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The New Meaning of Corporate Social Responsibility

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"Corporate social responsibility" is hardly a new refrain, but it now comes at an awkward moment. To an ever-larger extent, it seems, corporations are being called upon to respond to the needs of "stakeholders" other than investors. At this writing, despite seven years of a healthy economic expansion and strong profits, the real median wage is still below where it was in 1989, before the last recession, and a significant portion of the American workforce continues to experience downward mobility. At the same time, federal and state governments have limited financial means to ease the stresses on the workforce. While the recovery has helped balance public budgets and even generated some surpluses, governments are under continuing pressure to rein in spending.

Yet this renewed interest in corporate social responsibility comes, ironically, at a time when investors—many of them large institutions with the capacity and will to topple underperforming CEOs—are escalating their demand that corporations maximize shareholder returns. The movement for better and more responsive "corporate governance" seeks to ensure that managers act in the best interests of their shareholders. Compensation of top corporate officers is more tightly linked to share prices than ever before. The steady improvement in corporate profitability over the last few years is due, at least in part, to restructurings that have resulted either in layoffs or in diminished wages and benefits.

Of course, many American corporations continue to be exemplars of "responsibility" to their employees and communities, and it is not my intention in this essay to criticize corporate behavior. The nation is now far more competitive—and, arguably, far more productive—than it was in the 1980s. This allows our society to achieve a whole range of social objectives that it otherwise could not achieve. Moreover, many companies have taken an active role in improving

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their communities and have given their employees a share in their new-found prosperity.

The issue here is not whether companies should be responsible in some way to society, but rather *how* they should be responsible: Is there a new meaning for corporate social responsibility, consistent both with the greater need for corporate responsiveness to employees and communities and with the greater demands from investors for performance?

Consider some recent activities of American companies in light of these intensifying demands:

- An American-based manufacturer of textiles and sporting gear subcontracts with producers in Latin America and Southeast Asia, whose employees, including some 13-year-olds, work twelve-hour days and are paid a small fraction of U.S. wages.
- A large corporation announces that it will be laying off a significant portion of its workforce, and then announces a pay increase for its top executives.
- A coalition of companies undertakes a major advertising campaign designed to convince voters to reject a plan to expand health-care coverage to all Americans.
- Companies mount an intensive lobbying effort directed at Congress and the White House to weaken certain worker protections; the lobbying effort includes substantial, although technically legal, contributions to the election campaigns of key legislators.
- After a major corporation announces that it's considering relocating a facility where it now employs several thousand people to any state in the region that will give it the largest tax break, it receives a package of tax abatements worth several million dollars—a sum which otherwise would have been spent improving the local schools.

Note that all of these actions were legal. Presumably, all were done for the purpose of improving profits and maximizing shareholder value. In several cases, chief executive officers claimed that they had no choice but to take these actions, given their responsibilities to shareholders. Institutional investors expected, or demanded, as much. But all of these instances also elicited public criticism and charges that the corporations in question were acting unethically or irresponsibly with regard to society at large.

Public Opinion

One way to sort through these examples is to begin with the now conventional proposition that a company has only one responsibility, both morally and legally: to maximize the value of the shares of those who have invested in it. Corporate board members and executives are "fiduciaries" under the

law—agents solely of those who have invested capital in the corporation. But in fulfilling their responsibility to their investors, according to this view, boards and executives also indirectly fulfill their core responsibility to the rest of society—to other "stakeholders" such as their employees, members of their community, and fellow citizens—because they help assure that society's productive assets are allocated to their most efficient uses. Robert Eaton, chairman and CEO of Chrysler, recently stated this proposition clearly: "Companies that focus on making money become more competitive, and that in turn means more economic growth, and more jobs, and all the other results that 'stakeholders' care about." By this logic, a corporate executive has an affirmative obligation to do any of the above-mentioned things where it can safely be concluded that doing so is more likely to improve shareholder returns than not doing so (and the executive must refrain where the likely calculus is just the reverse).

The "efficient" deployment of productive assets doesn't include everything that society may want of or need from a corporation, of course. But it might be argued that other social concerns extending beyond mere efficiency could still be tucked into this simple calculation if executives took full account of public opinion as it affected the bottom line. Most companies are concerned about their public images because they sell their products directly or indirectly to the public; indeed, companies spend billions of dollars each year burnishing their public images. Anything that tarnishes that image may result in lost sales, and also may make it more difficult for the company to receive permits, subsidies, or other discretionary benefits from government.

