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Managerial Conflicts of Interest: Heterogeneous Sustainability Outcomes Through Actions Directed at Primary and Secondary Stakeholders

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ABSTRACT

This paper investigates whether firms' sustainability actions aimed at serving multiple stakeholders lead to similar or differing sustainability outcomes depending on the manager's stakeholder focus. It proposes a conceptual framework distinguishing between primary and secondary stakeholders, wherein managers can face conflicts of interest when aligning their actions with the preferences of these different stakeholder groups. Findings indicate that firms whose managers prioritize secondary stakeholder preferences experience better sustainability outcomes but worse financial performance, while the opposite is true for primary stakeholders. Supporting our theory, these findings shed new light on the often-debated question of why sustainability efforts do not consistently lead to improved financial performance. They also align with policy efforts to improve transparency on non-financial sustainability outcomes and highlight an ethical dilemma for managers when they have to trade off different outcomes.

1 | Introduction

This paper investigates the following research question: Do firms' sustainability actions aimed at serving multiple and diverse types of stakeholders result in heterogeneous sustainability outcomes depending on the manager's stakeholder focus? This question is important, as firms with multiple and diverse stakeholders with different kinds of influence (Thijssens et al. 2015) present a challenge to managers, who must formulate a coherent strategy that aligns the firm's sustainability practices with the often-varying interests of its stakeholders (Aghion et al. 2023; Edmans et al. 2024; Hart and Zingales 2022; Mitchell et al. 1997). Some stakeholder interests in sustainability are short-term and relate to financial outcomes; others are long-term and more oriented toward non-financial or societal outcomes. While scholars have discussed this challenge conceptually (Freeman 1984, 2010; Harrison and Wicks 2013; Hörisch

et al. 2014; Laplume et al. 2008; Parmar et al. 2010), empirical analyses of the effects of sustainability practices have produced mixed results (Eccles and Viviers 2011; Eccles et al. 2019; Friede et al. 2015). We contend that whether good sustainability practices lead to better financial or societal outcomes remains an open question. In this paper, we offer a framework to explain this issue, supported by empirical findings, wherein managers act to deliver different sustainability outcomes to serve stakeholders with heterogeneous preferences.

Our framework, built on the well-established distinction between primary and secondary stakeholders (Brower and Dacin 2020; Clarkson 1994; Godfrey et al. 2009; Hillman and Keim 2001; Perrault and Quinn 2018) and prior analytical work (Geelen et al. 2024; Hart and Zingales 2022), reveals two countervailing forces. On the one hand, potentially in response to investor pressure, managers direct their

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sustainability actions toward primary stakeholders to improve financial outcomes (Hillman and Keim 2001; Sprengel and Busch 2011). On the other hand, managers may direct their sustainability actions toward secondary stakeholders to yield favorable societal yet potentially unfavorable financial outcomes (Aghion et al. 2023; Carroll and Brown 2018; Hawn and Ioannou 2016; Nardi 2022).

Achieving an ideal balance that appropriately recognizes diverse stakeholder group preferences can be challenging for managers, requiring tradeoffs due to constrained resources that could lead to misaligned effort. This potential misalignment—whether deliberate or as an unintended consequence of the difficulty in determining how to allocate resources across multiple stakeholders—risks generating conflicting outcomes. Our framework, which explicitly incorporates this conflict, leads to the following research prediction: managers' value-maximizing sustainability actions aimed at serving multiple and diverse types of stakeholders reflect tradeoffs, whereby positive financial outcomes can occur at the expense of negative societal outcomes and vice versa.

We empirically test this prediction in the setting of large publicly listed US firms from 2007 to 2019 (Section 3.1). We use ESG incidents from RepRisk and Violation Tracker as outcome-oriented measures of sustainability performance. Firms with fewer ESG incidents are said to exhibit more favorable sustainability outcomes. To measure managers' actions toward primary and secondary stakeholders, we use input-oriented environmental, social, and governance (ESG) measures from LSEG (formerly Refinitiv), which we then separate into two categories depending on whether managers' actions favor primary or secondary stakeholders (Brower and Dacin 2020, 816). We conduct regression analyses to test our predictions and answer our research question.

We report the following findings. We first find that firms led by managers whose actions prioritize secondary over primary stakeholders are likelier to experience fewer ESG incidents, that is, achieve better sustainability outcomes. Moreover, the opposite holds for firms whose sustainability focus is directed toward primary stakeholders. Second, we find that when managers' sustainability actions shift dynamically from serving primary to serving secondary stakeholders, ESG incidents also decrease. Third, we test whether firms with managers who prioritize primary stakeholders' interests achieve better financial outcomes than firms that do not, either as a way to countervail their higher likelihood of having worse ESG incidents or possibly as a casualty of having over-emphasized financial performance (Edmans et al. 2024; Galbreath 2006; Hillman and Keim 2001). Supporting this idea, we find that financial performance measured as return on assets (ROA) or return on equity (ROE) is higher (lower) when managers' sustainability actions lean more (lean less) toward primary versus secondary stakeholders.

Hence, managers' sustainability actions that prioritize secondary stakeholders improve sustainability performance and weaken financial performance. Conversely, managers' sustainability actions that prioritize primary stakeholders improve financial performance and weaken sustainability performance. Grounded in

a conceptual framework whereby conflicting stakeholder preferences result in managers making tradeoffs among stakeholder groups, our findings address the long-standing puzzle of why managers' sustainability efforts do not always translate into improved financial performance. Our results persist under alternative measures and regression designs.

We contribute to at least four strands of literature. We first advance the stakeholder literature (Galbreath 2006; Hillman and Keim 2001) by documenting heterogeneous and dynamic sustainability outcomes through actions directed at primary and secondary stakeholders. This distinction is particularly relevant when viewed in conjunction with the rise in power and influence of the latter group from social media (Jurgens et al. 2016). Second, we add to the sustainability literature by confirming the predictions of a conceptual framework with value-maximizing agents (Geelen et al. 2024; Hart and Zingales 2022). Our framework explains under what circumstances managers' efforts to promote sustainability outcomes can backfire. Third, our findings provide a deeper understanding of the diversity of results regarding the relationship between sustainability and financial outcomes, a topic that is still largely unresolved in the empirical management literature (Friede et al. 2015; Gillan et al. 2021). While many studies attribute this diversity of results to methods, data, and design choices, fewer explanations in the literature confirm or reject conceptually grounded hypotheses, other than arguments on the direction of causality (Endrikat et al. 2014). Fourth, our findings support policymakers' and standard setters' efforts to expand disclosure beyond financially material sustainability topics, to include firms' sustainability outcomes affecting society and ecosystems, also known as impact materiality (CSRD 2022; ISSB 2023). While information on firm-related societal outcomes is important for stakeholders, and for managers to correctly balance sustainability actions, most non-financial sustainability outcomes are viewed by firms as immaterial and not disclosed in corporate reports under current rules (Haley et al. 2026). This lack of corporate report disclosure raises the ethical issue of moral licensing, which can further disserve the needs of stakeholders interested in societal outcomes (Liu et al. 2024).

Section 2 discusses the related literature, develops the conceptual framework, and states the hypotheses. Section 3 describes the sample, data, and empirical strategy. Section 4 presents the results. Section 5 concludes.

2 | Related Literature, Conceptual Framework, and Hypotheses

2.1 | Related Literature

A growing literature in sustainability management calls for a shift in focus—from analyzing firms' intentions and symbolic engagement with sustainability to assessing actual sustainability outcomes (Donaldson and Preston 1995; Eccles et al. 2014; Schaltegger and Hörisch 2017). While many studies examine how managers should engage stakeholders or adopt sustainability practices, fewer investigate when and why such engagement fails, leading to corporate social irresponsibility. In their theoretical framework, Clark et al. (2021) argue that the field must

pay greater attention to the gray zones between responsible and irresponsible behavior—spaces in which firms' actions may not be explicitly illegal or regulated, but still produce negative externalities for stakeholders. This call to focus on observable harms rather than aspirational responsibility aligns closely with our outcome-oriented measures of sustainability performance.

In parallel, stakeholder theory has long sought to explain how managers prioritize competing demands, often emphasizing power, legitimacy, and urgency (Mitchell et al. 1997). While this work offers insight as to why certain stakeholders receive more attention, it largely treats managerial engagement as a strategic input—assuming value creation or legitimacy is the goal—without thoroughly examining the tradeoffs that emerge when different stakeholder groups value different outcomes. Put differently, what is good for one stakeholder group may not be good for another, and not best for the firm. Thus, the calculus of choosing an ideal combination can be challenging for a manager, with recent work acknowledging the complexity of these tradeoffs (Barnett et al. 2020; Wood et al. 2018) but tending to underemphasize the costs or consequences of neglecting certain stakeholder groups, particularly in the form of ESG-related incidents.

Freudenreich et al. (2020) extend this line of reasoning by emphasizing that managers are not neutral agents in executing stakeholder demands but, rather, shape how stakeholder interests are interpreted and acted upon. Stakeholder assumptions and priorities can influence how firms approach their relationships and navigate competing demands. Building on this idea, we offer a framework that explicitly assumes that managers themselves hold preferences for sustainability outcomes—ranging from financial to societal—and exercise discretion in how they allocate effort across primary and secondary stakeholders. We examine how this allocation of effort affects observed sustainability outcomes, measured as ESG incidents, and highlight how imbalanced attention toward certain stakeholder groups can lead to worse societal outcomes.

Clark et al. (2021) help reframe the discussion on tradeoffs in stakeholder prioritization by emphasizing managerial discretion and the ambiguity of decision-making in sustainability “gray zones.” They argue that irresponsibility often stems not from overt malfeasance, but from selective inattention, rationalization, or the misalignment of managerial goals with the preferences of broader stakeholder groups. This is particularly relevant for firms navigating resource constraints, where satisfying one group (e.g., shareholders or customers) implicitly deprioritizes others (e.g., affected communities or those supporting the natural environment). Their framework also highlights how structural ambiguity allows managers to justify inaction or an insufficient response to emerging societal expectations—especially when those expectations are diffuse or lack formal enforcement. Some recent examples are managers' role in addressing the impact of climate change, biodiversity loss, and workplace inequality, and how their operations affect external stakeholder groups in general (Edmans et al. 2024; Hart and Zingales 2022).

Another strand of literature indicates conflicts of interest in managerial stakeholder prioritization. The literature on how

sustainability performance (spanning either all three ESG pillars or just one) affects corporate financial performance (CFP)—although quite broad—does not find consensus on this issue. For example, Friede et al. (2015) report that 48.2%, 10.7%, 23%, and 18% of the studies, respectively, show a positive, negative, neutral, and mixed sustainability/CFP relation. These findings, however, could also be interpreted in light of a range of sustainability actions with different financial versus societal effects and varying stakeholder preferences for sustainability outcomes. Thus, the Friede et al. (2015) conclusion that 51.8% (1%–48.2%) of all sustainability/CFP studies show a non-positive association could also reflect the reality that not all stakeholders prioritize sustainability outcomes equally. This view suggests that if not all stakeholder sustainability preferences can be fully satisfied, then managers' sustainability actions will have to involve tradeoffs among the different groups (Bartke and Schwarze 2015; Haffar and Searcy 2017; Hahn et al. 2010; Hart 1995; Minoja 2012). In our case, tradeoffs from a potential conflict of interest can occur when managers deprioritize societal outcomes for some stakeholders at the expense of prioritizing financial sustainability outcomes for others, and vice versa.

