Center for American Progress

SPECIAL PRESENTATION:

"THE BIG UNEASY: A DEBATE ON CORPORATIONS' ROLE IN 21ST CENTURY SOCIETY."

INTRODUCTIONS BY:
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MODERATOR:

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SPEAKERS:

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MS. SUSAN LEE: This is a very quiet group. Good morning, everyone. Good morning. I'm Susan Lee, the vice president for economy policy here at the Center for American Progress. And thank you for joining us for what should be a very lively discussion about the role of corporations in 21st-century society.

Here at the Center, we recognize that corporations have a really critical role to play in shaping our economic, social, and political landscape, and indeed even across our world as multinational corporations begin to take a much more active role. As a result, we're very keen to host today's and future discussions about the way corporations and public policy can work together to achieve the types of outcomes that all of us would like to see.

Before we begin, I would just like to make a couple of announcements. The first, as many of you may have seen already as you walked in, is that there are many handouts from both of our debaters about this particular topic, and if you haven't done so already, we encourage you to pick those up on your way out.

Also, I would just like to mention briefly an event that will be happening here at the Center next Thursday at noon which will be hosted by our national security colleagues. It is somewhat related to today's topic in that they will be introducing a paper that looks at the role of market-based approaches to enhancing private sector security. In essence, the paper will call for an enhanced role of the SEC to require greater disclosure about matters related to material homeland security measures.

And also before I introduce our panelists, I would like to thank many people here at the Center, in particular Michael, Alex, Anna, Paige, and other colleagues who have done so much to help bring together our event today. And then finally, of course, I need to thank our debaters and our moderator, who I will now go ahead and introduce.

First, to your left is Leo Hindery, who is managing partner of InterMedia Partners, which is a media industry private equity firm. Until October, 2004, Mr. Hindery was chairman and until May of 2004, the CEO of the Yes Network, which is the nation's premiere regional sports network and the television home of the New York Yankees. Mr. Hindery won five executive producer Emmys for outstanding programming on this network. He is also the former president and CEO of AT&T Broadband and has received numerous honors, including international cable executive of the year, the Foundation Award of the International Radio and Television Society, cable television operator of the year, and was also named by *Business Week* as one of the top 25 executives of the year and by the cable television industry as one of its 25 most influential executives over the past 25 years. He is currently executive in residence at Columbia Business School and a member of the board of advisors of the Columbia School of Journalism. He's on the board of Teach for America and vice chair of the Global Business Council on HIV and

AIDS. And finally, he is a member of the Council of Foreign Relations.

With both of our debaters today, their bios are much longer and much more distinguished. I'm just highlighting a few of the points here, so please take a look at the event invite for more information.

And now here on your right is Fred Smith, who is the president and founder of the Competitive Enterprise Institute, a free-market public policy group established in 1984. He is well known in academic and professional circles and is a popular speaker at universities and conferences around the world on a wide range of issues.

Mr. Smith is also a frequent guest on national television and radio programs, providing both analytical and political insights. Among other programs, he has appeared on CNN's *Crossfire*, PBS's *NewsHour with Jim Lehrer*, *Now with Bill Moyers*, ABC's *20/20*, *This Week*, NPR's *Talk of the Nation*, the *Diane Rehm Show* and the *G. Gordon Liddy Show*. He is also a prolific writer and his works have been published in leading newspapers and magazines such as the *Wall Street Journal, National Review, Economic Affairs*, and the *Washington Times*. He has also contributed to the *Harvard Journal of Law and Economics*, *Cato Journal* and *Liberty* magazine.

And finally, it's my pleasure to introduce Alan Murray, who will take my place here on the podium on just a moment. He is the assistant managing editor of the *Wall Street Journal* and author of the paper's business column, which runs on Page 2 every Wednesday. He is also a regular contributor to CNBC. Previously, Mr. Murray served as CNBC's Washington, D.C., bureau chief and was co-host of the *Capital Report* with Alan Murray and Gloria Borger. While working at CNBC, he also wrote the *Journal's* weekly political capital column. He spent a decade as the Washington bureau chief for the *Wall Street Journal*. He joined the Journal in 1983 as a reporter covering economic policy. He was named Washington deputy bureau chief in January, 1992, and became bureau chief the next year in September of '93.

During his tenure as bureau chief, the Washington bureau won three Pulitzer prizes, as well as many other awards. He is also a regular panelist on PBS's *Washington Week in Review* and the author of two best-selling books called, *The Wealth of Choices: How the New Economy Puts Power In Your Hands and Money In Your Pocket*, and *Showdown at Gucci Gulch: Lawmakers, Lobbyists and the Unlikely Triumph of Tax Reform*, which was authored with Jeff Birnbaum.

So without further ado, I'm going to turn it over to Alan to kick off our debate for today. Thank you.

(Applause.)

MR. ALAN MURRAY: Thank you, Susan, for those fulsome introductions. I think you told us things about ourselves we didn't even know. (Laughter.)

MR. : Our mothers did.

MR. MURRAY: Well, yeah, my mother would have even believed some of that stuff.

I think there's something very important going on here. I'm just going to take a minute to set this up because I think this is significant – something very important going on in the world of corporations right now. It's a major power shift in the way public companies operate. If you go back to the 1990s, that was, in my mind, kind of the age of the CEOs – enormous publicity, cover of *Time Magazine*. And if you looked at how the CEOs of these large public companies, many of which rivaled countries in terms of their size and their influence – if you look at the unilateral power they were able to exercise within their organizations, it was pretty extraordinary.

And, of course, there was also a period when thanks to the miracle of stock options you saw pay for CEOs reach extraordinary levels. Then came the market crash of 2000, September 11th, most importantly a host of corporate scandals – WorldCom, Enron, Adelphia – all of which caused a dramatic change in the world of the public company CEO. There was a sharp reduction in power and a kind of a swirling of influences around the CEO's office of people who wanted to fill that power vacuum. Congress obviously got into the game with the Sarbanes-Oxley bill. You had regulators, the SEC, Eliot Spitzer and other attorneys general. You had public pension funds becoming much more activist, labor unions, hedge funds, NGOs, and so on, all of whom had their own ideas about how public companies should be used in society. And that, of course, is what we're going to talk about today.

Who really does run the corporation? For whom is it run? What are the purposes? What are the goals of the corporation? How is all of that changing? How much will it change in the future? And is it a good thing or is it a bad thing?

I sat yesterday afternoon in the office of a woman by the name of Patricia Wolf, who is a nun, a sister of mercy, and has become one of the very significant players in corporate America. She is the head of a group called the Interfaith Center on Corporate Responsibility. She has from that perch – she started working with them back in the 1970s during the – when South Africa and Vietnam were sort of the issues on their agenda and they couldn't get the time of day from top corporate executives. Last year, they introduced, what, 130, 140 proxy resolutions at major corporations. But more important than that, she will tell you, is that these companies are now engaging with the group. And she had meetings with the CEOs of four or five major corporations in the last year, met with the executives of dozens of others, and has really had an effect on the policies of those corporations.

On Monday I'm going out to California and talking to a group called the Rainforest Action Network. Tiny – they've got about a $2 million budget, and I would argue a very radical agenda. I mean, these are people who basically believe that we ought not have extractive industries. And if you kind of think about a world without energy and without metal and so on, you're thinking of a world very different than the one we live in. Yet they've been able to get all the major banks in New York to sign onto a list of investment rules working with them. They've had a direct effect on the policies of Home Depot in terms of where and what kind of lumber it buys. And they're now starting a major campaign against Ford Motor Company – extraordinary story of the influence of a small organization like that and it really tells you that something very different is going on in the corporate world than has in the past.

