What is the purpose of the corporation? This is one of the most controversial and perhaps one of the most important questions that we need to address in this course and that you will need to address as the next generation workforce leaders. Why is this the case? Well, because American CEOs have answered this in two different ways.

From the 1940s through the ’70s and ’80s and into the 1990s, there was a broad view of the corporation that has now narrowed down to focus on maximizing shareholder value in the short run. Here's a quote from the CEO of Sonesta Hotels, Roger Sonnabend. He says, "Social responsibility and expanding profitability are not at odds with one another. Quite the contrary. They are two faces of the same coin." That view was shared by a lot of CEOs of his era-- best illustrated perhaps by graduates of this important institution called the Harvard Business School.

The class of 1949 is known for producing an enormous number of CEOs that spread across the economy over the next decade or two. Many of them had been veterans of World War II. In fact, 90% went to the Harvard Business School on the GI Bill. Many of them were first-time college students in their families. Many of them grew up during the Depression, and they were imprinted by the hardships of that time as well as a commitment to community service that was embedded in them during World War II. So they had a particular view of their responsibility.

Let's start with an example from one of the best-known companies of the 1950s through the ’80s. Xerox-- one of the companies that was a pioneer high-technology company-- lead in the development of office products. And it was led, from 1968 to 1982, by Peter McColough-- one of those graduates of Harvard Business School, class of 1949. Peter McColough graduated and went to work at Xerox, worked his way up through various managerial capacities, became CEO in 1968. Xerox was located in Rochester, New York, where they had manufacturing operations, and McColough believed very strongly that the role of the CEO was to be a good corporate citizen in the community. He worked very hard to improve education, to build strong community colleges, which then provided a very competent workforce for his organization and for others in the region. He worked on local and national politics. He worked closely with the labor union that represented the manufacturing employees at Xerox. They were among the first to develop, for example, quality-of-working-life programs and quality circle improvements to improve productivity and to compete with growing international competition in the 1970s and 1980s. And in particular, he believed very strongly at developing talent from within the organization and particularly led the way for developing talent among women and among minorities within Xerox.

So it's not an accident that, in 2002, Anne became the CEO of Xerox-- one of the first women to rise to that level of authority in American industry. And it's not surprising then, in 2012, that when Anne retired, the first African American CEO of a very large Fortune 100 company-- Ursula Burns-- succeeded her. And the culture carried
forward. The same view of corporate social responsibility can be seen in the words of these CEOs as was the case with Peter McColough.

So if you look on Xerox's Social Responsibility Report on the web, you'll find currently the same words that mirror what McColough stood for. Quote, "Since our earliest days, Xerox's has embarked on a neverending journey to demonstrate that good business and good citizenship are not only compatible but are synergistic." The report then goes on to talk about customer satisfaction, innovation via patents, community participation, avoidance of workforce injuries, and so on, employee participation in community affairs, all as part of what they believe are the responsibilities of the modern corporation.

This was the dominant view, not only of Xerox, during this time, but also of other corporations-- best-illustrated by the statements of the Business Roundtable, the largest corporate association of executives from the 200 largest companies in the United States. And as late as 1990, the Business Roundtable made the following public statement: "Corporations are chartered to serve their shareholders and society as a whole. The interests of shareholders are primarily measured, of course, by economic returns over time. The other stakeholders in the corporation are its employees, its customers, its suppliers, its creditors, its communities where the corporation does its business and society as a whole, and all of these are vital to the long-term economic performance of the corporation."

That's the view up until around the mid-1990s. By this time, business is convinced that it should focus on shareholder value. And so the Business Roundtable says, "In our view, the paramount duty of management and the board of directors is to the corporation's stockholders. The interests of other stakeholders are relevant only as derivative of the duty to stockholders. The notion that the board of directors must somehow balance all of these other stakeholder interests fundamentally misconstrues the role of the directors and the responsibility of the corporation."

Well, this is a big change. What caused this change? Well, it was a revolution in ideas about the corporation that came largely from the academic literature of the time.

The leading finance professors of the time, Fischer Black and Bob Merton at MIT and their colleague Myron Scholes at the University of Chicago had developed a formula for better ways of pricing options-- that is, shareholder stock-- so that you could use stock options to compensate for CEOs. Their formula made it easier to use these processes, and then colleagues at the Harvard Business School published a number of papers saying we ought to tie shareholder value to CEO compensation through the use of stock options. And you saw the role of stock options grow. You saw the CEO compensation grow from what used to be about a ratio of 30 to 1-- that is, the CEO earned about 30 times the average employee in the firm-- to today, where it's well over 300 to 1. Well,
what was the consequence of all of this? One of the examples that we could turn to is another venerable company, STANLEY Tools-- a company that was a household term because every toolbox in America had good wrenches and other tools made by the STANLEY Corporation in Connecticut. It was a very socially-responsible company until the board of directors got taken over, and someone said let's really focus on shareholder value. And so a new CEO was brought in place and started to lay people off, not as a last resort because of economic necessity, but as a preemptive step to try to boost shareholder value.

More and more companies did that. And in fact, that led New York Times reporter Louis Uchitelle to write a very well-known book called The Disposable American basically chronicling how American corporations changed their behavior over time. Did it really benefit shareholders all that much? Well, if you look at the data, the data show that shareholders got about the same rate of return-- about 7%-- in the old stakeholder era as they were getting in the shareholder era. If you had just forced some of this restructuring, in fact, their rate of return goes down a little bit from the previous time period.

So we've imposed a lot of costs on society, but have we really benefited the shareholders as the theory might suggest? That's a question that you will have to answer. The era of maximizing shareholder value in the short run is still with us. Does this work for the future? Does it work for your generation? That's a question that you will need to address as you shape the work, the workforce, and the corporation of the future.