This leads to the question of which stakeholder groups might prioritize societal versus financial sustainability outcomes. We draw on the literature on primary versus secondary stakeholders to answer this question. On the one hand, Mitchell et al. (1997) emphasize the role of managers in dealing with different stakeholders and provide a categorization based on possible overlap among legitimacy, power, and urgency. Those categories can help managers to define “who and what really counts.” However, as those attributes are variable and socially constructed (Mitchell et al. 1997), they are not suitable for distinguishing between financially versus societally focused stakeholders. Thus, we draw on the narrower, risk-based approach of Clarkson (1994), defining that primary stakeholders are those that face the risk of loss of human or financial capital invested in the firm. As a result, we assume that groups such as customers, suppliers, investors, and employees are likelier to prioritize financial sustainability outcomes, in part to decrease their risk of capital loss. On the other hand, secondary stakeholders such as citizens or local communities without risk of capital loss or interest from a formal relationship (Clarkson 1994) might prefer societal sustainability outcomes as the net bearers of externalities.

Both primary and secondary stakeholders can influence the respective manager and firm. The former have direct influence through their invested capital; the latter a more indirect influence mainly through the legitimacy of their claims (Thijssens et al. 2015), which has arguably become increasingly far reaching due to social media (Jurgens et al. 2016). This means that the firm as well as the manager can receive different types of pressure from different stakeholders—from shareholder interventions to major publicity crises. Taken together, our study builds directly on the lines of reasoning in these literatures. We focus on ESG incidents as observable indicators of negative sustainability outcomes and theorize how they arise from managerial decisions about stakeholder prioritization. Specifically, we distinguish between primary stakeholders—who tend to emphasize financial outcomes from sustainability actions and secondary stakeholders—who more often demand that managers consider societal actions and non-financial impacts.

2.2 | Conceptual Framework

To derive our hypotheses, we present a conceptual framework linked to prior studies that focuses on three groups—managers and two outside stakeholder groups—all with potentially varying preferences for sustainability outcomes.¹ We specify the two outside stakeholder groups as primary stakeholders such as investors, creditors, employees, and customers, whose preferences can directly affect firm-level sustainability outcomes; and secondary stakeholders such as citizens and communities, whose preferences mainly indirectly affect firm-level societal sustainability outcomes. Next, we include key elements of the governance models of Hart and Zingales (2022) and Geelen et al. (2024).² Their models show that rational value-maximizing stakeholders can in combination produce better or worse sustainability outcomes depending on how managers reflect their preferences for financial or societal sustainability outcomes. We then assign this classification of preferences to primary and secondary stakeholders. Because primary stakeholders face the risk of loss of human or financial capital invested in the firm (Clarkson 1994, 1995; Hillman and Keim 2001), we assume that this group versus secondary stakeholders is likelier to favor actions to improve financial versus societal sustainability outcomes.

While not directly observable, the key in our framework is the extent to which managers are able to consider and balance the assumed preferences of the outside stakeholders plus their own. In the case of an imbalance, we assume that this generates a conflict of interest that intensifies when the preferences are significantly different (Schaltegger et al. 2017), implying that not all stakeholders' demands can be equally met (Hart and Zingales 2022). We contend that a significant conflict of interest can misalign managers' actions with outside stakeholders' sustainability preferences and promote second-best or off-equilibrium decision-making. Empirically, we infer misaligned actions from differences in sustainability outcomes.

Our conceptual framework requires certain assumptions. We first assume that the manager has preferences for financial or societal outcomes and enjoys delegated and operational decision rights to invest in sustainability projects to satisfy the needs of outside stakeholders, who have their own preferences for financial or societal outcomes or a combination of both. We thus assume that two outside stakeholder groups (i.e., primary and secondary stakeholders) bear the consequences of managers' decisions. Second, we assume that these two groups form their sustainability preferences independently of each other. Third, we assume that variation in preferences across the stakeholder groups is more salient for determining outcomes than within a group. Lastly, we assume that firm resources are constrained such that all stakeholder preferences cannot be fully met. We next describe two scenarios implied by the framework to test our hypotheses.

In the first scenario, the manager exerts effort resulting in actions that generate balanced financial and societal outcomes. With this scenario, akin to a near-equilibrium allocation, both stakeholder groups are made better off, as their preferences are (at least partially) satisfied, and the manager's effort incentives are aligned. The financial and societal outcomes should therefore improve (or not deteriorate) for both outside stakeholder groups, in our case, primary and secondary stakeholders.³

In the second scenario, the manager's actions do not agree with the preferences of the outside stakeholders. The manager—assuming that the outside stakeholders are unable to quickly rectify the disagreement—fails to correctly trade off the expected outcomes from the divergent preferences to resolve the conflict of interest, potentially exerting misaligned effort as a result. While some misalignments stem from bounded rationality, because the equilibrium of addressing the needs of primary and secondary stakeholders is unknown, others can occur for behavioral reasons, such as managers not adequately aligning their actions with stakeholder preferences, even though they are known (e.g., investor proposals to emphasize sustainability topics). This off-equilibrium scenario, due to divergent preferences, if sufficiently serious, could result in inefficient decision-making and a decline in firms' overall sustainability or financial performance. For instance, dysfunctional effort could occur because of a flawed ESG compensation plan (Bebchuk and Tallarita 2023) or managers' focus on different personal goals (Bushee 1998; Stein 1988). Dysfunctional effort could also occur if managers overreact to pressure from creditors (more interested in financial performance) or the proposed resolutions of some shareholders (more interested in societal outcomes). At the extreme, if we assume that the manager pays all attention to primary (secondary) stakeholders' preferences, then no attention or effort would be applied to secondary (primary) stakeholders' preferences, resulting in worse sustainability (financial) outcomes.

2.3 | Hypotheses

Applying scenarios one and two to our setting of primary and secondary stakeholders and measures of sustainability outcomes based on ESG incidents, which we view as equivalent to negative societal outcomes, we can state our first hypothesis in the alternative form as follows:

H1a. *A manager's focus on actions toward primary stakeholders increases ESG incidents.*

H1b. *A manager's focus on actions toward secondary stakeholders reduces ESG incidents.*

In line with the second scenario of our conceptual framework, Figure 1 shows the expected outcomes from a shift in managers' sustainability actions from secondary to primary stakeholders. As managers direct their sustainability actions toward primary stakeholders (moving to the right on the x axis), societal outcomes deteriorate (y axis, green line), whereas pro-financial outcomes improve (y axis, red line).

Based on the foregoing, we can also theorize that if a manager's actions were to shift toward achieving more societal outcomes without a commensurate shift in primary or secondary stakeholders' preferences for those outcomes, this would intensify the conflict of interest for primary stakeholders and ease or eliminate it for secondary stakeholders. As such, we can state a second hypothesis, in the alternative form, relating to the dynamic effects of managers' actions on stakeholders' preferences.⁴

H2a. *A manager's shift in actions from a focus on primary stakeholders toward secondary stakeholders reduces ESG incidents.*

H2b. *A manager's shift in actions from a focus on secondary toward primary stakeholders increases ESG incidents.*

3 | Sample, Variables, and Method

3.1 | Sample

We start with the S&P 500, which is a well-studied sample in the management and finance literature (Alareeni and Hamdan 2020). The S&P 500 represents slightly more than 80%

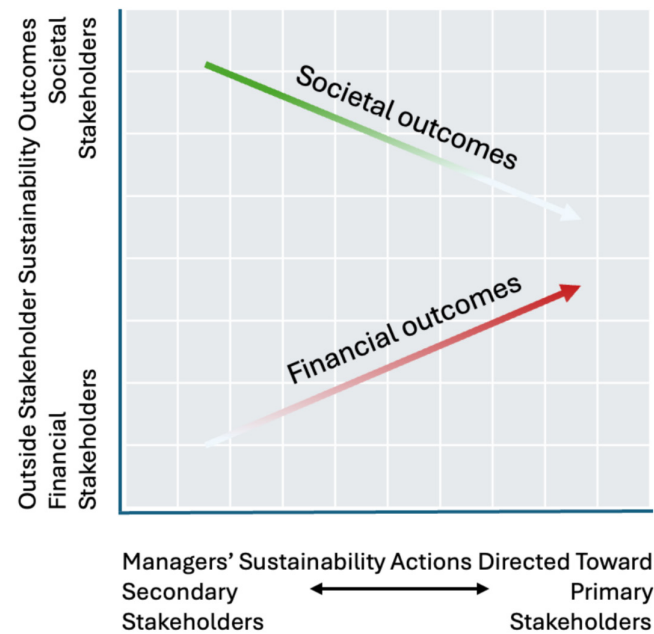


FIGURE 1 | Theoretical effects of sustainability actions on stakeholders.

TABLE 1 | Sample by year and GICS sector.

Year	N obs.	%	GICS sector	ID.	N obs.	%
2007	112	3.08	Energy	10	213	5.86
2008	173	4.76	Materials	15	178	4.90
2009	201	5.53	Industrials	20	705	19.39
2010	233	6.41	Consumer discretionary	25	745	20.49
2011	249	6.85	Consumer staples	30	371	10.20
2012	278	7.65	Health care	35	423	11.63
2013	299	8.22	Information technology	45	392	10.78
2014	313	8.61	Communication services	50	123	3.38
2015	333	9.16	Utilities	55	307	8.44
2016	356	9.79	Real Estate	60	179	4.92
2017	358	9.85				
2018	361	9.92				
2019	370	10.17				
Total	3636	100.00	Total		3636	100.00

Note: This table summarizes the panel data set observations for the S&P 500 firm sample by year and sector. Because the panel dataset requires no missing observations for the dependent variable and all covariates and excludes the GICS sector for financial firms, the sample size each year is less than 500. Based on a chi-square test, the sector distribution of the sample is statistically equivalent to the sector distribution of all S&P 500 firms (other than financials).

of the capitalization of the U.S. equity market. We drop financial institutions due to their unique capital structure and business model (Brav 2009; Kim and Lee 2018). Our final panel dataset comprises a maximum of 3636 firm-year observations from 2007 to 2019 relating to 376 firms in the S&P 500.⁵ We focus on the 2007–2019 period because RepRisk incident data are available from 2007 onward, which determines the start of our merged panel. We deliberately end the panel in 2019 to avoid contamination from the SARS-CoV-2 pandemic and the heightened salience of ESG issues from 2020 onward, both of which may have changed managers' and stakeholders' sustainability perceptions and introduced a structural break into the analysis. Firm-level data are downloaded as of the end of each fiscal year from LSEG. Table 1 summarizes the sample by year and industry. Based on a chi-square test, the industry distribution in Panel B is statistically the same as the composition of the full S&P 500 (as of 2019). To mitigate the influence of outliers and to generate more symmetric distributions for analysis, we log transform some specific variables, such as total assets (Hastie et al. 2009). Appendix A lists the variables and states the units of each variable.

3.2 | Variables

3.2.1 | Dependent Variable

While studies of the outcomes of responsible business conduct are not mainstream in the management literature (Barnett et al. 2020), given our research question and hypotheses, we necessarily require an event-based measure that identifies well with a societal sustainability outcome plausibly linked to firms' actions or behavior (i.e., is not exogenous). Data on incidents from RepRisk to measure (negative) outcomes satisfy this requirement. Measures of sustainability performance published by other ESG raters do not meet this requirement,

however. This is because they either comingle firms' actions, policies, and outcomes or incorporate factors conveyed by the firm to the rater indicative of greenwashing. Measures of emissions are also prone to error, lack comparability, especially regarding Scope 3 emissions, and can represent omitted covariates (Cohen et al. 2020).