Now, is all of this a good thing? Are we turning the massive power of corporations to solving big social problems like global warming or AIDS? Or is a bad thing? Are we destroying the great wealth-creator, job-creator, engine of economic growth of the last century? The answers to those questions depend on who you ask, and we've got the perfect two people here to ask.

The way we're going to do this is Leo Hindery is going to go first. He's got ten to 15 minutes – 15 minutes max – to make some opening remarks. Then Fred Smith will take ten to 15 minutes. Then they'll each get five minutes of rebuttal. And then we'll have a discussion among ourselves, and then we'll open it up to questions from the audience.

Let me say in advance, if I can, Leo – Mr. Hindery recently had a knee operation, so if you see him making use of his chair over there, it's only to give his knee a little bit of rest. With that, why don't you start?

MR. LEO HINDERY: Thank you. It's a privilege I know for Alan and Fred and me to be with you this morning. This is an important debate. Alan is right. It's certainly topical. It's a lot longer standing than it appears to some. It's a privilege also to go first. Fred said that he wanted to use my ten to 15 minutes to sharpen his notes. I think he's actually going to be sharpening his knives. (Laughter.)

For me, I was in my second year of business school at Stanford in September of 1970. We'd come out of a generation where we had just left the Vietnam War, which Alan alluded to. I was at Stanford when Milton Friedman on September the 13^{th} of 1970 wrote what became a truly seminal piece in the *New York Times*. He entitled it, "The Social Responsibility of Business is to Increase its Profits." "The Social Responsibility of Business is to Increase its Profits," and it truly was seminal. It was seminal for me. I think it was seminal for my classmates. It stood the non-business world on its head for over a decade.

In 1981 – and this really does put some dates on the length of this debate. In 1981, largely at the urging of Reginald Jones, a gentleman now known familiarly as Reg Jones, the chairman and CEO of the General Electric Company, a much esteemed individual, deserves much more credit for his leadership I think of GE and is swamped only by the incredible success that followed of Jack Welch, but the Business Roundtable in 1981, largely at Reginald Jones' urging, officially endorsed a policy – they had reflected for now a decade on Milton Friedman's article. It said, quote, that "shareholder returns had to be balanced against other considerations," and they went on to specifically include employees and customers.

And that became for me no less seminal; in fact, perhaps on a personal level more so. Jones believed that it was ultimate responsibility to preserve an honorable General Electric Company into the long term. And he and a bunch of us began to argue in writings and in speeches that a vibrant, prosperous middle class growing from the bottom up was the very best thing for his company – his specific company, GE – and for the rest of corporate America. Again, the premise was a vibrant middle class growing from the bottom up.

Twenty-three years later, 2004 – 23 years later, after Enron, after WorldCom and Tyco, after Adelphia, after all of the corporate misbehaviors that we've read about in Alan's papers and others, the very same Business Roundtable with no urging formally said with the outspoken support of the U.S. Chamber of Commerce that the job of business in only to maximize shareholder wealth. It was a total crib off of Dr. Friedman's title of his speech and article back in 1970. And all this while, from 1970 until today, U.S. consumers consistently have been saying by a wide margin that the most important thing a company can do to be regarded as socially responsible is to treat its employees fairly.

I believe that Dr. Friedman was wrong in 1970. I believe that the 2004 version espoused by the Business Roundtable is wrong, and I believe that Tom Donohue at the U.S. Chamber of Commerce is wrong. Focusing only shareholder wealth may in the short term – in fact, it almost always does – improve efficiency and productivity. But in my opinion, in the longer term it is far too narrow and in fact it is self-defeating of this premise, this imperative to preserve a vibrant consuming middle class. The Business Roundtable with wisdom, in my opinion, in 1981 acknowledged four other constituencies beyond shareholders which need to be equally tended to, and they are specifically employees, customers, community, and for the nation's larger corporations of the ilk of a General Electric, the nation itself. And they said in 1981, and I say today, that it is wrong to aggregate these – or to see these as anything but aggregated responsibilities. I think it's wrong to prioritize them. They shouldn't be ranked or prioritized.

The debate, as we'll hear this morning, over corporate social responsibility as it digs down has taken some very strange twists over the years. There have been diatribes against addressing such basic issues as workplace safety, basic environmental protection, and diversity. I've even heard it argued post-Enron that the company – Enron's failure to prevent internal fraud, its failure to prevent internal fraud was because the company had been diverted from its responsibility to create wealth by its, quote, "championing of environmentally conscious global warming policies." Friends, I will tell you that Enron failed to prevent internal fraud because it was run by crooks and by a board that was an embarrassment.

The corporate social responsibility debate also suffers, in my opinion, from the misguided belief in the minds of many that there are only two possible views of the firm:

either it is designed to create wealth, or it is a social institution with the duty to resolve the larger problems of society. My belief is somewhere in the middle. The middle ground that concludes that by being honestly responsible to multiple constituencies the firm or corporation is in fact more likely to be viable into the long term with greater profitability and thus greater wealth creation for shareholders. It seems to me, and I've said it before in this town, that the sine qua non going forward are CEO-statesmen who believe in a collaborative effort by the administration, congressional leaders, business leaders, labor leaders, to enact realistic and politically achievable responses to the problems of the country. Most specifically, the ever-growing income and education disparities, the needless and economically draining off-shoring of jobs which is underway, and to the now monumental health crises and pension crises.

Clearly, in my opinion, government has to work with the CEO community and vice-versa, but remedies to the ills that I have described, in my opinion, need to start with enlightened and responsible CEOs, as Reginald Jones once concluded.

Let me if I can quickly go to an area that Alan has written about ably, and it's what happens when corporate responsibility is shirked and shareholder returns dominate, and that's in CEO compensation. At the beginning of the last century – the beginning of the last century, J.P. Morgan said, quote, "I would never lend money to a company where the highest paid employee is paid more than 20 times the lowest paid, as such company would be unstable." The much esteemed Peter Drucker at the end of that century near the end of his own life said, "It is a business responsibility but also a business self-interest to develop a sensible executive compensation structure that portrays economic reality and asserts and codifies what I hope" – what Peter Drucker hopes – "will be the greatest achievement of U.S. business in this century, namely the steady narrowing of the income gap between the boss man and the working man." As know firsthand, there has been no narrowing.

Some very informed people would identify a lower figure than I'm about to, but I believe that an unbiased and all-inclusive approach in analysis would show that the average CEO today in this country is making something in excess of 400 times his or her average employee. And the lowest figure I've seen in Alan's newspaper and elsewhere is about 179 times. But whether the number is 179 times or 400 times, as I believe it is, it's obscene at every level because the comparison points are 22 times in Britain, 20 times in Canada, and 11 times in Japan. A colleague of Alan's, Jesse Eisinger of the *Journal*, has calculated that in the five years 1999 to 2003, the top managers of the 1,500 largest companies in the country took down $122 billion of compensation – the top five people in 1,500 companies. In the prior period of time, five years, that number was $68 billion.

And yet as we hear over and over again, this is despite institutional investors saying – the people that Milton Friedman, the Business Roundtable, and others suggest are the ultimate owners of the corporation – 90 percent of institutional investors in the United States today would suggest that the executive compensation practices of the country are hurting the nation.

We as a country, in sum, we're relentlessly optimistic. It's one of the fun things about what we're talking about this morning. We all believe that this country is the very embodiment of a meritocracy. It's a country where people are judged on their individual abilities. But we also know, sadly, that salaries in the U.S. are now the most unequal since 1927, and that the gains have gone mostly to owners of capital and not to workers. We also know that incomes have failed to rise for a record five straight years. Addressing and rectifying these inequities are much more than ethical imperative, as we'll talk in the Q&A. And needless and insensitive off-shoring, the recent deterioration in jobs quality and health and pension benefits in my opinion has substantially broken the contract with the middle class.

