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The Impacts of Social Activism and Corporate Social Responsibility on Food Fraud

A recent report finds that 86% of Americans expect for-profit companies to be active in addressing social and environmental issues (Porter Novelli/Cone 2019). In addition to benefiting society, engagement in prosocial behavior, known as corporate social responsibility (CSR), can improve a firm's competitiveness and economic performance. Engagement in proactive CSR can enhance a firm's relationship with the public by building its reputation of being a trustworthy, credible and responsible citizen. Studies have argued that the reputation firms develop through CSR activities can provide 'insurance-like' protection from future negative publicity and attacks on the firm (Godfrey et al. 2009; Gardberg and Fombrum 2006). However, firms engaging in CSR practices may choose to exploit public trust by engaging in fraudulent behavior, which often takes the form of making false or misleading claims about their product quality and/or production practices.

Food firms' engagement in CSR has been increasing in recent years, taking multiple forms ranging from reducing plastic waste to tackling youth unemployment. Interestingly, investment in CSR does not shield firms from scrutiny from activist organizations but could make them, instead, easier targets (King and McDonnell 2015). In the food sector, there are numerous examples of food firms with significant CSR investments that have been targeted by different activist organizations that accuse these firms of making false and misleading claims about their products and services. For instance, Nestlé has invested heavily in CSR activities, ranging from reducing plastic waste to educating pregnant women and young children on the importance of health and nutrition. In India, Nestlé supported the project Jagriti, collaborating with a local NGO named Mamta Health Institute of Mother and Child, with the primary objective of creating peer mentor groups that educate and counsel pregnant and lactating mothers on the importance of healthy nutrition, initiation of exclusive breastfeeding, and improved breastfeeding practices. At the same time, however, Nestlé is being accused by two activist organizations, the Changing Markets Foundation and the International Baby Food Action Network (IBFAN), for making false claims about its product being a close substitute for breastmilk and for breaking established standards set by the World Health Organization (WHO) and UNICEF.

The relationship between a food firm's investment in CSR and its decision to engage in fraudulent behavior, as well as the effect of CSR on the likelihood a firm will be targeted by activists whose objective is to increase market transparency, are not well understood. On one hand, a firm's CSR investment may make it harder for activist organizations to gain support from the public when they launch a campaign against the firm (e.g., a boycott) due to the goodwill the firm has created through its CSR activities. This can decrease the activists' incentive to monitor and target the firm and may increase the firm's incentive to engage in fraudulent behavior. On the other hand, the public expects more from socially responsible firms and, if an activist is able to expose fraudulent behavior, socially responsible firms could suffer greater reputational damage. This is especially true for food firms because the food sector is responsible for fulfilling basic human needs and food consumers are highly opinionated with respect to the activities of, and the products provided by, the food sector (Hartmann 2011). In this context, investment in CSR can invite more scrutiny by activists and can increase the activists' incentive to target the firm.

Research in the Department of Agricultural Economics at the University of Nebraska-Lincoln sheds light on the above issues by examining the relationship between a food firm's CSR investments, its product quality choices, and its decision to engage in fraudulent behavior in the presence of an activist whose goal is to uncover market fraud. Specifically, the research develops a sequential game-theoretic framework to examine how a firm's CSR investments affect its product quality choice, its incentive to misrepresent its true product quality and the incentive of an activist to challenge the claims made by the firm.

The model includes the following players:

- Two food firms – a CSR firm that provides a credence attribute[1] and a non-CSR firm that provides a basic good
- A continuum of heterogeneous consumers
- An activist

Consumers differ in their strength of preference for the credence attribute, and they revise their valuation of the firm's product when the firm is targeted by the activist (this accounts for the reputational harm faced by the targeted firm if the activist's campaign succeeds). The activist values market transparency and, even though monitoring and targeting the firm is costly, she experiences economic gains (e.g., donations) when she manages to uncover fraudulent behavior through an organized campaign.

The strategic interaction between the food companies and the activist is captured in a five-stage game. In the first stage, the firm that has invested in CSR chooses its product quality and, in the second stage, it chooses the claims it makes about the quality of its product given its beliefs of whether it will be monitored by the activist. In the third stage, after observing the firm's quality claims, the activist chooses whether to monitor the firm. If the activist chooses not to monitor the firm or if she monitors and does not find fraud, then the game ends with the firms choosing their respective prices and consumers choosing the product they will consume. If the activist monitors the firm and finds that it has misrepresented its product quality, the activist launches a campaign against the firm and a contest game is played between the activist and the firm. In this contest, the activist chooses the level of effort to exert to convince the public that the firm's claims are fraudulent, while the firm chooses the level of effort it will exert to contest the activist's claims. The outcome of the contest game is determined by a contest success function that, in addition to the effort levels exerted by the two players, also depends on the level of the firm's CSR investments. Finally, after the contest outcome has been realized, firms choose their respective prices and consumers choose the products they will consume.

Analytical results show that the relationship between the firm's CSR investment, the cost of providing the credence attribute and the degree of reputational harm the firm will suffer if the activist runs a successful campaign against the firm is critical in determining the firm's quality choice and the likelihood it will misrepresent its true quality. Moreover, the activist's decision to monitor the firm depends on the degree to which CSR influences the probability of success/failure of the campaign. Results also reveal that, when the cost of providing the credence attribute is high, the greater is the firm's CSR investment, the more likely it is that the activist will monitor the firm but the lower is the likelihood that the firm will misrepresent its quality, even though greater levels of CSR investment reduce the probability of success of the campaign against the firm. Carefully designed economic experiments can test the theoretical predictions of the model under different scenarios (no CSR versus high CSR investments) and sectors (food versus automobile) and are the focus of future research.

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[1] Credence attributes are attributes that are unobservable through search or experience (consumption and use) and are often related to a product's production process (e.g., 'raised without antibiotics', 'GMO free', 'gluten free', 'fair trade').

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