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Editorial

The legitimacy of governance to public and private sectors

While governance practice has its legitimacy grounded in the corporate laws and various guidelines issued by stock exchanges and professional associations in the private sector, this edition of the Law and Governance Journal returns to questions raised by implementation of governance in the public sector.

Commitment to public sector governance has been driven by the mounting debts of governments, and lack of solutions. The issues are raised at this time because of the worldwide disenchantment of the populace with their governments and leadership, and the impact of major social and technological change. The 21st century has seen the rise of conflicts not only within so many different countries but also, as indicated by the conflicts in Syria and Iran, an increase of tensions between countries. With this political unrest, the impact of Brexit, and fears of another economic crisis, has come a pervading sense of uncertainty.

The digital revolution changing society is reinforcing the structural changes taking place. The emergence of high unemployment, especially among youth, is giving impetus to their perceptions of little prospect of future economic prosperity and subsequent increases in crime. There is evidence; too, of a rise in excessive use of law enforcement, that is, police appear to be adopting practices that indicate a lack of respect for citizens and their lives. The regular shootings of civilians occurring in the US is an example. The use of social media and its unfettered and unprecedented license to criticise and denigrate traditional institutions may be a contributing factor. WikiLeaks for example has been a leader in promoting disclosure of corruption through the internet. The corruption seen at all levels of society from governments to sporting bodies reinforces a related loss of confidence in our institutions.

That people are seeking changes to leadership and more stability is evident in the rise of specific interest groups and ‘popular’ members of Parliaments, such as Donald Trump.

This edition of Law and Governance is set in this context. It reflects our growing concern with the institutions of society and desire for government initiatives that can achieve a stable and sustainable future. The papers deal with different aspects of uncertainty and threats posed in today’s world.

The first paper by Dr. Michael Longo explores the role of government in the EU. He argues that poor governance in the European Union (EU), in terms of lack of leadership, uncertainty of purpose and inequity associated with lack of integration, raises questions about the legitimacy of the EU. He concluded that the future of the EU is dependent on addressing these issues.

The second paper is also concerned with conflicts, in this case a government’s response to terrorists and their impact on the economy. The paper describes the actions of a government constrained by terrorism. The Government of Nigeria had initiated numerous programs with the purpose of stimulating the agricultural sector. This paper by Adebisi, S. A., Azeez, O. O. and Oyedeki, R. investigated the impact of the Boko Haram terrorist group on agriculture and GDP in the Nigerian economy. The paper concluded by suggesting strategies to promote the sector that the Nigerian Government should include in its policies.

While the above papers are focused on public policy and governments’ response to governance issues, the final two papers in this edition return to the core issues in governance, the performance of directors and corporate social responsibility.

The first of these reports the results from a study of state owned enterprises (SOEs) in Indonesia by Agus Widodo. Indonesia follows the legal system in which corporate laws direct companies to form two boards of directors, a commissionaire in which members are responsible for the direction and objectives of a company and a board of directors which undertakes the executive management of the operations of a company. In his PhD thesis, Widodo investigated the consequences of the different conflicts of interest which can emerge when a director holds a position on the boards of both a parent SOE and its subsidiary. This paper reports the investigation of the potential conflicts of interest for the directors and whether, should a conflict emerge, would the directors serve the interests of the parent company or those of the subsidiary.

Corporate social responsibility is often equated with compliance with the spirit of the law, ethical standards and engaging in social actions that are beyond the direct interests of a corporation. Dr. Heenetigala investigated the CSR practices of 50 companies in Sri Lanka. The majority of their activities were directed to improving better education, health facilities and livelihood development of rural communities. She concluded that in developing countries these activities can have a major role in facilitating community development.

This edition of the Law and Governance Journal includes papers which address both the legal and the social implications emerging from governance practice. Whether in developed economies such as the EU or developing countries such as Indonesia and Sri Lanka, good governance makes an important contribution to both the government and private sectors. The above papers illustrate that while governments have a direct role in developing economic stability, corporations can also play a complementary role in promoting community development.

Professor Anona Armstrong AM
Editor

Inequality, Poor Governance and Legitimacy Deficits in the European Union

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ABSTRACT

This article offers an interdisciplinary perspective on the drivers of political and economic crisis in the European Union. A growing body of literature highlights the detrimental effects of extractive institutions on opportunity, sustainable growth and social cohesion. The article therefore examines the link between income inequality, corruption and perceptions of illegitimacy in the European Union. It conjectures that poor institutional quality and governance are critical drivers of the European Union's legitimacy deficit. The article concludes that for the European regional project to advance there is a need for greater institutional convergence amongst member states and a renewed commitment to social cohesion.

Key Words

European Union, inequality, governance, legitimacy.

Introduction

From its inception the European Union (EU) has drawn generously, and gained inspiration, from the imperative of an ever-closer union. An epoch-making vocabulary emerged over half a century of development, which seemed to express the EU's objectives to improve the lives of all of its citizens. Words and sentiments such as 'solidarity', 'cohesion', and 'integration' itself, proved self-fulfilling as the EU marched towards peace and prosperity – the original twin imperatives of European integration (EI). However, the upheaval following the financial crisis of 2008 and the onset of systemic financial-economic-political crises unprecedented in the post second world war period have challenged the tenets of EI while austerity has consigned debtor states to recession or low growth, accentuating social inequalities.

As the economic and social problems persist, the disintegration of the Eurozone still appears plausible. While the European Commission pleads for greater unity, its federative proposals are not enthusiastically received by many EU citizens who are increasingly disenchanted with globalisation and its European counterpart, Europeanisation. Populism is on the rise across Europe, and many citizens are now viewing the EU as the source of their problems (Longo and Murray 2011). More and more citizens in many member states have lost faith in the EU as a system, most now thinking that EI has weakened their country.¹ The prescription of austerity is nourishing existing divergences in the economic and social condition of member states. While purporting to present a critical solution to

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sovereign indebtedness, austerity seems incapable of simultaneously resolving sovereign debt problems and stimulating sustainable growth. Furthermore, citizens are challenging the wisdom of austerity in the light of inequality, continuing governance failures and poor institutions² that distort markets (i.e., barriers to entry, tax avoidance, corporate welfare, monopoly rights, policy capture or

corruption) and lead to social exclusion (e.g., youth unemployment and poverty).

This article examines the substantive dimensions of the Eurozone crisis emphasising interconnections between inequality, exclusion and legitimacy. Section II briefly interrogates globalisation, the monetary union and austerity as central to current debates on the crisis. In Section III, the article seeks to develop a fresh critique of the crisis to argue that deep-seated institutional deficiencies and corruption are key drivers of rising inequality. Further, it proposes that the interaction of inequality and social exclusion is a critical element of the EU's legitimacy crisis. There are links between inequality, corruption and legitimacy. Finally, the article concludes with the assessment that austerity will fall short of the desired outcomes in the light of extreme divergence in economic conditions and governance practices.

European Crisis: The Big Issues

As key drivers of the legitimacy crisis, regional inequalities have been attributed to three major factors: accelerated globalisation; monetary union; and fiscal discipline.

Globalisation and the loss of sovereignty

The globalised economy of the 21st century appears to have diminished the capacity of national authorities to exercise effective regulatory control over economic policy. The challenges posed by the Eurozone crisis have highlighted the need for well thought out policy responses that reach beyond the national sphere to correct institutional deficiencies and economic imbalances. Yet national responses still seem to be expounded as if the nation state were fully sovereign and dominant. Arguably, globalisation and Europeanisation have rendered moot the proposition that nation states are the masters of their destiny. A reluctance on the part of national elites to present the idea of 'more Europe' as a response to the economic rise of 'population behemoths like China and India' (Hill 2013) means that the starkness of the choice between 'banding together' or becoming 'less relevant and secure' is being obscured.

The process of European integration has lately coincided with the rise of China, India and Brazil as the expanded domains of global capitalism. Globalisation brings innovation, 'creative destruction' and inevitably winners and losers (Roubini 2012). The emerging economic powers have exerted much pressure on wages and the employment prospects of low-skilled and unskilled workers in the West (Roubini 2012). Europeanisation, exacerbated by the Global Financial Crisis (GFC) and the Eurozone crisis, has motivated many to resent free trade and the further surrender of national sovereignty to 'free' markets. Moreover, markets have recognised the flaw in the EU and Eurozone's architecture. Markets are spurred to action by decisions of credit agencies and institutional players in the global financial system, many of whom have to shoulder some responsibility for the GFC and its aftermath.

Yet, markets do not have long memories and the GFC testifies to the fact that they can fail to assess and even ignore valuable information to the detriment of taxpayers, jobs and the vulnerable (Taleb and Spitznagel 2012; Stiglitz 2012a). Former Italian Prime Minister Monti lamented, during a period of persistently high yields on Italian Government Bonds, the inability of financial markets to recognise the progress made by his government on fiscal and structural reforms (Wall 2012). Markets have longed for clear policy statements, backed up with unequivocal action that demonstrated beyond a doubt that the Eurozone and the ECB would provide protection for struggling states against insolvency, if only to ensure the integrity and continuing viability (and investor-friendly status) of the Eurozone. They were often left wondering.

In theory, were they to be efficient, as economic theory suggests, the Euro markets ought to account for differences in productivity, risk, and frugality. The experience of the toxic lending in the USA and sovereign debt in Europe shows that, in reality, markets can fail to accurately assess risk (Weidmann 2012) and are prone to contagion (Stiglitz 2012b). Moreover, critical flaws in the financial architecture of EU have meant that stronger economies have little incentive to circulate surplus funds while weaker regions are exposed to panics and bank runs (Auerback 2012; Bibow 2012). Habermas notes that '[f]inancial markets have developed beyond the control of even the most powerful nation states' (Habermas 2012, 53). Only by acquiring greater 'political steering capabilities' and working towards 'a convergence of the member states' economic and social development' can the EU 'withstand the financial speculation' (Habermas 2012, 50). Market speculation has indeed prompted political elites to strengthen the executive capacity of the European Council to deal with the crisis, but the European Council's interventions have proved neither popular nor effective. Under German leadership it has pushed for tough austerity to balance national budgets and reforms to restore competitiveness.

There is a growing gap between the EU's supranational institutions and the European publics (Hill, 2013). Financial globalisation and the current finance-led model of growth have demanded the prioritisation of financial interests over all others. While banks have been bailed out by taxpayers, states are struggling to tame budgets to meet European and market demands – all at the cost of social cohesion. Not surprisingly, Europeans are judging this model negatively.

The inadequacy of monetary union

A key aspect of monetary union, as expressed in the Maastricht convergence criteria and the subsequent rules-based Stability and Growth Pact (SGP), was to target inflation expectations through monetary policy, restrict national budget deficits to less than 3% of GDP and limit total national (sovereign) debt to 60% of GDP. The Maastricht criteria and SGP essentially featured a system of surveillance and coordination of fiscal policies among its member states.³ Despite the rules and the pro-SGP rhetoric, the failure of so-called 'core' governments to adhere to the limits has been striking. Germany departed from the Maastricht regime of 2% unit labour costs by wage deflation (Bibow 2012) and both France and Germany violated the 60% debt rule (Feldstein 2011). This departure from the fiscal rules by the Eurozone's leaders was to have a detrimental effect when the GFC prompted stimulus spending in member states in a climate in which those states believed that the rules were meant to be violated.

The Fiscal Compact, a stricter version of the SGP, came into force on 1 January 2013 for ratifying states. The compact seeks to enforce budgetary discipline and, effectively, commits participating states to long-term austerity. It represents an intergovernmental response to a problem that demands an integrated political response. Hill (2013) has observed that '[t]he eurozone crisis has stretched EU governance to its limits because the EU's current political institutions are mostly adequate for a loose confederation of member states – but a loose confederation is inadequate for a monetary union.'

Indeed, as currently calibrated and constituted, monetary union is unable to deal with persistently divergent movements in prices and competitiveness across member states (De Grauwe 2012). It is worth noting that monetary union evolved at the heyday of deregulation and free-market ideology promising level-playing field, competition, market efficiency and welfare improvements. Also, the imperatives of financial deregulation and inflation targeting, as sufficient conditions for innovation and growth, reigned supreme.

However, it has now emerged that regulation and taxation can improve welfare (Stiglitz 2012b; Frank 2011) and a nation's capacity to adapt to economic change and convergence can be severely curtailed by extractive institutions (Acemoglu and Robinson 2012b). In addition, it is now apparent that pay does not always reflect productivity for all workers (Diamond and Saez 2012) and countries new to financial liberalisation are more vulnerable to debt crises than others (Reinhart and Rogoff 2011).

Principal elements of the EU such as monetary union, free trade and capital movements, and fiscal discipline all rest on the contestable premises that (a) markets are always more efficient than government; that is, labour markets and prices adjust to reflect differences in productivity and social norms, and (b) adjustments are independent of institutional constraints, and income distribution. However, these assumptions are hard to reconcile with the Great Recession and even economic intuition (Stiglitz 2012b, Aghion and Cage 2012). The Great Recession has exposed the flaws of a monetary union as a mechanism of integration, in view of free capital movements, a restrained European Central Bank, and rigid fiscal rules. Moreover, this union seems incompatible with the ultimate goals of stability and prosperity for *all* the EU member states.

Austerity and economic growth

Sovereign debt crisis is often interpreted as a sign that a people live beyond their means and lack fiscal discipline. All too often the remedy proposed by the IMF in such cases has been austerity and the reduction of debt as a means to recovering business confidence and investment. Highly controversial claims of a direct link between public debt and stagnation (Herndon *et al.* 2013) have given impetus to the drive for austerity.

However, it has been argued that the focus on austerity when the servicing of the debt exceeds growth rates is a misdiagnosis of the problem. In fact, the right focus for Europe in that case should be on growth (Summers 2012). Although growth seems to be what Europe needs, the lack of fiscal discipline can be a risky strategy in the global world of banking and finance (Deen and Worrachate 2012). Austerity is thought essential to reduce debt and restore credit worthiness as well as market confidence in Europe, but the debt to GDP ratio will only increase in a recession which, in turn, perpetuates the austerity policy (Schulmeister 2012). The answer may be to strike a balance between growth and moderate inflation.

The debate on growth strategies so far has centered on structural reforms that foster competition and remove product and labour market rigidities. In theory, these reforms ought to enhance competitiveness, business confidence, and ultimately economic growth (ECB 2012). Although there is an increasing willingness to examine EU investments in education, innovation and growth-enhancing sectors such as energy (ECB 2012), there is still a pervasive emphasis on fiscal discipline and national stereotypes such as ‘grasshoppers and ants’ (Steffen 2012) or tax cheating (Elliot and Aitkenhead 2012).