And I think that as we talk this morning we'll find that there are in fact solutions that are respectful to the shareholder interests, to the nation's interests. And it just seems that as we talk through these issues this morning that we've got to be careful about not focusing on the short term. Again, in the short term very, very egregious behaviors I think can be justified by an over-reliance on the shareholder criterion. Reginald Jones in 1981, the Business Roundtable in 1981, proved ably to me anyway, that a vibrant middle class growing from the bottom up is the best thing for GE, it's the best thing for corporate America, and it's certainly the best thing for this country.

I look forward to the Q&A. I know that'll be the fun part. But again, a privilege, my thanks to CAP for helping arrange this and the privilege of being invited to share some comments with you.

MR. MURRAY: Thanks. I now understand why Fred wanted you to go first. Because I've been –

MR. : You've lined him up.

MR. HINDERY: Scribbling.

MR. MURRAY: I was watching him, you know, he scribbles.

(Cross talk.)

MR. MURRAY: Have at it, Fred.

MR. FRED SMITH: Well, if the FDA gets out of the way I'll probably have both of my knees replaced (unintelligible).

I agreed with some of the things that Leo said, and as you'll see we have some areas of disagreement. To me, corporate social responsibility is a very confused and counterproductive response to what I view as a very real challenge, a very real problem we face in the world today. Business and more generally economic liberty are under attack today in an era very reminiscent of the way they were at the end of the 19th century when the onslaught of the industrial revolution with its massive amounts of creative destruction disturbed society; and not surprisingly, various forces found it possible – we'll have all the goods of a market economy without any of the creative destruction. We had, of course, our attacks on business that we all learned in our history books, the robber barons, the muckrakers, and so forth. Today we have similar attacks going on not against the corporations so much today, against the multinational corporation, the anti-globalist thing, the role of the muckrakers of the 19^{th} century. Upton Sinclair's replacement is Michael Moore in our new visual world – it's quite a reasonable substitution. And Teddy Roosevelt trust-busters with our ever-vigilant Attorney General Eliot Spitzer makes a good playoff, too.

The way business gets treated in media and in discussions is sort of unfair I think. Competition is always cutthroat. Prices are either predatory, gouging, monopolistic, or collusive. The CEOs wake up each morning, according to Hollywood and many of our shows, thinking, what new evils will I perpetuate today? What workers can I exploit around the world? What species can I drive to the brink of extinction? And, of course, what rivers or forests can I despoil? The businessmen seem to have no role other than creating problems for around the world. Business gets no respect, I regard, in the modern world, and is, I'll argue, largely I think – and there I think I do agree with Leo – I think a lot of it is their own problems. They haven't adequately explained to the world what their role is – what their social role is in this society.

And there's a risk as they lose legitimacy – and they certainly have lost massive legitimacy over the last – since post-World War II period. They've become increasing vulnerable to our ever-crusading, populist politicians – and sometimes you think there are nothing but populist, crusading politicians in America today – and their chattering class allies. This is not new. As I mentioned, the muckraker era is being replicated today.

There's a book out there that I recommend to everyone: *Creating the Corporate Soul*. It's not a policy book. It discusses the way the business community responded to the anti-business assaults of the muckrakers and argues that they were somewhat successful in that process. At the end of World War I, most of you will recall, industry was the merchants of death. At the end of World War II, industry was the arsenal of democracy. I think part of that changed image of the business community came about because they aggressively tried to explain themselves, legitimize themselves to the American people. It's something I think they should do again.

The role of the corporation, as Leo said, (inaudible) as Alan even went on further to say – and I think there's a real failure to understand just what we've benefited from, from the creation of the modern corporation. The industrial revolution was not just a revolution about technology, very important though that was. It was also a revolution about institutional forms, and the creation of the modern corporation with its highly-specialized role of focusing in on a narrow part of the world's problems, and in that narrow role trying to expand wealth and knowledge, essentially created a very targeted way of moving the world into the future. Trying to do everything, trying to load all of society's problems on each institution, sort of the Marxist idea of in the morning we write our symphony, at lunch we plow the fields, in the afternoon we cook a gourmet meal, and then at night we write the great Russian novel, is an ideal utopian concept, but it's not the way the world has advanced so much over the last several centuries. We have specialized and by specializing we have been able to move much more quickly into the future.

There's an ad campaign out there, and I forget who actually does it, but it has inappropriate business models and one of them is fish cleaning and cosmetic surgery or something like that on their ad strategy. It's a good idea that we have specialized institutions, and the attempt to make everyone responsible for everything is counterproductive.

The corporation should be responsible. I mean, I think we want responsible corporations. But when we add the term social, I think we blur a concept that is meaningful and make almost not meaningful at all. Robert Samuelson of the *Washington Post* column – he's one of the *Washington Post* columnists – pointed out that the socially responsive era that Leo talked about earlier, the post-World War II age of the great CEOs of history, according to Leo, was a world in which business, community, and many people in America believe we could combine – there was a third way – we would combine the fierce competitiveness of a market economy with the welfare state for the worker goals of the new third way capitalism with a human face.

In that era, and I was just back to where we were talking CSR in the 1950s, everyone would say, thank God we have these large corporations willing to allocate some of their gains to making a better future world for the workers.

Today, of course, we recognize that those pension plans and those retirement plans were illusory. We promised utopian goals and we delivered lies in effect. I think Samuelson pointed out that – he said, I knew that the welfare state would eventually collapse; I just didn't realize GM would be the first to go. How do we feel about the social responsibility of firms that made promises which economic reality has now made it very difficult for them to fulfill, and we find under a pension fund subsidy programs and so on? Many of them are now trying to shift those responsibilities to the corporation. Those socially responsible programs of the 1950s, I think today many – certainly I – believe socially were very socially irresponsible.

Corporate social responsibility itself is a backhanded compliment in a way to the success of the market. Once the progressive elements in America wanted government to play a much more aggressive role. Government agencies would provide the direct leadership to these errant economic forces and they would guide the world into a better, more utopian future. Today, there's not much faith in the ability of political bureaucracies to be much useful on any side of the coin. Today we're going to do it differently. We're going to let the corporations be free, but they're going to be guided into a more utopian future by NGO's such as Rainforest Action Network, by socially responsible investment funds like Sister Pat, by shareholder activists, and by other socially progressive forces in our society.

And that poses the challenge I think we face, and I think Leo put this very, very well. Is the Milton Friedman model that the best role for business – the most responsible role for business is to let business be business, or is the business community – the corporation – a privileged entity in our society and as such has a social political responsibility to address other social issues? Should, under the Milton Friedman role, the profits be earned by the corporation and then be distributed to shareholders who in their highly individualized ways will each then pursue their utopian goals for a better tomorrow, or is it better to have the corporation act in loco parentis, to act as sort of the elite disburser of the wealth of a modern economy and make the decisions for all of us?

In a world, should power be disbursed to the individual shareholders of America, or should power be concentrated in the hands of a few CEO elites, who according to Leo are very overpaid already? Isn't it better that we disburse that information? Isn't it better that in a heterogeneous world or heterogeneous value world such as America, we allow more voices to use more of the wealth of our society to make more choices rather than the fewer voices that would be the case if the corporation makes them for us?

What about CSR itself? Is it feasible – CSR itself – corporate social responsibility – makes these judgments that we want to do what? Well, we want to worry about workplace safety, the environment, community reinvestment, displacement of other industries, no creative destruction we'd like to see in our world, human rights, be more or less positive towards unions, and of course they have to avoid certain investment strategies: tobacco, alcohol, gambling, nuclear power, firearms, defense, abortion, birth control, (foreign?) – and on and on.