By contrast, RepRisk offers a rich array of data exclusively based on external information after screening over 100,000 public sources, thus mitigating the concerns of greenwashing, lack of transparency, or error in the calculation. RepRisk tracks actual ESG incidents (such as injuries of workers) on 28 ESG issues, spanning from the environmental pillar including climate change incidents, to the pillar including incidents on human rights abuses and child labor, and to the governance pillar including bribery, fraud, and tax evasion. RepRisk calculates its ESG incident scores daily. This contrasts with other data providers likelier to capture firms' input or actions such as investments to improve working conditions and workplace safety, as well as firms' internal disclosures. With RepRisk, each incident is evaluated throughout the evaluation process on three parameters: severity, reach, and novelty. As such, a firm's RepRisk incident score not only captures the number of negative outcomes but also the relative harm to stakeholders (RepRisk 2024). A firm's date-stamped score ranges from 0 to 100, where 0 is the best possible performance (i.e., no incident for the respective firm) and 100 is the worst (i.e., many current and severe incidents with far reach). Given its use by stock market analysts (Luo et al. 2015) and firms (BASF 2023; Qontigo 2022) to assess outcomes, we are confident that a firm's RepRisk incident score is suitable for our endeavor. Li and Wu (2020) and others use RepRisk data to measure sustainability outcomes. Nevertheless, for robustness, we examine incidents in Violation Tracker (Violation Tracker 2024) and variables from MSCI-ESG (MSCI 2024) as alternative outcome and management preference measures, respectively.

As with most archival studies, despite RepRisk being an accurate identifier of ESG incidents at the firm level, we still face the challenge of whether firm managers' sustainability actions (or even primary and secondary stakeholders' preferences) might have contributed to a RepRisk incident. This challenge is also intensified because we cannot unambiguously relate a manager's societal or financial sustainability action to a unique RepRisk incident, although it is reasonable to assume that RepRisk incident scores reflect adverse societal outcomes. Our results are, therefore, primarily associative and not directed at establishing clear causal inferences. Nonetheless, we consider the potential for causal inference in the research design by addressing endogeneity using lagged covariates and instrumental variable (IV) regression and by exploring two plausibly exogenous shifts in sustainability preferences from outside-the-system shocks.

3.2.2 | Independent Variables

We access LSEG ESG legacy category scores—used by clients until the LSEG score redesign in 2026—to measure managers' focus on actions toward primary and secondary stakeholders for

our sample. In 2024, LSEG provided ESG information on over 14,000 public entities globally with time series from 2002. Most scores are available for firms in North America (5900 firms) and Europe (3700 firms). Its assessment procedure extracts data in the public domain, such as from annual reports, sustainability reports, NGO websites, and news sources. The evaluation process is also highly sophisticated, since human and algorithmic auditors analyze more than 800 metrics concerning materiality, data availability, and industry relevance. In sum, the applied LSEG scores represent a plausible indicator of managers' focus on actions taken toward stakeholders. For our sample period, the category scores range between 0 and 100, where 0 is the worst and 100 measures the best possible relative effort in a category of ESG activity.

This data choice offers several advantages: Studies (i) indicate that LSEG legacy scores are less prone to selection bias (Dorfleitner et al. 2015; El Ghoul et al. 2017), (ii) show more relevant results in terms of the variability and distribution of scores than comparable ESG scores (Desender and Epure 2015; Dorfleitner et al. 2015; Ioannou and Serafeim 2011), and (iii) report more frequent use of LSEG legacy scores, which helps commensurability (Dyck et al. 2019; Habermann and Fischer 2023; Liang and Renneboog 2017). Thus, we expect both high quality and consistency in our ESG data.⁶

We exploit the depth of LSEG ESG legacy category scores to derive firm-year-specific measures of managers' actions toward primary and secondary stakeholders. Distinguishing between direct (likelier financial) and indirect (likelier societal) outcomes for primary versus secondary stakeholders based on similar allocations (Brower and Dacin 2020; Hillman and Keim 2001; Perrault and Quinn 2018), we assign firms' individual LSEG category scores to one of two groups. As with the prior work, we contend that the product responsibility score (*ProductResponse*), the workforce score (*Workforce*), and the governance score (*Governance*) serve as indicators of managers' focus on actions toward primary stakeholders. For secondary actions, the category scores for environment, community involvement, and diversity and human rights serve as indicators of managers' focus on actions toward societal outcomes.

We use aggregate measures for primary (*PrimStkAct*) and secondary (*SecStkAct*) stakeholder actions by calculating the mean of the respective scores (i.e., $[ProductResponse + Workforce + Governance]/3 = PrimStkAct$). Initially, we calculate *SecStkAct* as $[Environment + Community + Diversity + HumanRights]/4 = SecStkAct$. Due to concerns that diversity issues also connect to a firm's workforce, we calculate an alternative score as *SecStkAct_Alt* being $[Environment + Community + HumanRights]/3 = SecStkAct_Alt$, although the same results hold when the regressions include *SecStkAct_Alt*. We also calculate a residual workforce score as $[Workforce - Diversity]$, based on the idea that diversity could either improve or constrain the outcomes of *Workforce* on the bottom line. In terms of our conceptual framework, *PrimStkAct* is the empirical proxy for managers' actions toward pro-financial outcomes, and *SecStkAct* is the empirical proxy for managers' actions toward societal outcomes. We also compute the difference between *PrimStkAct* and *SecStkAct* as a relative measure of managers' actions toward financial over societal outcomes.

3.3 | Method

We first run a standard OLS panel regression with controls and fixed effects (FE). For each model, we perform the *Breusch-Pagan* test (Breusch and Pagan 1979) to check for heteroscedasticity and an *F* test to check for overall significance. RepRisk ESG scores vary widely cross-sectionally. They also show limited variation for a specific firm over time. As the most stringent test for each coefficient, we absorb firm-level and year fixed effects in the regressions. In addition, we apply year-level clustered standard errors to make robust inferences in light of heteroscedasticity and serial correlation concerns. We lag all explanatory and control variables by 1 year to address potential endogeneity (Brower and Dacin 2020). We test our hypotheses H1a and H1b with Equations (1) and (2) as follows:

$$Y_{it} = \alpha + \beta_1 \text{PrimStkAct}_{it-1} + \beta_2 \text{SecStkAct}_{it-1} + \beta_3 Y_{it-1} + \sum_k \beta_k \text{Controls}_{it-1} + \eta_i + \theta_t + \varepsilon_{it} \quad (1)$$

$$Y_{it} = \alpha + \beta_1 (\text{PrimStkAct}_{it-1} - \text{SecStkAct}_{it-1}) + \beta_3 Y_{it-1} + \sum_k \beta_k \text{Controls}_{it-1} + \eta_i + \theta_t + \varepsilon_{it} \quad (2)$$

Y_{it} represents *ESGincident* score as the proxy for sustainability outcomes. To test H1a and H1b, the predicted signs of the coefficients are $\beta_1 \geq 0$ and $\beta_2 < 0$ in Equation (1) and $\beta_1 > 0$ in Equation (2). While it is possible to estimate Equation (1) and Equation (2) without Y_{it-1} as a covariate, its exclusion makes the results mainly dependent on cross-sectional variation. To increase time-series variation in the outcome variable and, therefore, to include the possibility that the results are driven by both firm-level and cross-sectional variation, we include Y_{it-1} as an additional covariate and add a vector of controls to exclude firm-level factors that do not vary with *PrimStkAct* or *SecStkAct* but could otherwise influence the test coefficients. Following prior work, we include firm *Size* (the natural logarithm total assets), *Leverage* (total debt divided by total assets), *Growth* (sales in t divided by sales in $t-1$ minus one), and *Efficiency* (total revenues divided by total assets) to control for other firm characteristics that might affect the outcome variable *ESGincident* but for *PrimStkAct* or *SecStkAct* (Capon et al. 1990). These variables are stored in the lagged vector indicated as $\text{Controls}_{i,t-1}$. For both models, i denotes the firm dimension and t is the time dimension. For both Equations, η_i represents firm fixed effects, θ_t denotes year fixed effects, and ε_{it} is the uncorrelated error term.

4 | Results

4.1 | Univariate Analysis

We first present the sample descriptive statistics in Table 2. The dependent variable *ESGincident* and the independent variables of *Size*, *Leverage*, *Growth*, and *Efficiency* all exhibit reasonably symmetric distributions. As expected, our S&P 500 sample comprises large and efficient firms that are more capitalized with equity than debt. Regarding stakeholder actions, firms perform best in the sustainability category of *Community* (mean = 76.18; median = 81.48). For both *PrimStkAct* and

SecStkAct, the scores vary widely across the sample. For *PrimStkAct*, the 25th percentile is 43.69 and the 75th percentile is 72.03. The average *SecStkAct* (mean = 55.19; median = 56.72) is lower than average *PrimStkAct* (mean = 57.31; median = 58.37). Overall, on average, the focus of our sample is slightly more on actions toward primary versus secondary stakeholders. However, these are average scores, and there are roughly equal instances where a firm's year-specific *SecStkAct* exceeds (49.9%) versus does not exceed (50.1%) its *PrimStkAct* measure. In addition, we note that the cross-sectional variance of the difference of *PrimStkAct-SecStkAct* is about the same as for the component variables, giving it roughly equivalent explanatory power.

To address computational problems with the regression models, Table 3 presents the Pearson correlation coefficients. The three highest (but still moderate) correlations between our explanatory (variables 1–9) and the control variables are between *Size* and *PrimStkAct*, *SecStkAct*, and *Environment*. It is important to control for size, as the correlations between *PrimStkAct* or *SecStkAct* and *Size* could imply that larger S&P 500 firms achieve higher ratings because they receive greater attention and can allocate more resources to ESG endeavors (Drempetic et al. 2020). Additionally, *PrimStkAct* and *SecStkAct* show a high correlation ($\text{corr} = 0.727$). That is, firms with a strong primary stakeholder orientation also tend to have a high secondary stakeholder orientation, although the two do not cancel out each other; that is, the difference is not zero. Since we incorporate both variables in Equation (1), we calculate variance inflation factors (VIFs) for all covariates to check for multicollinearity. Following Aouadi and Marsat (2016), we derive the uninflated VIF factors for Equation (1). None of the VIF factors is crucial (i.e., exceeds 6.13).

4.2 | Effect of Primary and Secondary Actions on RepRisk Incidents

Table 4 summarizes the results of regressing RepRisk ESG incidents on measures of managers' actions toward primary and secondary stakeholders. Panel A shows the results of estimating Equation (1). Whereas the coefficient for *PrimStkAct* is positive (0.008) but not significantly different from zero ($p > 0.10$), the coefficient for *SecStkAct* is negative (−0.046) and significantly different from zero ($p < 0.05$). This indicates that RepRisk incidents decrease when managers orient their decision-making toward secondary versus primary stakeholders. However, focusing on *PrimStkAct* and *SecStkAct* as separate covariates could be throwing away some explanatory power, as a firm with lower *PrimStkAct* could also be a firm that emphasizes secondary over primary stakeholders in some respects.

Panels B and C summarize the regressions for Equation (2). Both panels show that the coefficients for *Primary-Secondary* (a continuous variable) and *Prim_Sec_PCRank* (the percentile rank of *Primary-Secondary*, calculated by converting the ranking of the difference of *Primary-Secondary* into percentiles), are significantly positive (Panel B, $p < 0.10$ and Panel C, $p < 0.05$). Table 4 thus supports H1a and H1b; namely, that a focus on secondary stakeholders compared to primary stakeholders reduces the likelihood of RepRisk incidents or,

TABLE 2 | Sample descriptive statistics.