Although these interpretations of sovereign debt allude to some core institutional failures, they fail to acknowledge that these failures associate with conflict of interest, uneven distribution of political power, and persistence of rent-seeking (Acemoglu *et al.* 2005, Bardhan 2005). Moreover, stark inequalities and social exclusion (e.g., youth unemployment) seem to perpetuate rent-seeking and severely impede institutional reform (Stiglitz 2012b; Alvaredo *et al.* 2013).

Furthermore, austerity, as a regressive policy, exacerbates inequality and undercuts a nation’s capacity for reform and economic growth (UNDP 2011). A positive association between fiscal imbalances and corruption (Mungiu-Pipidi 2013) may give credence to the view that austerity may act as an antidote to corruption. Yet again, causation may run in reverse – i.e., corruption and weak institutions in general lead to sovereign debt problems. If the latter holds true, austerity may reduce the resources available for corruption but it would not necessarily lead to better institutions.

With the swearing in of the new Juncker European Commission in November 2014, and the introduction of a Quantitative Easing (QE) program by the European Central Bank in January 2015 there is renewed hope that changed political circumstances will favour growth and investment over austerity. The full extent of the damage (material and symbolic) that austerity and inequality are inflicting on European societies has emerged. The IMF has questioned the effectiveness of its own bailout policies on Greece.⁴ Apart from burgeoning unemployment, social exclusion and poverty, there is a growing sense that the ideals of EI are vanishing. There is rising anger with political elites and

general disenchantment with the EI project (ETUI 2013a). Moreover, the current EU failure to deliver adaptation and convergence to a European standard of living for all is raising questions of capacity, performance and legitimacy. The EP vote in May 2014 revealed the extent of disillusionment with the EU as Euroscepticism gained ground in core and peripheral member states alike.⁵ The outcome of the snap Greek election in January 2015 signalled the popular defeat of the bailout/austerity program in that country.

Political legitimacy and resilience in the era of globalisation also rest on the robustness of the European Union and the quality of institutions that have long-term impact on incentives and markets, and ultimately on growth and prosperity. The multi-dimensionality of legitimacy and its orientation to performance and social acceptability means that institutions that function optimally and deliver desired social and economic outcomes are more likely to be deemed legitimate. A more detailed discussion of legitimacy follows.

Institutions, inequalities and democratic legitimacy

Although globalisation, monetary union and fiscal austerity are important sources of discontent in the EU, it is intuitive that inequality can be the product of social progress or policy errors. We maintain that these sources of inequality cannot rationally explain a sustained legitimacy crisis in the EU, for in the longer term, all other things being equal, creativity should dominate destruction and policy ought to be corrected.

Persistent popular challenges to the EU's legitimacy point to more fundamental causes of inequality that relate to social justice and fairness. Recent advances in economics advocate that institutional quality⁶ is a critical element of economic development (Acemoglu and Robinson 2012b). By its effect on transaction costs and incentives, institutional quality critically impacts on prices, innovation and economic growth. An important dimension of institutional quality is corruption in member states which can contribute to unsustainable deficits, market distortions, and extractive institutions. Corruption may be driven by either agency problems (Blackburn *et al.* 2010) – the principal (i.e., the public) delegates authority to an agent (i.e., executive government or public officials) who may use privileged information to their benefit and at the expense of the public – or 'collective action' problems (Persson *et al.* 2010) whereby lack of trust is so pervasive that the costs of containing corruption are much greater than the benefits for the perceived majority.

'Rent seeking' behaviors, such as corruption, monopoly power, and 'regulatory capture' exacerbate income inequalities (Stiglitz 2012b). Roubini (2012, 163) suggests that 'any economic model that doesn't properly address inequality by providing public goods and opportunity to all will eventually face a crisis of legitimacy.' Corruption and rent seeking undercut opportunities for the disadvantaged to upgrade their skills and to adapt to technological transformation. Consequently, rent seeking ultimately undermines macroeconomic stability, structural reform, and economic growth (Johnson *et al.* 2011; Stiglitz 2012b).

It has been argued that entrenched inequality associates with higher public debt, political instability (Roubini 2012; Kumhof and Ranciere 2010), extractive institutions (Krugman and Wells 2012; Acemoglu and Robinson 2012a) and the depletion of social capital (Wilkinson and Pickett 2009). The current focus on austerity and market reform does nothing to address the yawning inequalities afflicting many of the member states in crisis. In fact it makes it worse, as austerity tends to affect the disadvantaged most.

In economic theory, rising income inequality is justifiable when it reflects shifts to new technologies or new products (Acemoglu 2011; Yun 2006). However, increasing inequality can be unacceptable for several reasons: (a) it can be due to corruption, and 'cognitive capture' of public policy by interest groups and the rich (Johnson *et al.* 2011; Krugman and Wells 2012; Stiglitz 2012b); (b) it can add to economic crisis and public deficits; (c) it can lead to intergenerational exclusion and poverty

(Alvaredo *et al.* 2013), and (d) it may lead to social unrest and political violence (Acemoglu *et al.* 2005; Bardhan 2005).

Social exclusion and unjustifiable inequality also impinges on economic growth. According to Aghion (2012), the success of EU reform hinges on the balance between fiscal discipline, growth, and social justice where the latter involves fairness and social inclusion. He argues that growth cannot be 'sustainable' when stark inequalities exclude many people from employment, dampen life aspirations and suppress work effort. Inclusive institutions are more conducive to skill development, innovation and growth (Acemoglu and Robinson 2012b). Commenting on the economic success of ancient Athens, Ober (2008, 266) also highlights the role of democratic institutions built on principles of accountability, transparency and legitimate dissent.

Until recently, the debate on institutional reform has been overly preoccupied with property rights (e.g., privatisation), labour market deregulation, and the inefficient state (Aghion and Cagé 2012; Bardhan 2005). For example, corruption is almost exclusively discussed in terms of a rigid and self-serving public service (Mungiu-Pipidi 2013; Bardhan 2005). Yet, the role of rent-seeking and market power often goes unchallenged, although Boldrin and Levine (2013) and Stiglitz (2012b) are exceptions.

Income inequality due to institutional failure leads to resource misallocation and distorted incentives as it can strengthen the bargaining power of the rich to influence public policy (Stiglitz 2012b) and the wage structure (Alvaredo *et al.* 2013), both of which accentuate existing inequalities. In the absence of a 'level-playing field', policy capture by vested interests inevitably undermines public confidence in reforms, innovation, and investment in human capital.

The current debate on austerity is characterised by two polar views that both ignore the fundamental role of institutions. One view insists on fiscal re-distribution and an increasing role for state intervention while the other extreme pushes for austerity, piecemeal reforms and deregulation. However, both neglect that the 'level playing field' is work-in-progress, a common-interest state can be efficient, neither austerity nor its opposite abolishes extractive institutions, and 'market-supporting regulation' is critical for innovation and growth (Besley and Persson 2011).

Legitimacy

Democratic principles pertaining to representative and/or participatory democratic processes, now codified in the Treaty on European Union (TEU),⁷ are means by which civic participation in EU decisional processes can be stimulated. Articles 9-12 of the TEU are intended to encourage democratic participation. Important as these provisions may be in addressing the purported democratic deficit of EU decision-making, they are not intended to bring about a convergence within and between the member states themselves towards accepted standards of good governance. The EU member states are characterised by extreme divergence in the adherence to principles of democratic governance, which has been shown to distort markets and hamper EI. Within the Eurozone itself are states at virtually opposite ends of the spectrum of global rankings for corruption.⁸ As poor governance has similar deleterious, market-distorting consequences for EI as important constraints on economic development, there is a strong case for coordinated action at EU level to work towards correcting institutional and related deficiencies in the interests of integration.

For scholars, European integration has accentuated dilemmas of legitimacy. The role of undemocratic European institutions has received considerable attention since at least the 1990s (e.g. Banchoff and Smith 1999; Beetham and Lord 1998; Scharpf 1999; Schmidt 2013). For some time the draft Constitutional treaty was seen as a likely antidote to the legitimacy problem; a fresh opportunity to negotiate a compact between the EU and its citizens and thereby correct the deficiencies of an emerging political system.

There are links between the failure of the Constitutional Treaty⁹ and the Eurozone crisis. Both may be attributed, at least in part, to a lack of certainty about the EU's direction. Whereas during the negotiation and ratification stages of the draft Constitutional Treaty, the single currency may have been seen as a stepping stone towards political union, the policy choices and loss of momentum associated with the eventual abandonment of the treaty meant that this perspective was lost (Pisani-Ferry and Sapir 2009, 69). The constitutional vision contemplated an acceleration of integration as a voluntary policy choice as citizens acknowledged the benefits of closer economic union and backed political union as a necessary corollary of economic and monetary union. Arguably the failure of the constitutional treaty stymied the push for greater political legitimacy and halted progress towards a form of political union that encompassed greater citizen participation in democratic processes and tighter fiscal integration. It is now evident that the imperfections of monetary union and the democratic deficit are both driven by a single cause: uncertainty about the aims of EI (The Economist 2012). Citizens are challenging the legitimacy of the EU's policies in the public space and in national constitutional courts.¹⁰

Legitimacy is often discussed in output-oriented and input-oriented terms (Scharpf 1999). Output-oriented legitimation is concerned with *effectiveness and performance*; effective results are *for* the benefit of the people. Instead, input-oriented legitimacy is about securing citizens' choices through participation *by* the people. Accordingly, political choices are legitimate if they are effective and reflect the 'will of the people'. To this analytical framework can be added so-called 'throughput' legitimacy' (Schmidt 2013). Having a focus on governance processes, throughput legitimacy is concerned with the efficacy, accountability and transparency of the EU's processes as well and their inclusiveness and openness to public consultation (Schmidt 2013, 2). While there are complementarities, interactions and tradeoffs between input and output legitimacy, it is thought that poor governance taints even effective and democratic outcomes:

[B]ad throughput – consisting of oppressive, incompetent, corrupt or biased governance practices – regularly undermines public perceptions of the legitimacy of EU governance, regardless of how extensive the input or effective the output (Schmidt 2013, 3).

The EU's traditional concern in dealing with transnational problems has tended to focus attention on output-oriented legitimacy. However, the growth of EU competence in areas of high electoral salience, such as monetary and fiscal policy, has drawn attention to the need for greater democratic input in EU decision making. It is in this context that the blurring of legitimacy and democracy is most critical (Banchoff and Smith 1999). With its noticeable democratic deficits, EU governance is readily susceptible to the conclusion that it suffers from a legitimacy deficit as well. The motto 'Lavoro é Democrazia' (Work is Democracy) – catch-cry of uniform trade union protests in Rome on 22 June 2013 (Ronchini, 2013) – demonstrate the connections between employment, equality, social cohesion and democratic legitimacy. The connections are substantiated by the not so implicit threat that executive inattention to growing citizen demands for work will result in social discord and the demise of governments. Voters in Greece have ultimately made good on this threat. The UK referendum on EU membership further illustrates the potential for disenfranchised voters to overturn unpopular executive bargains.

Although it is evident that nation states are no longer the repositories of undiluted national sovereignty and that membership of the EU and the Eurozone brings with it a surrender, or *pooling*, of national sovereignty in supranational institutions, the current concentration of legal powers in the Commission and the shifting of moral authority to the European Council (*viz*, Germany) to deal with the crisis have raised significant questions of legitimacy. These developments have effectively severed the long-standing binary between national and supranational institutions, introducing for the first time a direct and explicit relationship of dominance-submission among member states themselves. Stratham and Trezn (2013, 168) observe that public contestation about the winners and losers of integration is shattering the old universal premise that the EU is an equal partnership between countries and their citizens.

The EU has taken a predominantly ‘hands-off’ approach on the question of correcting national maladministration. The Commission did not, until recently, have the power to bring national executives to account on issues of high political salience such as budgets. On the instigation of Germany and France in the mid-2000s the Commission’s power to impose sanctions on member states in breach of the Stability and Growth Pact was deactivated. With Germany’s insistence on fiscal consolidation and austerity during the debt crisis, divisions with other member states have surfaced. Moreover, by Germany assuming a leadership role in the crisis, the Commission has appeared, rightly or wrongly, as less of a policy innovator and more as an agent. This fundamental change raises new questions of legitimacy in terms of the authority of a powerful member state to impose unpopular solutions on the citizens of other member states.

The perennial question surrounding the absence of citizen approval of elite decisions on Europe has assumed new dimensions in the light of the current crisis: ‘has anyone asked Europeans how much sovereignty they are ready to surrender to save the euro?’ (The Economist 2012). If Europe chooses to continue to develop as an autonomous political system in order to make the euro work, it would ultimately need authority to do so. Conversely, the need to democratically legitimise EU would diminish if strategic institutional choices were exercised in favor of limited political integration.

Hix (1999, 364) suggested almost two decades ago that for integration to proceed much further the EU would need increased policy competence and greater democratic participation to legitimise outcomes. While increased policy competence has materialised in the monetary and fiscal spheres, this has not been accompanied by greater democratic participation. Habermas (2012, 50) opines that political legitimacy requires greater democratic influence by citizens over what their national governments may negotiate. Though irrefutable, these principles do not find firm expression in the EU’s current institutional and governance arrangements.

Furthermore, it is becoming increasingly apparent that the legitimacy crisis afflicting EU institutions has also been driven by EU indifference or impotence to deal with bad governance and corruption at the national level (Mungiu-Pippidi 2013). This issue is closely connected with the EU’s lack of leadership and problems of institutional design both at the EU and the member state level. Stark differences in equality within the EU, combined with persistent extractive institutions (Besley and Persson 2011) such as corruption, are inimical to the promise of shared prosperity and solidarity.

There is also growing fragmentation in the EU with the emergence of a multi-speed Europe (ETUI 2013a). With growing divergence there is social polarisation, increased risks of social exclusion and poverty (ETUI 2013b). If monetary union is not sustainable without social convergence, and monetary union is currently producing divergence, then it is clear that the EU is caught in a legitimacy trap that can only lead to Euroscepticism and populism. To gain greater acceptance Habermas (2012) suggests that the EU must demonstrate that it has the capacity to secure the EU’s objectives in the interests of *all* of its member states and citizens. For this to come about the EU must acquire the capacity to confront institutional deficiencies in the member states, which impact on inequality and sustainable growth.

The need for effective institutions invites discussion of how the EU can promote convergence among its members around the principles of good governance. This imperative has been a point of discussion since at least the Commission’s White Paper on Governance.¹¹ The degree of divergence on this issue between and within member states suggests the need for concerted action on improving institutional frameworks and the targeting of specific problems in order to promote core principles of good governance, the absence of which has been shown to negatively impact on economic growth and development.

