PRACE NAUKOWE
Uniwersytetu Ekonomicznego we Wrocławiu

RESEARCH PAPERS
of Wrocław University of Economics

Nr 387

Social Responsibility of Organizations
Directions of Changes

edited by
Magdalena Rojek-Nowosielska

Publishing House of Wrocław University of Economics
Wrocław 2015

Copy-editing: Marcin Orszulak

Layout and proof-reading: Barbara Łopusiewicz

Typesetting: Małgorzata Czupryńska

Cover design: Beata Dębska

Information on submitting and reviewing papers is available
on the Publishing House's website
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www.pracenaukowe.ue.wroc.pl

ISSN 1899-3192
e-ISSN 2392-0041

ISBN 978-83-7695-502-5

The original version: printed

Printing: EXPOL

Publications may be ordered in Publishing House
tel./fax 71 36-80-602; e-mail: econbook@ue.wroc.pl
www.ksiegarnia.ue.wroc.pl

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RESEARCH PAPERS OF WROCŁAW UNIVERSITY OF ECONOMICS nr 387 • 2015

Social Responsibility of Organizations. Directions of Changes

ISSN 1899-3192
e-ISSN 2392-0041

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THE PREMISES FOR CORPORATE SOCIAL RESPONSIBILITY IN INSOLVENCY PROCEEDINGS

Summary: Corporate social responsibility concept is frequently discussed in the literature in the context of its positive impact on the value creation and the company's long-term development. However, it can also be applied with regard to companies facing bankruptcy. Perceiving bankruptcy as a social problem allowed formulating the objective of the research presented in the paper, which is to present the premises for CSR concept in insolvency proceedings. The analysis of the domestic and foreign literature on the subject together with appropriate legislative documents allowed stating that CSR is used in the insolvency proceedings practice. Such an approach is consistent with the idea of the institution of insolvency, which is based on the socially responsible distribution of losses between the stakeholders of a bankrupt company or on the verge of bankruptcy. The paper contributes to the scarce literature on the implementation of corporate social responsibility assumptions in insolvency proceedings. It also discusses the stakeholder theory and attempts to relate it to insolvency proceedings practice, as well as indicates the direction of changes which may have a positive impact on the socially responsible conduct of these processes.

Keywords: corporate social responsibility, bankruptcy, insolvency proceedings, stakeholder theory.

DOI: 10.15611/pn.2015.387.02

1. Introduction

The model concept of corporate social responsibility (CSR) as proposed by Carroll [1979, p. 500] includes economic, legal, ethical and discretionary (volitional) responsibilities. This model assumes the need for doing business in the way that generates profits necessary for a company to continue operations and develop (economic responsibility) [Rojek-Nowosielska 2011, p. 33]. It can, however, be expected that

the CSR concept also applies when a company is not profitable or even on the verge of bankruptcy.

It should be stressed that the problem of CSR in relation to the companies at risk of bankruptcy is not common in literature where the concept is mostly discussed in terms of its positive impact on the value creation and company's long-term development. Banasiewicz [2011, p. 79], referring to the ten phases of the organization's life, clearly indicates that there are no manifestations of CSR at the tenth phase, death, which is a stage likely to "continue or occur suddenly." Yet, according to the author, "it is to be hoped that organizations will realize that their socially responsible actions may help them to avoid the decline phase-death" [Banasiewicz 2011, p. 82].

It is important to note that in *The Polish Bankruptcy and Reorganization Law* the word "insolvency" means not only liquidation of debtor's assets, but also bankruptcy with a possibility of making a settlement [Ustawa z 28 lutego 2003 r.]. The purpose of this type of insolvency proceedings is to restructure a company and restore its full ability to continue operating. Nearly 20% of the bankruptcy proceedings in Poland lead to the restructuring of a company. In addition, work is currently under way in Poland to change the bankruptcy law so that it facilitates settlement and restructuring of a company. This work is consistent with the European Union's "second chance" policy. It means that insolvency restructuring proceedings could be more frequent in the future and the CSR idea implemented in this special case of the company's life would become more important.

In the light of the above, it seems essential to identify the time frame (stages) preceding the final bankruptcy of a company and consider the occurrence of the CSR concept in its relations with stakeholders at this stage.

The purpose of this paper is to present the premises for CSR concept in insolvency proceedings. In order to do so, the authors analyzed domestic and foreign literature on the subject together with appropriate legislative documents. The analysis allowed them to determine the basic assumptions of the stakeholder theory, consider them in the context of the insolvency proceedings and indicate the direction of changes which may have a positive impact on the socially responsible conduct of these processes.

