Plus Corporate Governance Factors, in: International Studies of Management and Organization, Vol. 38/No. 3, 10-42.
- Hall, R. B./ Biersteker, T. J.* (2002): The Emergence of Private Authority in Global Governance, Cambridge, UK, New York: Cambridge University Press.
- King, A./ Lenox, M.* (2000): Industry Self-regulation Without Sanctions: The Chemical Industry's Responsible Care Program, in: Program Academy of Management Journal, Vol. 43, 698-716.

- Meyer, J./ Rowan, B. (1977): Institutionalized Organizations: Formal Structure as Myth and Ceremony, in: *American Journal of Sociology*, No. 83, 340-364.
- Moffet, J./ Bregba, F./ Middelkoop, M. J. (2004): Responsible Care: A Case Study of a Voluntary Environmental Initiative, in: Kernaghan Webb (Eds.), *Voluntary Codes: Private Governance, the Public Interest and Innovation*, Ottawa: Carleton Research Unit for Innovation, Science and Environment, 177-207.
- Pastré, O./ Vigier, M. (2003): *Le capitalisme déboussolé: après Enron et Vivendi: soixante réformes pour un nouveau gouvernement d'entreprise*, Paris, Éditions La Découverte.
- Porter, T. (1999): Hegemony and the Private Governance of International Industries, in: Cutler C./ Haufler, V./ Porter, T. (Eds.), *Private Authority and International Affairs*. Albany, NY: State of New York Press, 257-282.
- Powell, W. W./ DiMaggio, P. J. (1991): *The New Institutionalism in Organizational Analysis*, Chicago: University of Chicago Press.
- PricewaterhouseCoopers (2005): *Global Economic Crime Survey 2005*, available at: http://www.pwc.com/fr_CA/ca/risk/forensic-services/publications/criminalite-economique-2007-fr.pdf (last visited on Jan. 3, 2011).
- PricewaterhouseCoopers (2007): *Criminalité économique: Personnes, contrôles et culture*, The 4th biennial Global Economic Crime Survey, Canada, available at: http://www.pwc.com/en_BE/be/dispute-analysis-and-investigation/PwC_2005GECS.pdf (last visited on Jan. 3, 2011).
- Priest, M., (1998): The Privatization of the Regulation, Five Models of Self Regulation, in: *Ottawa Law Review*, Vol. 29/No. 2, 233-302.
- Sales, A./ Beschormer, T. (2006): The Domestic and Transnational Expansion of the Private Sector and Ethics in Businesses, in: Stehr N./ Henning, C./ Weiler, B. (Eds.), *The Moralization of Markets*, New Brunswick, NJ: Transaction Publishers, 227-254.
- Sales, A., in collaboration with Lacruz, T. (2000): The Expansion of the Private in a Globalized World. Presentation at a plenary session of the 2000 Conference of the Research Council of the International Sociological Association: Social Transformations at the Turn of the Millennium/Les transformations sociales au tournant du Millénaire, Montréal, July.
- Sassen, S. (1996): *Losing Control?: Sovereignty in an Age of Globalization*, New York: Columbia University Press.
- Sassen, S. (1998): *Globalization and its Discontents*, New York: New Press.
- Scott, R. (1987): The Adolescence of Institutional Theory, in: *Administrative Science Quarterly*, No. 32, 493-511.
- Scott, R. (1994): Institutions and Organizations. Toward a Theoretical Synthesis, in: Scott R. / Meyer, J. (Eds.), *Institutional environments and organizations*, Thousand Oaks/ London: Sage, 55-80.
- Scott, R. (1995): *Institutions and Organizations*. Thousand Oaks/ London: Sage.
- Stiglitz, J. E. (2003): *The Roaring Nineties: a New History of the World's Most Prosperous Decade*, New York: W. W. Norton.
- Zucker, L. (1977): The Role of Institutionalization in Cultural Persistence, in: *American Sociological Review*. No. 42, 725-743.
- Zucker, L. (1983): Organizations as Institutions, in: *Research in the Sociology of Organization*, No. 2, 1-47.
- Zucker, L. (1987): Institutional Theories of Organizations, in: *Annual Review of Sociology*, Vol. 13, 443-464.