New initiatives and ideas by EU leaders have recently emerged that promise to revitalise the European vision for stability and shared prosperity. The Juncker Commission’s focus on investment is an attempt to shift focus from austerity to growth. For some time the EU leadership has acknowledged the inadequacies of the existing system and has actively sought further integration with a more robust institutional structure of EU. Economic and political pressures in Italy, France, Spain and Greece

motivated the former EU Commission president to call for a federation of states,¹² and the ECB president for a 'banking union'. These announcements were designed to contain bank runs and relieve national governments from the responsibility to recapitalise banks, and for rising sovereign debt, and contagion. Institutional reform has been slow and piecemeal. The main focus of reform has been the strengthening of monitoring of national budgets by the Commission and greater coordination of fiscal objectives. Despite these changes, questions have persisted as to whose interests are being secured by EU policies and with what consequence. Doubts will remain until the citizens' interests in being represented by inclusive institutions that adhere to principles of good governance are prioritised over others. If this analysis is valid, it follows that the EU will fail to assert its legitimacy if it fails to achieve sustainable reductions in inequality and greater democratic participation.

Conclusion

The EU is confronted with division and extreme uncertainty regarding its future. The response to the fallout from the Great Recession has been piecemeal and inadequate. Seriously compromised now is the EU's core founding myth that integration leads to stability and growth for all its members; there are new power-holders, winners and losers of integration (Statham and Trez, 2013, 164,168). The North, the rich, the banking sector may all be labeled winners at present, much to the dismay of ordinary workers and the newly unemployed in Southern Europe. Having played a leading role in causing the crisis, banks are dictating solutions despite evidence of 'regulatory capture' by ideology and vested interest (Stiglitz 2012b).

The sovereign debt crisis has revealed the inadequacy of the SGP and the absence of an effective crisis management system. Proposals for a banking union, eurobonds or other means of debt mutualisation have met resistance. Although the notion of collective responsibility – the defining element of solidarity – would provide a conceptual basis for burden sharing (Cook 2012, 508), it is not currently in evidence. Economic and social conditions in the member states differ widely.

There is general recognition among EU policy makers that the EU must act to achieve a degree of convergence in the fiscal and economic governance domain. Without some form of fiscal union, monetary union is incomplete. The latter requires a degree of homogeneity in regulations, public sector administration and governance rules. However, standards differ substantially amongst member states.

Moreover, the deficits are acquiring new dimensions. The *performance* or output-based legitimacy of EU decision-making, rarely seriously questioned in the past, has come into critical focus, with EU policymakers presenting austerity as the primary cure for the Eurozone's problems. EU policies that aim to avoid systemic risk in the Eurozone appear to be penalising debtor states and favouring others. Ultimately, austerity will not produce the desired effects against a background of extreme divergence in economic conditions, institutional quality and governance practices.

Equity considerations demand that the EU act to overcome the structural imbalances and deficiencies of monetary union and that it contribute to redressing national impediments to growth and development, whatever the source of such constraints may be, as such impediments distort the market. Just as the EU seeks to narrow development disparities among regions and member states through structural and cohesion funding, there is a need for the EU to act to equalise and optimise conditions for economic governance. Whether this can be achieved through monitoring and supervision or sanctions and incentives is a matter of debate. Lately, the European Commission has signaled its intention to adopt a stronger EU anti-corruption policy, although new EU legislation on corruption does not seem to be the favored approach at this stage.¹³ It appears the EU's commitment will not progress quickly beyond a reporting function in the absence of political will.

The abandonment of the Constitutional Treaty in 2005 set the scene for the erosion of EU centeredness over the last decade. The EU must tackle its legitimacy problem if it is to regain lost ground.

Concerted EU action to achieve greater convergence towards good governance and growth can lay the foundations for a workable fiscal union, a reduction of inequality and, arguably, a more legitimate EU.

There is general recognition that the EU faces an unambiguous choice between the collapse of the European project or further integration towards a financial or fiscal union (Bibow, 2012). In response, and at the insistence of the Commission and Germany, debtor Southern states are making adjustments to align more closely to the Northern model of economic organisation. At the same time austerity, budgetary restraint and stronger fiscal coordination among Eurozone states with sanctions for non-compliance are being promoted as necessary safeguards against the collapse of the euro currency.

A lesson we are learning from the current crisis is that equity and social justice concerns must assume greater prominence in the hitherto arid discourse on the interventions necessary to stave off the collapse of the euro and economic decline. At stake is the legitimacy of EU action itself. The article has sought to demonstrate the link between poor institutions, persistent inequality, and the legitimacy deficit, assessed against output, input and throughput criteria. There is a need for further empirical research to establish the links between inequality, corruption and legitimacy and to complement the growing body of literature in this field. An examination of EU policy and scholarly literature invites the conclusion that the EU will continue to struggle to maintain its legitimacy unless it acts decisively to bring about a convergence of governance and sustainable growth to the benefit of *all* its citizens.

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Notes

¹'The New Sick Man of Europe: The European Union', Pew Research Global Attitudes Project, 13 May 2013, <<http://www.pewglobal.org/>>

² Institutions are 'humanly devised' rules and constraints that impact on economic behavior through incentives (Acemoglu *et al.* 2005).

³ Council Regulation (EC) No.1466/97 of 7 July 1997 on the surveillance of and coordination of budgetary positions and economic policies OJ L209 02/08/1997, 1-5 as amended and Council Regulation (EC) No.1467/97 of 7 July 1997 on the implementation of the excessive deficit procedure OJ L209 02/08/1997 6-11 as amended.

⁴ European Trade Union Institute, 'IMF internal report on Greek bailout questions troika's austerity policy' 11 June 2013. Online version accessed 5 July 2013 <http://www.etui.org/News/IMF-internal-report-on-Greek-bailout-questions-troika-s-austerity-policy>.

⁵ There was a particularly strong showing by populist anti-EU parties *Front National* in France and UKIP in the United Kingdom. See: European Parliament election: Eurosceptic parties claim victory in UK, France' *ABC News*, 26 May 2014. Online version accessed 26 May 2014 <http://www.abc.net.au/news/2014-05-26/european-election-ukip-national-front/5476776>

⁶ Key elements of institutional quality are voice and accountability, political stability, government effectiveness, regulatory burden, rule of law, and control of corruption (Dixit 2008),

⁷ Title II, OJ C 326, 26.10.2012.

⁸ For instance, in the 2014 Corruption Perceptions Index, Denmark ranked first, while Italy, Greece, Bulgaria and Romania ranked equal 69th out of 175 countries. Online version accessed 18 March 2015 <http://www.transparency.org/cpi2014/infographic/global>

⁹ The failure of this explicit constitutional process followed the rejection by French and Dutch voters of the draft Constitutional Treaty in 2005.

¹⁰ For instance, the German Constitutional Court has made it clear that the transfer of sovereign powers to EU institutions in certain areas including finance is circumscribed. See, for example, the Maastricht Treaty Case (12 October 1993, BVerfGE 89, 155), and the recent judgment regarding the European Stability Mechanism (ESM), the EU's permanent bailout fund (12 September 2012, 2BvR 1390/12, 2BvR 1421/12, 2BvR 1438/12, 2BvR 1439/12, 2BvR 1440/12, 2BvE 6/12).

¹¹ White Paper on Governance, COM (2001) 428 final, 10. In its White Paper, the Commission identified the emerging norms of governance, derived from a liberal conception of democracy and democratic accountability – openness, participation, accountability, effectiveness and coherence – as markers of legitimate action.

¹² Olli Rehn, opening address to Brussels Economic Forum, 31 May 2012; Barroso, Annual State of the Union address, Strasbourg, 12 September 2012.

¹³ Cecilia Malmstrom, 'Fighting Corruption: From intentions to results', speech by the EU Commissioner for Home Affairs, 5 March 2013.

Appraising the Effect of Boko Haram Insurgency on the Agricultural Sector of Nigerian Business Environment

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ABSTRACT

The study is an appraisal of Boko Haram's insurgency on the agricultural sector of the Nigerian business environment. A time series analysis research method was adopted, while descriptive statistics and t-test were used to analyse the secondary data before and during the insurgency. The result of the findings showed that agricultural valued added to the GDP was high before Boko Haram disruption and has reduced during the period of insurgency. Based on the findings, the study recommends that Government should take legal and justifiable action to ensure that the ills caused by Boko Haram to the agricultural sector are arrested and farmers encouraged with better incentives to go back to farm.

Keywords

Boko Haram, Agriculture, Government, Business and Environment

Introduction

Agriculture in Nigeria is the most important sector of the economy from the standpoint of rural employment, sufficiency in food and fibre, and export earning prior to the discovery of oil (Towobola, et.al 2014). The above assertion is based on the fact that as at independence in 1960, little was known of petroleum as a source of revenue for the Nigerian economy. There was sustained emphasis on agriculture such that Nigeria was a major exporter of agricultural products like palm produce, cocoa, groundnut, cotton and rubber. In addition to these cash crops, the national agricultural system produced enough food crops such as yam, cassava, maize, millet, sorghum and soya beans so that there was practically no need for food importation. Hitherto, agriculture accounted for over 60% of the nation's Gross Domestic Product (GDP) (Francis and David, 2012).

According to Akinwumi (2014), in the 1960s, before the discovery of oil, Nigeria was known to be a major agricultural producer in the world. Between 1962 and 1968, export crops were the country's main foreign exchange earner. Nigeria was number one amongst other countries like Malaysia and Indonesia in products like palm oil and groundnuts, even ahead of the US and Argentina. Nigeria's status with 47% in these products which made her as an agricultural centre has declined steeply. While Nigeria once provided 18% of the world demand of cocoa, second in the world in the 1960s, that figure has drastically reduced to 8%. Also the country which was known to produce 65% of

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tomatoes in West Africa has become the leading importer of tomato paste. Despite the poor performance of the agricultural sector which is below economic expectation, the sector is still capable of aiding socioeconomic development of people living in rural areas, most especially in the northern states as they engaged more in agriculture in order to sustain themselves, and traded within their

capacity or capabilities for profit. However, the on-going Boko Haram insurgency has affected the rural agricultural economy the northern, part of Nigeria, hence, this work is an appraisal of the impact of Boko Haram insurgency on the agricultural sector of the Nigerian business environment.

Statement of Problem

Reduction in the production of agricultural outputs in Nigeria began with the discovery of crude oil in 1956 while commercial exploitation commenced in the early '70s. The discovery of oil in Nigeria which was supposed to be a blessing and an additional source of income to the country has become a means of distorting our economy. Kathleen (2014) observed that Agricultural products which were the main exports and major source of foreign exchange earnings for the country declined suddenly. In the same vein, Lawal (2012) noted that many government policies have been enacted to develop the sector but these have not achieved much. This situation is further worsened by the advent of Boko Haram (a sect of violent people). Boko Haram which means "denouncing western education" has led to the displacement of farmers in Northwest and Northeast of Nigeria. This insurgency has made many farmers relocate to other places where there is peace in order to save their lives, causing them to leave their farmlands behind as it is not mobile as highlighted by (Mustapha, 2015).

According to Lawal (2012), agriculture is not limited to crop production alone. The Northerners also involve in animal husbandry and they were engaged in business even before the colonial era. The manifestation of Boko Haram recently has been a great threat to the Nigeria business environment as farming and other business activities are being harmed (Council on Foreign Relations, 2015). Nomadic cattle rearers who have been taking their cattle out for grazing have abandoned their business, as the environment is no longer safe for them. The lives of those that are still involved in the business are also at stake, because an attack of Boko Haram can occur at any moment. This has led to decreases in milk production, meat production and by extension an increase in the price of the cattle. Poultry farmers also do not find their business lucrative anymore, as the people purchasing the goods have been displaced.

Some of the crops they produced are also perishable and need to be consumed on time. Consequently, this has also led to poor transportation, high transport cost, displacement of properties and high risk to lives. These crops get spoiled leading to wastages. Also some of these crops need to be marketed on time but due to imposed curfew and several restriction of movement; they perished and become unmarketable (Mustapha, 2015).

The hazard caused by Boko Haram is not only felt in Nigeria but in some other parts of the Africa. Cameroon, a country sharing border with Nigeria in the North East part is also affected. Traders from this country can no longer come to Maiduguri (Nigeria) to buy or sell. The border was closed some time ago, restricting importation or exportation from the countries which affected their economy. The Niger Republic economy is also affected, as she shares border with Nigeria and both countries practise goods exchange with one another.

Akinwumi (2014) revealed that climate favours the Nigeria agriculture business environment and the country needs World Bank assistance to boost the sector. Dabugat (2013) identified that the present problem of low agricultural productivity is due to violence in the Northern States. This forms the basis of arguments of this paper which examines the effect of Boko Haram on the agricultural sector of the business environment of Nigeria.

Objective

This paper is aimed at investigating the impact of Boko Haram insurgency on the agricultural output with respect to Gross Domestic Product (GDP) in Nigeria within the period under investigation.

Hypothesis

- (Ho) Boko Haram insurgency has no significant effect on the Agricultural Sector of Nigerian Business Environment: Percentage of *output to GDP from 1994 to 2003 and percentage of output from 2004 to 2013*.
- (Hi) Boko Haram insurgency has significant effects on the Agricultural Sector of Nigerian Business Environment: Percentage of *output to GDP from 1994 to 2003 and percentage of output from 2004 to 2013*.

Literature Review

An Overview of the Nigerian Agricultural Economy

Agriculture is the cultivation of land, raising and rearing of animals for the purpose of production of food for man, animals and raw materials for industries. It involves and comprises crop production, livestock, forestry, and fishery, processing and marketing of these agricultural products (Mabuza et al, 2008). In the early 1950's to 1960's agriculture played a vital role in stimulating economic growth and development in Nigeria. It provided employment to millions of Nigerians and over seventy percent (70%) of the labour force which are mostly from rural areas were employed in agriculture (Abayomi, 2006). In the same period, agriculture contributed over 70% to the country's export earnings (CBN, 2007). Indeed agriculture provided the main stimuli to the Nigerian economic growth despite the small farm holding and primitive systems. The contribution of agriculture dominated other sectors' contribution to the GDP.

Usman (2006) reported that Nigeria has about 140 million people of which about 70% are engaged in agricultural production and this provides subsistence for two-thirds (2/3) of Nigerians who are low income earners, while the Northern part can guarantee the production of cereals such as sorghum, maize, millet, groundnut, cowpea and cotton, the Middle Belt and the South have the potential to produce tubers such as cassava, yam, cocoyam and other crops like plantain as well as maize (Abdullahi, 2003). In addition to crops, the country is also involved in the production of livestock, fisheries, forestry and wildlife. Ukpong and Iniodu (1995) also supported the view that Nigeria is generally endowed with abundant natural resources, numerous perennial sources of water and a favourable tropical climate. Rainfall is generally adequate and fairly well distributed throughout the country. Out of the 98.321 million hectares of land available in Nigeria, about 75.30% may be regarded as arable land, 10% is under forest reserves and the remaining 14.70% is assumed to be made up of permanent pastures, built up areas and uncultivable waste (Olajide, 1980). Igboeli, (2000), noted that agriculture is still a major sector and remains the cornerstone of the Nigerian economy. In the pre-and post-independence era (1930 to 1965), the Nigerian economy was predicated on agriculture. Agriculture employed about 70% to 80% of the country's labour force (CBN, 1995), and contributed 60% of the nation's gross domestic product (GDP) and foreign exchange earnings (Ugwu and Kanu, 2012).