The examples I listed at the start come from stories in the national press, reflecting badly on the companies in question or at least highlighting certain activities of which a significant portion of the public disapproves. Under this refined calculus, we might conclude that the companies behaved "socially irresponsibly" to the extent that their actions generated negative publicity which, in turn, harmed the company to a greater extent than the actions otherwise benefitted the company.

Such a seemingly simple calculation offers little by way of practical guidance, however. In the first place, company officials may have difficulty gauging the likelihood of "bad press" before the fact. How was Nike to know that it would be reproached for the way it dealt with Asian workers when U.S. manufacturers had been outsourcing to Asia for years? Likewise, AT&T arguably had no way of predicting that its announcements at the start of 1996 would ignite a firestorm of protest, since downsizing already had been a major business strategy and CEO compensation packages had been rising quickly for more than a decade. And there was nothing unusual about any of the examples of corporate political activities: Corporations have become steadily more aggressive and effective in the political arena during the past several decades. One might argue that the executives should have been more sensitive to public opinion, and perhaps they and their peers will be in the future when similar situations arise. But, by these lights, the fault lies not in their lack of social responsibility but in their

lack of foresight of public opinion; the failure is one of public relations rather than ethics.

Even where public criticism can be anticipated and its magnitude estimated, there is almost no way to judge whether investors nonetheless are likely to be better off, on balance, for the companies engaging in such activities. Public outrage can be fleeting; memories as short as one news cycle or the days until the next public-affairs talk show or edition of a weekly news magazine. The outrage may be confined to a relatively small but noisy group, with no appreciable negative effect on sales. On the other hand, the ongoing benefits to shareholders of engaging in these activities can be considerable. Perhaps the above-mentioned decisions were "wise," negative reactions notwithstanding. Bad notices about sweatshops may cut into profit margins, but maybe not as much as the cost of shifting production to places that treat employees better, or regularly inspecting every cutting and sewing shop around the world. In the wake of AT&T's bad press, big companies refrained for a time from trumpeting major layoffs. But eight months later, the trumpeting resumed. Likewise with corporate politics: Financing a public-relations campaign against a complex and costly health-care plan, pouring "soft money" into elections, and contriving special tax breaks may all elicit unfriendly comment, but their benefits for shareholders are potentially far greater than such costs.

Long-Term Convergence

Some advocates of corporate "social responsibility" take a somewhat different tack. They argue that what's good for the company's shareholders over the long term is also good for its other stakeholders over the long term (and, presumably, what's bad for these broader interests is also bad for shareholders, eventually). That is, if one looks far enough in the future, all interests converge; all stakeholders are ultimately the same. All have an interest in a strong economy, well-paid employees, a healthy and clean environment, and a socially tranquil society. This sunny view was perhaps best memorialized in the words of Charles Erwin ("Engine Charlie") Wilson, president of General Motors when Dwight Eisenhower tapped him to become Secretary of Defense in 1953. When asked at his confirmation hearing whether he would be capable of making a decision in the interest of the United States that was adverse to the interests of GM, Wilson replied, "I cannot conceive of one because for years I thought what was good for our country was good for General Motors, and vice versa. The difference did not exist. Our company is too big. It goes with the welfare of the country."

Surely, there is something to this argument even today. Consider Nike's plight: American clothes and sporting-goods manufacturers need strong export markets for their products, so presumably they have a long-term interest in creating large and acquisitive middle classes in the developing nations where they now pay workers pennies an hour. Or consider a company, like AT&T, deciding

whether to lay off a large portion of its workforce. Companies want their employees to be loyal and dedicated. They have a long-term interest in fostering an atmosphere in which workers aren't constantly frightened of losing their jobs. They also want employees in general to have enough purchasing power to be able to buy the goods and services they produce. By this logic, companies will generally refrain from mass layoffs unless such layoffs are necessary in order to stay competitive. Finally, consider the last three examples, involving corporate political activity. American companies want to be based in a stable society with a legitimate government, so presumably they have a long-term interest in making sure that corporate power does not distort the responsiveness of elected officials to public needs.

