**Can Excellence in Corporate Social Performance Improve Investors’ Financial Assessments and Credibility of Managers’ Forecasts?\***

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**Abstract:**

In contrast to the extensive archival research on the relation between corporate social performance (CSP) and financial performance, behavioral studies are very scarce. We respond to a recent call for further experimental research on this issue by exploring to what extent excellence in CSP affects investors’ judgments of financial assessments (i.e., future profitability, liquidity and financial risk) and credibility of management’s forecasts. Following recent research suggesting that the CSP-financial performance link is U-shaped, we define excellence in CSP as the case of a firm simultaneously showing high and permanent social performance and being provided with professional assurance on social reporting. We design a 2x2x2 experiment by manipulating CSP (high vs. low), assurance (present vs. absent) and order of evidence, in which investors are asked to provide their judgments on the financial status of the firm. Our results indicate that CSP excellence has an impact on both investors’ financial assessments and their reliance on management forecasted information. Therefore, we find support for the argument that only the combination of superior and permanent CSP and reliable CSR disclosure pays off.

**Key words:** Corporate social responsibility; corporate social performance; assurance services; investors; forecasts

**INTRODUCTION**

The link between corporate social performance (CSP) and corporate financial performance has been intensely examined by the strategic, marketing, and related business ethics fields. Different theories suggest that corporate social responsibility (CSR)[[1]](#footnote-1) activities can contribute to improve the relationship of the company with stakeholders, influencing financial performance positively (Freeman 1984; Ruf et al. 2001; McWilliams and Siegel 2001; McWilliams et al. 2006; Orlitzky et al. 2003; Orlitzky and Benjamin 2001; Blanco et al. 2012).[[2]](#footnote-2) However, in spite of the massive archival research on the topic, results on the relationship between CSP and financial performance are far from being consistent (Orlitzky 2008; Hull and Rothenberg 2008; Peloza 2006, 2009). While there appears to be empirical support for the view that CSP is positively related to financial performance, a large number of studies find mixed and even negative evidence on this link.[[3]](#footnote-3) Therefore, results from archival research seem to suggest that CSP can add value to the firm but only under certain conditions (Servaes and Tamayo 2012; Barnett and Salomon 2006, 2012).

In comparison with the aforementioned extensive archival research, behavioral studies on the CSP-financial performance link are very scarce. Indeed, a top accounting journal has recently emphasized the need of further behavioral research in order to answer unresolved CSR questions and complement archival research findings (Moser and Martin 2012). In this regard, it is argued that behavioral research can help improve our understanding of the motivations for, and consequences of, CSR activities. The few existing behavioral papers on the topic seem to suggest that (1) investing in CSR activities has a positive impact on financial statement users’ judgments and decisions (Guiral 2012; Elliott et al. 2012) and (2) professional assurance on CSR disclosure is also interpreted as having positive information content, especially, when a firm’s CSP is high (Coram et al. 2009; Brown-Liburd et al. 2012).

We extend the existing literature in two ways. First, considering that previous research on the CSP-financial performance relationship has mainly focused on the role played by temporary CSP, we take advantage of the behavioral approach to analyze to what extent investors assess social involvement. Following recent works of Barnett and Salomon (2012, 2006), we assume that the CSP-financial performance link is U-shaped. This argument implies that the effort to become a good corporate citizen pays off only when the firm combines a permanent and remarkable CSP with a trustworthy CSR disclosure. Otherwise, the pursuit of social betterment entails financial detriment. Therefore, the CSR effort should be considered as a long-term investment of which outcome is subject to a permanent learning process. To this end, we come up with the term “excellence in CSP” to test whether only those firms simultaneously showing permanent and high CSP and being provided with CSR assurance by a professional accountant have the ability to profit from social responsibility. Second, we extend previous archival findings by suggesting that firms that exhibit CSP excellence tends to behave in a more responsible manner by delivering transparent and reliable financial information. In this regard, we examine how CSP excellence affects investors’ reliance on the forecasted information elaborated by managers.

We design a 2×2×2 controlled experiment using one hundred twenty-two students from a top-100 M.B.A. program as reasonable proxies for non-professional investors. CSP (high vs. low) and professional CSR assurance (provided vs. not provided) are our main manipulations. We also manipulate order of the evidence to test for any potential order effect in our results. After receiving the case materials participants are asked to provide their financial assessments on the firm’s ability to increase future profitability and liquidity and its ability to reduce future financial risk. They also provide their assessment on the accuracy of management forecasted financial information.

Results show that CSP excellence has an impact on both investors’ financial assessments and their reliance on forecasted information. These findings suggest that just disclosing CSR and having this information assured by a professional accountant does not guarantee a positive impact on investors’ assessments and their credibility of forecasted information. Rather, we find support for the argument that only the combination of superior and permanent CSP and reliable CSR disclosure pays off. Our findings have important implications for managers and financial statement users. We show that excellence in CSR might provide managers with a powerful competitive advantage difficult to be imitated by competitors which would lead to an increase in their financial performance. Otherwise, investing in CSR activities might be interpreted by stakeholders as an unnecessary waste of financial resources.

We organize the remainder of the paper as follows. The following section briefly reviews the prior literature. The third section develops our hypotheses based on a framework describing CSP-financial performance link. The fourth section discusses the research design. We present our results in the fifth section and the sixth section concludes.