The support of Government towards the development of the Agricultural Sector

The government of Nigeria usually allocate some amount of money to the agricultural development yearly (Lawal, 2011). Although these allocations have not been in linear progression method due to political instability, some agricultural policies have served as back-up so as to boost output which has a multiplier effect on Gross Domestic Product (GDP) and the standard of living of its populace (Ogen, 2007). Agriculture was the major source of employment, foreign income, and has been feeding about 70% of the citizens in pre and about 10 years post-independence. The discovery of oil led to the neglect of the sector in the 1970s and a shortfall of its contribution towards GDP. The government then reacted quickly by establishing the Nigeria Agricultural and Cooperative Bank (NACB) in 1973. The bank's main function was to provide loans to farmers in order to increase production in areas like fisheries, cattle rearing, poultry, piggery, land cultivation and planning, timber production, horticulture and the likes. It also includes storage and processing, distribution and marketing (Lawal,

2011). As part of government interest in agriculture, the capital base of the bank was increased from ₦2.0million to ₦10.0million. This was done to encourage new farms and protect existing agricultural businesses seeking agricultural loan. The establishment of Agricultural Development Projects in 1975 were to provide assistance to farmers in their different locations. The introduction of Operation Feed the Nation (OFN) was good news to everybody which helped to heal and improve agriculture especially in small scale levels (Iwuchukwu and Igbokwe 2012).

Agriculture represents a veritable vehicle for social economic development of the country by which the government provided financial incentives and promoted, encouraged and supported the growth and development of agriculture through the establishment of The Agricultural Credit Guarantee Scheme (ACGS) Fund in 1977 which commenced operation in 1978. The fund was meant to provide loans to farmers (individual, cooperative society and limited liability company) beginning from ₦5000 to ₦10million with or without collateral depending on the amount. This was done through commercial and merchant Banks by the Central Bank of Nigeria (Lawal, 2011 and Evbuomwan, et al., 2003). More to the list is the establishment of Rural Banking Programme launched in 1977 and the River Basin Development Authority in 1977.

Daniel and Ihechituru, (2012) and Olugboyega and Kolawole, (2012), posited that Governments over the world recognised the importance of agriculture, because it creates employments, foreign exchange and helps to feed the growing population and Nigeria is not an exception. Nigeria government has hitherto helped to start and grow agriculture business through the establishment of the Green Revolution Programme launched between 1980 -1983. This was meant to make Nigeria self-sufficient in food designed for five years. The Directorate for Foods Roads and Rural Infrastructure (DFRRI) scheme was launched in 1986. Nseabasi (2012) opined that the aim was to ease the storage, distribution and marketing of farm products through the creation of good roads and other infrastructures for rural dwellers who are mostly farmers. The establishment of Federal universities of agriculture in some part of the country was also to encourage students and youths to develop interest in agriculture.

According to Okogun and Abang (2012), the Nigeria Insurance Scheme established in 1987 by the federal government was to protect farmers and also reduce their loss arising from natural disaster. The government continued its effort by establishing the Nigeria Agricultural Land Development Authority (NALDA). This policy was imbibed at State and Local government levels. The objective was to make farmers have access to large farm land without stress. Successive government in Nigeria have initiated numerous programme and policies to generate employment, reduce poverty and improve the growth of the economy through agriculture by supplying farmers with fertilizer and distributing it at subsidized prices, low interest rate on loan to farmers, and 100% tax reliefs on farm products. As observed by Nwachukwu and Ezeh (2007), the Strategic Grains Reserve Authority (SGRA), the Accelerated Crop Production (ACP) and the Better Life Programme for Rural Dwellers which was replaced by Family Support Programme (FSP), and was gender specific (rural women) were all established to improve the productive capacities of peasant farmers as well as improving their incomes and well-being. The Nomadic Education was to encourage mobile farming while schooling. In a nut shell all these programmes were geared towards a well sustained economic growth and by extension its development.

The Effect of Boko Haram Insurgency on the Nigerian Agricultural Sector

Terrorism is becoming a global phenomenon. The world is becoming an evil jungle. The killing of people and destruction of properties are seen as an everyday affair and gradually becoming a way of life. The safety of lives and properties are no more guaranteed. Terrorist attack is in the news on a daily basis and the intensity of religious terrorism is increasing every day (Council on Foreign Relations, 2011). The number of death from terrorism is increasing on yearly basis and the world death toll in 2013, increased by 61% when compared to 2012. And about 10,000 attacks in 2013. It has been observed that the 21st century terrorism is done through religious ideology supported by some Islamic groups called Al-Qaeda, Islamic State, Boko Haram and the Taliban. These groups are Islamic militant that do irrational bombing and suicide killing of innocent people. The worst terrorist attack ever noticed in the 21st century was September 11, 2001 attacked on the World Trade Centre in New York which killed about 3,000 people, the terrorist attack on India Parliament in December 13, 2001 and the July 7, 2005 attack in London city. These attacks are in connection with Al-Qaeda militant group. The violent gun shot in a shopping mall in Kenya in 2013 and the recent killings of innocent university students in the country have made the world very unsafe to live. The persistent attack by Islamic sect called Boko Haram in Nigeria and some of the neighbouring countries are unbearable. These groups attack on different countries is a fight against Western culture and education (Olaide, 2013).

There has been a general notion by some Islamic extremists that Western education is bad and must be eradicated. This has been followed by terrorism in different countries aimed at destabilizing the peace of the world and making living together in harmony without discriminating against any other forms of worship. Religious violence and terrorism are increasing and becoming a threat to the world business environment. These notorious groups are violent Muslim extremists who interpret religious ideologies to suit self-desires. The 21st century religious terrorist group such as Al-Qaeda, Taliban, Boko Haram etc justify their actions on Islamic principles. They believed that violence is the only means to fight an existing government and to cause change.

Literature has adduced that terrorism in Nigeria and some other countries in Africa is caused by porous borders, poverty, weak security, inconsistent government policies and disagreement among Muslim scholars. The Boko Haram group in Nigeria and neighbourhoods and the Al-Shabaab in Kenya are enough to discourage Westerners from doing business with Africa. More than 1.5 million people, mostly farmers, have been forced to flee their homes as Boko Haram intensified its insurgency in the past years according to the United Nations High Commissioner for Refugees. The worst-hit states of Borno, Yobe and Adamawa produce staple foods such as cowpeas, rice, millet, sorghum, corn and yams as well as tomatoes, onions, fish and livestock for both local consumption and export markets.

Maiduguri, the capital of Borno state in Nigeria has been deserted by both indigenes and foreigners, as the people there have been jobless. The movement of these people is under restriction due to the curfew imposed by the government or the Boko Haram activities. This violent set of people have bombed bridges, communication gadgets and other social amenities which are necessary for habitation linking Nigeria with neighbouring countries in the north eastern part of Nigeria. Some bridges linking villages where major famers dwell in Yobe State have been blown up. Fish farmers in Yobe State are unable to transport their products to the South. Instead of forty trucks per week, only a maximum of seven trucks of fish products can be transported to South thereby causing increase in prices. The fear of the notorious group has stopped farmers from going to farm even when the climatic condition is very favourable and could have led to a bountiful harvest. The attacks on villagers, burning down homes and indiscriminating shooting have forced survivors to relocate to the South especially in Borno State (Sahara Reporters, 2015).

The government has also been spending a lot to cater for refugees. The situation has led to an increase in government expenditure. Boko Haram has brought pain and death to Nigerian business especially in the agricultural sector of the nation. The aftermath of Boko Haram is hunger as it has displaced

farmers from their settlements and buyers into untold hardship. Each attack in Borno, Yobe or Adamawa States kills human beings and destroys farm products. The Boko Haram insurgency which started in 2002 lunched its full-scale attack in 2009 and since then became more violent each day. The hot zones are Borno, Yobe and Adamawa States which have the largest farm land in the country dominated by different kinds of farmers. These States produce staple foods such as corn, cowpeas, rice, millet, tomatoes, yams, onion, fish and livestock. The fear of Boko Haram has prevented farmers from cultivating their farm land and the few that did have lost their farm products to the terrorists who set them ablaze, killing the farmers and destroying their products. These States are closer to Niger, Chad and Cameroon where agricultural business activities were booming especially in area of export of groundnuts and groundnut oil (Mustapha, 2015). These activities are now becoming history due to Boko Haram attacks. The government must use all means to fight these terrorist to allow farmers go back to business in order to boost the Gross Domestic Product (GDP) of the country.

Moreover, agriculture's decline as a share of GDP has more implications in the Northern States, where it is a source of livelihood. With the influence of Boko Haram, the share of people engaged in subsistence agriculture will continue to reduce if nothing is done to arrest the situation. Although GDP can depend on macroeconomic activities, agriculture in Nigeria is also a major source of GDP and therefore cannot be left to be destroyed by a violent sect called Boko Haram. The main thing that will reduce poverty and create employment in Nigeria is agriculture. Agriculture in Nigeria is beyond food for man and animals. It is a source of income to the country through exportation and raw materials for industries in the country. The importance of agriculture in the creation of employment, industrialization and poverty reduction cannot be over emphasized.

In summary, the contribution to government revenue has been decreasing since independence due to the oil boom, political instability and lack of continuity in government policies coupled with corruption. The recent reoccurrence of Boko Haram is very devastating to the Nigeria business. The contribution of agriculture to Gross Domestic Product (GDP) has reduced drastically due to the discovery of oil and neglect of the agricultural sector, and to worsen the situation is the displacement and death of farmers', their products and their marketers. Business thrives only in stable environment. Boko Haram has made agriculture business environment in the Northern States of Nigeria very turbulent. The factors of production which are land, labour, capital and entrepreneurship are not stable. The bombing of farm products and lands destroys both the future outputs and makes the lands not viable for the next farming season. The killing of youth and also using them for violence complicates the situation. The male youths who are more active with much strength and can be a good source of labour are people the Boko Haram is using for attacks. Capital is the amount invested in the business. Capital can only be invested when the risk associated with it can be controlled or minimised. No farmer will want to invest in a business where the risk in the business environment is very high. Entrepreneurs are the owners of the business. They have to run for safety and divert to another business in a peaceful environment

No nation can afford to treat with levity the security of its territorial region and of its people. Indeed every aspect of human endeavour, be it health, environmental, food, economy, political, social, education, sport and physiological etc, stands to be greatly affected by the state of security or insecurity of that nation. It is no longer news that in recent time, Nigeria has been burdened with challenging security issues chief among which is the Boko Haram insurgency (Adebayo, 2014). According to Abidde (2014), Boko Haram made its presence known in 2004, in Yobe State and by 2011 it made its presence known to the global community by bombing the United Nations headquarters in Abuja. Especially in the last two years, it has wilfully attacked hundreds of buildings and killed many innocent Nigerians. Until recently, the Nigerian security and intelligence agencies knew very little about the group's origin and philosophy, its *raison d'être*, and its goals and end game (Abidde, 2014). In the past, Boko Haram insurgents have used Cameroon as a safe haven for initiating hit-and-run attacks on neighbouring Nigerian territory. The Nigerian government responded by deploying a military presence on the northern border. Further attempts to prevent the sect extremists from accessing targets across the porous boundary have culminated in official closure of the Cameroon border (Merrick and Li, 2014).

The North yields 78% of Nigeria's land which supports most of Nigeria's agriculture (food, cash crops and livestock) (Innocent, 2012). With increased intensity of bombings in the north, there was strategic mass movement of individuals from the most affected northern states especially in early 2012. This was accentuated by the uncertainties surrounding the fuel price crisis at the time. The movements were of a strange kind since both Southerners and Northerners simultaneously moved from Boko Haram strongholds. While the affected areas of North move to the South-East in hundreds, others relocated to the South-West (Innocent, 2012).

According to Merrick and Li (2014), the sect has inflicted violence in northern Nigeria for the past five years. Boko Haram means "western education is forbidden." It upholds its principles by targeting schools, Christian churches, and more recently, the entire towns. Since 2009, Boko Haram insurgency is believed to have killed thousands of people and destroyed properties valued at over a billion dollars. This includes government buildings, livestock and produce. The insurgents continue to torch public buildings and steal large quantities of produce, thereby destroying livelihoods of farmers and forcing hundreds of businesses to close or relocate. With Boko Haram's northern insurgency concentrating where agricultural activity is highest, Nigeria's national government is becoming increasingly concerned with threats to food security (Merrick and Li, 2014). Either way one looks at the group, its activities have been very damaging both physically and psychologically (Abidde, 2014).

Implication of Boko Haram Insurgency on Agriculture in Nigeria

Margarita, (2013) explained that more recently, the Boko Haram insurgency in northern Nigeria, ethno-religious conflicts in Central Nigeria, as well as conflicts originated by the Niger Delta militants in response to oil exploitation and environmental degradation in the Niger Delta area. These conflicts have negatively affected the availability and affordability of food items in these areas. Many rural farmers have been displaced while others are restricted from going to their farms because of security checks and the militaristic counter-terrorism approach of the government (Dabugat, 2013).

Merrick and Li (2014) explained that over the past five years, the Nigerian government has kept mostly closed borders with Cameroon, Chad and Niger. This has crippled the agricultural export market in northern states, resulting in the loss of one of Nigeria's largest potential revenue sources. Almost 80% of Nigeria's northern population are active farmers. But beyond decreased agricultural consumption, higher density insurgence has affected northern locals in other major ways. Millions of livestock have been adversely affected while the region's thriving fishing industry has plummeted. New security measures have been adopted by the state to reduce the impact of Boko Haram's insurgence in the north. An imposed curfew has shortened business hours in some affected areas. Others have increased the use of checkpoints and made everyday movement extremely difficult.

Over a million fishermen in the region have been forced to immigrate with their families to Niger Republic. With insurgents terrorising the citizens in the north, there are fears that even higher levels of the population will take to emigration to ensure their livelihoods and safety. Although there have been no reports of a major attack on the northern state of Kano in recent years, violence in neighbouring states continue to negatively affects its commerce. Closures of northern borders have decreased trade in Kano by half, thus increasing regional food shortages and poverty levels. As such, the National Emergency Management Agency estimates that over 152,000 people have been internally displaced mostly farmers due to attacks on more than 100 communities in north central Nigeria alone, and are unlikely to return to their homes anytime soon (Usman, 2006). Violence in Borno, Yobe and Adamawa states gained momentum with the emergence of President Goodluck Jonathan in May 2011. Over 1.5 million people have fled their homes and at least 13,000 people mostly farmers have died in these states due to violence killing and gun shots (Mustapha, 2015). Maiduguri, the capital of Borno state had witnessed multiples of bombing explosion making the town very insecure for farmers and other businesses. Major markets in the town have become ghosts' area due to insurgency. It is on record that among the six geo-political zones in Nigeria, the North-east and North-west are the poorest zones and these are the zones where Boko Haram originated from and very active (Council on Foreign Relations 2015).