Yet, the "long-term" argument doesn't offer much more practical guidance than does the calculus over public opinion. The criterion is simply too broad and ill-defined. Long-term profit-maximization could be made to seem compatible with almost any socially worthwhile thing—and incompatible with almost anything deemed socially questionable—for the simple reason that corporations are social creations whose very existence depends on the willingness of societies to endure and support them. On the other hand, profit-maximization also enhances growth and allocative efficiency, which over the long term make it possible for a society to achieve all sorts of social objectives.

Moreover, fuzzy long terms are no match for hard-nosed short terms. Capital markets are notoriously impatient, and are becoming less patient all the time. Most of today's institutional investors have no particular interest in a "long term" that extends much beyond the next quarter, if that long. Chrysler's Bob Eaton sounded a common refrain: "Institutions have one central goal, and that's to get consistent, year-in and year-out returns from the companies in their portfolios. They need these returns because their individual shareholders do follow the old Wall Street rule—if they're not satisfied, they sell. At the same time, people like me and others who run companies like to think of ourselves as builders. We think five and ten years ahead. We like to invest in the future . . . So there's some natural tension between the need to provide returns and the need to build the company."

In principle, of course, ambiguities about long-term convergence could be reduced if a society's political and moral leaders clarified what is expected of corporations beyond maximizing shareholder returns. Presidents once routinely "jaw-boned" major industries into postponing price increases. Now, presidents exhort them to hire welfare mothers. But to the extent that these exhortations are directed at all companies, they are unlikely to have much affect on the decision making of any one of them. There's no reason to assume that any single company's investors would willingly forego returns for the sake of achieving some articulated social purpose. It's the classic free rider problem: Let the other guys take the responsibility, we're taking our profits.

The same free-rider problem arises in many other contexts. It is in the long-term interest of all companies (and their investors) to have a well-trained

workforce, for example. But it is not in the interest of any single company to train their workers in skills that could be applied anywhere in the industry or beyond. Thus, firms provide their employees with a great deal of company-specific training, but little or no generic skill development.

Stakeholder Democracy

We need not accept the initial proposition that the only responsibility of corporate executives is to their shareholders. At the time of "Engine" Charlie's dictum, it was widely assumed in America that corporate executives' responsibilities extended beyond their shareholders. These social responsibilities were quite independent of any potential effects on share prices of public opinion or of long-term social consequences of corporate action. In fact, they were to be balanced against the interests of shareholders. "The job of management," proclaimed Frank Abrams, chairman of Standard Oil of New Jersey in a 1951 address that was typical of the era, "is to maintain an equitable and working balance among the claims of the various directly interested groups...stockholders, employees, customers, and the public at large. Business managers are gaining in professional status partly because they see in their work the basic responsibilities [to the public] that other professional men have long recognized in theirs." The top executives of America's major corporations had emerged from World War Two as "corporate statesmen," who had overseen defense production for the nation as a whole. Many continued to view themselves more as professionals with public responsibilities than solely as agents of private interests. And, importantly, they possessed significant autonomy. Because capital markets were far less efficient than they are today—boards were often hand-picked and docile, investors were quiescent—these executives had substantial discretion to implement their quasi-public visions.

The lofty sentiments of the mid-century "corporate statesmen" may have sounded admirable, but they posed a dilemma for democracy because these statesmen were unelected. Accountable neither to shareholders nor to the public, society could not trust that the balance they reached was the best. Profitable companies did not lay off their employees, for example, even when it may have been in the best interest of their shareholders for them to do so; yet it was also the case that entire regional industries, like Northeastern textile manufacturers, abandoned their workforces in pursuit of lower wages elsewhere. Without any clear principles for differentiating one set of actions from another, it was impossible to know where corporate responsibility ended and political responsibility began.

If a society wants corporate decisions to reflect something more than a mere calculation of what's best for shareholders, and yet society is uncomfortable giving corporate officials sweeping grants of discretion over how to do the balancing of interests, it has two further options. The first is to impose, by law, procedures by which stakeholders other than investors can participate directly

in corporate decisions. Such procedural accountability has been attempted in various settings. Collective bargaining, as codified in the National Labor Relations Act, is the most obvious example in the United States. Denmark, Sweden, the Netherlands, Austria, and Luxembourg have "co-determination" laws requiring employee representation on company boards. Most of the rest of Western Europe mandates works councils, in which employees participate. South Korean law mandates labor-management councils for all companies with more than fifty employees. American employees who have agreed to forego wage increases in exchange for shares of company stock have occasionally gained similar representation, as at Chrysler and United Air Lines. Japanese and German bankers have acted as proxies for their broader societies when they hold stock in or lend money to major firms.