And they have to do that not only for themselves but they have to do it under the concept of extended stewardship responsibility for everyone upstream and downstream of them. The corporate CEO's job in a CSR is not small. Can this be done? You know, it's hard enough to run a profitable business in today's fiercely competitive world, but we have a metric in the economy. We have something called money, and we can compare an investment in strategy A versus strategy B, new worker benefits. Does that increase or decrease worker turnover? Are there gains to be made by reaching out to some of our constituency groups or not? Well, it's hard to make those decisions, and there are time problems and so on, and discounting, but at least we have a metric to do that. How feasible is it to do that in a world where we lack that metric, where we have no things? How do we compare?

You're a CEO of a major corporation. And your environmental vice president comes in and says, "This is a cleanup investment. It'll involve $100 million, but our contribution to water pollution and air pollution will be massively reduced. I think it's worthwhile." And then your human rights individual comes in and says, "Look, there's $100-million opportunity to invest in country Y, but that country has a horrible human rights violation and I think we should forego that. We'll lose some money, but we'd be on the right side of morality." Well, they obviously both have some value to them, but how does a CEO decide which is better than the other? We know the dollar side of the equation, but we don't know how to trade off one set of moral values versus another as corporations, as societies. Each of us makes those choices in our own life. What makes us think the corporation has any comparative advantage in making those complex moral choices for the rest of us?

And we're not just talking about human rights. We're talking about unions, we're talking about the pros and cons of child labor in third world countries versus child prostitution in third world countries. These are complicated, very difficult decisions. As individuals, we may well come to morally different choices. Do we really want to relegate that to a much smaller group of corporations? Should they? They have no specialized knowledge. They aren't equipped to make morally – they're not preachers. These are businessmen. They're not Mother Theresa. They're not that common in any institution, certainly not in corporate boardrooms. Should we really be relegating these decisions to them? In a world of heterogeneous values, to seek to reduce that heterogeneity by assigning a homogenous mission to the modern corporation is, in my view, silly.

Why do firms sign up? That's something we can actually deal with. It is a real threat, and I think industries have tried desperately to find ways of re-legitimizing themselves. There are three strategies that we probably should discuss later that industries have adopted. I call them the Pharisee strategy, the mafioso strategy, and the Captain Hook strategy. (Laughter.) The Pharisee strategy is the one that we quite often in business community: the CEO having signed away some of his company's future, stands up in front of the group and says, "Oh, God, I thank you. I'm not a sinner like my fellow businessmen. I have found the true light. I have now signed my way in CSR. No longer will I deal with the evil forces of society. I'm a good businessman." Well, the Bible suggests the Pharisee strategy has some drawbacks. Empirical work we've done suggests so, too.

The mafioso strategy is a little different. The mafioso strategy says, you've got us, we're slimy, greasy businessmen, but what the hell. Who funded the last three novenas at the Cathedral? (Laughter.) Or in the art museum and so on down the line? The idea that doing something bad is legitimized by doing something offsettingly good is not likely – just stop doing the bad stuff and keep doing the good stuff.

And the there's the Captain Hook philosophy, which I find – it's from Peter Pan, another public policy group I read often. (Laughter.) And you remember Captain Hook's philosophy of addressing animal predators was if you feed the crocodile your leg, it's likely to become a vegetarian. This seems to be the strategy that Wal-Mart has now embarked upon. Having found that it's having trouble in one area – the union activism in Maryland up to today – predation against its benefit plans, we now find itself inviting Al Gore down to dance around the green totem pole and sign on to a future that is green, green, green.

It's interesting how businessmen are perfectly willing to assign cost to other parts of the economy. George Stigler I think made his point quite clear. George Stigler said that businessmen believe that competition like exercise is very good for other people. And I think we're seeing that with Wal-Mart.

We need to recognize that we have – if the CSR policies are completed, we're going to be delegitimizing one of the major forces for economic and technological growth. We should think about that. We are going to delegitimize a lot of investment opportunities in the third world. We're going to divert corporate attention to other areas. We're going to be encouraging rent seeking. I don't think, incidentally, the rent-seeking problem at Enron was – I mean it wasn't so much the diversion problem; it was the rent seeking. Enron saw vast profits in making energy less affordable and more scarce, and they were lobbying aggressively to be the leaders of a new carbon scarce world. It deifies the privileges and there's little evidence that corporate social responsibility buys into much of anything.

There are some interesting questions about what industry should do about this, what would be a responsible corporation, and that's worth talking about, but generally I think the major thing business needs to do is to get over its guilt feelings about itself, recognize the value it brings to society, and essentially find ways of communicating the virtues of a market economy of economic liberty. And basically I think the base thing business should do is teach the rest of us to enjoy capitalism. (Laughter.)

MR. MURRAY: Well, this the first session I've been in where Reg Jones and Peter Pan have come up within the same 15 minutes. (Laughter.) But Leo, maybe you can – you've got five minutes to square the circle.

MR. HINDERY: It won't take anywhere near that. This is much more important than a semantic debate. If you don't want to call it corporate social responsibility, call it whatever you want.

The concern I have is that whenever we have this debate we throw out extreme examples and we scare the pants off of people. And the rainforest organization is obviously extreme, and nobody could countenance its suggestions that we cease all extractive industries. And we do that over and over again, and it's because we don't want to find a middle ground that's fair and honest, in my opinion.

Workplace safety, pension plans, employee benefits, verifiably – because I have been a CEO; of the three of us, I've done this. I can make more profit for my shareholders by sensitively addressing the needs of my employees and my customers and my community, and I can prove it to you. What I don't like is a debate where we throw out extremes and then we throw out everything. That's what Friedman tried to do in September of 1970 – That the only social responsibility was to increase profits. I have no problem with profitability. I don't decry or deny the benefits that business has brought to society; it's brought it to my family. And I don't ascribe malevolence to business. There's not an implicit malevolence to corporations. These entities, however, and I've run them, are simply incapable of self-policing. That is the premise that drives me: that if you turn them loose only against the profit standard, they are structurally and individually incapable of self-policing. There is a middle ground that will comfortably embrace workplace safety, treating employees fairly, paying them fairly, having a sense of community and national responsibility.

I come from the media industry. I've had the privilege of running some of the larger media companies in this country. If I want to maximize profits, I will broadcast the first execution on television, I will have no barriers on pornography, on debasement programming, I will tip the scale so deeply in ways that debase society and cheapen it, and I will make money like you've never made money. Can you imagine the pay per view event that shows the first execution in this country? There have to be standards of reasonableness and moderation, and there has to be a sense of responsibility to the nation, to the community, to customers, and the employees.

What I want to get into on these issues is a negotiation. I have standards that you may not agree with, but I cannot negotiate with somebody who says the only social responsibility is to increase profits. Again, this group of people, of which I am one, is not capable of self-policing. We've seen it over and over again. It's not malevolence. It's structural incapability of self-policing and so standards and conducts that are important for society are not inappropriately placed on corporations.

Thank you.

MR. MURRAY: For a minute there I thought when you were talking about a media executive whose only goal is to make money, I thought you were talking about Rupert Murdoch, and you could have been. (Laughter.) Fred, go ahead.

MR. SMITH: Well, first, I think those weird ratios of executive salaries to individual salaries I think are in the for-profit sector. Those of us in the public (unintelligible) probably, I suspect, CAP is not all different from CEI: 10-to-one would be a great ratio in our organization of CEO at that point. We're more like six-to-one I think.

Friedman and groups like that have been, I think, interpreted quite too narrowly. I think Leo interprets them too narrowly. Friedman was arguing that the role of business is to make profits, but as we all understand a profitable corporation does have to look at the worlds in which it operates, not just its internal structure, which is very important, but it has to look externally, too. Business links up with two constituencies, and I make a distinction in the writing I've done, what I call the nexus community, those whose relationship to the company is directly relevant to profits. Of course, it's customers. We've made that point. But also its shareholders, its suppliers, because a reliable customer makes it easier to get better relations with suppliers, to its employees quite critically, and to its fencepost neighbors – the ones around it who actually see the firm and deal with it on a daily basis.