The bombing of bridges and roads have made land transportation risky and difficult. Movement of goods and man have hence been restricted. Animal husbandry is a common farming business in the north especially with nomadic cattle rearers who have to move from one place to another to feed the cattle. Other farm animals need to be fed to grow well for business and most of the animals' food are obtained from farm products. Insecurity has led to drastic reduction in agricultural output and increase in prices in other parts of the country (Sahara reporters, 2015, Kathleen, 2014). The closing of borders have affected more than just the Nigerian population. Cameroon has been negatively affected by this closure, especially communities closest to the Cameroon-Nigerian border. With no movement between states, there has been a sharp fall in food exports to Nigeria and in commodities such as oil to Cameroon. The border closure has had disastrous consequences for both merchants and residents of Northern Cameroon. Such consequences are seen through these merchants' and residents' dependence on oil and Nigeria as an export community for their produce. With closed borders, the price for commodities has skyrocketed, while transport fares increased by 70%. For these reasons, many of these citizens are unable to export their goods to Nigeria, leaving them to stockpile large quantities of produce. The town of Amchide has been reported to have taken the hardest hit. Amchide has become a ghost town, where the merchants who formerly constituted 90% of the population have left, giving way to the patrol teams stationed there by Cameroon's military. The increase in violence leaves little hope for those within the region to return home and continue their trades (Merrick and Li, 2014).

Okechukwu (2014) explained that the federal government's effort at augmenting food production at the Chad Basin has come under serious threat from the activities of Boko Haram insurgents in the area. An investigation shows that the several hectares of arable land prepared for the cultivation of rice and other grains in Borno has been abandoned because of the activities of the insurgents. It was gathered that virtually all the farmers involved in rice cultivation and other agriculture-related activities have abandoned the vast expanse of land at the Chad Basin because of the activities of the insurgents. The investigation further showed that the suspension of farming activities in the Chad Basin has resulted in the scarcity of food stuff and an increase in the price of rice (Okechukwu, 2014). All fiscal and domestic policies enacted by the government to boost agriculture especially in the northern states have proved abortive. A sector of the economy which provides employment for more than 70% of the population cannot be handled with insecurity (Adebayo, 2014, Kathleen, 2014).

Nigerian poultry farmers under the auspices of the Poultry Association of Nigeria (PAN) have also raised concern over the activities of Boko Haram insurgents stating that it is taking a toll on sales of poultry products in Northern Nigeria. The National President of PAN made this clear during the Second Poultry Summit held at the Lagos State Chamber of Commerce and Industry, Alausa. Oduntan (2014) lamented that the activities of the violent sect had resulted in a daily drop in sales due to non-availability of some raw materials for feeds such as maize and groundnuts which were usually sourced from the affected states. He also revealed that export to neighbouring countries had become impossible. Oduntan (2014) explained that the insurgency had killed retail sales in the North as night-life has become non-existent. It was during this time that Northerners usually buy eggs in very large quantities from tea sellers. He called on the Federal Government to provide support for the poultry business as it currently cannot satisfy the volume of demand for poultry products in the entire country (Okojie, 2014). The health implication of Boko Haram in the bringing of epidemic in Ideal Dispose People (IDP) areas leading to death of young men and women who could be workers in the agriculture sector.

It is a known fact that a reasonable number of school pupils, youth, women and children have been killed through the indiscriminating gun shots by the terrorist. It is certainly no good news that Boko Haram attacked the College of Education in Yobe leaving over 30 students dead (Ikeji, 2013). It is very pathetic to read that the militants stormed the village of Debiro in Hawal local government area of Borno state and slit the throats of 20 villagers. Debiro is a small village not far from Maiduguri the capital of Borno state (Sahara reporters, 2015). The abattoir in Maiduguri that used to kill hundreds of cows and goats meat suddenly shut itself down due to a bomb explosion (Okojie, 2014). Boko Haram has ruined agricultural business in Nigeria. A business survives only in a peaceful and stable environment.

Methodology

Secondary source of data was used for this study. Data were obtained from World Bank showing Nigerian agricultural value added percentage of GDP from 1994 to 2013 a period of twenty (20) years in order to determine the extent of agricultural contributions to Gross Domestic Product (GDP) in Nigeria. It is necessary to use data that had been generated to show the time series effect. Descriptive statistics and T-Test were used in analyzing the data collected. This is with a view to enabling the researchers to obtain the effect of Boko Haram insurgency on the agricultural sector of the Nigerian business environment. The time series method is a set bivariate data of quantitative observations collected over a period. It shows how economic, social, psychological and other factors have changed over time, which could be daily, monthly, quarterly or yearly.

The expression of time series is given by:

$$Y = F(t)$$

Where

T is the time;

Y, is the variable of interest and;

F, is the Function of the model

Results and Discussion

This section presents analysis and interprets the data generated for the study. The data was generated from the World Bank for twenty (20) years, (1994-2013).

Table1. Agricultural output (kg) on yearly basis in Nigeria.

YEAR (Period 1, 10 years 1994-2003 before the insurgency)	Agricultural output to Nigeria GDP	YEAR (Period 2, 10 years 2004-2013 during the insurgency)	Agricultural output to Nigeria GDP
1994	38.8108824	2004	34.21028658
1995	32.06099353	2005	32.75542177
1996	31.13372236	2006	31.9987955
1997	34.03135991	2007	32.71417898
1998	39.0478495	2008	32.85021918
1999	35.30644453	2009	37.05016484
2000	26.03397777	2010	23.89370408
2001	33.7537884	2011	22.28919858
2002	48.56594018	2012	22.05428761
2003	42.70726998	2013	20.99639753

Source: World Bank 2015

Analysis of the period of 1994 to 2013

T-Test was conducted to show an Appraisal of the Effect of Boko Haram insurgency on the Agriculture Sector of Nigerian Business Environment: Output from 1994 to 2003 and output from 2004 to 2013.

Table 2: Group statistic of Agricultural output in Nigeria.

Group Statistics

Group Variable		N	Mean	Std. Deviation	Std. Error Mean
Output	Output (1994-2003)	10	36.1452229	6.39261667	2.02152289
	Output (2004-2013)	10	29.0812655	6.02781669	1.90616301

The table above shows the evaluation of the descriptive statistics i.e. the mean scores of the two groups concerned, the output from 1994 to 2003 and the output from 2004 to 2013. It was noted from the table that a difference (7.06395739) existed between two groups, as the output from 1994 to 2003 had a mean score of 36.1452229 while the output from 2004 to 2013 had a reduced mean score of 29.0812655. Furthermore, as the numbers of years for 1994 to 2003 output were ten (10) years, while the numbers of years for 2004 to 2013 output were ten (10) years, the observed difference of 7.06395739 in their mean of their total performance scores could be as a result of the difference in reduction in the output in 2004 to 2013, which could not be avoided due to insecurity. This implies that the output was affected between 2004 to 2013 compared with 1994 to 2003. The two groups are really different. The significance of the groups' is tested and presented in the table below.

Table 3: T- Test output performance

	T-Test for Equality of Means						
	t	Df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
						Lower	Upper
Output Performance	2.542	17.938	0.020	7.06395739	2.77849099	1.22512277	12.90279201

T-test Calculated (Statistic) = 2.542, Degree of freedom = 17.938, Level of significance = 0.05, Returned p-value = 0.020

Interpretation

The t-test statistics was calculated as 2.542, at 5 percent level of significance under 17.938 degrees of freedom, the output p-value of 0.020 was found less than the accepted level of significance $p < 0.05$. Thus the null hypothesis was rejected. Hence, *(Hi) Boko Haram insurgency affects the Agricultural Sector of Nigerian Business Environment: Output from 1994 to 2003 and Output from 2004 to 2013*. This implies that between the periods of *2004 to 2013* Boko Haram insurgency had negative impact on Nigerian Agricultural Sector *Output*.

Conclusion and Recommendations

Boko Haram insurgency in Nigeria and some of its neighbouring countries have adverse consequences on the economy. The agricultural business environment has been affected. This has been evidenced by the reduction of valued added to the economy between the periods under investigation. Evidence has also shown that the conflict or terrorist activities have disrupted the agricultural output and economy

of the people living in the Northern states as most inhabitants and farmers have migrated to a better and safer place. The insurgency has also affected the exportation of agricultural inputs needed for conversion and transformation in other industries that rely on inputs like rubber, cocoa, fertilizer, etc.

In addition to revamping and controlling the country's agricultural business sector as it was in the 1960s, the government should take drastic action to stop this unbearable act of Boko Haram in addition to its other agricultural policies. Also, State governments should engage in specific agricultural activities on the basis of the principles of comparative advantage. This is because less dependency on the Northern states for agricultural products or inputs would likely reduce the effect of this insurgency on food prices in other states.

The neglect of agriculture which was an important source of revenue most especially in the area of foreign exchange earnings for the government has become reduced drastically due to over reliance on oil and corruption in the country. It is recommended that government should encourage youths to imbibe farming as part of Nigerian culture by providing basic amenities and social infrastructures in rural areas.

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Board Member Duality and Its Relationship with Corporate Performance in State-Owned Enterprises in Indonesia

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ABSTRACT

This paper presents preliminary findings from a survey about board member duality and agency cost in state-owned enterprises in 2014 in Indonesia. Board member duality is defined as the appointment to the position of director in a parent company while at the same time also holding a position as a commissioner in its subsidiary company. Agency cost refers to the cost which arises as a consequence of an agent and principal relationship. The principal expects that agency cost incurred in the relationship, will, in turn, increase corporate performance. Director's remuneration, as one of the proxies for agency costs, is tested together with several variables involved in the respondent attributes, namely gender, age, and education in order to find the best predictor of the dual director response regarding his/her role in parent and subsidiary governance. The preliminary finding reveals that Director's remuneration is the best predictor of the dual director response against three propositions, namely (1) Dual directors use their experiences to the advantage of both companies; (2) Dual directors tend to choose the interests of the parent rather than those of its subsidiary; (3) Dual directors increase subsidiary performance.

Keywords

Parent-subsidiary Governance, State-owned Enterprise, Board Member Duality, Agency Cost, Financial Accountability

Introduction

'Director' duality, which generally falls into three types of duality called CEO Duality, Interlocking Directorship and Multiple Directorship, attracts researchers to investigate its relationship with corporate performance. Inconsistent results regarding the relationship between director duality and corporate performance drawn from prior empirical research (Kim and Buchanan, 2011) can be grouped into studies which have produced three different results: (1) giving a positive impact on performance such as empirical research conducted by Donaldson and Davis (1991) and Boyd (1995); (2) giving a negative impact on performance, such as empirical research conducted by Daily and Dalton (1994) and Pi and Timme (1993); and (3) no systematic relationship such as empirical research conducted by Baliga et al. (1996) and Rechner and Dalton (1989).

A new construct for director duality, called 'board member duality' (Widodo, 2012), is slightly different compared to the three types of director duality mentioned previously. This research addressed board member duality in a survey conducted during October—December 2014. The participants in the survey were shareholders, commissioners, and directors in both parent and subsidiary state owned enterprises (SOEs) in Indonesia.

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'Board member duality' is new terminology in the director duality concept introduced by Widodo (2012) to describe the type of director duality appearing in parent and subsidiary companies adopting a two-tiered board system. Board member duality refers to the situation in which a parent's director at the same time also has a position as a commissioner in its subsidiary company.

This type of director duality popularly occurs in a country which follows the code of law system which instructs company boards to follow a two tier board system of governance (Benedicte and Ronald, 2010). The board member duality has two roles at the same time, the first role is serving as a director and the second role is as a commissioner.

Directors and commissioners which follow the two-tiered board system, have different tasks; the first one has an executive function which involves day-to-day business activity (decision-management), whereas the second one respectively is more heavily focused on an oversight function that includes advice giving (decision-control) and company direction and objectives (Maassen, 1999). This study examined the potential conflicts of interest arising when directors sit on the two boards. The very different foci of the director and commissioner tasks raises the main research question: *does the duality position as a director on a board in a parent company and as a commissioner in a subsidiary company impact on the agency cost of the SOEs? Or, from another point of view, does the duality position described above impact on corporate performance?*

This research will contribute to the literature by reporting the results of a study of board member duality and corporate performance in the context of a two-tier board and in the state owned enterprise in Indonesia.

Literature Review

Research on director duality, in most cases falls into three categories, namely: CEO Duality, Interlocking Directorship, and Multiple Directorship. CEO Duality refers to the position in which a CEO of a company also holds a position as a chairman of the board of director (Baliga et al., 1996). There are two types of an Interlocking Directorship; firstly, a direct interlocking directorship, the situation in which a director of a company A also serves as a member of the board of director of company B; vice versa, a director of a company B can also serve as a member of the board of director in company A. Secondly, an indirect interlocking directorship, the situation in which a director of a company A and a director of company B serve on the board of directors in company C. (Chhaochharia and Grinstein, 2007). Multiple Directorship occurs when a person serves as a director in more than one company (Scott, 1997).

Board member duality refers to a situation in which a parent company's director also holds a position as a commissioner in a subsidiary company (Widodo, 2012). This situation only occurs in companies which adopt a two-tier board in their corporate board structure. The differences with the three categories of dual directors mentioned before are depicted in the table opposite.

Table 1 Director Duality Comparison

	CEO Duality	Interlocking Directorship	Multiple directorship	Board Member Duality
<i>Definition</i>	Chief Executive Officer who also holds as a Chairman of the Board of Director	A direct interlock occurs if two companies, let say A and B, share a same director, while an indirect interlock occurs when director of company A and B hold a position as a board member in a third company (company C).	A person who holds a position as a director in more than one company	A parent's director who also holds as a commissioner in its subsidiary company
<i>Board system</i>	One-tier	One-tier and two-tier	One-tier and two tier	Two-tier
<i>Entity</i>	one entity	$2 \geq$ entities	$2 \geq$ entities	$2 \geq$ entities, and in a parent and subsidiary relationship
<i>Main role and function</i>	Execution and oversight function in the same company	The same roles in more than one company	The same roles in more than one company	Execution function in Parent company and oversight function in subsidiary company
<i>Ownership Structure</i>	He/she may not be a shareholder	He/she may not be a shareholder	He/she may not be a shareholder	For SOE, By law the CEO is the Ex Officio Shareholder of a subsidiary company

Based on the context of agency theory constructed in the parent-subsidiary relationship of a state owned enterprise, there are two uniquely legal subjects that govern the principal-agent relationship. The first legal subject is the company where it comprises parent company as the principal and subsidiary company as the agent. The second legal subject is a member of the board of directors of a parent company who acts as an agent of a SOE, and at the same time, is delegated by parent company to the principal or shareholder of a subsidiary company. This principal-agent relationship will incur costs called agency costs summarised by the sum of total monitoring expenditure by the principal, the bonding expenditure by the agent, and the residual loss (Jensen and Meckling, 1976).