**LITERATURE REVIEW**

For more than three decades the CSP-financial performance link has been extensively examined by archival research. While several reviews (McWilliams et al. 2006; Margolis and Walsh 2003; Roman et al. 1999; Griffin and Mahon 1997; Pava and Krausz 1995; Wood and Jones 1995; Ullmann 1985), meta-analysis (Orlitzky et al. 2003) and special issues in top management journals generally tend to suggest that CSR efforts improve a firm’s financial performance, results are still mixed (Orlitzky 2008).[[4]](#footnote-4)

Moser and Martin (2012) have recently invited accounting researchers to explore through controlled experiments CSR issues that are difficult to address effectively in archival studies. Obviously, archival research has certain limitations to examine the impact that CSP and CSR assurance may have on the judgments and decisions of particularly relevant financial statements’ users, such as loan officers, financial analysts, auditors, managers and investors.

Some behavioral research has examined the CSR-financial performance link. Guiral (2012) finds evidence supporting that CSR investment is interpreted by loan officers as an indicator of superior corporate financial performance of the potential borrower. Martin (2009) provides evidence that some managers and investors are willing to accept lower payouts in exchange for the societal benefits of going green. Elliott et al. (2012) run a 2 (prompted to assess CSP vs. without being prompted to assess CSP) x 2 (positive CSP vs. negative CSP) experimental design. These authors find that for investors who are exposed to, but do not explicitly assess CSP, better CSP increases their estimates of fundamental value.[[5]](#footnote-5) Other behavioral studies also explore the role play by CSR assurance on investors’ and other financial statements users’ decisions. Pflugrath et al. (2011), by manipulating both the degree of CSR assurance (non-assured vs. assured by an auditor vs. assured by a consultant) and industry (mining industry vs. retail industry) in an experimental design, find that investors’ credibility of a CSR report is greater when it is assured and when the assurer is a professional accountant.[[6]](#footnote-6) Coram et al. (2009) design a 2×2 experiment with CPAs by manipulating the sign of non-financial information (positive vs. negative) and the provision of assurance for the disclosed non-financial information (assured vs. non-assured). They find a significant effect of non-financial information on stock price estimates. According to attribution theory, the provision of assurance also affects stock price estimates but only when non-financial information is positive.[[7]](#footnote-7) Brown-Liburd et al. (2012) employ a 2×2 experimental design in which both the degree of investment in CSR activities (high vs. low) and the provision of professional CSR assurance (assured vs. non-assured) are manipulated. Results are similar to those of Coram et al. (2009) since higher CSR investments influence investors’ stock price assessments revisions and CSR assurance only has a positive impact when the disclosed CSR information is positive. Dilla et al. (2012) conduct a 2×2 experimental design by manipulating environmental performance (high vs. high) and assurance on environmental information (assured vs. non-assured). These authors find that neither environmental performance nor assurance has a significant main effect on investors’ judgments who consider environmental performance information to be less important than the financial one. Further, CSR assurance does not influence investment amount when environmental performance is low, but it has a negative influence on investment amount when environmental performance is high.[[8]](#footnote-8)

Therefore, results from the existing behavioral research suggest that investing in CSR activities has a positive impact on financial statements users’ judgments and decisions and that professional assurance on CSR disclosure, with the exception of Dilla et al.’s (2012) results, is also interpreted as having positive information content, especially, when a firm’s CSP is high.

Even though these behavioral results provide a better understanding of the causes and consequences of performing CSR activities, we believe the CSR-CSP link deserves further exploration through controlled experiments. In this paper, we rely on Barnett and Salomon (2012, 2006) who offer a novel approach to interpret the lack of consistence shown on previous archival literature. These authors provide theory and empirical evidence supporting the idea that the CSR-financial performance relationship is U-shaped.Accordingly, our study differs from previous research in that we investigate whether the achievement of permanent, remarkable and trustworthy CSR efforts is the most important reason by which we can expect a positive impact of CSR activities on financial performance.

**RESEARCH QUESTIONS**

Barnett and Salomon (2012) find that achieving CSP excellence is subject to a certain learning process, i.e., firms searching for benefits from CSR activities might have to endure a period of decreased financial performance. This learning process relies on sacrificing performance on the short term in an effort to improve financial performance in the long term after building successfully relations with stakeholders.[[9]](#footnote-9) Proactive and sustainable CSR that supports firm reputation, longevity in profitability and economic growth goes beyond short-term profit maximizing issues and emphasizes long-term performance (Torugsa et al., 2012). Considering that sustainable CSR requires a significant resource allocation for a long period of time, the return on that investment should be expected in the long-term rather than in the short-term financial performance (Eisenhardt and Martin 2000; Barnett and Salomon, 2012). This argument suggests that firms should invest in proactive CSR activities continuously, not temporarily, in order to achieve long-term financial performance and accounting transparency. Further, both the archival and behavioral literature suggests that investors trust CSR disclosure when it is assured and when the assurer is a professional accountant (Pflugrath et al., 2011; Dhaliwal et al. 2012)[[10]](#footnote-10)

According to Barnett and Salomon (2006, 2012), we posit that the achievement of permanent, remarkable and trustworthy CSR efforts is the most important reason by which we can expect a positive impact of CSR activities on financial performance.[[11]](#footnote-11)This argument is consistent with the view that investors are sensitive to the scrupulous public scrutiny of the firms’ CSR merits made by independent parties, such as KLD Research and Analytics, Fortune MAC, or the Corporate Responsibility Magazine (Barnett and Salomon 2006).[[12]](#footnote-12) Therefore, we argue that just investing in good corporate citizenship and disclosing CSR activities for the concurrent period might not be a guarantee of superior financial performance. Some previous research suggests that both the adoption of CSR and the development of ethical \*\*\* can be perceived by stakeholders as a window-dressing rather than a moral imperative when firms pertain to the pursuit of self-interest in an attempt to cover up the impact of some corporate misconduct (Hemingway and Maclagan 2004; Peloza 2006; Stevens 1994; Prior et al. 2008; Davidson and Stevens 2012). However, when the firm shows a permanent, remarkable and trustworthy social involvement, investors can perceive CSP as a proxy for sustainable financial performance. This argument leads us to our first research question:

**RQ1:** To what extent are investors’ financial assessments affected by a firm’s excellence in CSP (i.e., a firm simultaneously showing permanent and high CSP and being provided with CSR assurance by a professional accountant)?