2. Stakeholder theory and corporate social responsibility

The stakeholder theory was popularized by R.E. Freeman. Stakeholders are all identifiable groups or individual entities which may affect the achievement of organization's objectives or which may be affected by organization's achievement of its objectives [Freeman, Reed 1983, p. 91; Rojek-Nowosielska 2006, p. 14]. The major stakeholders of a company therefore include shareholders, employees, creditors, suppliers, customers, banks, government, community, public interest groups and the general public [Ogan, Ziebart 1991; Tilt 2007].Within the wide range of stakeholders it is possible to identify three groups, such as constitutional, contractual and contextual stakeholders [Paliwoda-Matiolańska 2009, p. 59]. Constitutional

stakeholders are indispensable for business to exist. Contractual stakeholders, as the name suggests, interact with an organization due to a formal contract. They include, above all, its business partners. A variety of communities, local, regional, national or global, are contextual stakeholders.

Other categories of stakeholders presented in the literature distinguish the following types: primary and secondary, internal and external, economic and social, environmental and process, strategic and moral, voluntary and forced [Rudnicka 2012, pp. 92–95].

All stakeholders, regardless of the group to which they belong, claim the right to affect the activities of an entity, which stems from the fact that they co-exist in a given economic environment. Therefore, an organization should also take into account the needs of its environment which have to be met, including compensation for any damages resulting from its operations.

Within the stakeholder theory there exist two branches: ethical (moral) also known as normative (prescriptive) and managerial (positive) [Deegan, Unerman 2011, pp. 348–355].

The ethical branch of the stakeholder theory implies that all stakeholders are entitled to be fairly treated by a company. A company is not perceived as a mechanism for generating profits for shareholders but as a medium which coordinates the interests of all groups. According to the ethical stakeholder theory, management should take into account all stakeholders' interests in equal measure, and where interests conflict, business is managed so as to attain optimal balance among them.

The managerial branch of the stakeholder theory implies that a company identifies groups of stakeholders with whom relationships must be properly managed in its own interest. These relations are not limited to the desire to obtain financial benefits. The more important the group of stakeholders is to a company, the more effort it puts to manage the relations with them [Ullman 1985]. In the managerial stakeholder theory a company is still responsible for responding to the needs of stakeholders, but it does not try to satisfy them in equal measure (this is also difficult from the practical point of view), giving priority to the groups that have the greatest influence. The impact of stakeholders on management is seen as dependent on the degree to which they control the resources needed by a company. The higher the importance of the resources owned by certain stakeholders for company's success, the sooner stakeholders' needs will be met. An organization is considered successful if it meets often contradictory expectations of various influential groups of stakeholders. An organization will survive if it is effective. Its effectiveness is shaped by the manner in which it manages the expectations of the interest groups which are vital to its functioning.

The importance of various stakeholder groups for company's operations changes over time. As a result, the greatest challenge that management has to face is constant adjustment of strategies and information policy to these changes. According to Evan and Freeman [1997, p. 82, as cited in Deegan, Unerman 2011, p. 354], the primary

objective of a company is to serve as a vehicle for coordinating stakeholders' interests. Owing to this, each stakeholders group achieves benefits through a voluntary exchange with others.

3. Stakeholders in insolvency proceedings

The importance of different groups of stakeholders for a business unit changes also at bankruptcy risk. The opening of insolvency proceedings causes a significant challenge posed to a debtor and a court representative (court supervisor, administrator or trustee). This challenge is an appropriate adaptation of strategy and information policy to changes caused by declaration of bankruptcy.

Bankruptcy is a social problem, therefore according to Wessels et al. [2009, p. 1] "There is a tremendous need for comprehensive insolvency law to achieve such goals as protection of consumers against the consequences of over indebtedness in today's credit society. (...) When insolvency law includes rules that foster discipline and honesty in financial management, it also protects creditors as such legislation increases their chances of at least a percentage of their claims will be paid."

Not only in Poland, but also in most countries, namely the United Kingdom, Germany, Japan and Sweden, traditional bankruptcy procedures are "creditor--friendly" and the key objective of bankruptcy proceedings is to protect creditors' interests [Smith, Strömberg 2004]. In Poland, the primary objective of insolvency proceeding is to satisfy the claims of creditors to the fullest extent possible, preferably in full. This means that in accordance with the idea of insolvency proceedings, the main group of stakeholders is creditors. At the same time, they are not the only group of stakeholders.

