Speaking Notes

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Meeting the Standard: The post GFC World of Responsible Business Practice

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Thank you to Leeora Black for the invitation to address you today from a variety of perspectives – as a consumer movement leader and head of CHOICE, as a regulator, and in general as a person with a long-standing interest in business practice and society.

I'm going to talk about markets today – and specifically in the GFC aftermath – about markets and regulation. A key issue on many minds at the moment is about the role of markets in our economy and the role of governments in the market and getting that right for the community's long-term benefit. Intersecting that discussion, I'll contribute some thoughts about how Corporate Social Responsibility might influence thinking on this issue.

The Productivity Commission, as you all undoubtedly aware, is rather interested in the topic of markets and regulation – in fact, that is the principal focus of the institution. For many years, politicians of both major parties clearly understood that policy reform to promote efficiency and community wellbeing could often be stymied by vocal minorities who might lose out from such reform even when the much larger community would benefit overall; the purpose of the Industries Assistance Commission and now Productivity Commission has been to expose these types of claims to careful scrutiny and analysis and to promote an informed discussion of the alternatives.

I should also note at this point that I'm not speaking on behalf of the PC but in a personal capacity but drawing on experience within the consumer movement, as a competition regulator and as someone long involved in policy considerations.

Markets

In the vehement debate about markets and how they've failed at the moment, I remain unapologetic about them. Markets, when they are working well, are a truly efficient way to achieve some of our society's goals. They help ensure, through the medium of prices, that a country's resources gets put to the best uses and that, through competing firms, businesses and people have the incentives and can get rewarded for innovation, either better quality or lower cost production. This underpins our economic growth and in significant measure our standards of living.

The important point is that our markets make this happen in a decentralised way – nobody is in the driver's seat except the collected decision making of many buyers and sellers.

Of course there are important things that markets do not do, can't do or can't do well – markets are not much good at delivering things that aren't in the market that we value highly, for example liberty, family relationships and friendships, and so on; markets are not good at fair distribution or redistribution, and we should not ask them to perform that task. They are also not very good at producing 'public goods' like clear air and water or protected parks – because it's hard to make a buck out of them unless you can find a way to make everybody pay.

One of things markets do well – but which we actually don't like – is that they punish poor economic performance as they should (firms *should* face the prospect of going out of business if they don't respond well in a changing market). Unfortunately, there is a serious impact on people when a firm fails, and community support is often necessary to help people over the difficulties that can ensue, and that is why a society such as ours has provision for that type of assistance and support. And as we've just seen, sometimes, governments can't afford for certain firms to fail if that is seen as too destabilizing.

<u>Regulation</u>

At the same time as I am unapologetic about well-functioning markets, I'm also unapologetic about well-functioning regulation – that's not a contradiction in terms.

Some of our regulation is in fact directed at ensuring that markets work well – the property rights legal framework, the laws against price-fixing or other cartel behaviour, as well as the regulations directed at informing and protecting consumers (such as disclosures of ingredients or nutrition values in food products, warnings on household chemical products, misleading conduct laws, and the product safety rules themselves). These regulations about firms' conduct or about products and services are often means used by a society to enable the market to work more effectively and efficiently through ensuring that consumers can exercise their informed choice and are not dealt with unfairly.

Other forms of regulation are directed and designed to try to align private sector imperatives with those of the society. Banning lead in paint in children's toy products, requiring lenders to assess ability to pay before giving a loan to a consumer, setting minimum workplace safety rules are examples.

While regulation often desirable to meet our society's goals and would pass a benefits/cost analysis, regulation is by its nature quite complex to design well and to implement well. And, unfortunately, we abound with examples of duplication, excess and regulation that doesn't do its job or has serious unintended consequences. That's especially true when you are attempting to regulate an interactive system like a market.

So, it's not hard to find examples of regulatory ineffectiveness and/or failure.

In the near collapse of the global financial system, we have seen a very serious regulatory failure (in the US and the UK in particular rather than Australia) but, I would argue, we have also seen a serious failure of corporate ethics. One of the generators of that crisis was a failure of consumer protection regulation – putting loans in the hands of many people who clearly could not afford and would not ever be able to afford the debt involved. That however would not have triggered the crisis in its own right; added to that was conduct towards investors which sliced and diced and hid the risk in a packaged product partly driven by a misplaced set of short-term executive incentives. The latter was a large contributor to the ensuring not least as it caused a major rethinking of the trust with which part of the financial system could be treated.

Markets, Regulation and Corporate Social Responsibility

So within that world-wide question that governments are now dealing with – the stability of global financial markets and the levels and methods of government intervention to ensure that – does Corporate Social Responsibility have a place?

I think it is reasonable to say that a great deal of behaviour in any market is 'self-regulating' – in the strictest sense of that word. It's behaviour that derives from individuals acting within the social and ethical norms of their society.

But we also know from a great deal of academic study, and from personal experience, that behaviour in the organisational setting of a business can have an inherent potential conflict between a performance imperative and the general ethical norms which would constrain how that performance is obtained.

So one of the things that CSR does – crucially – is put in place a normative value set that influences the behaviour of everybody in the company. CSR legitimates a framework where:

First, questions of ethics are allowed to be more easily raised – and this can be a real problem otherwise. So there is an 'empowerment' – if I can be allowed use of the old social work term – of that ethical dialogue within the business framework.

When I was at the ACCC and looking over the years at the litigation that we took against companies, for legitimate companies (not fly-by-night operators), there was usually a leadership failure that disabled others to raise questions of appropriate ethical behaviour in the circumstances [it was often a leadership attitude of 'what can we get away with' in a competitive environment rather than an attitude of 'is this appropriate' action]. So leadership and commitment to CSR from the top level of a company is really necessary for any real impact on organisational behaviour and attitudes.

Secondly, CSR is important in a regulatory sense for ensuring that the society is in focus, for acknowledging that business decisions have significant effects for good or ill within a society – on people and on the environment.

The third advantage of a CSR approach is that, as part of solid risk assessment processes, it involves the people who are likely to be affected – the range of stakeholder groups. This is not a 'feel good' issue. The Chairman of the PC is fond of noting that the law of unintended consequences holds most firmly when consultation has been weakest – consulting stakeholders makes a lot of business sense.

The fourth advantage of CSR, within a context of a globally-agreed standards and reporting frameworks, is to objectify and measure performance in a way which requires transparency. It's much harder to mis-behave in those circumstances, and there is advantage in a global approach here because so much of business crosses our nation state territorial borders.

Given all of this, one would think that an outcome of CSR – done seriously and properly - might be less regulation; but I think that's probably a bit naïve in the sense of counting the number of rules. There are always the rogue players in a market – and also those that will push the boundaries in their own self-interest to the disadvantage of others. That's not going to change, so the laws will be needed to protect both consumers and also other businesses who are behaving properly.

But CSR might well mean less prescriptive and intrusive regulation where companies or industries are actually doing some of the job of regulating themselves through these frameworks; and it might even less enforcement on legitimate operators – where the context of employee behaviour and the incentives themselves are aligned and more conducive and supportive of acceptable behavioural norms. That's not to suggest that CSR is a panacea, but it certainly helps set the framework for the standards that are expected by that company.

Conclusion

So to conclude, when looking at CSR from a markets and regulation perspective – in other words a public policy perspective – essentially, what Corporate Social Responsibility helps to achieve is to put business and markets more firmly within an overall framework that includes the societies in which they operate – that makes business decision-making rather more complex, but it should also make for better overall decisions and outcomes.