In this paper we also attempt to extend the CSR literature by examining investors’ credibility of managers’ forecasts. In contrast to historical financial information, forecasted financial information is not subject to the restrictions of accounting standards, and managers can use such voluntary disclosure to communicate their private information to investors and deliver more transparent and reliable information (Zhang 2012). But forecasted information can be also viewed as an opportunity for those unethical managers pursuing their self-interest to reach certain goals or even distort the financial reality of a firm (Hilary and Su 2011).[[13]](#footnote-13) However, one of the goals of pursuing social responsible activities is to achieve legitimacy, which is gained when stakeholders support the company’s goals and activities (Blanco et al. 2012). In this context, credibility is an essential factor that plays a critical role for companies pursuing legitimacy (Leary and Kowalski, 1990). Managers of remarkably good corporate citizens may have fewer incentives to engage in earnings manipulations (Kim et al. 2012) which, in turn, may help them achieve legitimacy and deliver transparent and reliable historical and forecasted financial information to investors. Therefore, we investigate whether investors are more willing to rely on forecasted financial information when the firm shows CSP excellence as compared with other firms that do not meet this high standard of social criteria. This argument leads us to our second research question:

**RQ2:** To what extent is investors’ reliance on forecasted financial information affected by a firm’s excellence in CSP (i.e., a firm simultaneously showing permanent and high CSP and being provided with CSR assurance by a professional accountant)?

**EXPERIMENT**

**Design and Participants**

The experiment employs a 2×2×2 between-participants design. As depicted in Figure 1, the two main manipulated factors were CSP (high vs. low) and CSR assurance (provided vs. not provided). We employ CSP and CSR assurance as our main independent variables. We also manipulate order of the evidence to test for any potential order effect in our results.[[14]](#footnote-14)

(Insert Figure 1 about here)

According to Elliot et al. (2007), we recruit M.B.A. students as reasonable proxies for non-professional investors in tasks that are relatively low in integrative complexity, such as the evaluation of CSR information. One hundred and twenty-two students from a top-100 M.B.A. program serve as participants.[[15]](#footnote-15) Participation in the study was voluntary. Students are randomly assigned to the experimental treatments. Participants averaged 8 years of work experience and were an average of 33 years old. Seventy-four percent are male (91 of 122). Around 67 percent (81 of 122) of the participants hold senior positions (e.g., Managing Director, Director, CEO/President) within their organizations, and just above one-third (41 of 122) hold junior positions.[[16]](#footnote-16)

**Task and Procedures**

The experimental design and number of participants in each treatment are summarized in Table 1. The experiment was conducted during the participants’ class periods, and took approximately twenty-five minutes. The case materials were built from a real financially healthy firm in the high-technology industry. First, we ask participants to provide some demographic information. The cases also include descriptive information about both the high-technology industry and the company, two years of audited consolidated financial information and another two years of unaudited forecasted financial information (i.e., Balance Sheet, Income Statements and Cash Flow Statements). After the aforementioned financial information, participants are provided with two types of CSR information. One type of CSR information is related to the firm’s CSP achievements in the last four fiscal years. Similar to Guiral (2012), subjects are told in the research instrument that a third independent party, i.e., KLD Research and Analytics, had evaluated the firm’s CSP according to five different social indicators, namely employee and customer satisfaction, corporate governance strength, community relation, and environmental commitment. While participants assigned to Groups 1 and 2 receive permanent high CSP scores during the last four years, those assigned to Groups 3 and 4 are provided with poor CSP scores. After this, participants answer a manipulation-check question about the company’s effort to become a good corporate citizen. The second type of CSR information refers to whether or not the firm had been received CSR assurance by a professional accountant. While Groups 1 and 3 receive CSR assurance, Groups 2 and 4 do not. Then, participants answer another manipulation-check question about the firm’s CSR reporting credibility after receiving the CSP assurance information.

To conclude, participants are asked to provide their financial assessments on the firm’s ability to generate future profitability and liquidity, and its ability to reduce future financial risk on 1-to-11-point scales anchored ‘‘Very Low’’ and ‘‘Very High’’. Finally, they are also asked to provide their reliance on the unaudited forecasted information on 1-to-11-point scales anchored ‘‘Very Low’’ and ‘‘Very High’’. We employ these four financial assessments as our dependent variables.

**RESULTS**

**Manipulation Checks**

We first investigated whether the experimental manipulations of CSP and CSR assurance are successful. After receiving the information about CSP, participants are asked to provide an assessment about the company’s effort to become a good corporate citizen. Subjects respond on an eleven-point scale, anchored by 1 (= very low) and 11 (= very high). While not reported for brevity, the mean response of participants in the high CSP condition is 6.31, and the mean response of those in the low CSP condition is 4.44. The difference is statistically significant (t= 3.98, p = .00). Further, participants are also asked to provide an assessment on the company’s CSR reporting credibility after receiving the information about CSP assurance. While subjects in the assured CSR scenario report a mean response of 6.71, the mean response of participants in the non-assured CSR condition is 5.81. The difference is also statistically significant (t= 2.36, p = .02). Overall, participants’ responses suggest that our experimental manipulations are effective.