Dependent variable	N obs.	Mean	Std. dev.	Min.	p25	Median	p75	Max.
<i>ESGincident</i>	3636	32.93	14.25	0.07	23.30	33.29	42.05	80.01
Controls								
<i>Size (log of TA)</i>	3636	23.62	1.14	19.87	22.80	23.61	24.34	27.41
<i>Leverage (Debt ÷ TA)</i>	3636	0.30	0.21	0.00	0.18	0.28	0.39	3.89
<i>Growth (in sales)</i>	3636	7.22	21.53	−88.87	−0.22	5.27	11.79	554.93
<i>Efficiency (Rev ÷ TA)</i>	3636	0.84	0.71	0.07	0.39	0.64	1.04	5.74
LSEG category score								
<i>PrimStkAct</i>	3636	57.31	19.35	1.59	43.69	58.37	72.03	98.96
<i>ProductResponse</i>	3636	52.64	29.46	0.00	27.67	51.72	80.00	99.61
<i>Workforce</i>	3636	61.69	25.06	0.48	43.01	64.37	82.97	99.87
<i>Governance</i>	3636	57.60	21.74	0.43	42.15	60.57	74.81	98.72
<i>SecStkAct</i>	3636	55.19	18.78	0.00	41.72	56.72	70.62	90.94
<i>SecStkAct_Alt</i>	3633	53.99	22.48	0.00	35.98	54.70	73.08	95.69
<i>Environment</i>	3636	48.95	27.63	0.00	27.97	54.12	72.07	98.53
<i>Community</i>	3636	76.18	19.91	0.00	64.82	81.48	92.40	99.89
<i>Diversity</i>	3636	58.79	19.03	0.00	58.62	63.16	67.61	92.48
<i>HumanRights</i>	3636	36.84	34.54	0.00	0.00	35.16	68.75	99.21
<i>Primary-Secondary</i>	3636	2.12	17.90	−60.63	−12.78	0.68	12.60	68.83

Note: This table summarizes the variables used in the regressions. The ESG incident scores range from 0 to 100, with higher numbers indicating more severe incidents. The LSEG category scores also range from 0 to 100, with higher numbers representing more ESG actions in the ESG category. *PrimStkAct* refers to ESG actions oriented to primary stakeholders. *SecStkAct* refers to ESG actions oriented to secondary stakeholders. The ESG incident scores are measured for year t whereas the controls and the LSEG category scores are measured for year $t - 1$. Appendix A lists the variables.

contrariwise, a focus on primary stakeholders increases the likelihood of RepRisk incidents.

These results are consistent with the theoretical green line in Figure 1, which shows that firms have more positive sustainability outcomes (in our case, fewer negative RepRisk incidents) when managers' emphasis is on secondary stakeholders. Relating these results to our conceptual framework (Section 2.2), they imply that sustainability performance improves when managers' actions for societal ESG outcomes agree with the preferences of secondary stakeholders, which the framework explains is due to aligned interests that generate efficient decision-making.

4.3 | Effect of Shifts in Sustainability Actions on Stakeholder Outcomes

To investigate the dynamics of manager–outside stakeholder conflicts of interest, we focus on shifts in managers' sustainability actions regarding stakeholder outcomes. For example, if from one year to the next, a firm's orientation toward sustainability actions *changes* from net *Secondary-Primary* > 0 to net *Primary-Secondary* > 0, we assume that this is equivalent to a year-to-year shift in a manager's orientation from pro-societal to pro-financial decision-making. We also assume in this scenario that primary and secondary stakeholders'

preferences do not change and that managers change their decision-making but do not simultaneously communicate that to outside stakeholders. For example, managers may consider the information proprietary (Dye 1985) or subject to communication frictions. This assumption, depending on the direction of the shift, could attenuate or intensify the potential conflict of interests among managers and the two outside stakeholder groups.

Table 5 presents the results. Panel A summarizes the results of Equation (1) for the subsample of managers' shifts to more societal decision-making. For primary versus secondary stakeholders, this increases (decreases) the conflict of interests for the former (latter) group. Supporting this interpretation, Panel A shows the coefficient for *PrimStkAct* is positive (0.1598) and significant ($p < 0.01$), whereas the coefficient for *SecStkAct* is negative (−0.1960) and significant ($p < 0.01$). Similarly, Panel B shows a significantly positive coefficient for *Primary-Secondary* ($p < 0.01$). Panels C and D assume the shift is in the other direction. Here, the coefficient signs reverse, but the coefficients are not significant, so there is no substantive change. Panel C shows the coefficient for *PrimStkAct* is negative (−0.0816) but not significant, and the coefficient for *SecStkAct* is positive (0.0825) but not significant.

Similarly, Panel D shows an insignificantly negative coefficient for *Primary-Secondary*. The coefficient levels in Tables 4

TABLE 3 | Correlations among the covariates.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
(1) <i>PrimSikAct</i>	1											
(2) <i>Product Response</i>	0.797*	1										
(3) <i>Workforce</i>	0.794*	0.436*	1									
(4) <i>Governance</i>	0.675*	0.272*	0.377*	1								
(5) <i>SecSikAct</i>	0.727*	0.511*	0.719*	0.420*	1							
(6) <i>Environment</i>	0.700*	0.501*	0.665*	0.425*	0.841*	1						
(7) <i>Community</i>	0.548*	0.340*	0.586*	0.328*	0.729*	0.569*	1					
(8) <i>Diversity</i>	0.328*	0.221*	0.361*	0.162*	0.510*	0.280*	0.316*	1				
(9) <i>HumanRights</i>	0.524*	0.393*	0.497*	0.296*	0.802*	0.548*	0.382*	0.154*	1			
(10) <i>Size</i>	0.361*	0.216*	0.357*	0.260*	0.404*	0.438*	0.319*	0.185*	0.243*	1		
(11) <i>Leverage</i>	−0.007	0.043*	−0.060*	−0.008	−0.049*	−0.004	0.007	−0.096*	−0.056*	0.038*	1	
(12) <i>Growth</i>	−0.145*	−0.098*	−0.107*	−0.130*	−0.149*	−0.159*	−0.106*	−0.064*	−0.100*	−0.057*	−0.049*	1
(13) <i>Efficiency</i>	0.022	0.027	0.003	0.017	0.008	−0.040*	−0.015	−0.014	0.066*	−0.190*	−0.147*	0.01

Note: This table summarizes the Pearson correlation coefficients among the covariates.

*denotes statistical significance at the ≤ 5% level. Appendix A lists the variables.

TABLE 4 | Regression of RepRisk incidents on primary and secondary stakeholder orientation.

Dependent variable = <i>ESGincident</i>	Coeff.	<i>t</i> stat.	Sig.
Panel A			
<i>PrimStkAct</i>	0.0080	1.22	ns
<i>SecStkAct</i>	−0.0460	−2.34	**
<i>Lagged ESGincident</i>	0.4722	13.96	***
<i>Size</i>	2.1449	6.52	***
<i>Leverage</i>	−0.5772	−0.34	ns
<i>Growth</i>	−0.0052	−0.66	ns
<i>Efficiency</i>	−1.0356	−1.78	ns
<i>Cons</i>	−30.3657	−3.62	***
Adj <i>R</i> -squared	0.7896		
<i>F</i> (7,11)	67.96		
Number of obs.	3255		
Panel B			
<i>Primary-Secondary</i>	0.0213	2.08	*
<i>Lagged ESGincident</i>	0.4718	13.83	***
<i>Size</i>	1.9814	5.8	***
<i>Leverage</i>	−0.4127	−0.25	ns
<i>Growth</i>	−0.0043	−0.55	ns
<i>Efficiency</i>	−1.1245	−1.87	*
<i>Cons</i>	−28.6279	−3.34	***
Adj <i>R</i> -squared	0.7892		
<i>F</i> (6,11)	80.75		
Number of obs.	3255		
Panel C			
<i>Prim_Sec_PCRank</i>	0.6410	2.52	**
<i>Lagged ESGincident</i>	0.4722	13.89	***
<i>Size</i>	1.9840	5.76	***
<i>Leverage</i>	−0.3292	−0.2	ns
<i>Growth</i>	−0.0047	−0.59	ns
<i>Efficiency</i>	−1.1165	−1.88	*
<i>Cons</i>	−30.6555	−3.69	***
Adj <i>R</i> -squared	0.7894		
<i>F</i> (6,11)	78.12		
Number of obs.	3255		

Note: This table summarizes the regressions for Equations (1) (Panel A) and (2) (Panels B and C). The regressions control for firm and year fixed effects. Since firm observations can enter each year, the regression errors are clustered by year. Statistical significance at the 1%, 5%, and 10% levels is denoted by

***,
**, and

*, respectively. Appendix A lists the variables.

TABLE 5 | Regression of RepRisk incidents on shifts to/from primary or secondary stakeholder orientation.

Dependent variable = <i>ESGincident</i>	Coeff.	<i>t</i> stat.	Sig.
Panel A: Shift to pro-societal orientation			
<i>PrimStkAct</i>	0.1598	3.73	***
<i>SecStkAct</i>	−0.1960	−4.32	***
<i>Lagged ESGincident</i>	0.7707	13.46	***
<i>Size</i>	0.8850	1.75	ns
<i>Leverage</i>	2.4697	2.17	*
<i>Growth</i>	−0.0282	−1.52	ns
<i>Efficiency</i>	−0.1620	−0.28	ns
<i>Cons</i>	−10.7276	−0.96	ns
Adj <i>R</i> -squared	0.7451		
<i>F</i> (7, 11)	254.6		
Number of obs.	275		
Panel B: Shift to pro-societal orientation			
<i>Primary-Secondary</i>	0.1616	3.74	***
<i>Lagged ESGincident</i>	0.7584	14.26	***
<i>Size</i>	0.8155	1.56	ns
<i>Leverage</i>	2.6348	2.46	**
<i>Growth</i>	−0.0279	−1.56	ns
<i>Efficiency</i>	−0.2029	−0.34	ns
<i>Cons</i>	−10.7919	−0.97	ns
Adj <i>R</i> -squared	0.7445		
<i>F</i> (6, 11)	202.06		
Number of obs.	275		
Panel C: Shift to pro-financial orientation			
<i>PrimStkAct</i>	−0.0816	−1.31	ns
<i>SecStkAct</i>	0.0825	1.32	ns
<i>Lagged ESGincident</i>	0.8105	24.19	***
<i>Size</i>	0.9384	1.92	*
<i>Leverage</i>	−4.0963	−1.49	ns
<i>Growth</i>	0.0057	0.78	ns
<i>Efficiency</i>	1.0158	1.77	ns
<i>Cons</i>	−15.3841	−1.39	ns
Adj <i>R</i> -squared	0.7485		
<i>F</i> (7, 11)	877.39		
Number of obs.	261		
Panel D: Shift to pro-financial orientation			

(Continues)

TABLE 5 | (Continued)

Dependent variable = <i>ESGincident</i>	Coeff.	t stat.	Sig.
<i>Primary-Secondary</i>	−0.0822	−1.33	ns
<i>Lagged ESGincident</i>	0.8107	22.76	***
<i>Size</i>	0.9411	2.02	*
<i>Leverage</i>	−4.1011	−1.49	ns
<i>Growth</i>	0.0057	0.77	ns
<i>Efficiency</i>	1.0174	1.76	ns
<i>Cons</i>	−15.4039	−1.41	ns
Adj R-squared	0.7496		
<i>F</i> (6, 11)	402.38		
Number of obs.	261		

Note: This table summarizes the regressions for Equation (2) for shifts in societal or pro-financial orientation. Due to the very low sample sizes, the regressions control for year fixed effects. Since firm observations can enter each year, the regression errors are clustered by year. Statistical significance at the 1%, 5%, and 10% levels is denoted by

***,

**, and

*, respectively. Appendix A lists the variables.

and 5 also suggest whether the conflicts of interest are greater for firms that switch away from or to a primary stakeholder focus. If the former, the *PrimStkAct* and *SecStkAct* coefficients in Table 5 should be greater in absolute value than the coefficients in Table 4. Indicating this result, Panel A of Table 5 shows *PrimStkAct* = 0.1598 and *SecStkAct* = −0.1960, whereas Panel A of Table 4 shows *PrimStkAct* = 0.0080 and *SecStkAct* = −0.0460. Some caution is warranted when comparing coefficients, however, because the switching subsamples could differ from the full sample for additional reasons. Overall, these results support H2a, that a manager's shift in focus in actions toward secondary stakeholders from primary stakeholders reduces ESG incidents. While a manager's shift in focus from secondary toward primary stakeholders increases ESG incidents (H2b), that shift is not significantly different from zero.