All of those groups are linked to the corporation in a win-win way. They may have antagonism in the company, there may be confusions, but a dialogue between those groups and yourself about why you're trying to be a good customer to your suppliers, why you're trying to be a good supplier to your customers, why you're trying to make the best deal over time that's viable to your employees, and so forth, all of those things are good. Being a good neighbor is important. In those situations, a dialogue, a certain amount of, "Look, here's what happened, we're sorry it got confused, but here's what we're doing," are sensible. The rational skills of corporations have been tuned to deal with these nexus conflict situations.

Business confusion, and the reason we're seeing CSR as such a mess, in my view, is that it doesn't understand that those rational tools of education and communication don't extend well to the broader citizenry, to the population as a whole, to the political environment in which it operates, and those where people hold opinions that are weakly linked to fact, and those opinions are critical because they define the parameters of politicians feel secure in either attacking or defending the corporation.

How does business deal in that world of what's called in political science rational ignorance? Rational ignorance is the term that applies to people's realization that information acquisition is expensive, and therefore we acquire information about our daily lives – where we should invest our pension funds, whether we should refinance our house, et cetera – and a lot less to the issues associated with whether we should trade with China, outsourcing issues, global warming, Rainforest Action Network and so on. People have opinions about those issues, but they're not well grounded in fact because spending time reading CAP's or CEI's white papers, while extremely enlightening and you all should do it, is not something that occupies most people.

Most Americans do not go to sleep reading the Federal Register. They read about things that are directly relevant to their lives, and they're not fully informed by the end of each night. To expect them to become experts on the myriad number of policy issues that we're discussing here today is fanciful, it's wrong. People aren't stupid in politics because they're stupid; they're stupid because they're smart and if we in the business community insist on trying to educate them, we're being stupid.

The political process is a world where we have – people's opinions are critical and those opinions are based on how they perceive, quite facilely, the corporation and its roles. And to treat the corporation as we have in the CSR today is to make people more suspicious, less accepting, of any role for the corporations at all.

Business has two responsibilities, it seems to me, in the social world. Businessmen's comparative advantage is in competition, not politics, so they should try to assure that the rules of the political – the political rules in which they operate, property rights, liability roles, are reasonable roles that allow the better businessmen to prevail against the less scrupulous, the more incapable, the more corrupt businessmen. That's a major challenge.

I was at the railroad industry as a senior economist. The railroads actually tried to do that. The railroads actually pushed for deregulation, for forcing themself out of the political subsidized regulated world into a world of competition. It was a desperation move. They're about the only industry that ever did that. But it would be great if industry was actually pushing for property rights in Zimbabwe, for liability rules in the United States that made any sense at all, for rules in the competition world that made sense. I'd like to see business move in that direction because that would be responsible, but they haven't done it yet. But until business gets over this view that somehow it's irresponsible to make money, I don't think they're ever going to be doing a good job.

MR. MURRAY: Fred, let me ask you, because every – I see the distinction you're making. The problem I have with the distinction is every CEO I have ever talked to – every CEO who sort of has a good record on corporation social responsibility, will tell you that they are doing what they are doing because it helps the bottom line. Jeff Immelt will tell you that he has imposed greenhouse gas restrictions on his company because he thinks it's good for the company's profits; it's going to help them develop the technology – first of all, we're going to face those limits eventually anyway, and it's going to help them develop the technologies to sell in the world.

The drug companies will tell you that the reason they are doing what they are doing about AIDS in Africa is partly to protect their patents. I talked to a CEO who devotes 1 percent of his profit to charitable enterprises. He said the reason he does it is to enable him to attract employees because he's attracting high-value employees who want that. So I've never met a CEO who says they are doing social responsibility for reasons other than to make a profit.

MR. SMITH: That's true: they say that and they sometimes I think are quite highly doing that. I mean General Electric, after all, does have a large portfolio in wind power and in nuclear power, so to some extent any carbon strategies selectively benefit their portfolio. On the other hand, the question of degrading the use of energy in society, which is a possible threat of the whole global warming endorsement, makes it worrisome that – after all when you actually look at the environmental movement, they're not overly enthusiastic about nuclear and – at least Robert Kennedy's endorsement of wind power is restrained in his own neighborhood.

I'm not sure at all that this policy of saying, you know – that's a Pharisee strategy. I think it's an interesting strategy. I don't think it works. And empirically ARCO, if you recall – an oil company that has now been amalgamated in the merger movement – once mounted a major green energy program in California. They produced a cleaner fuel. It was a few cents a gallon more. The state government, the environmental movement, ARCO had major campaigns in saying how wonderful ARCO was and all of us as green consumers would now march hand in hand with ARCO into a more socially responsible profitable future. That didn't work. People didn't buy the more expensive gas. They were perfectly willing to endorse the sentiments, the rhetoric; they weren't willing to endorse the reality. I think there's a lot of fanciful thinking.

And the fact that Rainforest Action Network has persuaded essentially every financial institution in New York to sign away their future to this group, who doesn't believe in investments in the third world, to me suggests that the industry is not thinking through what happens when it signs its name.

MR. MURRAY: I think that's a great question for Leo, because I take your point that we're using an extreme example here with the Rainforest Action Network, but in some ways it illustrates Fred's point that corporations may not be very good institutions for dealing with this. The Rainforest Action Network could not win an election in this country. They simply don't represent the – people kind of like driving in cars, not riding on bicycles, and I don't know what the bicycles would be made of anyway. They'd have to be made of bamboo or something. (Laughter.)

MR. SMITH: Renewable bamboo.

MR. MURRAY: Renewable bamboo. So I don't think the Rainforest Action Network could win an election in this country. On the other hand, they succeed at companies by using tactics – like what they did at J.P. Morgan was they got a bunch of school kids – well, first of all, they went to the home of the CEO in Greenwich, Connecticut, and put signs on all the phone poles in the neighborhood saying William Harrison is a criminal. And then they went to the schools in Greenwich, Connecticut, and they got a bunch of kids to do posters, "Save the Rainforests," and marched them all down to the company's offices in New York, and eventually Bill Harrison said, this is really a hassle, it's really getting on my nerves, fix the problem.

To get to Fred's point, is that the way we should – shouldn't these problems be solved by governments, which are set up to deal with these kinds of problems, rather than by corporations?

MR. HINDERY: I remember a friend of mine in the cable industry when Sumner Redstone in a little town in Texas turned all the teenagers loose on him to make sure he carried MTV. (Laughter.) Certain behaviors and certain reactions can't be, Alan, the point of this debate. What I think is important more than – the Rainforest group is using tactics that I deplore. It stretches into extremes that I can't countenance. Yet there are things it says and does that I'm very comfortable with. And my problem with that organization is its throwing too much under one umbrella, so I have no interest in that group.

The issue I think for this audience is to parse Fred's comment and your question back, and that Jeff Immelt can – and now Jamie Diamond at Morgan Chase, they can comfortably sit down -- these are not ignorant people and they can comfortably sit down and find those issues that you talked about that in fact bring profit to the corporation in a responsible way into the long term: the Reginald Jones premise.

What I want you to think about is when we were all in school, the teachers would always tell us that cheaters will get theirs. They never did. This premise that the scrupulous in corporate America will override the unscrupulous, it ain't going to happen. You can't premise that right wins out here with these kinds of financial incentives to misbehave. And as you have aggregated so much of society – corporate society in these powerful companies – Enron's tragedy wasn't its failure; it was the breadth of its failure.