**Descriptive Statistics**

Table 1, Panels A and B, present the descriptive statistics, by experimental condition (i.e., cells U22, U21, U12 and U11,), for participants’ responses regarding their assessments on the firm’s ability to improve its future profitability, future liquidity, and its ability to reduce future financial risk. Further, subjects are also asked to provide their assessment on the accuracy of forecasted financial information. Overall, the pattern of means suggests that participants predict higher future profitability, higher future liquidity, lower financial risk and rely more on forecasted financial information when the firm achieves excellence in CSP, i.e., when the firm shows high CSP and its CSR report has been assured by a professional accounting firm (U22).

Further, results tend to indicate that participants view high CSP as providing superior information content in comparison with low CSP. Mean responses for the high CSP and assured CSR condition (U22) are higher than those in the low CSP and assured CSR condition (U12). Similarly, participants’ mean responses are also higher for the high CSP and non-assured CSR scenario (U21) than those for the low CSP and non-assured CSR scenario (U11). However, the pattern of means does not clearly suggest whether participants view assured CSR as providing superior information content in comparison with non-assured CSR, especially for the low CSP condition (see Figures 2 and 3). While participants’ responses regarding financial risk and accuracy of forecasted information assessments in the low CSP and assured CSR condition (U12) are higher than those in the low CSP but non-assured CSR condition (U11), profitability and liquidity assessments in the low CSP and assured CSR condition are slightly lower than those in the low CSP but non-assured CSR condition.

(Insert Table 1 about here)

(Insert Figures 2 and 3 about here)

Table 2 displays mean differences by main manipulated variables (CSP and CSR Assurance). Results in Panels A and B of Table 2 suggest that means for profitability, financial risk and reliance on forecasted information in the high CSP scenarios are significantly higher than those in the poor CSP conditions (i.e., U22+U21 vs. U12+U11). The mean for the liquidity assessment in the High CSP condition is slightly higher than in the low CSP condition but not statistically significant. The results report in Table 2 also suggest that means in the assured CSR conditions are higher but not statistically significant than those in the non-assured CSR conditions (i.e., U22+U21 vs. U12+U11).

(Insert Table 2 about here)

**Multivariate Analysis**

We perform a set of MANCOVAs using *CSP*, *CSR Assurance*, and *Order* as independent variables, and *Experience* and *Position* as covariates. Table 3, Panel A reports the results of MANCOVAs for the participants’ assessments on the firm’s ability to improve its future profitability and liquidity. Results show a main significant effect of *CSP* on investors’ assessments of the firm’s future profitability (F = 2.63, p= .10) and liquidity (F = 2.87, p= .09; two-tailed). Main effects for *CSR* *assurance* (p= .54 and p= .39, respectively) and *Order* (p= .12 and p= .16, respectively) are not significant. None of the *CSP× CSR Assurance*, *CSP× Order*, *CSR Assurance× Order* interaction effects are significant for either profitability (p = .35, p= .31, and p = .23, respectively) or liquidity assessments (p = .17, p= .33, and p = .13, respectively). Further, the triple interaction effect, *CSP×* *CSR* *assurance×* *Order*, is not significant either for profitability (p = .74) or firm’s liquidity (p = .64).[[17]](#footnote-17)

Panel B of Table 3 presents the results of MANCOVAs for the investors’ assessments on the firm’s ability to reduce its future financial risk and their reliance on forecasted financial information. Results reveal a main significant effect of *CSP* on subjects’ assessments of financial risk (F = 3.25, p = .07) and accuracy of forecasted information (F = 3.63, p= 0.05). Similar to the profitability and liquidity assessments, we do not find main effects either for *CSR* *assurance* (p= .33 and p= .28, respectively) or for *Order* (p= .60 and p= .25, respectively). However, Panel B of Table 3 reports a significant interaction effect, *CSR* *assurance×Order*, on the assessments of accuracy of forecasted information (F = 4.01, p = .04).[[18]](#footnote-18).[[19]](#footnote-19) (Insert Table 3 about here)

**Pairwise comparisons**

To explore our research questions in more depth we test to what extent excellence in CSP (i.e., both high CSP and CSR assurance by a professional accountant) affects investors’ financial assessments. To this end, we conduct a planned contrast by comparing the CSP excellence condition to the other grouped conditions (i.e., U22 vs. grouped U21, U12, and U11, see Table 4). Planned contrast comparisons indicate that participants’ assessments in the CSP excellence scenario are more favorable in terms of profitability (t = 2.26, p= .02), liquidity (t = 2.41, p= .01) and reliance on forecasted information (t = 2.02, p= .04).[[20]](#footnote-20)

Taken together, the evidence from our experimentation seems to suggest that CSR assurance, rather than being interpreted as a solely source of information, is viewed as a first order mechanism for the interpretation of the CSP excellence which, in turns, has a positive impact on investors’ assessments and their reliance on managers’ forecasts when CSR reporting has been assured by a professional accountant. Otherwise, CSR assurance does not provide additional information content per se on investors’ judgments.

(Insert Table 4 about here)

**Further Analysis**

Previous literature points out that order effects may arise when individuals engage in sequential information processing (Hogarth and Einhorn, 1992; Nelson and Tan, 2005). A key prediction is that recency effects occur for short series of complex, mixed evidence. In this regard, individuals may overweight evidence received at the end of a sequence. Previous research in auditing has generally observed a recency effect (Frank et al., 2012; Nelson and Tan, 2005; Trotman and Wright, 1996). However, no order effects are found in series of consistent evidence, either all positive or all negative (Tubbs et al., 1990: Guiral-Contreras et al., 2007).