4.4 | Effect of Primary and Secondary Actions on Financial Outcomes

While our conceptual framework does not directly predict financial outcomes, if our theory is correct, we should observe as an implication an increase in financial performance when firms orient their actions more to primary versus secondary stakeholders (Hillman and Keim 2001)—as shown by the red line in Figure 1 (Section 2.3). To conduct a corroborating or testable implication of our theory, we estimate the following regression.

$$ROA_{it} \text{ or } ROE_{it} = \alpha + \beta_1 \text{Primary-Secondary}_{it-1} + \beta_2 \Delta Y_{it} + \sum_k \beta_k \text{controls}_{it-1} + \eta_i + \theta_t + \varepsilon_{i,t} \quad (3)$$

ROA_{it} is operating profit scaled by lagged total assets, ROE_{it} is net income scaled by lagged common equity, ΔY_{it} is the change in ESG incidents from the prior year, and the other variables are the same as in Equations (1) and (2). We include ΔY_{it} ($Y_{it} - Y_{it-1}$)

as a covariate, as an increase in ESG incidents should decrease ROA_{it} or ROE_{it} ceteris paribus. We also estimate Equation (3) without η_i (firm fixed effects) and ΔY_{it} because η_i can subsume some variation in ROA or ROE , and *PrimStkAct*_{it-1}, *SecStkAct*_{it-1}, and ΔY_{it} are related as per Equations (1) and (2).

Table 6 summarizes the results. In 15 of the 16 regressions (4 panels × 4 specifications), the coefficient for *Primary-Secondary* or *Prim_Sec_Rank* is positive and significant. Moreover, for the same regressions, the size of the β_1 coefficient is larger positively if we exclude ΔY_{it} from the regression. Thus, when managers orient their actions toward primary stakeholders with preferences for financial outcomes compared to secondary stakeholders without such preferences, firms report higher financial performance. Thus, whereas an emphasis on primary stakeholders associates with more negative RepRisk incidents (Tables 4 and 5), those stakeholders are rewarded with higher financial performance (Table 6).

We also compare the theoretical relationship with the empirical one. Whereas the theoretical relationship is depicted by the red line in Figure 1, the unconditional relationships (without adjusting for controls and fixed effects) for the sample are shown below in Figure 2. The x axis is the quintile ranking of the difference of *PrimStkAct-SecStkAct*, which is the same as *Primary-Secondary* in Equation (2). The y axis depicts the mean of each variable. Figure 2 clearly shows that the reduction in RepRisk incidents (the green columns) is highest for firms with a low ranking of *Primary-Secondary*, which is tantamount to a high ranking on secondary relative to primary stakeholders. By contrast, *ROA* and *ROE* (the red columns) are highest when *Primary-Secondary* is ranked highest. These offsetting trends represent evidence of a corporate sustainability trade-off as discussed in the literature (Bartke and Schwarze 2015; Haffar and Searcy 2017; Hahn et al. 2010; Hart 1995; Minoja 2012). This is because they depict that declining sustainability performance (the green columns) is accompanied by improved financial performance (the bright or dark red columns) the more that primary stakeholders are emphasized in management decision-making.

4.5 | IV Regression

While the tests so far confirm our predictions (i.e., *SecStkAct* reduces *ESGincident* whereas *PrimStkAct* does not), they do not allow for a causal interpretation. This is because managers' choice of a level of orientation toward primary and secondary stakeholders is an endogenous decision and not random. To examine this endogeneity issue and, thereby, arguably raise the possibility of a causal interpretation, we employ a two-stage IV approach. We specify the first stage with industry (π_i) and year (θ_t) fixed effects as follows:

$$\begin{aligned} \text{PrimStkAct}_{it-1} \text{ or } \text{SecStkAct}_{it-1} &= \alpha + \beta_1 \text{PrimStkActPeer}_{it-1} \\ \text{or } \beta_2 \text{SecStkActPeer}_{it-1} &+ \beta_3 Y_{it-1} + \sum_k \beta_k \text{controls}_{it-1} + \pi_i + \theta_t + \varepsilon_{i,t-1} \end{aligned} \quad (4)$$

Following Cheng et al. (2014), we define our IVs, namely *PrimStkActPeer* and *SecStkActPeer*, as the industry mean (excluding the focal firm) of the respective variable to be

TABLE 6 | Regression of ROA and ROE on primary and secondary stakeholder orientation.

Dependent variable	ROA			Excl. ROA > 20%			ROE			Excl. ROE > 20%		
	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig
Panel A												
Primary-Secondary	0.0156	2.19	*	0.0144	2.37	**	0.0333	2.55	**	0.0162	2.25	**
Δ ESGincident	−0.0212	−1.48	ns	−0.0184	−1.44	ns	−0.0304	−0.79	ns	−0.0255	−1.52	ns
Size	−1.0992	−5.75	***	−0.8734	−8.43	***	−0.0980	−1.04	ns	−0.0124	−0.11	ns
Leverage	−1.8108	−0.96	ns	−5.3973	−5.07	***	−14.1996	−19.40	***	−9.0626	−13.07	***
Growth	0.0118	1.29	ns	0.0062	0.67	ns	0.0051	0.28	ns	0.0027	0.23	ns
Efficiency	2.0906	8.19	***	1.3461	7.30	***	4.0032	8.17	***	1.5010	7.52	***
Cons	31.8242	8.29	***	27.6789	13.10	***	22.3507	9.65	***	13.7293	5.24	***
Adj R-squared	0.1110			0.1240			0.1061			0.1439		
F(6, 11)	199.75			524.63			294.3			98.02		
Number of obs.	3259			3119			2863			1614		
Panel B												
Prim_Sec_Rank	0.2015	2.21	**	0.1878	2.44	**	0.4261	2.35	**	0.1987	1.9	2**
Δ ESGincident	−0.0213	−1.47	ns	−0.0184	−1.44	ns	−0.0304	−0.79	ns	−0.0254	−1.53	ns
Size	−1.1029	−5.72	***	−0.8766	−8.46	***	−0.1021	−1.04	ns	−0.0110	−0.10	ns
Leverage	−1.8071	−0.96	ns	−5.3869	−5.07	***	−14.1902	−19.59	***	−9.0510	−13.7	***
Growth	0.0119	1.31	ns	0.0063	0.69	ns	0.0054	0.29	ns	0.0029	0.23	ns
Efficiency	2.0883	8.21	***	1.3449	7.31	***	3.9971	8.19	***	1.4976	7.52	***
Cons	31.2954	8.39	***	27.1764	12.91	***	21.1401	10.27	***	13.0834	5.21	***
Adj R-squared	0.1109			0.1239			0.1059			0.1433		
F(6, 11)	199.57			527.85			324.14			78.03		
Number of obs.	3258			3118			2862			1613		
Panel C												
Primary-Secondary	0.0196	2.62	**	0.0172	2.78	**	0.0360	2.96	**	0.0129	1.83	*
Size	−1.2862	−5.21	***	−0.9724	−7.15	***	−0.1261	−1.29	ns	−0.0397	−0.36	ns
Leverage	−1.1372	−0.71	ns	−4.4899	−3.68	***	−13.4451	−12.91	***	−9.0618	−15.30	***
Growth	0.0106	1.31	ns	0.0057	0.71	ns	0.0059	0.37	ns	0.0025	0.22	ns
Efficiency	2.0545	9.25	***	1.3191	7.79	***	4.1717	8.90	***	1.4367	7.15	***
Cons	35.9693	6.65	***	29.6612	10.32	***	22.5749	10.08	***	14.2551	5.63	***
Adj R-squared	0.1121			0.1183			0.1110			0.1447		
F(5, 12)	215.11			364.01			199.75			111.31		
Number of obs.	3633			3469			3259			1792		
Panel D												
Prim_Sec_Rank	0.2407	2.69	**	0.2121	2.88	**	0.4605	2.72	**	0.1614	1.63	ns
Size	−1.2897	−5.20	***	−0.9747	−7.20	***	−0.1309	−1.30	ns	−0.0384	−0.35	ns

(Continues)

TABLE 6 | (Continued)

Dependent variable	ROA			Excl. ROA > 20%			ROE			Excl. ROE > 20%		
	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig	Coeff.	t stat.	Sig
<i>Leverage</i>	−1.1269	−0.70	ns	−4.4747	−3.65	***	−13.4369	−12.96	***	−9.0544	−14.87	***
<i>Growth</i>	0.0106	1.32	ns	0.0058	0.71	ns	0.0061	0.39	ns	0.0027	0.23	ns
<i>Efficiency</i>	2.0507	9.25	***	1.3163	7.77	***	4.1621	8.92	***	1.4332	7.18	***
<i>Cons</i>	35.3125	6.73	***	29.0622	10.39	***	21.2766	10.65	***	13.7283	5.48	***
Adj R-squared	0.1118			0.1180			0.0999			0.1447		
<i>F</i> (5, 12)	218.62			340.39			111.54			111.31		
Number of obs.	3632			3468			3171			1792		

Note: This table summarizes the regressions of ROA and ROE on primary versus secondary stakeholder orientation. Panels A and B add a control for the change in ESG incidents from 1 year to the next. Panels C and D do not control for the change in ESG incidents. As a robustness check, Cols. 2 and 4 remove observations with |ROA| or |ROE| > 20%. The regressions control for year fixed effects. Since firm observations can enter each year, the regression errors are clustered by year. Statistical significance at the 1%, 5%, and 10% levels is denoted by

***,

**, and

*, respectively. Appendix A lists the variables.

instrumented (i.e., *PrimStkAct* and *SecStkAct*). Both IVs must fulfill the relevance and exclusion conditions. Panel A of Table 7 shows that both *PrimStkActPeer* and *SecStkActPeer* satisfy the relevance condition because they have an economically sizeable and statistically significant effect on the respective explanatory variable (i.e., *PrimStkAct* and *SecStkAct*). Regarding the exclusion condition, it is likely that the respective *Peer* variables (i.e., *PrimStkActPeer* and *SecStkActPeer*) satisfy this condition. We follow prior studies and argue that our *Peer* variables may provide plausibly exogenous variation to the extent that they overwhelmingly capture decisions made by persons other than a focal firm manager (Cheng et al. 2014; Habermann and Fischer 2023). Further, it is unlikely that a *Peer* variable affects *ESGincident* through channels other than the variable to be instrumented because the respective *Peer* variable represents an exogenous subset of the potential variables to be instrumented, although residual industry and reflection effects can occur (Angrist 2014; Manski 1993). To motivate the use of our IVs, we compute the Durbin–Wu–Hausman statistic, which assesses whether the original regressors are in fact exogenous. The Durbin–Wu–Hausman tests reject the null hypothesis that the regressors are exogenous, as the reported *p*-values are below 0.01 (Durbin 1954; Hausman 1978; Stock et al. 2002; Wu 1973). This finding supports the use of an instrumental-variable approach.

