To Pillory and Punish—or to Praise and Preserve?

The Economic and Political Life of the for-profit Corporation

Climate change, millionaires and inequality, civil unrest and social justice, socialism, immigration, health care in general and the coronavirus in particular were familiar refrains on debate stages in the 2020 election cycle. But implicit themes were a few all tied to one economic entity: corporations, including corporate welfare, Wall Street, profits, CEOs, and anything with the modifier "big" in it—Big Banks, Big Oil, Big Tech, and Big Pharma.

Given the rapid, low-cost, effective development of covid-19 vaccines, Big Pharma has received a temporary reprieve from vilification. But lurking just below the surface, the swipes and assumptions are never far removed. For example, in the popular novel *The Art of Racing in the Rain*, the author couldn't resist taking a swipe: "Pharmaceutical companies profit from the misery of others." Adam Smith would likely have phrased it differently.

In the agricultural era, the family was also a firm. Self-sufficient Jacks and Jills of many trades grew their own food and made their own clothes and furnishings. What changed? The emergence of efficiency gains from specialization, trade, and being able to exploit comparative advantages. As Adam Smith wrote in *The Wealth of Nations*: "Specialization and division of labor are limited by the size of the market." Enter stage right—the business sector.

BY ALLEN R. SANDERSON

Some household production still exists. We cook dinner and clean, at least occasionally. But we also "farm out" or outsource childcare and many personal services. (Firms also outsource; then they, unlike households, catch political flak for doing it. The federal government also outsources the financing—a sizable fraction to China and Japan—of its budget deficits, but largely gets a pass.)

In a 1937 article, *The Nature of the Firm*, written while he was still an undergraduate, later University of Chicago faculty member and 1991 Nobel laureate Ronald Coase laid out the economic explanation for why firms exist at all. This seminal piece on transactions costs, production efficiencies, and coordination mechanisms that produce organizational benefits led economists and other social science scholars to extend their thinking and research.

As the 20th century moved along and large factory production and new technologies offered innovators and entrepreneurs the opportunity to take advantage of economies of scale to increase productivity, expand output, and lower costs, along came the corporate form of business enterprise.

Argued before the Supreme Court in 2009 and decided in 2010, in the Citizens United case the Court held that our First Amendment free speech rights prohibit the government from restricting political spending by corporations—and labor unions. Cue Mitt Romney's 2011 remark that "corporations are people too." Another factoid sidebar: corporations actually spend relatively little of their shareholders' earnings on political advertising; there is no point in picking sides and alienating half your customer base, whereas unions far outspend them, and virtually all of it goes to just one of our political parties.

Today there are more than 30 million for-profit businesses in the U.S. The vast majority of them are small retail businesses—mom & pop stores, single-owner proprietorships, the self-employed and small farms. While they are the most numerous, they account for a tiny fraction of total sales or employment.

At the other end of the spectrum, the most influential type of organization is the corporation, a legal entity that confers ownership to shareholders; the fact they have limited liability in terms of absorbing losses facilitates amassing funds and preserving continuity. Corporations constitute under 20 percent of all businesses but account for more than 80 percent of sales and employment in this country. We would be a far different, and far poorer, nation today without this economic staple.

All firms have to pay for their activities, and how they are financed is closely related to how they are owned. Who bears the risk and thus is responsible for the losses, and who is entitled to the spoils, is a related consideration. As is to whom the company has any social or economic responsibility—to its employees, the unemployed, the community and general public, the environment, customers, creditors, and shareholders.

This was raised boldly by Milton Friedman in a 1970 *New York Times Magazine* article: "The Social Responsibility of Business is to Increase its Profits". In that famous piece Friedman argued that the CEO does not have the right to spend stockholders' money on anything that does not augment the worth of their investment, and that the executive should pursue "activities designed to increase profits so long as it…engages in open and free competition without deception or fraud." In the last two years this statement has resurfaced as a serious debate topic.

When American philosopher Nicholas Murray Butler, president of Columbia University for 43 years, William Howard Taft's running mate in 1912, and recipient of the 1931 Nobel Peace Prize (shared with Jane Addams) was asked what he considered the most important discovery of modern times, his answer? The limited liability corporation. ❏