In our experimental design potential series of mixed evidence are illustrated by cells U21 (high CSP and non-assured CSR) and U12 (low CSP and assured CSR) (see Table 1 and Figure 1). To check for recency effects we run non-parametric pairwise comparisons controlling for order of evidence. Untabulated results of Mann-Whitney U and Kruskal-Wallis tests do not provide support for the presence of recency effects. This evidence seems to suggest that CSR assurance might have been interpreted by participants as a neutral piece of evidence. Additional Mann-Whitney U and Kruskal-Wallis tests (untabulated) also discard the presence of order effects in series of consistent positive evidence (i.e., cell U22, high CSP and assured CSR) and consistent negative evidence (i.e., cell U11, low CSP and non-assured CSR).

**CONCLUSION, LIMITATIONS AND FUTURE RESEARCH**

CSR is an issue of growing interest among the research community and practitioners. Indeed, the reporting of socially responsible activity is becoming more prevalent as investors, customers, employees, and other stakeholders demand greater transparency about non-financial aspects of business (Kim et al. 2012). Despite the remarkable volume of archival research on the CSP-financial performance link, results are not consistent. In addition, behavioral research on this issue is scarce.

Recently, Barnett and Salomon (2012, 2006) provide theory and empirical evidence suggesting that this lack of consistency is due to a linear assumption on the CSP-financial performance relationship. Instead, these authors posit that this association is U-shaped. Therefore, CSP should be considered as a long-term investment which outcome is subject to a permanent learning process. In this paper we follow Barnett and Salomon’s view and come up with the term “excellence in CSP” in an attempt to investigate in a controlled experiment the impact that the combination of robust and permanent CSP and CSR assurance may have on investors’ financial assessments and their reliance on managers’ forecasts. Our findings indicate that CSP excellence does have a positive influence on investors’ financial assessments and also improves the credibility of managers’ forecasts.

The results from our experimentation should be of interest for both academics and managers. From the academic perspective, this study fills a gap in the literature. There is a lack of research investigating the effect of sustainable CSR on financial performance. The study also has a clear implication for managers. Given the results, managers pursuing to transform social efforts into benefits should maintain a robust, permanent and transparent CSR commitment. Excellence in CSR might provide managers with a powerful competitive advantage difficult to imitate by competitors and which will lead to an increase in their financial performance and, in particular, will positively affect market reaction (Barney, 1991). Otherwise, investing in CSR activities might be interpreted by stakeholders as a unnecessary waste of financial resources.

This paper is subject to some limitations. First, we explore the impact of CSR excellence on investors’ judgments but not on their decisions. Future research could cover this issue. Second, we do not control for investors’ indirect exposition to CSP assessment. Indeed, we explicitly ask all participants to provide an evaluation of CSP and CSR assurance through our manipulation-check questions. Our findings are contrary to those of Elliot et al. (2012) since we find that the impact of CSR excellence remains significant even when investors are explicitly exposed to assess CSP performance. Third, the results should be interpreted with some degree of caution since we focus our experimentation on the case of a financially healthy technological company. Future research can be expanded by analyzing whether the results are consistent in different industries.

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**Figure 1**

**CSP Excellence (High CSP and CSR Assurance)a**



a Cells are coded in the form Uik the subscript i and j denote CSP (high vs. low CSP) and CSR Assurance (Assured vs. non-assured CSR) conditions, respectively. Cell U22 represents excellence in CSP, i.e., a firm with a high level of CSP and CSR assurance by a professional accountant.

**Figure 2**

**Effects of the Interaction of CSP and CSR Assurance on Profitability and**

**Liquidity Assessments**

 **Figure 3**

**Effects of the Interaction of CSP and CSR Assurance on Financial Risk**

**Assessment and Reliance on Forecasted Information**



**Table 1\***

**Investors’ Financial Assessments by Experimental Groups Panel A: Assessments on Profitability and Liquidity by Experimental Groups (Mean and Standard Deviation)**

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Groups**  **N=122** | **Order** | **Manipulations** | **Cella** | **Profitability** | | **Liquidity** | |
| **Mean** | **S.D.** | **Mean** | **S.D.** |
| 1 (n=33) | O1=18; O2=15 | High CSP + Assured CSR | U22 | 7.15 | 1.33 | 6.94 | 1.52 |
| 2 (n=30) | O1=16; O2=14 | High CSP + Non-assured CSR | U21 | 6.67 | 2.06 | 6.23 | 1.98 |
| 3 (n=30) | O1=17; O2=13 | Low CSP + Assured CSR | U12 | 6.33 | 1.97 | 6.00 | 1.64 |
| 4 (n=29) | O1=14; O2=15 | Low CSP + Non-assured CSR | U11 | 6.38 | 1.86 | 6.21 | 1.88 |
| **Total** | | | | **6.65** | **1.82** | **6.36** | **1.77** |

**Panel B: Assessments on Financial Risk and Forecasted Information by Experimental Groups**

**(Mean and Standard Deviation)**

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Groups**  **N=122** | **Order** | **Manipulations** | **Cella** | **Financial Risk** | | **Accurate Forecasted Information** | |
| **Mean** | **S.D.** | **Mean** | **S.D.** |
| 1 (n=33) | O1=18; O2=15 | High CSP + Assured CSR | U22 | 5.97 | 1.74 | 6.40 | 1.93 |
| 2 (n=30) | O1=16; O2=14 | High CSP + Non-assured CSR | U21 | 5.80 | 2.05 | 5.89 | 1.68 |
| 3 (n=30) | O1=17; O2=13 | Low CSP + Assured CSR | U12 | 5.57 | 1.65 | 5.60 | 1.58 |
| 4 (n=29) | O1=14; O2=15 | Low CSP + Non-assured CSR | U11 | 5.10 | 1.86 | 5.44 | 1.99 |
| **Total** | | | | **5.62** | **1.83** | **2.56** | **1.82** |

a Cells are coded in the form Uik the subscript i and j denote CSP (high vs. low CSP) and CSR Assurance (Assured vs. non-assured CSR) conditions, respectively. Order (O) = 1, if participants receive first CSP information and then CSR assurance information, 2 if participants receive first CSR assurance information and then CSP information; Profitability = Ability of the company to generate future profits (on a 1-to-11-point scale); Liquidity = Ability of the company to generate future cash flows from its operating activities (on a 1-to-11-point scale); Financial Risk = Ability of the company to reduce its future financial risk (on a 1-to-11-point scale 1); Accurate Forecasted Information = Likelihood that forecasted financial information is accurate (on a 1-to-11-point scale 1). a Two tailed p-value.