Having motivated the use of IVs, we now specify the following second-stage regression:

$$Y_{it} = \alpha + \beta_1 E(\text{PrimStkAct})_{it-1} + \beta_2 E(\text{SecStkAct})_{it-1} + \sum_k \beta_k \text{controls}_{it-1} + \eta_i + \theta_t + \varepsilon_{i,t} \quad (5)$$

$E(\text{PrimStkAct})_{it-1}$ and $E(\text{SecStkAct})_{it-1}$ are the predicted values from the first stage. Panel B of Table 7 shows the results of the second-stage regressions. While higher levels of $E(\text{PrimStkAct})$ (col. 1, coeff. = −0.3128, $p < 0.01$) and $E(\text{SecStkAct})$ (col. 2, coeff. = −0.4840, $p < 0.01$) both reduce Y_{it} (*ESGincident*), the effect for $E(\text{PrimStkAct})$ does not survive when we include

both second-stage variables in the same model (Panel B, col. 3, coeff. = −0.0979, $p > 0.10$). Thus, the estimates from our IV approach support H1b, possibly indicating a causal link between our primary and secondary stakeholder test variables and *ESGincident*. We also find support for H1a, as our proxy for RepRisk incidents (*ESGincident*) is not reduced when the managerial focus of decision-making is on primary stakeholders (col. 3).

4.6 | Outside Shifts in Stakeholder Preferences

To further identify a possible causal pathway, we explore whether our results are responsive to plausibly exogenous “outside-the-system” shifts in stakeholder preferences. We identify two such shifts. We first contend that outside stakeholders’ and managers’ preferences for actions to generate financial versus societal outcomes became more aligned when many US states joined the Climate Alliance⁷ to commit to a 95% reduction in greenhouse gas emissions by 2050 compared to 1990 levels in line with the Paris Agreement.⁸ The enactment of state-level constituency statutes (Bainbridge 1992) is a second potential outside shift in stakeholder orientation. State-level constituency statutes have been shown to associate with increases in firm patenting activity, arguably because firms were prompted to focus more on non-investor preferences, resulting in less short-termism and more innovation (Flammer and Bansal 2017; Flammer and Kacperczyk 2015). Because Climate Alliance membership and the constituency statutes should encourage firms to consider the widest range of stakeholders’ interests, we predict that the societal and financial foci of outside stakeholders versus inside managers should conflict less when firms operate in a Climate Alliance or constituency statute state versus other states.⁹ In other words, the change in ESG incidents for primary and secondary stakeholders should be more similar on average for firms whose stakeholders have a financial focus versus a societal focus when the firms operate in a Climate Alliance or constituency statute state.

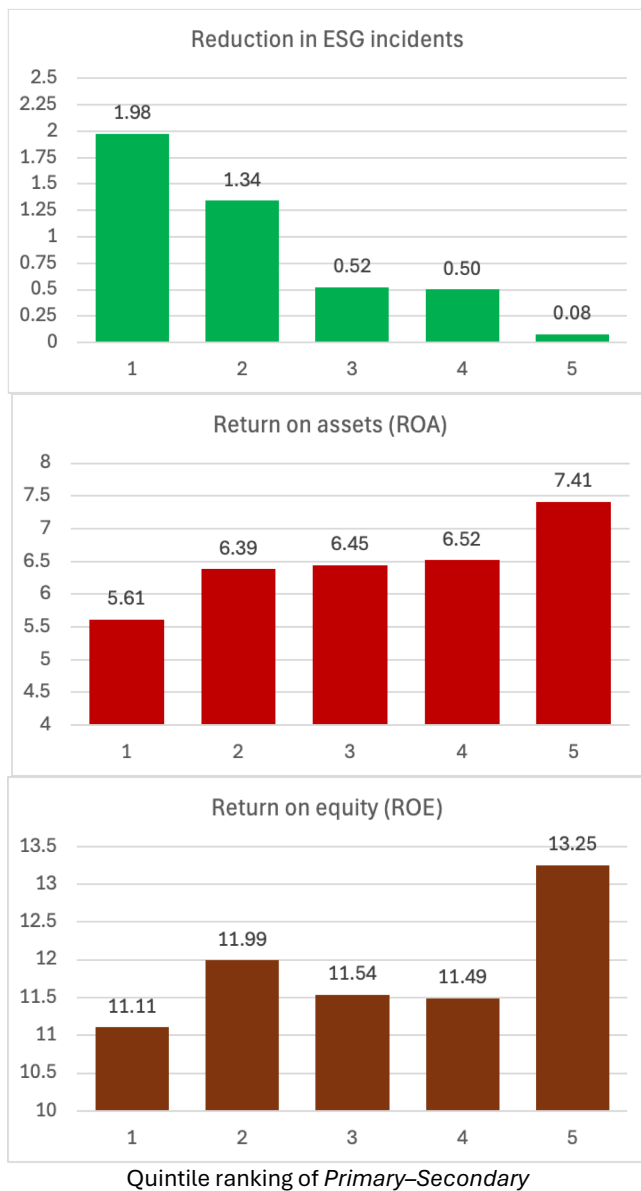


FIGURE 2 | Actual effects of sustainability actions on stakeholders.

The regressions in Appendix B support this prediction. In all cases, the stakeholder coefficients are insignificant (vs. significant in the predicted direction) when the firms join or operate (vs. do not join or operate) in a Climate Alliance or constituency statute state. For example, comparing Panels 1 and 2 of Appendix B, the coefficient for *Prim_Sec_Rank* is not significant for firms operating in a Climate Alliance state (coeff. = -0.0901 , $p > 0.10$) but positive and significant for firms not operating in a Climate Alliance state (coeff. = 1.1013 , $p < 0.01$). Comparing Panels 7 and 8, the coefficient for *Primary-Secondary* is insignificant for firms operating in a constituency statute state (coeff. = 0.0083 , $p > 0.10$) but significant and positive for firms not operating in a constituency statute state (coeff. = 0.0390 , $p < 0.10$).

We also illustrate the effect of an outside shift in stakeholder preferences by plotting the mean $\Delta ESGIncident$ and ROA by *Prim_Sec_Rank*. Figure B1 shows the trend in reduction of ESG incidents and firm's ROA (y-axis) as a function of the quintile

ranking of *Prim_Sec_Rank* (x axis). Consistent with the coefficients from the regression analysis, the plots are flatter for firm-year observations in constituency states (Panels A3 and B3) than in non-constituency states (Panels A2 and B2). In sum, we observe the predicted differences in the regression coefficients based on two different outside-the-system shifts in stakeholder preferences.

4.7 | Additional Robustness Tests

To strengthen our findings, we conduct the following additional robustness tests. We first address measurement error using Violation Tracker data as an alternative outcome variable (Violation Tracker 2024). This dataset lists the charges filed against firms by U.S. government agencies for safety (50% of all charges), employment (23%), environmental (14%), healthcare (7%), consumer (4%), and finance-related offenses (2%). It has been used in accounting, management, and strategy research to assess corporate misconduct (Abebe and Acharya 2022; Campbell and Shang 2022; Merkley 2014; Raghunandan 2021). We match Violation Tracker data with our sample firms and test whether the effect of primary and secondary actions on Violation Tracker data reveals a pattern similar to that for RepRisk ESG incidents. We describe the model settings in detail and show the results in Online Appendix S1 (Table S1 and Figure S1). In short, we draw the same inferences about how a primary versus secondary stakeholder orientation affects sustainability outcomes regardless of whether we use Violation Tracker data or RepRisk ESG incidents.

Second, in Online Appendix S2, we estimate Equations (1) and (2) with different variable and fixed effect specifications, including additional covariates used in prior similar studies of primary and secondary stakeholder orientation (Cuervo-Cazurra et al. 2023; Graf-Vlachy et al. 2020; Padgett and Galan 2010; Ramaswamy et al. 2017; Servaes and Tamayo 2013; Strike et al. 2006; Udayasankar 2008). For instance, we use alternative definitions of *PrimStkAct* and *SecStkAct*, including a test using MSCI-ESG data to measure actions directed toward stakeholders. Table S2 summarizes the regressions. Taken together, the results across 24 different sensitivity tests do not qualitatively change the overall conclusions of this study.

Third, in Table S3 of Online Appendix S3, we estimate whether the *PrimStkAct* and *SecStkAct* coefficients in Equation (1) differ for higher versus lower levels of pressure from monitoring by creditors (favoring financial results) or from the voting proposals of sustainability-minded shareholders (favoring pro-societal results). This creditor or shareholder additional pressure does not fundamentally change our findings or refute our theory.

Fourth, we respecify Equations (1) and (2) where the dependent variable (*ESGIncident*) can lead the regressors by up to 4 years. As reported in Online Appendix S4 (Table S4), the association between a primary versus secondary stakeholder orientation and ESG incidents holds at several horizons up to 3 years ahead and attenuates thereafter, consistent with sustainability-related effects that accrue over multiple periods (Eccles et al. 2014; Ortiz-de-Mandojana and Bansal 2016).

TABLE 7 | IV regression of RepRisk incidents on primary and secondary stakeholders.

Panel A: First-stage regression									
Dependent variable	PrimStk Act			SecStk Act			PrimStk Act		
	Coeff.	t stat	Sig.	Coeff.	t stat	Sig.	Coeff.	t stat	Sig.
<i>PrimStkActPeer</i>	0.7248	15.70	***				0.9016	16.55	***
<i>SecStkActPeer</i>				0.6004	7.26	***	−0.2907	−6.00	***
Controls	Yes			Yes			Yes		Yes
FE = industry, year	Yes			Yes			Yes		Yes
Number of obs.	3254			3254			3254		3254
Durbin–Wu–Hausman (<i>p</i> value)	0.0000		***	0.0000		***	0.0000		***
Panel B. Second-stage regression									
Dependent variable	ESG incident			ESG incident			ESG incident		
	Coeff.	t stat	Sig.	Coeff.	t stat	Sig.	Coeff.	t stat	Sig.
<i>E (PrimStkAct)</i>	−0.3128	−4.34	***				−0.0979	−1.28	
<i>E (SecStkAct)</i>				−0.4840	−6.44	***	−0.4382	−5.30	***
Controls	Yes			Yes			Yes		Yes
FE = industry, year	Yes			Yes			Yes		Yes
Number of obs.	3254			3254			3254		3254
Adjusted <i>R</i> ²	0.7448			0.7352			0.7289		
Durbin–Wu–Hausman (<i>p</i> value)	0.0010		***	0.0001		***	0.0002		***

Note: This table summarizes the results of instrumental variable (IV) regressions for *RepRisk incidents* and *PrimStkAct* and *SecStkAct*. The firm-specific control variables are the same as in Table 4. Partial *R*² refers to the respective instrumental variables. Durbin–Wu–Hausman test *p* values are also reported. The regressions control for industry and year fixed effects. The regression errors are clustered by year. Statistical significance at the 1%, 5%, and 10% levels is denoted by
 ***,
 **, and
 *, respectively. Appendix A lists the variables.