Director Duality in Indonesia

In Indonesia, the duality position in the public service, where there is a relationship between a political party and state-owned enterprises, is always controversial. In the New Order periods (1968—1998), directors with a duality position in the three possible domains listed above were a common occurrence. Since 1998, the number of duality position has tended to decrease. This was because of an outcry from governance observers criticizing law makers and the government. In response to the critics, the government and the house of representative issued regulations prohibiting the duality position in several situations. For example, a legislative appointee is not allowed to have a duality position in a state owned enterprise, regional owned enterprise or an institution which is funded by the state budget¹. Nor is a Minister allowed to hold a duality position as: (a) another state official, (b) a commissioner and a director in the state-owned enterprise or private corporation, and (c) a leader of an organisation funded by the state budget²; and government officers are not allowed to become commissionaires and/or managers in state owned and regional owned enterprises³. The duality position

¹ Undang-Undang Nomor 32 Tahun 2004 Tentang Pemerintahan Daerah [Law No.32 of 2004 on Regional Government] (Indonesia) art 54(1)

² Undang-Undang Nomor Nomor 39 Tahun 2008 Tentang Kementerian Negara [Law No.39 of 2008 on State Cabinet] (Indonesia) art 23

³ Undang-Undang Nomor 25 Tahun 2009 Tentang Pelayanan Publik [Law No.25 of 2009 on Public Service] (Indonesia) art 17

in corporations is regulated more comprehensively by a guidance note established by the Commission for the Supervision of Business Competition which identifies the monopolistic practices and unfair business competition that could happen in a dual director and/or commissioner position⁴. The Ministry of State Owned Enterprise also prohibits a State Owned Enterprise' Director from holding duality positions at the same level in their corporate board and in other corporations⁵. In addition, Bank Indonesia, the central bank which regulates the financial sector, enacted rules that prohibit a director from holding another position as commissioner, director or executive officer at a bank, company and/or other institution⁶.

The State-owned enterprises in Indonesia follow a two-tiered board structure. As indicted above, the first board is called the board of commissioners or supervisory board which has an oversight function, including any proposal for appointing directors, and monitoring of operations. The second board is called the board of directors or management board which focuses on managing the operations of the company (Belot et al., 2014). In short, the main duty of the board of commissioners is to give advice and control to the board of directors, whereas the main duty of the board of directors is to be in charge of day-to-day activities.

Parent-Subsidiary Relationship and Director Response

A corporation needs to grow in order to sustain its business. Consequently, it will require more capital which frequently cannot be met by only the single owner. Thus, alternative financing originates from other parties (external financing), who do not intend to be involved in the company management, but are frequently available to invest in various schemes in the capital market. This is a characteristic of the modern corporation which was already conceptualized years ago by Berle and Means (1932) in the concept of separation of ownership and control. In time, the corporation may form a subsidiary company if situations arise, such as, anticipating the local changes and opportunities in the market and responding quickly; needing to delegate some authority to lower management; and developing succession plans for managers and directors for the next generation (Strikwerda (2003). Huston and Edward (2013) identify four common reasons why a corporation forms a subsidiary company. The first reason is a corporation develops a new line of business which is unrelated to current business. The second reason is a corporation develops a new business that carries risk which is unacceptable to parent. The third reason is that the shareholder has a specific reason, and the last reason is to shield a parent's assets. Even though the subsidiary is part of the parent company, it is a legally independent entity that is differentiated from the parent company.

In the context of parent and subsidiary relationships of State Owned Companies in Indonesia (BUMN) which follow two-tier board system, it is very common that the director of a parent company could also be appointed as a commissioner in a subsidiary company. In this case, therefore, board member duality would occur. An implication of board member duality constructed from the agency theory is that there is a difference in the interests of principal and agent, and a possibility in board decisions for a director to incur a conflict of interest. This situation raises the question of to whom will the agent give their loyalty: to parent company or subsidiary company.

Corporate law⁷ does not prohibit a director from serving as a commissioner in a subsidiary company. As a result, if a parent company has many subsidiary companies, then parent directors could hold more than one position as commissioner in its subsidiary companies. In fact, the tasks of director and

⁴ *Undang-Undang Nomor 5 Tahun 1999 Tentang Larangan Praktek Monopoli dan Persaingan Usaha Tidak Sehat* [Law No.5 of 1999 on The Prohibition of Monopolistic Practices and Unfair Business Competition] (Indonesia) art 26

⁵ *Peraturan Menteri BUMN Nomor PER-01/MBU/2012 Tentang Persyaratan dan Tata Cara Pengangkatan dan Pemberhentian Anggota Direksi Badan Usaha Milik Negara* [Ministerial Decree No. PER-01/MBU/2012 on Terms and Procedures for Appointment and Dismissal Director of the State owned Enterprises] (Indonesia) art 36

⁶ *Peraturan Bank Indonesia Nomor 8/14/PBI/2006 Tentang Amandemen peraturan bank Indonesia Nomor 8/4/PBI Mengenai Penerapan Tata Kelola Yang Baik bagi Bank-Bank Komersial* [Regulation of Bank Indonesia No. 8/14/PBI/2006 on amendment to Regulation of Bank Indonesia Number 8/4/PBI/2006 Regarding Impelmentation of Good Corporate Governance for Commercial Banks] (Indonesia) art 22

⁷ *Undang-Undang Nomor 40 Tahun 2007 Tentang Perseroan Terbatas* [Law No.40 of 2007 on Limited Liability Companies] (Indonesia) art 93 and art 110.

commissioner are different; director tasks are more focused on execution functions whereas commissioner tasks are more focused on oversight functions. This duality situation leads to some classic issues of corporate boards such as span of control, conflict of interests, dual roles, efficiency, and control. Will these positions potentially leverage the SOE's performance by aligning, accelerating, and arriving at a cost-efficient decision making process in both parent and subsidiary company? Or will the duality position holders abuse the position to promote their self-interest even if that means inflicting a financial loss to companies? And, are there predisposition or individual attributes of a director influence a director's response? The research questions, individual attributes, propositions, and hypothesis are presented in the next section.

Research Questions and Hypotheses

Research Questions

- Does the duality position as a director on a board in a parent company and as a commissioner in a subsidiary company impact on the agency cost of the SOEs?
- Can the individual attributes of respondents, namely gender, age, education and remuneration predict the dual director response in parent and subsidiary company relationship?

The level of agency costs was assumed to represent efficiency in corporate performance.

Research Propositions

- Dual directors use their experiences to the advantage of both companies;
- Dual directors tend to choose the interests of the parent rather than those of its subsidiary;
- Dual directors increase subsidiary performance.

Hypotheses

- That there is a significant difference between the dual director's responses. That director used their experience to the advantage of a) both boards; b) only the parent company; and c) only the subsidiary company.
- That there is a significant relationship between the dual director response and the demographics of the responding directors. Specifically, there is a difference due to a) gender predictor; b) the age predictor; c) the education predictor; and d) the remuneration predictor.

Methodology

This survey used a close-ended questionnaire which was grouped into 6 dimensions to explore: *ethics and integrity, costs and benefits of the board member duality, regulation of board member duality, role of board member duality, financial accountability, and leadership*. All of those dimensions are designed to explore the issues explored in the parent and subsidiary relationship. The survey uses a five point agree-disagree Likert scale to measure respondent's attitude to the topic (Komorita, 1963).

Questionnaire Development

The questionnaire development was adapted from the corporate integrity assessment instrument constructed by Ismail (2013); then the questionnaire draft was reviewed by experts from the corporate governance and corporate board members in the departments responsible for state owned enterprises in Indonesia. In order to get a significant number of respondents who were willing to respond to the survey, the questionnaires were made into three versions: the first was a hardcopy questionnaire version, the second is softcopy questionnaire version, and the third is on-line survey questionnaire version. The *Qualtrics on-line survey software*⁸ is was used for the third version.

⁸ Qualtrics is a company running business in research software, based in Provo, Utah USA. The qualtrics on-line survey software enables researchers to undertake various online data collection and analysis.

Population and Sample Selection

The total number of state-owned company in Indonesia was 139 companies⁹ which comprise 74 parent companies and 65 stand-alone companies¹⁰. The total subsidiary companies retrieved from <http://bumn.go.id/halaman/240/Profil.BUMN> were 270 companies¹¹. The total corporate board members for all those companies are estimated about 2,510¹² members. The details of the corporate board member population is shown in table 2 below.

Table 2 Corporate Board Member Population

No.		Companies	Directors	Commissioner	Total
1.	Parent Companies	74	399	366	
2.	Stand Alone Companies	65	207	188	
3.	Subsidiary Companies	270 [*])	810 ^{**})	540 ^{**})	
	Sub Total	409	1,416	1,094	
	Total board members		1,416	1,094	2,510

^{*}) There is no formal disclosure about the number of subsidiary owned enterprise; ^{**}) estimated figures

The sample for the survey was 496 respondents which covered shareholders, directors and commissioner in both parent companies (375 respondents) and their subsidiary companies (121 respondents).

Distribution Process and Response Rate

The distribution of the survey basically used both off-line and online methods. The off-line method comprises fax (35 copies), courier (296 copies), and soft-file (5 files). Using the off-line method, out of 336 respondents, 101 respondents answered the survey questionnaires completely. The response rate for the off-line method was 30.06%. Online methods enable respondents to answer the survey questionnaires by internet. Using the online method, out of 160 respondents, 24 respondents answered the survey questionnaires completely. The response rate for the on-line method was 15% which is half of the off-line method response. This means that respondents still prefer to use an off-line method than the on-line method in answering the survey questionnaires.

Data Analysis

Primary data produced from the survey based on the off-line method was duplicated and sent to a temporary dummy e-mail addresses created earlier. Then, the duplicate results were inputted to the *qualtrics online survey software* combined with the online results. Statistical procedure using non-parametric statistics (since the data are nominal) analysed the nominal data comprising the questionnaires exploring the role of the dual director grouped into gender, age, education, and average monthly income. Total respondent who completed the survey is 135 respondents who have a position as corporate board member, either director or commissioner in parent company, subsidiary company, and in both parent and subsidiary company in the state-owned enterprise in Indonesia. The individual attributes of respondent were the predictors of the dual director response. The composition of each predictor was as follows:

1. Gender

Total respondent is 135 directors and/or commissioners comprising 125 males (93%) and 10 females (7%) who served in parent company, subsidiary company, and in both parent and

⁹ Position per 31 December 2013, Position per 31 December 2014 is 119 SOEs

¹⁰ Stand-alone companies mean that the company does not have a subsidiary.

¹¹ There is no formal disclosure about the number of the subsidiary owned enterprise.

¹² This figure is a prediction because of lack information of corporate board member for subsidiary companies.

subsidiary company. The total number of respondent gender based on the company in where their serve as director and/or commissioner is presented as follows: (1) Parent company: 94 % male, 6% female; (2) Subsidiary company: 92% male, 8% female; and Both Parent and subsidiary company: 94% male, and 6% female.

2. Age

Total respondent is 135 directors or commissioner comprising 85 respondents (63%) who have age between 50—60 years old, 41 respondents (30%) who have age between 40—50 years old, 7 respondents (5%) who have age above 60 years old, 2 respondents (1%) respondents who have age between 30-40 years old.

3. Education

Total respondent is 135 directors or commissioner comprising 85 respondents (63%) who have a master degree, 42 respondents (31%) who have a bachelor degree, 8 respondents (6%) who have a doctoral degree.

4. Remuneration

Total respondent is 135 directors or commissioner comprising 57 respondents (42%) who have average monthly income between US \$2,000.00—5,000.00, 43 respondents (32%) who have average monthly income between US \$5,000.00—10,000.00, 26 respondents (19%) who have average monthly income between US \$10,000.00—20,000, 4 respondents (3%) who have average monthly income, 1 respondents (0.74%) who have average monthly income between US \$20,000.00—25,000, 1 respondent who have average monthly income above US \$25,000.00, and 3 respondents (2%) who kept average monthly income is confidential.

Results

The results of the survey regarding the dual director responses against four predictors, namely gender, age, education and remuneration as the response predictors using the level of confidence 95%, or $\alpha = 5\%$, is summarised in Table 3.

TABLE 3 THE SIGNIFICANT LEVEL OF THREE PROPOSITIONS AGAINST THE FOUR PREDICTOR VARIABLES

	GENDER	AGE	EDUCATION	REMUNERATION
5. <i>Dual directors use their experiences to the advantage of both companies</i>	Not Significant	Not Significant	Not Significant	Significant P-Value = 0.00 X ² = 59.33 DF = 24
6. <i>Dual directors tend to choose the interests of the parent rather than those of its subsidiary</i>	Not Significant	Not Significant	Not Significant	Significant P-Value = 0.03 X ² = 39.27 DF = 24
7. <i>Dual directors increase subsidiary performance</i>	Significant P-Value = 0.01 X ² = 12.44 DF = 4	Not Significant	Not Significant	Significant P-Value = 0.00 X ² = 69.59 DF = 24

From the Table 3 above, it can be concluded that:

Proposition 1

“Dual director use their experience to the advantage of both companies”;

The relationship between dual director response in the proposition 1 and the predictors which has **P-VALUE <0.05**, is only the remuneration i.e. **P-VALUE =.0.00, X² = 59.33, AND DEGREE OF FREEDOM (DF) = 24** which is nearly the normal distribution. Thus, the results will reject the Null Hypothesis, meaning *that there is difference between the dual director response of the proposition 1 and the remuneration predictor.*

On the other hand, since the gender, age, and education have **P-VALUE > 0.05**, then the results will accept Null Hypothesis meaning *that there is no significant difference between the dual director response of the proposition 1 and the three predictors, namely gender, age, and education.* The deviation is too small that chance alone accounts for it.

Proposition 2

“Dual directors tend to choose the interests of the parent rather than those of its subsidiary”;

The relationship between dual director response in the proposition 2 and the predictors which has **P-VALUE <0.05**, is only the remuneration i.e. **P-VALUE = 0.03, X² = 39.27, AND DEGREE OF FREEDOM (DF) 24** which is nearly the normal distribution. Thus, the results will reject the Null Hypothesis, meaning *that there is a difference between the dual director response of the proposition 2 and the remuneration predictor.*

On the other hand, since the gender, age, and education have **P-VALUE > 0.05**, then the results will accept Null Hypothesis meaning *that there is no significant difference between the dual director response and the three predictors, namely gender, age, and education.* The deviation is too small that chance alone accounts for it.

