

On Fraud and Certification of CSR*

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Abstract

We analyze the strategic decision of firms to invest in corporate social responsibility (CSR) and to subsequently certify (or not) its production in settings where there is scope for fraud in uncertified products. Equilibrium outcomes crucially depend on endogenous consumers' beliefs about the credibility of firms' uncertified claims. We show that the key feature that makes fraud likely is the less than complete consumers' trust on uncertified claims, which arises under intermediate costs of CSR production relative to fraud costs. Our results support that the scenarios where certification is the largest do not correspond with those where CSR investments are at its highest. A reduction in CSR production costs relative to the costs of committing fraud extends the likelihood of CSR production, but this does not generally increase the likelihood of certification. In fact, certification is the largest for an interior level of CSR production costs. In addition, although we see that generally price premia match the corresponding marginal production costs, under Cournot competition the presence of fraud results in a differentiation price premium below the marginal CSR production costs and a certification price premium above marginal certification costs.

Key words: asymmetric information, credence good, certification, fraud, environmental quality, corporate social responsibility.

JEL codes: C72, D43, H23, Q58.

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