5 | Conclusion

The literature on stakeholder theory reveals limited empirical evidence on the heterogeneous and dynamic outcomes stemming from the actions of firm managers directed toward different stakeholder groups. We address this research gap by examining whether and how firms' relationships with primary and secondary stakeholders generate positive or negative sustainability outcomes. As an explanation of why and how these different outcomes can occur, we construct a cross-disciplinary conceptual framework. We specify two categories of outside stakeholders: primary and secondary stakeholders. Our framework also includes managers—to whom some outside stakeholders (e.g., investors and creditors) delegate their decision rights—whose actions can affect firm-level financial and societal sustainability outcomes.

We find support for our conceptual framework. In particular, we find that when managers' actions focus on or shift in focus toward secondary stakeholders—who likelier prefer actions to improve societal sustainability outcomes—this associates with a reduction in ESG incidents compared to when managers align their actions toward primary stakeholders, which relates to an increase in ESG incidents. We also find, consistent with a conflict between managers and outside stakeholders for different sustainability outcomes, that when managers focus on secondary stakeholders, this leads to better societal outcomes for this group but at the expense of worse financial outcomes for primary stakeholders. For managers, these findings suggest an ethical dilemma. Finding the right balance for both groups requires that managers identify and align their decisions to the heterogeneous and dynamic preferences of all outside stakeholders. Our results also suggest that near-equilibrium financial and societal sustainability outcomes are best achieved when managers and outside stakeholders share common views on those preferences.

We recognize that our study has limitations. First, our analysis focuses on large United States-listed firms. Accordingly, the findings may not generalize to smaller or privately held firms, nor to firms operating in other institutional settings such as Europe or emerging markets, where stakeholder preferences, regulatory environments, and reporting practices can differ. Second, although we employ rich archival data and multiple robustness tests, our empirical design remains mainly associative. In particular, managers' preferences and stakeholder-specific sustainability demands are not directly observable, and we cannot fully attribute individual ESG incidents to a specific managerial action. Third, our measures of actions toward primary and secondary stakeholders necessarily rely on proxies constructed from ESG data providers, which may not capture the full complexity of managerial tradeoffs across stakeholder groups. These limitations notwithstanding, we believe our findings offer a useful starting point for understanding how managerial sustainability actions can generate heterogeneous financial and societal outcomes across stakeholder groups.

Thus, our study reveals several avenues of future research. First, future work could delve deeper into whether and how managers trade off outcomes associated with their own preferences against outcomes preferred by the different stakeholder groups. One consideration is the role of ESG compensation.

Recent work (Bebchuk and Tallarita 2023; Chaigneau and Sahuguet 2025) indicates that the adoption of ESG compensation plans does not always lead to improved sustainability outcomes. A second area for future work is to study the quantity and quality of available firm-level financial report information that would enable primary and secondary stakeholders to assess better whether managers' sustainability actions are consistent with their own. The way managers introduce sustainability disclosures into corporate reports—whether to enhance their reputation or to cater to specific stakeholder groups (e.g., institutional vs. retail investors)—could also be investigated (Pawliczek et al. 2021; Perrini and Tencati 2006). A step in this direction is the European Parliament's CSRD directive (CSRD 2022), requiring greater disclosure and discussion by large companies operating in Europe of material non-financial impacts that are now mostly revealed through commercial platforms such as RepRisk and Violation Tracker. Third, our study could be applied to smaller firms, as ESG and impact investing could have more success in private equity firms (Abraham et al. 2024; Wiek and Villegas 2024), possibly because it is easier to align stakeholders' preferences with those of the manager, who can often be the same person.

Author Contributions

Felix B. Fischer: conceptualization, writing – original draft, writing – review and editing, project administration, validation. **Paul A. Griffin:** conceptualization, methodology, software, data curation, investigation, validation, formal analysis, visualization, resources, writing – original draft, writing – review and editing. **Florian Habermann:** conceptualization, methodology, software, data curation, investigation, validation, formal analysis, visualization, resources, writing – original draft, writing – review and editing.

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Endnotes

¹ While the prior literature uses the term “outside” (or “external”) to describe stakeholders outside the traditional boundary of the firm such as suppliers and communities (Harrison and St. John 1996), we use the term for both primary and secondary stakeholders without operational decision rights.

² As such, our conceptual framework is essentially an abstraction of a governance structure, where we focus on the tension between primary and secondary stakeholders with competing interests in firm outcomes (divergent preferences) requiring prioritization by the firm manager.

³ While such a scenario is a near-equilibrium solution, it is unlikely to be identifiable in practice given that stakeholder preferences are not holistically known by the manager, or if known for some stakeholders, can result in misaligned sustainability actions by managers for behavioral reasons.

⁴Our two scenarios are not unlike the theory in Aghion et al. (2023; Figure 1) in the setting of societal attitudes to innovation and price competition. They show that when citizens have strong pro-social attitudes—which we interpret as broadly the same as having societal preferences—price competition in the product markets increases firms' sustainability performance, in particular, generates the outcome of reduced pollution. The opposite occurs when citizens have weak societal attitudes.

⁵Some analyses (e.g., Table 4) employ slightly smaller sample sizes due to lagged covariates.

⁶Nevertheless, ESG scores are not free of criticism (Berg et al. 2022). We also use similar MSCI scores in a robustness test (see Table S2).

⁷<https://usclimatealliance.org/>.

⁸In terms of our conceptual framework, this corresponds to a shift from an “off-equilibrium” scenario in the direction of a “near-equilibrium” scenario.

⁹This view may not apply uniformly to all firms, however. Bebchuk and Tallarita (2020, 91) argue that this shift toward stakeholderism in response to constituency statutes is “mostly for show rather than a reflection of plans to improve the treatment of stakeholders.”

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Supporting Information

Additional supporting information can be found online in the Supporting Information section. **Appendix S1:** Alternative outcome variable. **Table S1:** Regressions based on Violation Tracker incidents. **Figure S1:** Frequency of RepRisk and Violation Tracker ESG Incidents. **Appendix S2:** Alternative regression specifications. **Table S2:** Regressions based on alternative specifications. **Appendix S3:** Capital structure analysis. **Table S3:** Regression tests of capital structure effects. **Appendix S4:** Long-term effects. **Table S4:** Effects of Primary and Secondary Stakeholder Orientation on future ESG incidents.

Appendix A: Variable Definitions

Variable	Description
Dependent variables	
ESG Incident (<i>ESGincident</i>). $\Delta ESGincident$ is the change in <i>ESGincident</i> from the previous year.	RepRisk incident score proxies a firm's (negative) sustainability impact. The score ranges from 0 to 100, where 0 is the <i>best</i> possible performance (i.e., no ESG incident for the respective firm) while 100 is the <i>worst</i> (i.e., many current and severe incidents with far reach). The RepRisk incident score covers 28 ESG issues spanning from the environmental pillar including climate change incidents to the pillar including incidents concerning human rights abuses or child labor to the governance pillar including bribery, fraud, or tax evasion.
Violation Tracker: Number of offenses	Count of offenses per firm over the study period.
Violation Tracker: Sum of penalty amounts > 0	Natural logarithm of the sum of penalty amounts > 0 over the study period.
Covariates	
Aggregated Primary Stakeholder Actions Score (<i>PrimStkAct</i>)	$[ProductResponse + Workforce + Governance]/3 = PrimStkAct$.
<i>PrimStkActPeer</i>	Average <i>PrimStkAct</i> for industry peers.
Workforce Score (<i>Workforce</i>)	LSEG legacy Workforce category score. Measures a company's effectiveness toward job satisfaction, healthy and safe workplace, maintaining diversity and equal opportunities, and development opportunities for its workforce.
Product Responsibility Score (<i>ProductResponse</i>)	LSEG legacy score. Does the company monitor the impact of its products or services on consumers or the community more generally.
Governance Pillar Score (<i>Governance</i>)	LSEG legacy Governance Pillar Score is the weighted average relative rating of a company based on the reported governance information and the resulting three governance category scores.
Aggregated Secondary Stakeholder Actions Score (<i>SecStkAct</i>)	$[Environment + Community + Diversity + HumanRights]/4 = SecStkAct$.
<i>SecStkActPeer</i>	Average <i>SecStkAct</i> for industry peers.
<i>Primary-Secondary</i>	$PrimStkAct - SecStkAct$.
<i>Prim_Sec_Rank</i>	Quintile ranking of <i>Primary-Secondary</i> based on rank order.
<i>Prim_Sec_PCRank</i>	Quintile ranking of <i>Primary-Secondary</i> based on percentile.
<i>PrimStkAct_Alt</i>	$[Environment + Community + Diversity + HumanRights]/4$
Alternative Aggregated Secondary Stakeholder Actions Score (<i>SecStkAct_Alt</i>)	$SecStkAct_Alt = [Environment + Community + HumanRights]/3$
<i>SecStkAct_Alt2</i>	$SecStkAct_Alt2 = [Environment + HumanRights]/2$
<i>Environmental Pillar Score (Environment)</i>	LSEG legacy weighted average relative rating of a company based on the reported environmental information and the resulting three environmental category scores.
<i>Community Score (Community)</i>	LSEG legacy Community category score measures the company's commitment toward being a good citizen, protecting public health and respecting business ethics.
<i>Diversity Score (Diversity)</i>	LSEG legacy score: Does the company have a policy to drive diversity and equal opportunity?
<i>HumanRights Score (HumanRights)</i>	LSEG legacy score for human rights score measured as a company's effectiveness toward respecting the fundamental human rights conventions.

Variable	Description
Other variables	
<i>Natural Log Total Assets (Size)</i>	Natural logarithm of the total assets of a company.
<i>Return on Assets (ROA)</i>	Operating profit for the fiscal period scaled by lagged Total Assets expressed as percentage.
<i>Return on Equity (ROE)</i>	Income After Taxes for the fiscal period scaled by lagged Common Equity expressed as percentage.
<i>Total Debt/Total Assets (Leverage)</i>	Total Debt Outstanding, which includes Notes Payable/Short-Term Debt, Current Portion of Long-Term Debt/Capital Leases and Total Long-Term Debt divided by the total assets.
<i>MSCI_PrimStkAct</i>	$MSCI_PrimStkAct = [HLTH_SAFETY_MGMT_SCORE + CORPORATE_GOV_THEME_SCORE + NATURAL_RESOURCE_USE_THEME_SCORE + CARBON_EMISSIONS_SCORE + CLIMATE_CHANGE_THEME_SCORE]/5.$
<i>MSCI_SecStkAct</i>	$MSCI_SecStkAct = [PRODUCT_SAFETY_THEME_SCORE + ENVIRONMENTAL_PILLAR_SCORE + LABOR_MGMT_SCORE]/3.$
<i>Climate Alliance</i>	State-level Climate Alliance membership = 1 for year of membership and thereafter, and 0 otherwise.
<i>Constituency Statute</i>	Constituency Statute state = 1 for year of passage of the law and thereafter, and 0 otherwise.
<i>Creditor Pressure</i>	High creditor pressure = 1 if the debt-to-equity is above the sample median by year, and 0 otherwise.
<i>Shareholder Pressure</i>	Incidence of a shareholder resolution on environmental matters in a firm's proxy statement filing = 1 if the firm was subject to a pro-societal shareholder resolution in a particular year, and 0 otherwise.
<i>Sales Growth (Growth)</i>	Sales in t /Sales in $t - 1$ minus 1.
<i>Efficiency (Efficiency)</i>	Total Revenue/Average beginning and the end of the year Total Assets.