**Table 2\***

**Investors’ Financial Assessments by Manipulated Variables**

**Panel A: Assessments on Profitability and Liquidity by Manipulated Variables**

**(Mean, Standard Deviation and Mean Difference)**

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Groups**  **N=160** | **Cella** | **Manipulations** | **Profitability** | | | | **Liquidity** | | | |
| **Mean** | **S.D.** | **Mean**  **Difference** | **t-test** | **Mean** | **S.D.** | **Mean**  **Difference** | **t-test** |
| 1 and 2 (n=63) | U22+U21 | High CSP | 6.92 | 1.71 | .56 | 1.72\* | 6.60 | 1.77 | .50 | 1.57 |
| 3 and 4 (n=59) | U12+U11 | Low CSP | 6.36 | 1.91 | 6.10 | 1.75 |
| 1 and 3 (n=63) | U22+U12 | Assured CSR | 6.76 | 1.70 | .48 | .51 | 6.49 | 1.63 | .40 | .71 |
| 2 and 4 (n=59) | U21+U11 | Non-assured CSR | 6.52 | 1.95 | 6.22 | 1.91 |

**Panel B: Assessments on Accurate Forecasted Information and Financial Risk by Manipulated Variables**

**(Mean, Standard Deviation and Mean Difference)**

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Groups**  **N=160** | **Cella** | **Manipulations** | **Financial Risk** | | | | **Accurate Forecasted Information** | | | |
| **Mean** | **S.D.** | **Mean**  **Difference** | **t-test** | **Mean** | **S.D.** | **Mean**  **Difference** | **t-test** |
| 1 and 2 (n=63) | U22+U21 | High CSP | 5.89 | 1.88 | .55 | 1.67\* | 6.16 | 1.82 | .66 | 1.94\*\* |
| 3 and 4 (n=59) | U12+U11 | Low CSP | 5.34 | 1.76 | 5.50 | 1.78 |
| 1 and 3 (n=63) | U22+U12 | Assured CSR | 5.78 | 1.63 | .33 | .34 | 6.02 | 1.81 | .31 | 1.04 |
| 2 and 4 (n=59) | U21+U11 | Non-assured CSR | 5.45 | 1.96 | 5.68 | 1.84 |

a Cells are coded in the form Uik the subscript i and j denote CSP (high vs. low CSP) and CSR Assurance (Assured vs. non-assured CSR) conditions, respectively.

\*, \*\*, \*\*\*, significant at the 10, 5 and 1 percent level, respectively (two-tailed). Profitability = Ability of the company to generate future profits (on a 1-to-11-point scale); Liquidity = Ability of the company to generate future cash flows from its operating activities (on a 1-to-11-point scale); Financial Risk = Ability of the company to reduce its future financial risk (on a 1-to-11-point scale 1); Accurate Forecasted Information = Likelihood that forecasted financial information is accurate (on a 1-to-11-point scale 1). a Two tailed p-value.

**Table 3\***

**MANCOVA Analyses**

**Panel A: Three-way MANCOVAs with Accurate Forecasted Information and Profitability as the Dependent Variables, Experience and Position as Covariates and CSP, CSR Assurance and Order as the Independent Variables**

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Source of Variation** | **Profitability** | | | | | **Liquidity** | | | | |
| **Sum of**  **Squares** | **d.f.** | **Mean**  **Square** | **F-statistic** | **p-value** | **Sum of**  **Squares** | **d.f.** | **Mean**  **Square** | **F-statistic** | **p-valuea** |
| Covariate |  |  |  |  |  |  |  |  |  |  |
| *Experience* | .06 | 1 | .06 | .02 | .88 | 3.54 | 1 | 3.54 | 1.23 | .27 |
| *Position* | .40 | 1 | .40 | .12 | .77 | 7.60 | 1 | 7.60 | 2.63 | .10 |
| Main Effects |  |  |  |  |  |  |  |  |  |  |
| *CSP* | 8.76 | 1 | 8.76 | 2.63 | .10 | 8.29 | 1 | 8.29 | 2.87 | .09 |
| *CSR Assurance* | 1.25 | 1 | 1.25 | .37 | .54 | 2.07 | 1 | 2.07 | .72 | .39 |
| *Order* | 7.98 | 1 | 7.98 | 2.40 | .12 | 5.64 | 1 | 5.64 | 1.95 | .16 |
| Interaction Effect |  |  |  |  |  |  |  |  |  |  |
| *CSP x CSR Assurance* | 2.87 | 1 | 2.87 | .86 | .35 | 6.13 | 1 | 6.13 | 2.11 | .17 |
| *CSP x Order* | 3.40 | 1 | 3.40 | 1.02 | .31 | 2.65 | 1 | 2.65 | .92 | .33 |
| *CSR Assurance x Order* | 4.78 | 1 | 4.78 | 1.44 | .23 | 8.27 | 1 | 8.27 | 2.55 | .13 |
| *CSP x CSR Assurance x Order* | .35 | 1 | .35 | .10 | .74 | .60 | 1 | .60 | .20 | .64 |
| Residual Error | 372.45 | 112 | 3.32 |  |  | 322.99 | 112 | 2.88 |  |  |