As a result of combining the stakeholder theory and insolvency proceedings rules, the following division of stakeholders can be made: based on the insolvency proceedings phase or based on the type of insolvency [Morawska, Roszkowska 2011, pp. 54–55].

In the initial proceedings on declaring bankruptcy stakeholders of an indebted company are:

a) internal stakeholders: managers, owners (shareholders) and employees;

b) external stakeholders: creditors, customers, suppliers, society, state, banks, the court conducting bankruptcy proceedings (see Figure 1).

The declaration of bankruptcy changes the approach of mapping stakeholders. The division into particular groups depends on the type of bankruptcy proceedings.

In the case of bankruptcy by liquidation of debtor's assets there are:

a) internal stakeholders: owners and trustee;

b) external stakeholders: creditors (among others: employees, suppliers, tax authorities, social insurance institutions), judge-commissioner, society, state (see Figure 2).

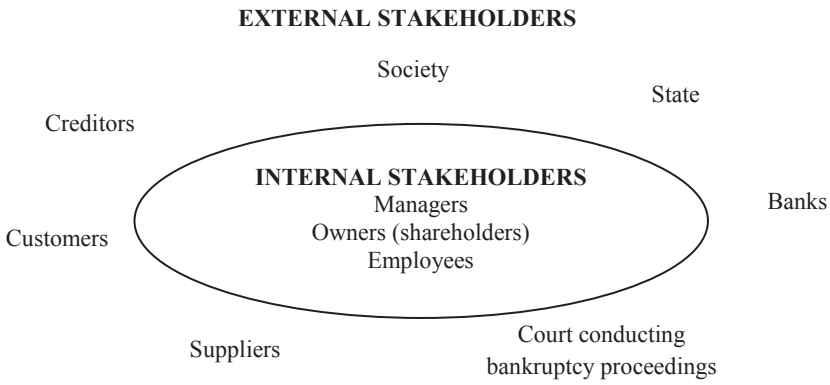

Figure 1. Stakeholders of an indebted company– initial proceedings on declaring bankruptcy

Source: own elaboration.

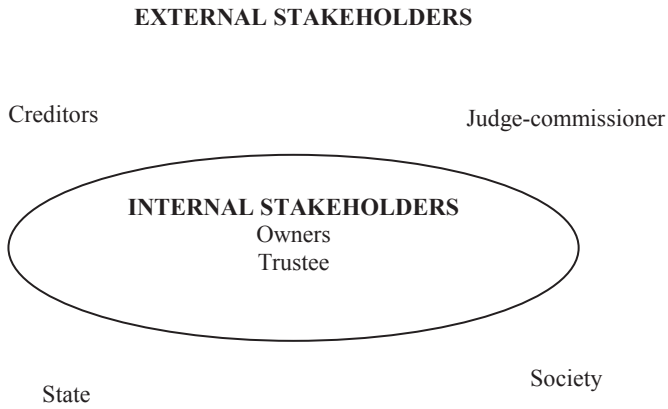

Figure 2. Stakeholders of an indebted company – bankruptcy by the liquidation of debtor's assets

Source: own elaboration.

In the case of the bankruptcy with a possibility to make an arrangement, a stakeholder is a person representing a bankrupt and court supervisor (or administrator) and:

a) internal stakeholders: employees, owners;

b) external stakeholders: judge-commissioner, creditors, customers, suppliers, society, state, banks (see Figure 3).

Under the colloquial theory of Banasiewicz [2011, pp. 79, 82] and regulations of *The Polish Bankruptcy and Reorganization Law* [Ustawa z 28 lutego 2003 r.], bankruptcy with the possibility to make an arrangement is the final phase of an

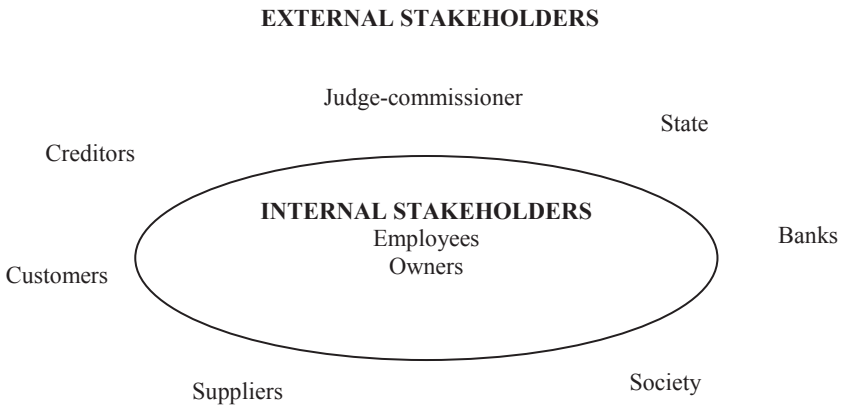

Figure 3. Stakeholders of an indebted company – bankruptcy with a possibility to make an arrangement

Source: own elaboration.

enterprise's life cycle. During this phase, organizations can become aware of the need for and undertake socially accountable actions to ensure survival of an enterprise on the market or even its development. Therefore, the division into groups of stakeholders at bankruptcy with the possibility to make an arrangement, is appropriate for the subject of the CSR conception in insolvency proceedings.