In theory, one can envision a wide range of means by which all stakeholders could be given voices in corporate decision making. Yet any system of representation tends to prolong and complicate decision making. Moreover, "agency" theory suggests that "stakeholder" representatives will only imperfectly reflect the interests of their constituents; it is difficult enough to overcome the relatively straightforward "agency" problems faced by corporate investors. Turning the modern corporation into a microcosm of national politics would be an extraordinarily inefficient way to achieve "socially responsible" corporate behavior, to say the least.

Government as Arbiter

The second option is to rely on government to define a corporation's responsibilities to society. Laws and regulations can be designed more or less efficiently, of course. "Command-and-control" regulations, requiring specific actions, tend to be less efficient than market-driven regulations seeking specific ends and leaving the means up to participants. Regulations themselves are sometimes less efficient means of achieving desired outcomes than are tax incentives or subsidies. But however administered, "corporate social responsibilities" are here determined by the public through its elected leaders.

This is not to suggest that other means of defining and understanding corporate social responsibilities are irrelevant: A society must still rely on the desire of company executives to be appropriately sensitive to public opinion and to the "long-term" consequences of their actions. Society needs executives who wish to act responsibly because they prefer to view themselves as good citizens and leaders of society. And society will continue to rely on procedures (such as collective bargaining) through which stakeholders other than shareholders can give voice to their needs. But political decisions must answer all the major questions.

Should American companies contract with sweatshops in Asia and Latin America? Consumers who believe they should not are free to take whatever action they want to force a change in corporate policy. But ultimately, this is

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not simply a matter of corporate ethics, it is also a complex question of public policy. How is a "sweatshop" to be defined? By what criteria are we to judge whether an American company has "contracted" with it? How is such a standard to be enforced? American law cannot reach foreign nations directly, of course, but it could establish minimum workplace standards and bar imports of garments and footwear unless reliably certified as meeting them.

Should profitable companies lay off redundant employees rather than redeploy them or retrain them for new jobs? Again, this is not only an ethical question, but also an issue of public policy. Layoffs can impose substantial costs on former employees, their families, and their communities. But prohibiting them could make the economy less flexible and could deter employers from hiring new workers. One way to "internalize" the social costs of layoffs without causing large inefficiencies might be to raise unemployment-insurance premiums on profitable companies that engage in them (in proportion to the frequency and number of employees who are let go) and cut premiums on companies that don't. Alternatively, if we want companies to take on the responsibilities of finding new jobs for employees who are no longer needed, and of retraining them for such jobs, perhaps government should offer these companies tax deductions or credits for doing so.

Other efficiency considerations enter here as well. To the extent that some action is in the long-term interest of all companies (and their shareholders), but not in the interest of any single company, government provides a classic means for overcoming such free-rider problems. Where all firms might benefit if all trained their employees in skills applicable to the entire industry or beyond, but no company would do the training unless others did it as well, government can improve efficiency by providing tax incentives for employee training in general skills, or by imposing a requirement that all firms contribute a small percentage of their payrolls to non-firm-specific training.

Some may object that I am setting the bar too low. By leaving to government the primary job of defining what is to be expected of corporate boards and executives—over and above their basic responsibility to maximize shareholder returns—I have drained any meaning from the concept of "corporate social responsibility." But this criticism misses an essential point. I am suggesting a deeper and more robust notion of responsibility—in effect, a "meta"-responsibility transcending a responsibility to investors.

Corporations are, after all, creations of law; they do not exist in a state of nature. Corporate officials are bound to two broad sets of laws, neither of which has greater moral or legal claim than the other. The first, embracing securities and corporate law, requires that they place the interests of their shareholders above all others. The second, comprising all other laws and regulations—labor, the environment, and so on—establishes a boundary around the first set of obligations. Board members and executives must place the interests of shareholders above all other interests except as limited by all other laws and regulations. The two sets of laws—the first, establishing their fiduciary responsibility

to investors, the second, their responsibility to other stakeholders in the rest of society—form an integrated system of corporate societal responsibility.