Proposition 3

“Dual directors increase subsidiary performance”

The relationship between dual director response in the proposition 3 and the predictors which has **P-VALUE <0.05**, is gender and remuneration. The gender predictor has **P-VALUE =.0.01, X² = 12.44, AND DEGREE OF FREEDOM (DF) = 4**, whereas the remuneration predictor has **P-VALUE =.0.00, X² = 69.59, AND DEGREE OF FREEDOM (DF) 24** which is nearly the normal distribution. Thus, the results will reject the Null Hypothesis, meaning *that there is difference between the dual director response and the two predictors, namely gender and remuneration.*

On the other hand, since the age, and education have **P-value > 0.05**, then the results will accept Null Hypothesis meaning *that there is no significant difference between the dual director response of the proposition 3 and the two predictors, namely age, and education.* The deviation is too small that chance alone accounts for it.

Discussion

The appointment of a parent company director to also serve as a subsidiary company commissioner (the board member duality) is intended to represent the parent company as a shareholder in its subsidiary company. Citing Biao et al. (2012) that there needs an interactive mechanism of control for the parent company regarding the two basic functions of parent company in regard to the subsidiary company, namely creating value and loss prevention, the board member duality as Widodo (2012) proposed as a new terminology, may offer the alternatives to what Biao et al. (2012) argue. However, this structure may be prone to the conflict of interest that Major et al. (1986) identified the three possibilities of director's duties that may give rise to conflict are: "the duty to act bona fide in the best interest of the company"; "the duty 'to have regard, among other things'", and "the duty to carry on the company' business" (the reasonable prospect rule). The three possibilities of conflict of interest mentioned above have a relatively positive connotation, in the sense that the conflict of interests may occur in the area of corporation and stakeholder scope, such as the availability of option and priority taken into consideration for the process of management decision making. Major et al. (1986) did not specify the individual/self-interests in those three possibilities of conflict of interests, which refers to the negative conflict of interests. The individual/self-interests is explored more comprehensively in Principal Agent Theory as the theory used in this study, in the sense that it could occur that individual/self-interests of the agent (director) may differ from the principal (shareholder) goals (see Jensen and Meckling (1976).

Remuneration Predictor. The board remuneration is the financial reward given to director and commissioner in order to motivate and leverage the firm performance (Talha et al., 2011). In SOEs, the remuneration of director and commissioner are obliged to follow the standard set by the Ministry of State Owned Enterprises. The finding of this study show that the board's remuneration is the best predictor of the dual director response for all propositions (1,2,3). Even though the finding reveals that the remuneration is the best predictor for the dual director response, however, it raises the possibility that higher remuneration will impact against the higher corporate performance. This perception is not always true as Brick et al. (2006) argue that excess income was associated with the underperformance of corporates, and also found evidence that excessive compensation is due to mutual back scratching or cronyism.

This finding also contradicts what Krauter and da Sousa (2013) found, that the hypothesis that there is a positive and significant relationship between executive compensation and company performance, was not supported; and Gill (2014) found that the remuneration-performance sensitivity and elasticity were weak. This contradictory results might be caused by the level of accountability of the executive compensation and scheme in selected ASEAN countries (see Talha et al. (2011) and differs from what Krauter and da Sousa (2013) and Gill (2014) found in their research. Talha et al. (2011) highlighted the director's remuneration in selected ASEAN countries needs disclosure, the shareholders' approval, the separation of CEO and chairman, and, the maximum length of period offered to director. In short, this preliminary finding need further research on the financial accountability of the board member duality compensation in parent and subsidiary of BUMN in Indonesia.

Gender Predictor. Interestingly, in proposition 3 that "the dual director increases subsidiary performance", not only the remuneration but also gender become the best predictor variables. Unfortunately, the proportion of female respondents was small. Only 7% of the respondents were female. The gender issue in a corporate directorship attracts researchers to investigate whether there are performance differences if women are given more chance to be a corporate board member. Farrell and Hersch (2005) and Daily et al. (1999) noted that the number of women who are appointed as directors increase significantly during the decade of the 1990s'. This trend is also found by Bilimoria and Piderit (1994) who investigated the specific view related to the "Effects of sex-based bias". The increase in women seated as corporate board members is not merely because of gender equality, but recent research shows that companies having an increased number of women on corporate boards

experienced higher corporate performance (see Lückerath-Rovers (2013), Liu et al. (2014), and Post and Byron (2015).

Age Predictor. There was no significant difference between the dual director response and the age predictor. The majority of respondents have age between 50—60 years (63%) old and if combined with the age between 40—50 years (30%) is equal to 93% which is relatively still in the productive age. Thus, the robust negative relationship between age of chairmen of the board and firm performance which was mainly influenced by the deterioration of cognitive ability and shifting in motivation found by Waelchli and Zeller (2013) and Taylor (1975) does not occur in the board member duality of parent and subsidiary relationship in the State-owned Enterprise in Indonesia.

Education Predictor. The education predictor does not have a significant level of support for any of the dual director propositions. The Level of education is very often used as a pre-condition requirement of the corporate board candidate in selection and as a proxy for formal knowledge. The experience of the candidates usually is more preferable than the education. This is consistent with what Ladegard et al. (2013) concluded that experience of the director candidate played a more central role in performance than formal knowledge.

In summary, the preliminary findings of the survey which investigated the best predictor of the dual director response on the three propositions in parent and subsidiary relationship in the State-owned Enterprise in Indonesia, namely: (1) dual directors use their experiences to the advantage of both companies; (2) dual directors tend to choose the interests of the parent rather than those of its subsidiary; and (3) dual directors increase subsidiary performance, based on the individual attributes of respondents, concludes that the remuneration is the best predictor for all propositions.

The gender predictor is also the best predictor for the third proposition, that “the dual directors increase subsidiary performance”. If, the finding holds true, then the research on the financial accountability of the board member duality in the State-owned Enterprise in Indonesia needs further research.

In addition, the number of female directors and/or commissioners should be increased, because several studies have shown that an increased number of female directors will impact positively on corporate performance. However, this survey only analyses the respondent’s attitudes, so that the additional method which compares the survey results with secondary data extracted from their financial reports should be carried out in order to draw accurate conclusions.

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Community Development as a CSR Strategy for Sri Lanka

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ABSTRACT

The purpose of this paper was to investigate the corporate social responsibility (CSR) practices related to community development (CD) by Sri Lankan companies. This article investigated CSR practices related to community development in Sri Lanka from secondary data in websites, integrated reports and sustainability reports from a sample of 30 companies in the top 50 Companies in the Sri Lanka's LMD 100 for the year 2013. Descriptive statistics were employed to investigate the reporting practices. Community development practices of the top 10 companies were investigated in-depth using content analysis. Results showed that 90% of the companies reported their CSR activities, and were moving towards integrated reporting. The majority of the CSR related CD practices were conducted to improve the quality of lives of people living in rural areas and they were mainly to provide better education, health facilities and livelihood development. However, education was the top most priority by the companies. In-depth analysis of this study is limited to the top 10 companies in the LMD 100 which are ranked among the most respected companies. This study implies that education is a top most priority among CSR practices in Sri Lanka because it improves the living standards and also contribute to economic development. This paper contributes to understanding the community development practices in developing countries in which a corporate sector should engage as their CSR if they are to have a strong impact on economic development.

Keywords

Corporate Social Responsibility, Community Development, Stakeholder Theory, Sri Lanka

Introduction

Community Development (CD) is an important aspect of corporate social responsibility (CSR) in developing countries. It can have a strong impact on economic development and enable social change through economic empowerment, reduced inequality and improvement in the health and welfare of the those socially excluded in the population (Werner, 2009). Rural communities form a large part of societies in developing countries and are considered poor (Heenetigala, 2011). Much economic development in rural communities, in both emerging market countries and developing countries, is hampered as a result of internal conflict, ethnic wars and floods. As a result, communities in rural areas are unable to reach a higher quality of life as well as lower access to education, medical and social assistance and under-developed infrastructure (Akresh, Lucchetti, & Thirumurthy, 2012; Dupas & Robinson, 2012; Van Niekerk, 2012).

Even though this is the responsibility of the governments of the countries, lack of resources has left this gap to be covered by the private sector organisations (Kolk & Lenfant, 2010; Valente & Crane, 2010). Furthermore, profits from businesses do not go to the poor directly from taxes as government

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revenue for the development of public services and infrastructure (Werner, 2009). Werner concluded that, leaving the development of communities to NGO's or other development agencies has little impact on the development. Attention of private sector companies to their CSR strategies has had an impact on the social status of socially excluded populations (Muthuri, Moon, & Idemudia, 2012;

Werner, 2009). It creates more jobs, better educated and healthy rural population who previously did not have access to health, education and training facilities. Muthuri et al. (2012) refers to work of Hamann, Woolman., and Sprague (2008) and Idemudia (2007) which states that companies in developing countries provide a range of social initiatives for the local communities such as health care, education, economic welfare, infrastructure development, communication and environmental protection. Hence, a community is an important stakeholder of a company operating in a developing country. The aim of this study was to investigate CSR related community development practices conducted by the corporate sector in Sri Lanka. .

CSR and Community Development

CSR has been referred to as “how companies mitigate any negative impacts, while at the same time maximizing the positive influences that their businesses have on society, the environment and the financial well-being within their communities of influence” (Fisher, Greenen, Jurcevic, McClintock, & Davis, 2009).

The World Business Council for Sustainable development (WBCSD) developed their definition for CSR based on the CSR dialogue with eight countries from developed and developing countries. Developed countries base their definition on corporate strategy and future generation, whereas developing countries emphasize CSR is related to community which has an impact on the economic development. As a result the following definition was developed at the CSR dialogue in the Netherlands in 1998:

‘Corporate social responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large’. (WBCSD, 1998).

In order to understand the role CSR plays in community development, it is important to define community. According to Ismail (2009 p 203) a community is “a group of people sharing a common purpose, who are interdependent for the fulfillment of certain needs, who live in close proximity and interact on a regular basis”. However, in the current society, identifying a community is a complex and contested task, due to the shared traits such as geographical territory, religion, culture, history, kinship etc. As well, people may have multiple and overlapping identities which can change overtime. As a result, definition of a community is a construct (Kapelus, 2002).

Ajayi (1995) considers community development is a process by which human beings can become more competent to live with and gain some control over local conditions and the changing world. Therefore, community development is a process by which the efforts of the people themselves are linked with those of the government to improve the socio-economic and cultural conditions of the community, thus enabling them to contribute more fully to national progress (Obibuaku, 1983). Accordingly, Ismail (2009 p 203) refers to Community development as the “initiatives undertaken by a community with partnership with external organisations or corporations to empower individuals and groups of people by providing these groups with the skills they need to effect change in their own communities”.

The key purpose of CSR in a community is to “ work with communities experiencing disadvantages, to enable them to collectively identify the needs and rights, clarify objectives and take action to meet these within a democratic framework which respect the needs and rights of others” (Ismail, 2009 p 204).

As a result of globalization, investment in developing countries has brought much attention to corporations responsibility to the local communities in which they operate. Mining operations can adversely affect the local communities as a result of degrading environment, diminishing livelihood prospects as well as displacing them from their homes (Kapelus, 2002). Few studies have been

conducted in relation to mining companies operating in developing countries (Ite, 2007; Kapelus, 2002). These studies show that corporations are recognizing their responsibilities towards local communities in relation to their rights, values and customs and are incorporating them in their decision-making. Introducing community development programs can benefit the local communities and reduce the negative impact of mining operations to some extent. In the case of the Ok Tedi Mine in Papua New Guinea, mining contributed to about 20% of the export income, provided employment for thousands of people, investment of \$ 300 million in infrastructure such as roads, power, water, communications, schools and medical facilities, education and training for over 1500 people, infant mortality rate declined from 33% to 3%, improved health increased the life span from 30 to 50 years. It also expanded the educational opportunities for children, established school building and provided small business assistance. Therefore, closing the mine for its negative externalities was not a solution as it was important to economic and social welfare resulting in community development for Papua New Guinea (Australian Graduate School of Management, 2014).

In exploring the issue of CSR, the World Business Council for Sustainable Development (WBCSD) discussed the importance of company involvement and investment in the local community (WBCSD, 1998). This was highlighted in the study conducted by Holme and Watts (2000) that in order to protect the community the company provided skills training and proper health and safety systems. In context of Sri Lanka, engagement of corporate sector in community development is an area currently under researched, requiring further attention.

Context of Sri Lanka

Sri Lanka is a developing country that emerged out of 30 years of civil war in 2009. During this period a large percentage of the budget was allocated to war expenses which deprived the country of resources for economic development. According to the World Bank (2014) around 80% of the population in Sri Lanka lives in rural areas and 90% are considered poor (World Bank, 2010). Even though raising the standard of living is the responsibility of the government of Sri Lanka, they do not have the capacity to reach the poor due to the income deficit in their budgets. As a result, the World Bank, NGO's and voluntary organisations are providing support for community development.

In 2013, a revision to the 2008 code of best practice on corporate governance was issued by SECSL and ICASL. (2013). Principle G of the code refers to sustainability reporting. Principle G1.4 states "society governance encompasses support for and building a relationship with the community and striving for sustainable development including responsible public policy participation, fair competition and responsible community involvement" (SECSL & ICASL., 2013 p 26).

However, in Sri Lanka, basic compliance and enforcement of laws is weak. Therefore, CSR as a corporate strategy that goes beyond legal compliance can have significant positive effects on the poor and minimize negative externalities (Werner, 2009).

CSR and Community Development in the Sri Lanka

Voluntary and Non-Government Organisation Involvement

In Sri Lanka, voluntary organisations play an important role in providing the basic human needs such as day care centres, nursery schools, health clinics, homes for destitute children and homes for the elderly; they also provide vocational training, non-formal education and sports and recreation programs. They operate rural development projects and community self-help programs providing social overhead capital such as roads, water tanks, irrigation canals, sanitation facilities and wells (Perera, 2001).

Many community development projects are also being carried out by Non-Government Organisations (NGO). Sarvodaya Shramadana Movement is the largest people's organization in Sri Lanka. It has reached the poor rural communities through rural community development programs throughout the island. They are currently involved in resettlement, reconstruction and reconciliation activities in the war affected North and East of Sri Lanka. Among the many community development programs they carry out are community capacity building, education, health, empowerment of women, entrepreneur development (Sarvodaya, 2014). Among other projects were Gemi Diriya project which enabled poor to improve their livelihood and quality of life through their various programs for skills development and employment (World Bank, 2010), Sevalanka, provides micro- finance to community organisations and rural entrepreneurs (Sevalanka Foundation, 2014) and Community Development Centre work to improve the livelihood of rural population through conservation of indigenous tuber varieties using seed banks managed by women-led self- help groups (UNDP, 2012).

Government organisations such as Economic Development Ministry has launched a special program and have trained over 1825 people under their Community Development and Livelihood improvement project (Ministry of Economic Development, 2014).