Individual stakeholders' goals will differ during ongoing insolvency proceedings. Creditors, who without a doubt are affected the most as a result of bankruptcy, strive to recover as much of their debt as possible (optimally the full amount) from a bankrupting enterprise. Owners strive to survive on the market, make a settlement with creditors and afterwards regain their position on the market. The court and its representatives focus on protecting the public interest [Bauer 2009, pp. 58–59]. However, the regulations of the bankruptcy law foresee benefits for those who manage a bankrupt enterprise in the form of remuneration based on profits [Ustawa z 28 lutego 2003 r., art. 163].

The existence of many groups of stakeholders, who often have conflicting objectives, can lead to conflicts during bankruptcy proceedings. Therefore, an effective execution of bankruptcy proceedings is an extremely difficult task. Court representatives play an important role in this execution [Prusak 2011, pp. 97–100].

In reference to the stakeholder theory, two directions of interest can be highlighted as part of the bankruptcy process, that is ethical and managerial.

The ethical direction gives creditors the right to be treated fairly. This means that, as result of bankruptcy proceedings, losses should be divided equally and creditors needs fairly fulfilled. The court and its representatives should see to it that all parties are treated fairly.

At the same time the bankruptcy law during the proceeding on declaring bankruptcy sets the petitioner as a party of the proceedings [Ustawa z 28 lutego

2003 r., art. 26]. Next, upon declaring bankruptcy, according to art. 342, the bankruptcy law divides creditors into five groups and sets the order in which their claims will be fulfilled. This approach follows the managerial direction of interest, where the law defines the claims of creditors and sets the hierarchy of importance and does not attempt to fulfill claims evenly.

The actions of a debtor and a representative of a bankrupt follow the managerial direction of interest. It is based on identifying groups of creditors – court representatives, main creditors, maintaining relations in such a way as to achieve maximum gains in the form of anticipated court decisions (e.g. type of declared bankruptcy) and settlements with creditors.

To sum up, the managerial direction of interest is dominant during bankruptcy proceedings. There is a set hierarchy of importance of creditors as well as economical incentives which in turn lead to the development of hierarchy by a debtor and a representative of a bankrupt.

4. CSR in practice of insolvency proceedings

Lack of publications in reference to the application of CSR in insolvency proceedings leads to the conclusion that this concept has not been adequately identified, which can also have an effect on the practical aspect of insolvency proceedings. However, the lack of reference to the concept of CSR in insolvency proceedings does not mean socially accountable actions are not undertaken in the case of bankruptcy and bankruptcy threat.

The theory that some entities are "too big to fail" or "too important to fail" can indicate which social presumptions can have an influence on bankruptcy decisions. Publications and scientific research lead to the conclusion that the problem of dealing with "too big to fail" pertains to insolvency of banks and other financial institutions [e.g. Goldstein, Véron 2011; Demirgüç-Kunt, Huizinga 2013; Nosek, Pietrzak 2009]. According to this doctrine, when a large bank encounters financial difficulties, steps are taken in order to save it. This is because the system of guarantee of deposit, in any country would not be able to survive the bankruptcy of its biggest bank. These steps are taken to protect people's savings [Iwanicz-Drozdowska 2007, p. 17].

Currently, references in literature to social effects of bankruptcy of entities other than financial institutions [e.g. Mączyńska (ed.) 2009] can indicate that the rule "too big to fail" can partially have an effect on insolvency proceedings of large enterprises. The basis for the court to rule in favor of insolvency with a possibility to make an arrangement is *prima facie* evidence that, as a result of this procedure, creditors' claims will be fulfilled to a greater extent than in the case of liquidation of debtor's assets. However, regardless of economic circumstances, creditors may decide to make an arrangement with an enterprise in debt. Agreement to restructure a large enterprise can positively affect future profits of owners but also save work positions. According to Verwijmeren and Derwall [2010, p. 956]: "Employees of

liquidating firms are likely to lose income and non-pecuniary benefits of working for the firm, which makes bankruptcy costly for employees." Therefore, an attempt to save work positions in an enterprise at risk of bankruptcy follows the CSR concept.

