Woman C.P.A.

Volume 40 | Issue 1 Article 3

1-1978

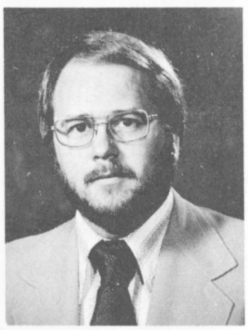
Change In Moral Awareness: A positive approach to social responsibility

Donald L. DeHaven

Carol S, DeHaven

Change In Moral Awareness

A positive approach to social responsibility



Donald L. DeHaven, CPA is a partner with DeHaven and DeHaven and an Instructor of Accounting at Southwest Missouri State University in Springfield. His professional memberships include AWSCPA, ASWA, the Missouri Society of CPAs, and the Greater Ozarks Chapter of NAA which he is serving this year as president.

Carol S. DeHaven, CPA, Instructor of Accounting at Southwest Missouri State University, is also a partner with DeHaven and DeHaven, in Springfield. She is a member of AWSCPA, NAA, the Missouri Society of CPAs, and the Springfield Chapter of ASWA, as well as AICPA.

What is the social responsibility of business? Many managers believe that their first responsibility is to earn a satisfactory rate of return on the investment of the owners. Social activity costs can be incurred only after the desired profit appears to have been earned.

Is this a constructive view of social responsibility? Will this attitude serve a company well in the long run?

In adopting such a philosophy, management is defining "profits" as an amount determined before a reduction for the cost of social activities. Therefore, in this view both the owners and social projects are competing for the same profit dollars with the consequence that each dollar given to social activities necessarily is to the detriment of owners, and vice versa. Since management is expected to control the allocation of profit it is caught between these conflicting demands.

An analogy from cost accounting serves to illustrate the point further. Suppose a company can produce eight units of product in an eight-hour work day and decides to produce nine units per day to meet the demand of normal sales (not a special order). To produce the ninth unit requires overtime and will thereby incur increased labor costs. Generally accepted accounting principles argue that the overtime premium incurred to produce the ninth unit should be allocated to all units produced on some proportionate basis. The logic employed is that, without the first eight units, the ninth unit would not have incurred the premium cost.

Business fails to apply that same logic to all costs in the long run when it defines profits as an amount before a reduction for social activity costs. The cost of many commonly accepted social activities (costs of providing decent working conditions or increased labor costs due to acceptance of the concept that children should not be part of the labor force) are now considered part of the normal cost of doing business while the cost of the ninth unit, the most recent social activity, is treated as an allocation of profits. In reality, all costs reduce profits; costs of new social activities are simply currently more controversial and more readily visible.

The negative aspects of relegating social responsibility to a second class status are clearly visible when management must defer or discontinue its social activities. It is generally recognized that management has the right to make the determination whether to give, to whom to give and the form of the gift. However, to make commitments and then to rescind them would appear a violation of trust with the blame attributed to the owners' priority demands on profit dollars.

A Positive Approach

The following definition of social responsibility provides insight into a means of avoiding the potential of conflict between owners' claims and those of social activities:

> *Corporate social responsibility is the voluntary response of corporations to those needs of society which would not normally be met within the framework of the profit motive. Corporate social responsibility goes beyond obeying laws and enlightened self-interest to require voluntary response. (There are many, however, who believe that providing a demanded product or service at a reasonable price is the "social" responsibility of the firm. This is not the generally accepted meaning of the term.)*[1]

This philosophy perceives the function of the normal business operation as that of providing an adequate rate of return on the investment of the owners while treating the "voluntary response" as a part of those normal business operations. In this concept of social responsibility, both the needs of society and of the owners are important and neither is subjugated to the other.

Using this approach, social activity costs can be treated as any other discretionary administrative cost. Flexibility to respond can be obtained by budgeting discretionarily fixed and discretionarily variable social commitments as business operations change. Management is still responsible for budgeting and controlling all costs;

"Social activity costs can be treated as any other discretionary administrative cost. Management...is freed from having to treat social activity costs as profit allocations or special items."

it is merely freed from having to treat social activity costs as profit allocations or special items.

