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BUSINESS DAY

Motivating Corporations to Do Good

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Is it naïve to expect corporations to assist in addressing the social, economic and environmental challenges of the day?

In 1929, several years before Social Security and the National Labor Relations Act cemented pensions and labor rights in law, workers at the Eastman Kodak Company already enjoyed profit-sharing, retirement bonuses and a pension plan. They had sickness benefits and accident insurance.

In 1914, Henry Ford decided to raise wages to $5 a day, doubling, in one stroke, most of his workers' pay. "We were building for the future," he later explained. "A low-wage business is always insecure."

Almost half a century later, Coca-Cola's chairman, William E. Robinson, argued that a corporate executive served not just stockholders, but also workers, customers and the community. "The neglect of the customers and his labor relations will seal his doom far faster than an avaricious quick-dollar stockholder or director," he said.

Today, we live in a different world. Energy companies both recognize that climate change is a problem and actively lobby against efforts to combat it. The nation's half a million fast-food cooks earn, on average, $9.07 an hour, which even on a full-time basis is not enough to keep a family of four out of poverty. Yet fast-food behemoths like McDonald's and Wendy's fight tooth and nail against efforts to raise wages.

Coming out of World War II, corporate America enthusiastically draped itself in the American flag. As General Motors' Charles E. Wilson famously told a Senate committee in 1953, "for years I thought that what was good for our country was good for General Motors, and vice versa."

G.M.'s star-spangled jingoism sits in awkward contrast to Pfizer's recent efforts — along with those of other companies — to rid itself of its status as an American corporation to avoid taxes.

"Over all, there is no question that the ethos of corporate America has changed dramatically over the past 40 years," said Rick Wartzman, executive director of the Drucker Institute at Claremont Graduate University, who is writing a book about how the social contract between workers and employers has changed since World War II. The belief that business must serve multiple constituents, he argued, has given way to an imperative "to make the shareholder king."

Milton Friedman, the economic thinker from the University of Chicago, argued that this was exactly as it should be. The social responsibility of business is to increase its profits, he stated in an essay published in The New York Times 44 years ago. For executives to devote resources to anything else would amount to doing charity with other people's money.

Friedman's maxim arrived just in time for the era of the hostile takeover and the leveraged buyout, when corporate raiders sold themselves as saviors liberating shareholders from misguided managers who paid too little attention to the stock price.

Though legally dubious, the argument that it is an executive's fiduciary duty to maximize the company's share price became a mantra from the business school to the boardroom. And it was nailed down with money.

In 1993, some 20 percent of executive compensation was based on stock, according to Lynn Stout of Cornell Law School. Today, equity accounts for about 60 percent of the remuneration of executives at companies in the Standard & Poor's 500-stock index. With so much money tied up in stock options and the like, it is not surprising that executives will do almost anything to give their share price a boost regardless of what costs this might incur after their options have vested.

These changes responded to economic forces. The 1970s and 1980s were an era of high inflation, high interest rates and low returns on investment. Globalization was exposing American companies to much greater competition from abroad, putting pressure on margins and redoubling executives' attention on cost cutting and short-term profitability.

George Eastman had a vested interest in maintaining a trained and motivated work force in Rochester. Steve Jobs did not have much of a factory work force to think of. Another company halfway around the world made most of Apple's devices.

Is there any hope that corporate ethics might swing back to something resembling the earlier era?

Corporate executives jumping on the "corporate social responsibility" bandwagon certainly want you to think so. In 2000, 44 businesses signed up to the United Nations' global standards on human rights, workers' rights, environmental stewardship and anti-corruption policies. By last year, 7,717 had signed.

Companies, of course, are not charities. Their main responsibility is to remain profitable.

Still, there is a case to be made that attending to workers' rights or environmental degradation might help the business in the long term. The housing bubble and subsequent financial crisis served as a stark reminder of the consequences of compensating bankers based on short-term returns regardless of whether their business would blow up a couple of years down the road.

More broadly, company executives are under a new form of pressure. George Serafeim of Harvard Business School points out that the information age has brought greater transparency to corporate operations. Customers, investors and employees know more about what businesses do around the world and can exert influence to change their behavior.

Some prominent businesses, like the American retailer Costco, the Danish pharmaceutical multinational Novo Nordisk or the Anglo-Dutch food conglomerate Unilever appear to take a serious stand on broader social and environmental issues.

Nonetheless, it would be wise to temper expectations that corporate ethics are about to turn the corner.

After all, the motivations go only so far: Notably, pressure to “do good” from investors, customers and employees is not likely to encourage much good-doing in domains that investors, customers and employees cannot readily see.

Remember Enron? A report by Jean Tirole of the Toulouse School of Economics and Roland Bénabou of Princeton University notes that even as the company was quietly cooking the books, it was visibly giving money to all sorts of philanthropies. “Companies may behave better where it is most visible and not where it is less visible,” Professor Bénabou told me.

Corporations of an earlier era were just as motivated by self-interest. Eastman Kodak’s mini-welfare state came about in part to keep unions at bay. Henry Ford wanted to encourage his workers to be more productive and hoped that many would ultimately be able to afford Model T’s for themselves. But he also wanted to limit the dividend he would have to pay to the Dodge brothers, Ford shareholders who needed the money to set up a rival carmaker.

Wilson’s patriotic take on G.M.'s interests occurred at a confirmation hearing in which he was trying to convince senators that he could be a fine defense secretary and still keep his G.M. stock.

Indeed, there is a corollary to Milton Friedman’s proposition: You can trust a business that merely wants to turn a profit in a way that you cannot quite trust one that wants to change the world, too.

“I don’t think we would get very far in addressing large social concerns if we left them to corporations,” said Margaret Blair of Vanderbilt Law School. “The ethic of shareholder values is just too strong, and our social problems are just too big.”

Elected governments are certainly imperfect. But to address our most intractable ills, they are the better tool.

Correction: July 16, 2014

An earlier version of this article referred incorrectly to the book being written by Rick Wartzman of Claremont Graduate University. It is about the social contract between workers and employers, not workers and employees.

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