The research on information management of companies in insolvency proceedings in Poland demonstrates that the trial documentation does not include clearly specified references to the CSR concept. Trial documentation does not include any citations that continuation of business activities by an enterprise at risk of bankruptcy is a social benefit [Bauer 2009]. However, empirical research carried out between 2011 and 2012 shows that steps taken to restructure entities at risk of bankruptcy can be considered complaint with the CSR concept. In the study sample the dominant restructure concept in reference to social accountability was an attempt to increase the effectiveness of operations carried out to ensure survival of an enterprise. The purpose of these operations was to settle liabilities towards the creditors, protect work positions, maintain positive relationships with contractors and cooperation with the economic environment. An enterprise which undertook environment friendly actions, that is the installation of eco-friendly devices, has been identified in the study sample. The purpose of these actions was reduction of operating costs, but at the same time they brought positive effects to the environment [Bauer 2014].

To sum up, it is possible to identify actions to restructure enterprises in insolvency proceedings which, despite the lack of clear references to CSR, ought to bring benefits to various groups of stakeholders. Therefore, they can be considered as part of organization's social accountability.

5. Conclusion

Despite the large interest in the CSR concept and its continuous development, there is still no clarity in its definition or interpretation although the number of studies and publications on the issue by authors representing different disciplines is growing.

The concept of CSR in insolvency proceedings is virtually unrecognized in theoretical terms. However, the review of literature and the results of empirical research referred to in the paper prove that it is used in the insolvency proceedings practice. Such an approach is consistent with the idea of the institution of insolvency, which is based on the socially responsible distribution of losses between stakeholders of a bankrupt company or at risk of bankruptcy.

With respect to large entities in the insolvency proceedings, CSR manifests itself in well known "too big to fail" or "too important to fail" expressions. Regarding small and medium-sized enterprises, CSR can be seen in the European Union's "second chance" policy, which is a comprehensive system of support to counteract the negative effects of company liquidation. It refers to the entities at insolvency risk, pursuing a process of restructuring and entrepreneurs which experienced defeat

in business and want to start a business afresh. In Poland the European Union's approach will be implemented as a change in the bankruptcy law.

According to Mączyńska, studies related to the bankruptcy of companies are still insufficient. At the same time, inadequate identification of risks related to economic activities and ways to counteract them can lead to the spread of bankruptcies wave [Mączyńska 2008, pp. 12–15]. Thus, in the authors' opinion, further research concerning the current state and the possibility of wider use of the CSR concept in insolvency proceedings is justified.

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PRZESŁANKI SPOŁECZNEJ ODPOWIEDZIALNOŚCI BIZNESU W POSTĘPOWANIU UPADŁOŚCIOWYM

Streszczenie: Koncepcja społecznej odpowiedzialności biznesu jest często podejmowana w literaturze w kontekście jej pozytywnego wpływu na tworzenie wartości i rozwój przedsiębiorstw w długim okresie czasu. Jednakże może ona mieć także zastosowanie w odniesieniu do jednostek stojących w obliczu ryzyka upadłości. Postrzeganie upadłości jako problemu społecznego pozwoliło sformułować przedstawiony w pracy cel badań, którym jest wskazanie przesłanek koncepcji społecznej odpowiedzialności organizacji w postępowaniu upadłościowym. Analiza krajowej i zagranicznej literatury oraz aktów prawnych pozwoliła stwierdzić, że CSR jest stosowane w praktyce postępowania upadłościowego. Takie podejście jest zgodne z ideą instytucji upadłości, u której podstaw leżą działania na rzecz społecznie odpowiedzialnego rozłożenia strat pomiędzy interesariuszy przedsiębiorstwa, które zbankrutowało, lub znajduje się na skraju bankructwa. Praca stanowi przyczynek do ograniczonej literatury dotyczącej realizacji założeń odpowiedzialności społecznej przedsiębiorstw w postępowaniu upadłościowym. Omówiono w niej również teorię interesariuszy i podjęto próbę odniesienia jej do praktyki postępowania upadłościowego, a także wskazano kierunek zmian, które mogą mieć pozytywny wpływ na społecznie odpowiedzialne prowadzenie tego procesu.

Słowa kluczowe: społeczna odpowiedzialność organizacji, bankructwo, postępowanie upadłościowe, teoria interesariuszy.