Budgeting

Budgeting social activity costs as discretionary costs is the same as any budget preparation process; planning must begin with the accumulation of relevant information and estimates. Specifically, planning social performance requires estimates of possible needs of various social activities or organizations in terms of resource requirements (funds, goods or time) and alternative ways that those needs might be met. Consideration will also be given to the time periods, perhaps in terms of several years, over which commitments might vary. Obviously, planning requires estimates relating to other operating functions as well.

Once the appropriate source data is gathered, management is equipped to integrate the information to derive projected ranges of activity in all relevant areas of normal operations. Subjective criteria will be employed to rank the many social activities to which resources could be committed. Based on the resultant projections, management will reject some activities and will assign priorities to the remainder.

Certain social activities may be considered of sufficient importance that management wishes to definitely commit resources to them. Once such a decision has been reached, this commitment will be treated as any other fixed cost in the budget process.

Other social activities may be considered of lesser importance or their desirability contingent upon the occurrence of some event. The circumstances or conditions that would trigger involvement in these activities should be specified, along with the method of participation and the basis for determination of the amount of resources included in the potential involvement. The formula to be used in determining the extent of the commitment can be established in any fashion desired by the company. Some bases that might possibly be used would include: a percent of net income, a percent of net income in excess of $x, a stated amount per unit of sales in a product line, or a stated amount per participant in the social activity. The important point is that the cost of this social activity is a variable cost, based on some predetermined formula and accounted for in the flexible budget in the same manner as many other variable general and administrative costs.

Communication

A crucial factor in attaining the goals of both the business and the social organization is effective communication. The business must be aware of organizations to begin its budget process. In the same way, a social organization requires information relating to the resources it may expect to receive over the coming budget period.

If the social organization is one to whom management decides to make a fixed commitment, communication of the terms of the commitment will assist the organization in planning and budgeting its own activities. Among the items of information of benefit to the social organization is a statement of the fixed amount of resources to be received and the anticipated timing of their receipt.

A social organization to whom a variable commitment is made will benefit in receiving specific information as to the terms of the commitment. This information would parallel the factors included in preparing the variable budget. Specifically, such information would include: the form of participation anticipated, the circumstances that would give rise to the company's participation and the formula to be used in determining the amount of the resource commitment. During the ensuing budget period, reporting to the social organization will keep it informed of the likelihood of obtaining the resources and enable it to modify its own planning and budgeting. These reports would be regularly scheduled and include a decision date when a firm commitment will be made or notice given that resources will not be forthcoming.

Implications

Budgeting allows business to forecast its involvement in social activities. Freedom to respond to changing business conditions is not sacrificed to obtain protection against the potential embarrassment of withdrawing commitments that have been made. For the many business and social organizations currently using an annual budget or review process, these suggestions should not require extensive changes in operating procedures. For organizations not utilizing flexible budgeting, some similar planning technique will need to be adopted.

Open communication with social organizations subjects management to a risk that its decisions may lead to criticism from society. Some negative feedback may occur whenever subjective criteria are employed in decision making and may be particularly strong if the effort at achieving social responsibility is perceived to be of a superficial nature. A business genuinely concerned with social responsibility, however, will be able to succeed in communicating to society its concern, the source of its ability to participate in social activities, and an understanding of the needs of owners.

A specific method of financial statement presentation for social activity costs is not part of this discussion because the goals to be achieved and a means of achieving them must be determined first. The flexible budget helps establish a definition (philosophy) of social responsibility, specific goals to be sought and, thereby, also establishes a basis upon which a reporting method can be designed.

Summary

Owners and society can reasonably expect management to find a practical approach to many questions including the question of social responsibility. Flexible budgeting, a proven tool, is practical and becomes a positive approach when it also avoids placing the owners and society in conflicting positions. Regardless of management's philosophy or concept of social responsibility, flexible budgeting a) plans social performance and thereby establishes a basis for reporting, b) controls costs while planning for profits and c) can avoid creating needless conflicts between business and society.

NOTE

[1]"*Certificate in Management Accounting Examination, Unofficial Solution for Part 2 — December, 1974, Organization and Behavior, including Ethical Considerations," Management Accounting, (March, 1975), p. 72.*

The authors chose to use the term "business social responsibility" rather than "corporate social responsibility" in recognition that the important part of the term is social responsibility, not the legal form of the organization.