\* CSP = 1 when firms shows high CSP and 0 when low CSP; CSR Assurance = 1 when the CSR reporting is assured and 0 when non-CSR assurance; Order = 1, if participants receive first CSP information and then CSR assurance information, 2 if participants receive first CSR assurance information and then CSP information; Profitability = Ability of the company to generate future profits (on a 1-to-11-point scale); Liquidity = Ability of the company to generate future cash flows from its operating activities (on a 1-to-11-point scale); Experience = Number of years of working experience; Experience = Number of years of working experience; Position = Position in the firm: Junior, Senior, Manager, Partner/CEO (from 1 to 4, respectively, from lower to higher positions).

a Two tailed p-value.

**Table 3 (continued)**

**Panel B: Three-way MANCOVAs with Liquidity and Financial Risk as the Dependent Variables, Experience and Position as Covariates and CSP, CSR Assurance and Order as the Independent Variables**

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Source of Variation** | **Financial Risk** | | | | | **Accurate Forecasted Information** | | | | |
| **Sum of**  **Squares** | **d.f.** | **Mean**  **Square** | **F-statistic** | **p-value** | **Sum of**  **Squares** | **d.f.** | **Mean**  **Square** | **F-statistic** | **p-valuea** |
| Covariate |  |  |  |  |  |  |  |  |  |  |
| *Experience* | .05 | 1 | .05 | .01 | .90 | 1.01 | 1 | 1.01 | .31 | .57 |
| *Position* | 11.92 | 1 | 11.92 | 3.59 | .06 | 1.86 | 1 | 1.86 | .57 | .44 |
| Main Effects |  |  |  |  |  |  |  |  |  |  |
| *CSP* | 10.76 | 1 | 10.76 | 3.25 | .07 | 11.66 | 1 | 11.66 | 3.63 | .05 |
| *CSR Assurance* | 3.14 | 1 | 3.14 | .94 | .33 | 3.77 | 1 | 3.77 | 1.17 | .28 |
| *Order* | .89 | 1 | .89 | .27 | .60 | 4.22 | 1 | 4.22 | 1.31 | .25 |
| Interaction Effect |  |  |  |  |  |  |  |  |  |  |
| *CSP x CSR Assurance* | .96 | 1 | .96 | .29 | .59 | 1.19 | 1 | 1.19 | .37 | .54 |
| *CSP x Order* | .84 | 1 | .84 | .25 | .61 | 2.10 | 1 | 2.10 | .65 | .42 |
| *CSR Assurance x Order* | .03 | 1 | .03 | .01 | .91 | 12.89 | 1 | 12.89 | 4.01 | .04 |
| *CSP x CSR Assurance x Order* | 4.01 | 1 | 4.01 | 1.21 | .27 | 4.91 | 1 | 4.91 | 1.52 | .21 |
| Residual Error | 370.91 | 112 | 3.31 |  |  | 359.58 | 112 | 3.21 |  |  |

\* CSP = 1, when firms shows high CSP, 2 when low CSP; CSR Assurance = 1, when the CSR reporting is assured, 2 when non-CSR assurance; Order = 1, if participants receive first CSP information and then CSR assurance information, 2 if participants receive first CSR assurance information and then CSP information; Financial Risk = Ability of the company to reduce its future financial risk (on a 1-to-11-point scale); Accurate Forecasted Information = Likelihood that forecasted financial information is accurate (on a 1-to-11-point scale 1); Experience = Number of years of working experience; Position = Position in the firm: Junior, Senior, Manager, Partner/CEO (from 1 to 4, respectively, from lower to higher positions).

a Two tailed p-value.

**Table 4\***

**Pairwise Comparisons**

**Planned Contrasts for CSR Excellence – Profitability, Liquidity, Financial Risk Assessments and**

**Accurate Forecasted Financial Information**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Comparison of Cell Means** | **Profitability** | | | **Liquidity** | | |
| **Mean difference** | **t-test** | **p-valuea** | **Mean difference** | **t-test** | **p-valuea** |
| U22 > (U21,U12, and U11)  (group 1 vs. group 2, 3 and 4) | .69 | 2.26 | .02 | .80 | 2.41 | .01 |

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Comparison of Cell Means** | **Financial Risk** | | | **Accurate Forecasted Information** | | |
| **Mean difference** | **t-test** | **p-valuea** | **Mean difference** | **t-test** | **p-valuea** |
| U22 > (U21,U12, and U11)  (group 1 vs. group 2, 3 and 4) | .47 | 1.33 | .18 | .74 | 2.02 | .04 |

\* Profitability = Ability of the company to generate future profits (on a 1-to-11-point scale); Liquidity = Ability of the company to generate future cash flows from its operating activities (on a 1-to-11-point scale); Financial Risk = Ability of the company to reduce its future financial risk (on a 1-to-11-point scale); Accurate Forecasted Information = Likelihood that forecast financial information is accurate (on a 1-to-11-point scale 1).

a Two tailed p-value.