It took down millions of people in one fashion or another. That's an inexcusable outcome.

So what I'd like you to think about is parsing this issue between scrupulous and unscrupulous, which is one aspect of social responsibility, and the bottom-line issues that Alan has referred us to. Don't throw out responsible activity because of extremism on one side or the other. Don't do what Friedman implored us to do, which is to suggest that Jeff Immelt isn't clever enough to figure out worker safety programs so let's just make profit. As a CEO in the past, I know how to make profits. I do it on the backs of my employees, the backs of my communities, the backs of my nation. It's a short-term perspective. I know how to do it. I just personally don't do it. And I am of the Reginald Jones school which said, the responsibility of a CEO is to build his company into the long term with a solid foundation that drives me to this middle class perspective that I've shared with you.

MR. SMITH: Well, two things. First place, middle class in most countries is middle. They're doing better than a lot of the poor are. And it seems to me the genius of capitalism, the genius of economic and technological growth is its democratizing influence. It takes the privileges of the elites throughout the world, including the American middle class, and begins to generalize those. When we give moral legitimacy to groups – and look, I don't think we should let Rainforest Action Network or J.P. Morgan and the banks of New York City off the hook. They have been willing to allow an NGO – a privileged group of very well-financed foundation finances, which is a much bigger aggregation of power in the United States and much less disciplined than the corporate world is, to be seen as the voice of the global poor. When you asked people in the global market do they like poverty, or as the NGO movement likes to say, preserving the indigenous way of life, they're basically opposed to this.

I grew up in a part of Louisiana that was very poor and when my neighbors who did not have electricity or running water got the opportunity to do it, they didn't rush out and demand preservation of their indigenous way of life. The immorality of allowing groups such as the Rainforest Action Network to put their privileges ahead of the poor of the world and to give no voice to those people – it's trivial for major corporations in the United States to say, we want to invest in country Y, or we'll start of this area. It's not much on their – or to stop using biotech products if you're a supermarket. But the victims of that decision to allow anti-wealth creating, anti-knowledge creating forces to dominate the political process is that we slow down the engine of economic and technological growth and we leave the poor of the world in poverty for longer periods of time. That is immoral. That's obscene. And it is irresponsible of corporations to endorse that form of elitism among the rich of the world.

MR. MURRAY: Okay. Let's go to the – I want to go to the CEO compensation issue a bit before we open it because I think that's a very important one and interesting one because one of the things that's happening – and you now are in the private equity business.

MR. HINDERY: Yes.

MR. MURRAY: Which is interesting, because one of the things that is happening is vast amounts of money are being poured into private equity – and I live in Greenwich, Connecticut now, so I see how these people live. I mean, you want to talk about exorbitant salaries, let me tell you. A vast amount of money is being poured into private equity firms which are taking public companies, often public companies that complain about the hassles of having to deal with Eliot Spitzer and the NGOs and public pension funds, taking them private where the opportunities for payment are much greater, taking them out of this world of public pressures that we've been talking about. More and more companies are going in that direction.

And, I mean, to me, one of the most ironic things is the public pension funds, which on the one hand are leading the push for – or part of leading the push for more responsibility, more transparent government, are at the same time pouring money into these private firms where none of those pressures exist. How do you deal with that sort of bifurcation of the American economy?

MR. HINDERY: Alan, I think it's obviously a completely different issue than CEO compensation, but it's one that needs to be part of this debate. I don't quarrel with wealth accumulation when you create wealth for investors and you did it honorably and well. I don't decry the creation of wealth based on creativity. If you come up with – if you're the next Bill Gates, if you're an artist, if you're an entrepreneur. I don't want to go into that area.

My interest in private equity – I've been in private equity and I've been in corporate roles. I'm now back in private equity. I believe that you are creating wealth for investors. But the investors that I deal with – the state pension plans I deal with are holding us to very high standards. We're not throwing the baby out with the wash. We are not allowed to not have standards of corporate behavior in terms of employees and community and personal compensation. The wealth that it's being created, and it's enormous, I don't deny that, is still wealth that's being created as investors are realizing returns that they weren't realizing otherwise. That is a form of shareholder appreciation –

MR. MURRAY: But the people who run those companies are often walking away with far more than the things we read about the CEOs of public companies.

MR. HINDERY: They are, but the CEO – take Bob Nardelli at Home Depot, stock down 30 percent on his watch, up $245 million in personal income. The absence of correlation between CEO compensation and shareholder return is deplorable. I find in private equity ills just like you do, but I do find a crisper correlation between the creation of wealth for investors and the compensation to the compensation of the individuals.

MR. MURRAY: Why don't we – go ahead. You want to –

MR. SMITH: Well, just briefly. The interesting shift of –

MR. MURRAY: Were you through?

MR. HINDERY: Go ahead.

MR. SMITH: – capital reallocation to private firms as opposed to public firms in my view represents the almost inevitable push to wherever we can get our hands on a corporation or acquire more accountability, more reporting, more transparency, more social duties and so on, we raise costs. We may or may not achieve any social value of that or return out of that, but the effect is for businessmen to say, as the Rainforest Action Network has found with CEOs, if I want to be treated respectably in a cocktail party, I'm going to get the hell out of the public sector. I'm going to either give in to the crazies on the anti-globalization side or I'm going to go private. If we really want to create a world in which there is no accountability except that of the market, we're doing it. I'm not sure that I oppose that. It doesn't appear to me that Sarbanes-Oxley has been a great benefit to society.

But if Leo's model is right, then we're going to see an increasing shift away from an over-regulated, overtaxed, demonized public accountable sector to a private sector that may actually enhance wealth creation, which I guess we both agree, but it certainly moves away from the kinds of concepts that Leo at least in his book talks about.

MR. HINDERY: Yeah, but it's the Q&A (inaudible). Let me just say, I am not drawing a distinction between the manner of ownership. Corporate responsibility does not fall off because you're public or not public. The Chocolate Shoppe across the sheet has corporate responsibility in its own context. We all have that responsibility. I'm absolutely not trying to carve out private ownership and say that's the dial-around to CSR.

MR. MURRAY: All right. Let's open it up. And by the way, I'm told the rule of the house is that members of the press get to go first, which I think is a great – I've never heard that before, but it sounds like a great rule to me. In fact, I did go first. But if there are other members of the press. Go ahead. Identify yourself, please.

Q: Well, I'm not a member of the press but I have the mike.

MR. MURRAY: Sorry, you can't go first.

Q: But I have the mike. (Laughter.)

MR. MURRAY: Are there any members of the press who'd like to ask a question before this gentleman does? I'm sorry. Right here.

Q: I will surrender the mike under protest. (Laughter.)

MR. MURRAY: We'll come back to you, I promise.

MR. HINDERY: The people who own the mikes make the rules. (Laughter.)

Q: Okay. I'm Mark Gruinberg (sp) from Press Associates, which is not to be confused with Associated Press. We're small; they're large.

A question for each of you and then a question for Mr. Smith. The whole basic premise of a corporation is based on a gilded-age era Supreme Court decision which gives corporations the same rights under the 14^{th} Amendment as persons. I'm going to explode the premise and ask you to defend it. Why should a corporation have the same rights?

And for Mr. Smith, you mentioned growing up in Louisiana. Let's go back to something else that Hindery talked about where the role of government originally would step in and not – and take care of things corporations didn't. Had government not been there, your growing up would have had no electricity. Louisiana Power and Light didn't want to string those rural areas. It wasn't profitable. Could you comment on that?

MR. MURRAY: Okay.

