Although the phrase is now somewhat out of fashion, the issue of corporate responsibility is at the heart of many of the debates on economic policies around the world. Should corporations simply maximize profits and let the invisible hand do its wonders, or do they have some obligation to be good corporate citizens as well?

As with many politicized debates, this one has been captured by two extreme positions, neither of which are, to my mind, particularly sensible.

At one extreme are “pro-responsibility” advocates. This camp is often pro-free-lunch, too. They think that companies have a responsibility to pay their workers higher wages, offer better benefits, yet still keep prices down. Good luck with that.

At the other extreme, is the “pro-profit” gang. These folks think that a company’s only responsibilities are to their shareholders. The pro-profit group worships at the shrine of Milton Friedman, the both deified and vilified former professor at the University of Chicago. Friedman called the concept of corporate responsibility a “fundamentally subversive doctrine.”

“In a free society,” he said, “there is one and only one social responsibility of business -- to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud.”

Forgotten Qualifiers

Unfortunately, the important qualifiers at the end that statement are often forgotten. Friedman urges companies to “stay within the rules of the game” and avoid “deception or fraud.” So I would like to push back a little on those who claim to be following Friedman’s tenets and offer my own alternative, middle-of-the-road view.

Consider this example: A young bank employee, Chris, comes up with a clever way to increase profit. It is a refinement of an existing policy that when a customer makes a
purchase that exceeds the account balance on his or her debit card, the bank allows that purchase to go through, “as a courtesy,” but charges the customer a $35 penalty for making that purchase, and the same amount again for additional purchases until the account is back in the black.

Chris’s idea is that when a bunch of charges come in on the same day, say when a customer is shopping at the mall, and these charges will together put the customer over the limit, the bank will process the biggest purchase first, thus immediately putting the customer over the limit, and enabling it to charge a $35 fee for that sandwich at the fast-food joint and another for the latte at the cafe, and so forth. This policy won’t be disclosed to customers.

Here is my question: If Chris’ idea is legal and profitable, is that a sufficient reason for the bank to adopt it? More generally, is any way of making money acceptable as long as it is both profitable and legal?

There is an interesting irony here. Those who would favor this narrow definition of corporate responsibility are typically very skeptical of governments. Yet, in their worldview, it is the government that decides the limits of what a company should do.

If an activity is legal, no matter how unsavory or unscrupulous it might be, then corporations aren’t merely allowed to pursue it, it is their corporate responsibility to do so.

Friedman’s Rule

What would Professor Friedman say about this if he were still alive? Recall that his rule was that to be responsible, a practice must avoid deception. Would he consider Chris’ idea deceptive? I hope so. But the policy I describe is one that was used by many banks. Bank of America Corp. recently was involved in a lawsuit in which this strategy was one of the policies under scrutiny. (Bank of America settled the suit without admitting any wrongdoing.)

Financial institutions don’t have a monopoly on questionable business practices. Hiding fees where they are difficult to find (or decipher) is widespread, from mobile calling plans to the travel sector. It is easy to find out how much it will cost to sleep in a hotel, but harder to find out how much it will cost to park your car, use the Internet or get a suit cleaned.
So where do I come down on corporate responsibility? Life is a matter of trade-offs. Yes, corporate officers have a duty to their shareholders, but they may also want to sleep well at night. Strategies that enrich shareholders at the expense of customers, employees, neighbors or the environment require scrutiny. The bottom line isn’t the only line to consider.

So here is some advice for companies. First, before taking some action, consider whether you would be willing to publicly announce the policy to your customers. If not, don’t do it.

Next, instead of encouraging employees to find new ways to make fees harder to find and more difficult to understand, concentrate on finding ways to deliver a high quality product at a competitive price and compete by developing a reputation for fair dealing.

Yes, at least in the short run you may lose some customers to competitors whose prices seem cheaper, but in the long run you may be able to make a profit with loyal customers who are confident that their pockets aren’t being picked whenever they let down their guard.

If most companies in an industry fail to take this advice, they shouldn’t be surprised if they later receive greater regulatory scrutiny. The Dodd-Frank law came about in part as a response to practices such as the one I described earlier.

As a matter of logic, if the only standard you are willing to live by is the letter of the law, then you should expect that the letter of the law will become increasingly specific.

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