Corporate sector involvement in CSR and Community development

Sri Lanka has a long history of corporate philanthropy. Charitable activities performed by the business communities to support various needs of the society is not a new concept in Sri Lanka (Ariyabandu & Hulangamuwa, 2002). The impact CSR has on economic development has resulted in Sri Lanka's corporate sector organisations including CSR in their strategy is evidenced in the annual reports of listed companies in Sri Lanka.

Ariyabandu and Hulangamuwa (2002) categorize the main forms of CSR activities observed in Sri Lanka as philanthropic and charitable activities, environmental conservation, public awareness and corporate sponsorships (Ariyabandu & Hulangamuwa, 2002). Many companies are engaged in CSR activities related to community development, due to the fact that CSR related activities provide competitive advantage and corporate reputation leading to better performing share prices (Husted & Allen, 2007). The CSR activities companies are engaged in Sri Lanka are related to education, health, unemployment, entrepreneur development, employee welfare and provision of infrastructure facilities. There are others who concentrate on environmental issues such as reducing the pollution associated with poverty, reduction of greenhouse gas emissions and cleaning beaches. The activities that relate to rebuilding the communities in Sri Lanka includes support educational needs, health and environmental issues, housing, providing entrepreneurship programmed and vocational training to youths to reduce unemployment. Improvement of local living conditions by providing water and sanitation are also included (Heenetigala, 2011).

The report from the survey conducted by International-Alert (2005) also states that the reasons for engaging in CSR activities in Sri Lanka were reported as image building, long-term benefits to current investment and a transparent relationship with society in dealing with controversial products. In 2007, 75% of the top fifty listed companies in Sri Lanka disclosed their CSR initiatives in their annual reports (Heenetigala, 2011). Fernando (2007) states that according to a survey conducted by International Alert in 2004, 73.2% companies had a CSR policy, and 17% of those, had a formal written policy with 84.1% of the companies engaged in CSR because they genuinely contributed to the betterment of society.

Today, corporate sector in Sri Lanka and around the world is engaged in corporate social responsibility activities as a part of their corporate strategy, because CSR is considered "an important tool to maximize the positive development impact of corporations and community development activity in the developing world" (Werner, 2009). Private sector participation in sustainable community development enhances their social status and competitive edge which is important to their existence (Moon, 2007).

Theoretical Perspective of CSR and Community Development

Based on the impact that the community development has on organisations, this study considers the importance of corporate social responsibility activities related to community development. Community is a major stakeholder who can substantially affect or be affected by the activities of others (Jensen, 2001). Therefore, the theoretical perspective of this research is based on the stakeholder theory. According to the view of stakeholder theory a corporation is a social entity and affects the welfare of many people who are considered to have a stake in the organisation (Donaldson & Preston, 1995; Freeman, 1984). They can be instrumental in the success of the corporation and have a moral and a legal right to have their claims recognised (Donaldson & Preston, 1995). Therefore, the claims of the stakeholders should be considered in their decision-making, because it enhances efficiency (Turnbull, 1994). Accordingly, those companies that are proactive establish necessary governance structures and integrate stakeholders concerns in their decision-making process (De Wit, Wade, & Schouten, 2006). These firms go beyond their financial responsibility and consider the impact of environmental and social aspects of their operations on society (Spitzeck, 2009).

A stakeholder theory perspective redefines the purpose of business and its method of responding to non-economic factors. From this perspective there are a number of stakeholders among which community is also important. Therefore, proponents of stakeholder theory argue that it is appropriate to sacrifice excess profits in the public interest (Rahim, 2011).

Clarkson (1995) identified two categories of stakeholders, who are considered as the primary and secondary stakeholders. Primary stakeholders are those that are essential to survival of the firm, whereas the secondary stakeholders are those that influence or are being influenced by the firm. Therefore, according to Adewuyi and Olowookere (2010) a community is a stakeholder in both categories.

The stakeholder model introduced by Heenetigala (2011) states that directors' accountability extends to all stakeholders who are directly or indirectly affected by the actions of the firm. Key features of the model in that study was that CSR of the firms that operate in Sri Lanka should focus on developing the communities in which they operate. As stated above, 80% of the population that lives in rural areas are considered poor. They lack basic infrastructure and facilities to improve their living standards. Therefore, firms and communities can benefit through the development of these communities and gain new markets, increase financial performance and obtain higher market value for the shares, and communities can benefit from economic development.

The stakeholder versus shareholder model (Heenetigala, 2011) suggests that CSR initiatives focused on lower income communities can improve their living standards resulting in increased performance of companies in the long term. As a result, the corporate strategy of boards needs to incorporate CSR strategies directed at the rural disadvantage communities to create jobs and improve income for socio-economic development.

Methodology

As discussed in the above, corporate sector involvement in community development practices as a CSR strategy can have a strong impact on improving the living standards and performance in the long term. To investigate the CSR practices related to community development in Sri Lanka, this study explored a sample of 30 companies from the top 50 listed companies in the Sri Lanka's LMD 100 for the year 2013. The companies selected were at the top rank based on their annual turnover. The companies were also ranked among the most respected companies in Sri Lanka. The ranking of the most respected companies was based on the opinions expressed by respondents through a survey conducted by Nielsen to find out why they perceived them as being the 'most respected' by their peers in the commercial capital.

The data were collated from secondary data disclosed in annual reports published on websites of companies. Websites of the 30 companies were examined for evidence of CSR reporting, whether they had a sustainability report, an integrated report, or if they reported their CSR in their website, as well as their community development practices related to CSR. The top 10 companies were examined in-depth to understand the CSR related community development practices. Information related to CD practices was reported under the themes of education, health, employment, community/livelihood development, disaster relief and corporate philanthropy. This is a qualitative study using content analysis to analyse the CSR information reported in websites as well as sustainability reports and integrated reports. Content analysis is a “set of procedures for collecting and organizing information in a standardized format that allows analysts to make inferences about the characteristics and meaning of written and other recorded material” (United States General Accounting Office, 1989 p 6). This methodology also helps to summarize the material by listing or counting the issues or statements, which has been addressed in the next section.

Analysis of CSR activities in Sri Lanka

Investigation of websites of companies in the sample revealed that 87% of the companies reported CSR activities through their websites, integrated reports and sustainability reports. CSR practices were reported in their websites by 40% of the companies, 66.67% had an integrated report, 10% had a separate sustainability report and 3.3% reported on the website as well as in the integrated report or sustainability report. This shows that the current trend is moving toward integrated reporting.

Over 73% of companies reported that they conducted CSR related to community development. CD practices of companies in the sample revealed CSR related community development practices varied from education, health, sanitation, clean water, infrastructure, entrepreneurial development, disaster management and employment..

Education, health and community and livelihood development activities were among the top community development practices conducted by the companies in Sri Lanka. As reported earlier, Sri Lanka is a developing country and 80% of the people live in rural areas and 90% of them are considered poor. However, according to UNICEF (2013) Sri Lanka reports a literacy rate of 91%, which is considered high for a developing country. As reported by Matten and Crane (2005) education is a major activity conducted by Toyota to be considered a good corporate citizen. CSR related to community development in Sri Lanka is also geared towards education which is also the reason for high literacy rate.

Eight out of the ten companies investigated reported on CSR initiatives in education. Education is considered important even among the poor people living in rural areas in Sri Lanka. Analysis shows that English education and IT is considered the top most priority among the companies. IT skills and English literacy is considered important for employability in the private sector as well as the public sector. Among other initiatives to promote education are infrastructure facilities for schools such as building class rooms, IT labs, sporting facilities, toilets, water filtration system and library facilities. A study conducted by Anthonisz (2008) reported companies in Sri Lanka provided scholarships, educational infrastructure and English language training for rural students.

Many companies also provided scholarships for outstanding under-privileged university students and for those studying for Ordinary level and Advanced level exams. The impact of education uplifts the socio-economic prospects in life, with trickle down effects to the entire society (Expolanka Holdings Plc, 2013). This confirms a previous findings in a study conducted by Jamali (2008) that CSR in a developing country context, education and learning programs were reported in their community investment related to CSR.

Nine of the ten companies that were examined in the sample carried out community/livelihood development projects. These CSR projects varied in their context. Different types of livelihood projects were carried out by the companies. They included cashew farming, milk collection, promoting home growing and gardening, use of local supplies and local services, provided support for farmers to

increase productivity and training farmers on best practices in crop and animal agriculture. Some companies provided empowerment programs for women and employment of women as well as micro-finance for villagers and entrepreneurship programs. Among others were, building water tanks, providing electricity, donation of houses and sporting activities.

Table 1: CSR Related Activities Conducted by Companies in Sri Lanka

Themes	Type of Activity
Education	<ul style="list-style-type: none"> • English Language education • Scholarship programs • Soft skills to enhance employability of local graduates • IT training, facilities and infrastructure • Infrastructure for schools • Donation of books to students • Providing opportunities for rural children to demonstrate their talents in art, speech, essay writing, singing and drama through competitions • Financial assistance for uniforms and books
Health	<ul style="list-style-type: none"> • HIV and AIDs campaign • Vision projects (Eye testing camps and donation of spectacles) • Donation of medical equipment to rural hospitals • Refurbishment of rural hospitals • Healthcare centres • Free consultation and medicine • Health Camps (general health, diabetes, cancer, AIDs, dengue, oral hygiene, checkup for children and free prescription medicine) • Dengue eradication programs • Blood donation campaigns • Dental clinics • Immunisation programs
Employment	<ul style="list-style-type: none"> • Employing locally, senior management and team members for their operations in the local areas.
Community/ Livelihood Development	<ul style="list-style-type: none"> • Programs for empowerment and employment of women • Building of rainwater harvesting tanks and Renovate water tank • Providing drinking water • Mobile water treatment plant • Water solutions to various schools around the island • Water, sanitation and other health related services • Hot water showers and water dispensers to ayurvedic hospital • Livelihood development and capacity building programs • Microfinance self-employment projects • Milk collection projects • Entrepreneur training programs • Promoting home growing/gardening • Donating seeds and fertilizer and agri equipment • Training farmers on best practices in crops and animal agriculture • Providing credit, infrastructure and transpor for farmers • Integrate business to community supply chain • Support micro and sole industry producing recycled paper products with low cost raw material • Provide electricity • Donation of tricycles for small scale vendors • Donation of houses for poor • Sourcing of vegetables, fruits, fish and meat within the community. • Use of local suppliers for vehicles for safari • Providing hearing aids for less fortunate children • Housing for plantation workers

	<ul style="list-style-type: none"> • Commitment to improve sports activities such as volley ball, football and cricket • Providing refreshments for pilgrims • SMS service for blood donor service
Environment	<ul style="list-style-type: none"> • Programs to raise the awareness on the need to protect the environment and biodiversity, eco-friendly practices and the importance of co-existing in harmony with the environment for school children and other interested groups • Paper conservation projects – waste paper collection, shredding and recycling: Aim is to save trees and reduce waste paper ending in landfills • Reduce using polythene bags in supermarkets and replace with reusable bags • Collection of plastic bottles for recycling • Providing solar power for selected number of villages: sustainable energy initiatives
Arts	<ul style="list-style-type: none"> • Support the annual fair to display and sale of art by artists around the island • Launched the first digital art gallery for Sri Lankan artists to show case their work at Sri Lankan art gallery • Support Sunera Foundation, a program aimed at fostering aesthetic talents of school children in national schools and also recognizing and rewarding for their skills
Disaster Relief	<ul style="list-style-type: none"> • Flood relief initiatives • Initiatives to assist internally displaced people 2009-2010 • Tsunami Relief • SMS service for flood disaster • Provide drinking water, sanitation facilities, food and clothing for internally displaced • Mobile water treatment plant
Corporate Philanthropy	<ul style="list-style-type: none"> • Holding medical camps • Blood donations campaigns • Donations of medical items and other supplies to Hospitals • Donation of school supplies such as school bags, bottles • Visit to cancer hospital children's section with gifts, sweets, entertainment and medication • Lending a hand to elders, time with children in orphanages, donation to Kidney protection society, help differently able persons, donation of bicycles to school children, support education of rural schools through contribution of stationery • Identify young sports talent and support them

Five out of ten companies reported on the health initiatives by companies. Among the health programs, they conducted were, HIV and AIDs awareness, eye testing, dental clinics, immunization for children campaigns, hospital refurbishment and free health clinics for people in rural areas.

Community development efforts by the companies are geared towards supporting the rural communities to improve and maintain their capabilities and to sustain their socio-economic progress and quality of life of the people living in the poor rural communities.

To a lesser degree companies were carrying out programs supporting art and fostering aesthetic talent among children in village schools. They were also providing relief for internally displaced people from North and East. These include food, clothing, water and sanitation. They also provided flood relief programs for effected flood victims and also created blood donor SMS and flood disaster SMS service.

It can be seen from this research that the key areas of CSR related community development are economic empowerment, human capital development, healthy living and provision of basic services by the companies in Sri Lanka. The following table shows the CD activities related to CSR that has been carried out by the private sector in Sri Lanka.

Community is a major stakeholder especially in developing countries such as Sri Lanka. The rural community is a major part of the population in Sri Lanka which lacks of facilities such as

infrastructure, education, healthcare and training to improve their level of income. Therefore, corporations' responsibilities to consider these stakeholders in their business strategies is important, as it can have a significant impact on the rural communities, increase in the demand for their products and services and on the corporate performance.

Therefore the companies that operate in Sri Lanka must listen to the needs of the rural communities in which they operate, because they make a large part of Sri Lanka's population and their ability to participate in the democratic political process is also influenced by not only their level of literacy but also their level of general education and their economic empowerment.

Conclusion

The findings of this study showed that the companies in Sri Lanka are moving towards integrated reporting and that the majority of the companies conducted CSR related to community development. Community development practices related to education, health and livelihood development activities were among the most important CSR practices that were conducted by the corporate sector. Companies that provide community related CSR in developing countries are considered good corporate citizens. In this context good corporate citizen not only must meet the legal, ethical and economic responsibilities placed on them, they must aim to create a high standard of living and quality of life in the communities in which they operate. It is only through this, that companies can create value for shareholders. Inclusion of CD in the business strategies can have a strong impact on the performance of private sector companies.

This study also shows that education is a high priority in Sri Lanka. As a result CSR strategies of the corporate sector concentrate on education as well as providing infrastructure for educational institutes in rural areas.

Companies that provide education, health facilities, employment and training and support community/livelihood development projects will be able to increase the share of the market for their products from the communities they develop as well have a positive impact on economic development of the country. In Sri Lanka, rural communities face many challenges due to lack of well-developed infrastructure that negatively affect the quality of lives of people which needs to be addressed by the governments. However, this study shows that the corporate sector is impacting the economic development to some extent through their CSR programs especially the community development component.

It can be concluded that corporate social responsibility policies such as education, health and community livelihood activities are adopted by companies not only because they are socially desirable, they also have a strong impact on the business. Therefore, in the context of Sri Lanka, companies need to identify the social demands of the communities and address those in their CSR strategies for development of the rural communities.

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