MR. SMITH: Well, you want to handle first the –

MR. MURRAY: I want you go on that Louisiana Power and Light Question. (Laughter.) Can I say one thing before we get into this? And I wish I had said this at the outset. It seems to me – and I'd like to get you two gentlemen to agree with me on this. It seems to me that some definition of terms here is useful. All of us agree – in terms of the responsibilities of corporations, all of I think could agree that the first responsibility of a corporation is to have a good going concern, a good business, create jobs, you know. I don't think anyone on this stage is going to disagree with that. That's step one.

Second, which is incredibly important, particularly when you're talking about Enron and WorldCom, the second responsibility of any corporation is to obey the law, and I don't think Fred or anyone else is suggesting otherwise. In other words, if the government decides that a company has to provide, you know, light and electricity to rural areas, the company does it. It's a question of what –

And then there is third category, and I think this is the category that we're really focused on here, is are there certain things beyond those two that companies should do in the name of social responsibility?

Anyway, with that, Leo.

(Cross talk.)

MR. SMITH: I'm going to miss – oh, the first question was whether or not the corporation – the status of a corporation –

MR. MURRAY: As a person.

MR. SMITH: – as a legal person is a good idea. I think social inventions are very good ideas. I think the corporation's value has demonstrated itself. The book by the economist authors, the company –

MR. MURRAY: Yeah. The new one? The (inaudible).

MR. SMITH: (Inaudible). Somebody.

MR. MURRAY: It's a great little book.

MR. SMITH: Illustrates that point, and there's other – and there's a book by Hessen, *In Defense of the Corporation*. It gets to an interesting question. The most interesting one I think is the limited liability, which I think there is some question there.

Going to Louisiana and my childhood, Louisiana is a petro-state, or was a petro-state. And those of you who know the literature, one of the great challenges of any political entity is to have too much easily acquired wealth. Louisiana had it. Louisiana became a populist, socially responsible welfare state. And the results are what we see today: a state that is now going head to head with Mississippi for the least productive, poorest state in the nation. The state, as I guess I mentioned earlier, that does not tolerate corruption; we insist upon it. It's a state that – it illustrates everything I believe wrong with an over-politicized economy.

I grew up in a very – in a part of the state that was rural, non-electrified in part, partly electrified, and the REA – Rural Electrification Administration – now – what is now called – RUS, Rural Utility System. It's interesting, because it does illustrate how government can create short-term gains and lose long term. We moved into the – as electricity became common in America at the turn of the nearly 20th century, everyone wanted electrification, and of course companies were rapidly producing it in densely populated parts of the United States. But in rural areas, of course, stringing those lines was quite expensive and therefore, alternative, what we would not call appropriate technologies, were emerging quickly.

If you look at the patent record of windmills and (inaudible) dams and generators and so on, the patent record was going straight up. And then the desire to have short-term gains pushed in, we created the REA, we subsidized lines across America. And as a result, we stopped in its tracks what would have been a wonderful technological gift, to give the poor of the world who do not have the opportunity of massive subsidies – they don't have the money to do that, they don't have the systems of honesty enough to do it – so in effect America gained a short-term gain and as a result the world suffers from an energy shortage.

MR. MURRAY: But let's not go too far down that road, because that's talking – that's about governments.

MR. SMITH: Yeah. That's (inaudible).

MR. MURRAY: The benefits are cost of government policies, and what we're trying to keep focused on here is, I think –

MR. SMITH: Yeah.

MR. MURRAY: – is the social responsibility of corporations –

MR. SMITH: Although I do suspect –

MR. MURRAY: – beyond obeying the law.

MR. SMITH: Although I don't know, but I would be willing to bet, there were businessmen's hands all over the REA bill because they got lots of money to build government projects.

MR. MURRAY: Well, that's a fair point. Go ahead.

MR. HINDERY: Let me try to give you like 30 seconds on your question. I believe in the corporate structure. I do believe that there are serious issues as to how liability is being attached to corporations. I think it needs to be revisited in a post-consolidation world. Too much potential damage arises – we should not have let industry consolidate to the degree it has without revisiting corporate liability concurrently. So I sort of answer both ways. I believe in the structure. I believe, however, in a re-visitation of the corporate liability issues.

Go to Alan's comment. He's absolutely right: you must follow the law first and foremost. That's why I find it sadly ironic that Sarbanes-Oxley, which has in my opinion been highly effective at preventing abuse, is so regularly attacked by business. It comes to my – reinforces my comment about the inability of these institutions to self-police. They don't like cops. That's the anti-Sarbanes-Oxley fight. They don't like cops. They want to jaywalk. They don't like cops. I simply do – I jump over law and I go where Alan was trying to take you, which is that I can't get to a long-term, sustained, profitable corporation without other constituencies, without other responsibilities.

MR. MURRAY: Well, let me let this gentleman, who is not a member of the press, in the back, ask his question.

Q: I guess I should have claimed that since I have a blog I'm a member of the press, but I (inaudible).

MR. MURRAY: It was totally acceptable.

Q: Ken Jarboe with Athena Alliance. Actually, a two-part question. First, Fred, thanks for your passionate outcry about the moral responsibility of the corporations and the poor not to give in. But that seems to make the opposite point, which is corporations are making moral decisions all the time. They can't help but do that in their ongoing action. So the question is, how do you then influence and how do you help the corporations make the decisions?

And the second part of that has to go to the role of the government. I mean one of the geniuses of capitalism is that we figured out there are externalities that the market doesn't take care of, and we've usually assigned the role of dealing with those externalities to the government. Isn't this rise of the NGOs and other organizations simply a reaction to that where we've spent, you know, we can say ten, 20, 30, 40 years eviscerating the ability of governments to deal with those externalities?

MR. MURRAY: Fred?

MR. SMITH: Very good questions. The first question, of course every decision is a moral decision in one sense of the word. What I was arguing was that the corporations should not be so quick to deed that moral responsibility, to transfer it to groups of elitists and (inaudible) mostly. I mean, what's happening in New York City seems to me classic in this case. No one wants to be in trouble at their cocktail party circuits, and so a lot of CEOs who are very distant from the agencies that are involved in environmental or human rights issues, basically as Alan said, say, get this off my back. The best way to get it off your back is to pay a quick bribe. And basically you have green bribes being paid around the world.

The Chamberlain strategy for corporations is very strong, but I don't think it's any more likely to bring green peace in our time than the other brought us peace in our time. There's a real irony of this abandonment of moral responsibility by corporations. I don't think because I have questions about whether corporations can handle moral decisions that I should endorse making immoral decisions.

The second point you asked was about the externality issue. There's a massive literature about market failures and the role of government. There's also a massive literature about the role of government failures. And in the real world you have to look at institutional problems. What does government do well and badly? What do markets do well and badly? And then you have to decide whether any institutional change would improve the overall outcome of society. Anyone who looks at the performance of government on things like the Enron situation or others must have some modest feelings that government is going to solve what markets find hard to do.

A corporation, remember, as (inaudible) told us, is a very, very interesting institution which has the problem of organizing a very large, disparate group of people into a team that pulls in the same direction. That is extremely hard to do because as Koss (ph) points out, when you create a hierarchic organization the people below you are going to lie to you. They're going to tell you what you want to hear, and your challenge is to find ways of cross-checking to make sure that your employees are not lying to you about what they're actually doing with these – what do you call them? – SPEs. These are not easily done. And when the industry is given – and when corporations are given a whole set of other even more complicated tasks to perform, the chances of breaking – of not solving that principal agent problem increase. And one of the reasons I think corporations are having some troubles today is they're trying to do too many things rather than focus on the Friedman task – complicated already – of creating wealth.

MR. MURRAY: Leo.

MR. HINDERY: Why don't we just go to another question?

MR. MURRAY: Whoa, a lot of questions here. Okay. Who's got the mike? Right here.