Appendix B: Outside Shifts in Stakeholder Preferences: Regression Analysis

	Coeff.	t stat	Sig.		Coeff.	t stat	Sig.
1. Climate alliance				5. Constituency statute			
<i>Prim_Sec_Rank</i>	−0.0901	−0.18	ns	<i>Secondary</i>	−0.0290	−1.22	ns
<i>Lagged ESGincident</i>	0.4325	12.26	***	<i>Lagged ESGincident</i>	0.4521	13.77	***
<i>Size</i>	2.4375	3.68	***	<i>Size</i>	2.5663	2.91	**
<i>Leverage</i>	3.2960	1.06	ns	<i>Leverage</i>	−2.6692	−0.95	ns
<i>Growth</i>	−0.0295	−1.73	ns	<i>Growth</i>	−0.0116	−1.04	ns
<i>Efficiency</i>	0.2991	0.23	ns	<i>Efficiency</i>	−0.5852	−0.66	ns
<i>Cons</i>	−39.5055	−2.68	**	<i>Cons</i>	−39.5377	−1.87	*
FE = year, firm	Yes			FE = year, firm	Yes		
Adj R-squared	0.8048			Adj R-squared	0.7985		
Number of obs.	1151			Number of obs.	1478		
2. Not climate alliance				6. Not constituency statute			
<i>Prim_Sec_Rank</i>	1.1013	3.83	***	<i>Secondary</i>	−0.0524	−2.01	*
<i>Lagged ESGincident</i>	0.4720	9.88	***	<i>Lagged ESGincident</i>	0.4819	12.30	***
<i>Size</i>	2.1702	3.68	***	<i>Size</i>	2.2059	4.72	***

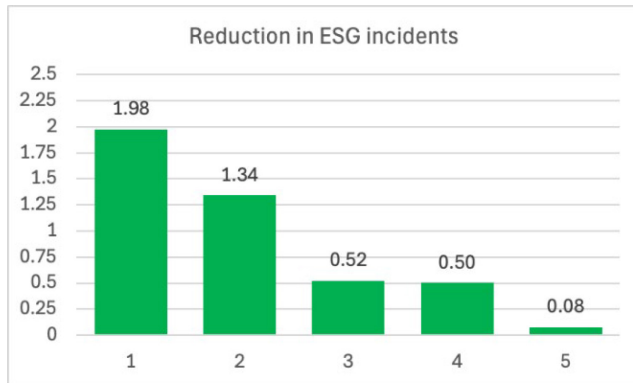
	Coeff.	t stat	Sig.		Coeff.	t stat	Sig.
<i>Leverage</i>	−1.2484	−0.79	ns	<i>Leverage</i>	0.9170	0.60	ns
<i>Growth</i>	0.0001	0.02	ns	<i>Growth</i>	−0.0012	−0.13	ns
<i>Efficiency</i>	−1.2365	−1.53	ns	<i>Efficiency</i>	−1.3627	−1.78	ns
<i>Cons</i>	−36.1687	−2.52	**	<i>Cons</i>	−31.9404	−2.90	**
FE=year, firm	Yes			FE=year, firm	Yes		
Adj R-squared	0.7849			Adj R-squared	0.7795		
F(6, 11)	117.50			F(6, 11)	93.85		
Number of obs.	2101			Number of obs.	1769		
3. Constituency statute				7. Constituency statute			
<i>Primary</i>	−0.0006	−0.03	ns	<i>Primary-Secondary</i>	0.0083	0.46	ns
<i>Secondary</i>	−0.0287	−1.11	ns				
<i>Lagged ESGincident</i>	0.4521	13.71	***	<i>Lagged ESGincident</i>	0.4513	13.70	***
<i>Size</i>	2.5673	2.94	**	<i>Size</i>	2.5407	2.89	**
<i>Leverage</i>	−2.6703	−0.95	ns	<i>Leverage</i>	−2.5485	−0.94	ns
<i>Growth</i>	−0.0116	−1.04	ns	<i>Growth</i>	−0.0110	−1.01	ns
<i>Efficiency</i>	−0.5830	−0.66	ns	<i>Efficiency</i>	−0.5903	−0.67	ns
<i>Cons</i>	−39.546	−1.88	*	<i>Cons</i>	−40.572	−1.94	*
FE=year, firm	Yes			FE=year, firm	Yes		
Adj R-squared	0.7984			Adj R-squared	0.7983		
F(7, 11)	52.90			F(6, 11)	56.35		
Number of obs.	1478			Number of obs.	1478		
4. Not constituency statute				8. Not constituency statute			
<i>Primary</i>	0.0225	1.25	ns	<i>Primary-Secondary</i>	0.0390	2.18	*
<i>Secondary</i>	−0.0629	−2.30	**				
<i>Lagged ESGincident</i>	0.4810	12.19	***	<i>Lagged ESGincident</i>	0.4804	12.01	***
<i>Size</i>	2.1213	4.40	***	<i>Size</i>	1.8729	3.87	***
<i>Leverage</i>	0.6974	0.43	ns	<i>Leverage</i>	0.7657	0.49	ns
<i>Growth</i>	−0.0010	−0.10	ns	<i>Growth</i>	0.0003	0.03	ns
<i>Efficiency</i>	−1.4861	−1.93	*	<i>Efficiency</i>	−1.6819	−2.14	*
<i>Cons</i>	−30.428	−2.69	**	<i>Cons</i>	−26.631	−2.30	**
FE=year, firm	Yes			FE=year, firm	Yes		
Adj R-squared	0.7795			Adj R-squared	0.7792		
F(7, 11)	106.36			F(6, 11)	108.86		
Number of obs.	1769			Number of obs.	1769		

Note: This table summarizes regressions that explore whether the coefficients for *PrimStkAct* or *SecStkAct* or *PrimStkAct* minus *SecStkAct* change due to an outside shift in stakeholder preferences. Panels 1 and 2 compare the coefficients for firms in states that joined versus did not join the Climate Alliance. Panels 3 and 4 compare the coefficients for firms in states that enacted vs. did not enact constituency statutes. Panels 5 and 6 compare the coefficients for *Secondary* stakeholder orientation for firms in states that enacted vs. did not enact constituency statutes. Panels 7 and 8 compare the coefficients for *Primary* minus *Secondary* stakeholder orientation for firms in states that enacted vs. did not enact constituency statutes. The regressions control for firm and year fixed effects. Since firm observations can enter each year, the regression errors are clustered by year. Statistical significance at the 1%, 5%, and 10% levels is denoted by

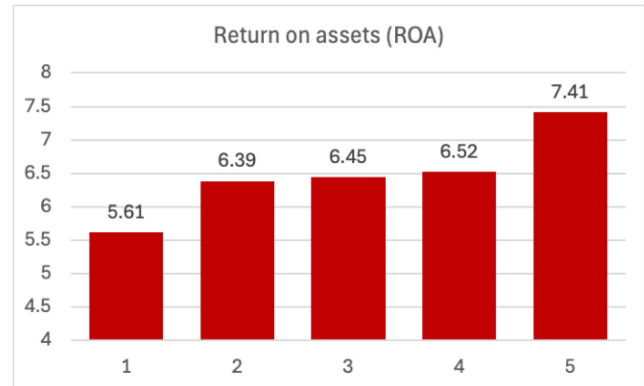
*** **, and

*, respectively. Appendix A lists the variables.

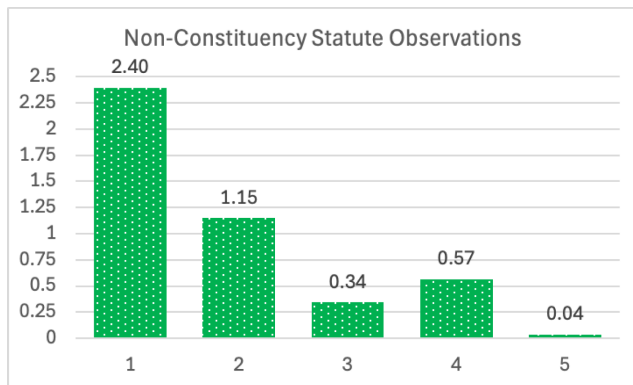
Outside Shifts in Stakeholder Preferences: Visual Analysis



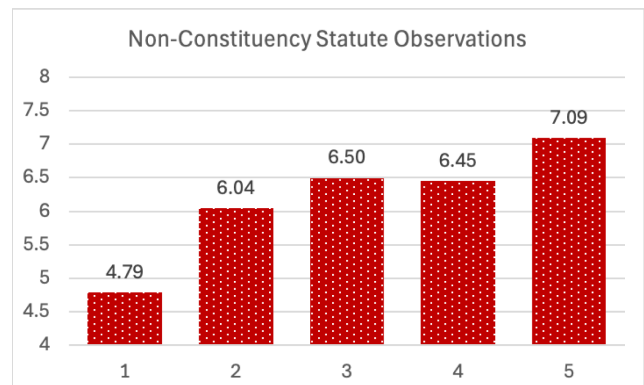
A1



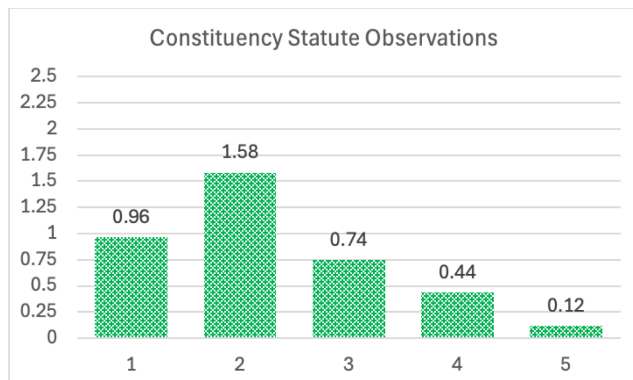
B1



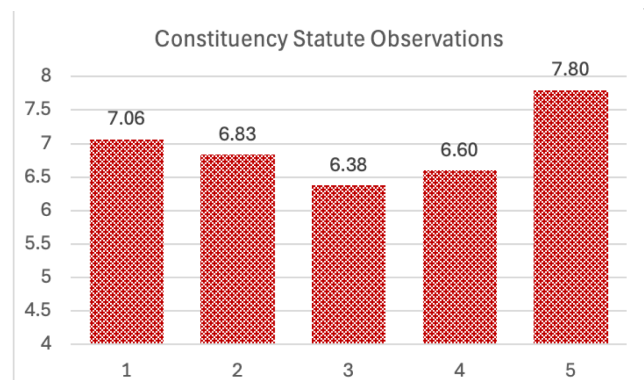
A2



B2



A3



B3

FIGURE B1 | Outside shifts in stakeholder preferences.

These figures provide a visual interpretation of the constituency statute results in Appendix B. Compared to Panel A1 (all observations), the green plots show that the decrease in ESG incidents (y axis) is *greater* when the quintile ranking of *Prim_Sec_Rank* (x-axis) is small (= 1) and the firm resides in a non-constituency statute (Panel A2) state versus a constituency statute state (Panel A3). Compared to Panel B1 (all observations), the red plots show that ROA (y-axis) is *lower* when the quintile ranking of *Prim_Sec_Rank* (x-axis) is small (= 1) and the firm resides in a non-constituency statute (Panel B2) state versus a constituency statute state (Panel B3). In general, the panels for the constituency statute states are flatter across the quintile ranking of *Prim_Sec_Rank*.