A Social Responsibility to Refrain from Politics

This meta-responsibility inherent in both sets of laws helps us assess the three instances of corporate political activity mentioned at the start of this essay: corporate advertising designed to affect a legislative outcome, corporate "soft money" contributions to candidates for elective office, and corporate instigation of bidding wars for special tax benefits and subsidies. By the logic I am offering, all of these political activities are questionable. This is because the latitude given corporations to pursue investor interests within the first set of laws implies a forbearance from pursing them within the second. Companies have no independent moral or legal authority to use their resources to influence the creation of laws defining their responsibilities to stakeholders other than investors. Society has ceded to them only the responsibility for maximizing investor returns, on the premise that in doing so they will spur growth and improve allocative efficiency. Society has not ceded to the corporation the responsibility to advance or protect other social interests. Indeed, this is the very point that corporate spokesmen such as Chrysler's Robert Eaton are quick to point out. The meta-social responsibility of the corporation, then, is to respect the political process by staying out of it.

It is not possible to have it both ways. The modern corporation cannot simultaneously claim, as a matter of public morality and public policy, that its only legitimate societal mission is to maximize shareholder returns, while at the same time actively seek to influence social policies intended to achieve all the other things a society may wish to do. It must respect the boundary between the two different sets of laws—the one governing its fiduciary responsibilities, the other reflecting political judgments about its social responsibilities.

The paradox of our time, of course, is that just the opposite is occurring. Even as institutional investors impose ever-greater pressure on management to maximize returns, causing corporations to loudly eschew broader social responsibilities, corporations are becoming more openly and aggressively involved in the making of social policy. They are underwriting advertising campaigns aimed at influencing legislation, such as the infamous "Harry and Louise" ads that were credited with turning the tide of public opinion against Bill Clinton's health-care plan. They are contributing hundreds of millions of dollars to political campaigns (according to Federal Election Commission filings, Eaton's Chrysler Corporation's "Political Support Committee" donated $704,114 to candidates and parties during the 1995-1996 election cycle). And they are actively courting tax abatements and subsidies as rewards for remaining in a particular jurisdiction or for moving elsewhere, often resulting in less revenue for roads and schools. To take but one example, the Albuquerque suburb of Rio Rancho spent $114 million to satisfy a list of financial criteria Intel had circulated to officials in several states in

order to build a large chip-making operation. The package included a thirty-year exemption from property taxes—the primary source of school funding. Subsequently, the school district was unable to fund school construction to meet the swelling enrollments created, in part, by the new plant.

Should not government enforce this meta-responsibility by passing laws and rules which constrain corporate political activity? Free-rider problems lurk here as well. It may well be in the interest of all companies to refrain from seeking tax abatements, for example, since an award to any one company imposes a competitive disadvantage on others. Many CEOs tell me they would prefer not to contribute money to political campaigns, but they fear they must do so because their competitors are doing so.

Indeed, there is much talk these days about "reigning in" corporate influence on the political process. At this writing, Congress is considering banning "soft money" contributions, to which American corporations are the major participants. Some have argued that the best way to deter tax-abatement "bidding wars" among states and among cities would be to treat all such subsidies as income in calculating federal corporate taxes. And one hears with increasing frequency the suggestion that, with regard to corporate advertising intended to sway public opinion on controversial issues, that the Federal Communications Commission revive and revise its "equal time" rule.

Ironically, of course, it is unlikely that any of these initiatives can succeed in a political environment over which corporate influence is as great as it is today. Yet over the long term (if anyone were paying attention to the long term), it will be in the interest of the corporation to support such constraints. They reduce free-rider problems. But they have a second virtue: They ensure that the voices of stakeholders other than shareholders are fully heard and considered. Unless such voices are allowed full expression within the political process, public pressure will grow to have these interests expressed within the system of corporate governance. Corporations must forbear from politics, or they are sure to invite, eventually, the politicization of the corporation.

Please answer the following four questions either in English or in Chinese

1. What are the two ways the author proposes for the society to encourage the corporates to fulfill social responsibility assertively? What is the rational behind his suggestions? Do you agree with the author's opinion? Do you think those two ways could be applied to Taiwan? Why or why not? 35%
2. There are five categories of activities that the author described which are related to the social responsibility, according to the opinion of the author, what is the different ways to deal with each category? 15%
3. Do you agree with the argument that there is a convergence of shareholders' and other stakeholders' interests? Explain your reasons. 25%
4. What are the possible problems top managers may face when a company applies "stakeholder democracy "as a mechanism to enhance corporate social responsibility? 25%