Q: Grant Stockdale. I run the news operation at the United States Energy Association, and I'm also the former associate publisher of the *Energy Daily* for the last 30 or so years.

Fred, you talk about the elitism of NGOs and the moral responsibility or not of corporations. In the energy world, give me your observations on CAFE standards and the moral or not responsibility of a very few companies who have tremendous sway over what happens in this country. And obviously GE –

MR. MURRAY: Is the question you're asking whether these companies should do this on their own?

Q: Yeah. Do they have a responsibility?

MR. MURRAY: To do it on their own –

(Cross talk.)

Q: – to do it on their own, or do they have a responsibility to fight that sort of thing? And if they do have responsibility for fight it, who's responsibility is to take it under its wing?

MR. SMITH: Corporate Average Fuel Economy, most of you would know, is a government-mandate during the Carter era basically to require that automobiles use less energy per year. That created a tension within the auto industry between consumer demands for products of performance, size, safety, and energy use, and the political demand that somehow in the face of all that energy use had to drop, too. We didn't create that across the board. For example, houses don't have a housing average fuel economy. If you look at the average energy of a house built today compared to a house built in the early post-War II period, it's very different. But they don't have to meet any average fuel economy because, for whatever, reason, our moral fervor didn't go to houses; it only went to cars.

Over the last – since 1997, the auto industry as a whole has improved – the weight of an automobile has gone up about 10 percent. The performance of an automobile in terms that some people care about, of acceleration, has gone up about 15 or 20 percent. And the – what's the third area they did, one other performance – oh, it's got a lot more appliances in it. And safety has actually improved in the situation. Fuel efficiency hasn't gone down or gone up much. It's about the same.

Now, to some – EPA did a report recently – that represents a moral failure. Why didn't they force consumers to do what was good for them? Well, they didn't because they're operating in a highly competitive world, and we have case study after case study where an innovation that reduced fuel usage was then used to provide a higher quality for the car, more hood space or something, more trunk space and so on.

It's very hard to please two masters. That's one of the reasons I'm so skeptical of social responsibility. The auto industry has one challenge: to meet the legal requirements of CAFÉ – it has to do that – and it has one market challenge, consumer challenge: providing cars that people are willing to do. I think that challenge is one of the reasons why the auto industry is in trouble. It's not the only one. The legacy costs are very big, too. But essentially, it's very difficult to meet these two challenges, and I think industry should spend a lot more time explaining to people why CAFE standards are bad ideas.

MR. MURRAY: Leo?

MR. HINDERY: A CAFE standard is no different than a $C0_2$ emission standard for a scrubbed or unscrubbed stack or water emission standards. The corporation is not going to be in a position to set a CAFE standard, nor is a public utility going to set a $C0_2$ emissions standard. There are government responsibilities to carve out CAFE from $C0_2$ or waterborne particulates is just – they're one in the same.

MR. MURRAY: Question from the back here. Yes, sir. Can you get him a microphone?

Q: Michael Nix (sp). I'm an energy consultant here in town. And I just wanted to follow up on that last set of questions with a little bit of background. Early 1990s, worked for an electric and gas utility. We supported the Clean Air Act with the $S0_2$ trading provisions in there. We took a no-regret strategy. We made money on trading $S0_2$ emissions. We're told in some parts of the press, and this isn't a slam on the press, that we were trading dirty air, but in other parts, you know, we received great acclaim for being supportive of this.

I think my question kind of goes to Mr. Hindery and the gentleman from CEI. What exactly is moral? Because there were some people that were saying, "Oh, this is just wonderful, you're supporting the Clean Air Act," people from both sides of the aisle

– and I’m a Democrat, people from both sides of the aisle were calling me up then and saying, “Michael, should we support the Clean Air Act? Is this good for your company in Wisconsin?” And we were saying, “Yes, we’re taking a no-regret strategy on this.”

How were we doing this? We had a really nice low-sulfur coal contract from Wyoming, so we weren’t taking coal from the Midwest where our company was, and we had a nuclear plant. Now, some people object to nuclear. Naming names here, John Podesta and I both support nuclear power, and I think the position of CAP is they’re very pro-nuclear power. It seems to me you get in a very slippery slope here when you start saying, well, it’s moral if you’re doing this issue, it’s moral if you’re doing that. I mean, I see my friends who represent California companies – they use an awful lot of renewable energy.

MR. MURRAY: I think that gets back to the question of are corporations the right place to make these decisions?

MR. HINDERY: And I think, Michael, you’re eminently qualified to participate in a morality debate on emissions standards, seriously. What troubles me about Fred’s comment is his assertion that that moral debate doesn’t belong in the corporation, only the immoral debate seemingly. You’re very clever. You’re the absolutely right person to sit down and discuss this sort of stuff and help figure out the issue. To suggest that you should not have morality debates internally and within yourself is just wrong in my opinion.

MR. SMITH: I don’t disagree with that.

MR. MURRAY: Wow, we have – could you give the microphone to this woman right here sitting against the wall. How are we on time? Last question?

MR. SMITH: Oh no, we’re just getting started.

Q: Hi. I’m Nicole Kurokawa with the Center for Global Economic Growth. I’m curious as to how the panelists would plan to solve the dilemma of corporation social responsibility because, Mr. Hindery, it seems like you advocate increased government intervention in this arena, whereas Mr. Smith advocates more individual responsibility, which seems not only more pragmatic but also a little bit more empowering to the individual.

MR. HINDERY: Well, it’s sure as hell more empowering. No, you know, the answer is absolutely. I am pro-regulation when necessary. I really believe in that. I come from the world that believes strongly, and based on personal experience, that these corporations are not capable of self-policing. At this magnitude of impact on society, they are simply not capable of self-policing. The protective organizations, the directors, the auditors, the regulatory community, the reason – to this gentleman in the back’s question in the back about NGOs – the reason it arose, a lot of people are frustrated at the absence of the oversight organizations. So I don’t believe that big business is capable of self-policing, and so I will help find the policemen for it.

MR. SMITH: There's a logo, some of you are Washingtonians who know, the Federal Trade Commission has its emblematic image over in front of it, it shows the Soviet realism statue of this struggling massively strong horse being held back by a noble Soviet-style worker with big muscles. Those of you who know the history of that, that illustrates the view I think Leo shares of the brute force of capitalism being restrained and guided by the wise enlightened hand of the political bureaucrat. And there's an awful lot of element in that –

(Cross talk.)

MR. SMITH: There's a lot of element in that, that essentially the belief that the role of the moral society is for the government to steer and the consumers – the taxpayers to row. I think that's wrong, but it is one vision and it's a vision that does motivate the CSR. I do agree that all human institutions need discipline. We're all fallen angels and the institutions we create will be prone to fraud, error, abuse, or just mistakes. The challenge we should all lead is, are the regulatory disciplines of a highly politicized bureaucracy more or less likely to advance the human condition, human societal goals, or are the competitive forces of a market stripped of its subsidy, stripped of its special interests pleadings – all hard to do – more than likely to discipline business to act in a more responsible way?

There's no easy answers in this area, and I think probably there is – where Leo and I both think on both sides of the coin – something really bad would happen. But those of us who see the history of politicized attempts to run economy do not see more virtuous societies; we see less virtuous societies. We don't see societies that are more effective in creating consumer choice, in creating wealth and knowledge, in creating a more democratized marketplace. We see societies where all of those virtues are less present.

In the world of the blind, one-eyed kings are necessarily more likely to lead. Markets to me – one last Milton Friedman quote. Milton Friedman said once when he was being attacked, you have a lot of faith in markets, he says, "No, I have evidence about markets. You have faith in government." (Laughter.)

MR. MURRAY: I'm sorry, we have to leave at that. We could do this for hours. But thank you all very much.

(Applause.)

(END)