1. While the term CSR refers to the involvement in social and environmental activities, CSP refers to the degree of achievement of social and environmental goals as perceived by stakeholders. [↑](#footnote-ref-1)
2. The *stakeholder theory,* the *transaction cost economics* and the *resource-based view* are the most important theories suggesting a positive impact of CSR on financial performance (Preston and O’Bannon 1997; Rodgers et al. 2012). [↑](#footnote-ref-2)
3. For example, Margolis and Walsh (2003) report that in their review of the 109 published archival articles only 54 studies document a positive impact of CSR efforts on financial performance, while 7 studies show a negative relation. More recently, some studies argue that CSR may even contribute to improve the financial performance of firms involved in controversial business, such as tobacco, alcohol, nuclear power, military weapons, etc. (Blanco et al. 2012; Cai et al. 2012). [↑](#footnote-ref-3)
4. Accounting archival research has recently examined the relationship between CSR reporting and both analyst forecast error and cost of equity capital. While Dhaliwal et al. (2012) find that the issuance of CSR reports is associated with lower analyst forecast error, Dhaliwal et al. (2011) find that CSR disclosure reduces a firm’s cost of equity capital. Further, other archival studies have explored the link between firms’ efforts in CSR activities and their involvement in earnings management. Chih et al. (2008) that CSR firms tend to smooth earnings less. Scholtens and Kang (2012) conclude that Asian firms that perform better on CSR are engaged significantly less in earnings management. Kim et al. (2012) find that firms that exhibit CSR, as compared to firms that do not meet the same social criteria, behave in a responsible manner to constrain earnings management. More recently, Choi et al. (2012) provide archival evidence suggesting that firms with permanent CSR efforts, in comparison with those with temporary CSR achievements, are less involved in real accounting manipulations. [↑](#footnote-ref-4)
5. Elliott et al. (2012) also provide evidence suggesting that investors subconsciously use their affective reactions to positive CSP to unintentionally increase their estimates of fundamental value. [↑](#footnote-ref-5)
6. Note that Pflugrath et al.’s (2011) findings are also supported by recent archival research of Dhaliwal et al. (2012) and Dhaliwal et al. (2011). [↑](#footnote-ref-6)
7. The attribution theory proposes that users attribute less (more) credibility to voluntary good (bad) news disclosures that is more (less) consistent with management incentives and thus require more (less) information searches for additional credibility cues (Mercer 2004). [↑](#footnote-ref-7)
8. Dilla et al.’s (2012) results seem to be contrary to those of Dhaliwal et al. (2011, 2012), Coram et al. (2009) and Brown-Liburd et al. (2012), since CSR assurance is found to have a negative impact on investors’ decisions in the case of high environmental andsocial performance. [↑](#footnote-ref-8)
9. Barnett and Salonom (2006) also investigate the CSP-financial performance link within mutual funds that practice socially responsible investing. Their results show that this relationship is curvilinear with the strongest financial returns to low and high levels of social responsibility, and significantly lower financial returns to moderate levels of social responsibility. [↑](#footnote-ref-9)
10. Note that previous experiments have not created scenarios of sustainable social performance. For example, consider the experiments run by Elliott et al. (2012) and Dilla et al. (2012) which only provide participants with CSP information pertaining to the concurrent period. Another example is the work of Brown-Liburd et al. (2012) which only provides participants with information about the degree of investment in CSR activities for the concurrent year. [↑](#footnote-ref-10)
11. The relevance of CSR efforts can be interpreted under the *instrumental* or the *normative* taxonomy (Marom 2006; Donalson and Preston 1995). The instrumental approach assumes that the ultimate objective of corporate decisions is marketplace success (Berman et al. 1999), where social investing is accepted only if it is consistent with wealth creation.On the other hand, the normative perspective conceptualizes corporate social effort as a moral imperative, rather than the business benefits it may provide (Marom 2006). [↑](#footnote-ref-11)
12. Further information about the CSR rankings performed by KLD Research and Analytics, Fortune MAC, and the Corporate Responsibility Magazine can be found at [www.thecro.com](http://www.thecro.com), [www.kld.com](http://www.kld.com), and money.cnn.com/magazines/fortune/mostadmired/2012/index.html, respectively. [↑](#footnote-ref-12)
13. Managers have both explicit and implicit motivations to bias forecasted information (Felleg et al. 2012). While explicit incentives reflect aspects of the manager’s environment that are publicly observable (e.g., litigation risk, financial distress, competitive environment), implicit incentives reflect aspects of the manager’s environment that may not be directly observable but are revealed through the manager’s forecasting behavior (e.g., manager’s performance contract, pending retirement). [↑](#footnote-ref-13)
14. The number of participants receiving first CSP information and, then, CSR assurance information are similar to the number of those receiving first CSR assurance information and, then, CSP information (See Table 1). [↑](#footnote-ref-14)
15. This program is currently ranked as one of the top-100 M.B.A programs by the Financial Times. [↑](#footnote-ref-15)
16. We include years of professional experience and position in the firm as potential covariates. [↑](#footnote-ref-16)
17. Position in the firm was found as a significant covariate in the liquidity assessment at the 10 percent level. [↑](#footnote-ref-17)
18. We conduct two planned contrasts to analyze in more detail the CSR assurance x Order interaction. Results suggest that those subjects receiving CSR assurance before the CSP information rely more on forecasted financial information than those receiving CSR assurance after the CSP information (mean = 6.20 and 5.14, respectively; F = 5.26, p = .02; two-tailed). Therefore, this significant interaction suggests that, for non-assured CSR scenarios (U21 and U11), participants’ reliance on forecasted information is more favorable when CSP information is processed last. Besides this interaction, considering MANCOVAs results we can assume that there is no evidence of a generalized order effect in our study.The potential order effect issue is further examined in the additional analysis section. [↑](#footnote-ref-18)
19. [↑](#footnote-ref-19)
20. However, the ability to reduce financial risk is not significantly affected by CSP excellence (p = .18). [↑](#footnote-ref-20)