

Wellington Central Rotary Club

Perceptions of Business

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Almost exactly three years ago, I had the privilege of speaking to your sister organisation, the Wellington Rotary Club, and chose as my topic the role of business in society.

The thrust of my remarks was that business is just the ordinary stuff of life. The owner of a stall at the Otara market, the farmer, the general practitioner, the driving school instructor, the performers at Circa and the Court theatre, the managers and employees of large companies - all are people in business. Their common role is to discover and meet consumers' needs - the primary role of business. If they do their job well and persuade customers to part with their money in exchange for useful goods and services, they will flourish. If they don't, they won't. I can think of no higher vocation than that of serving the needs of fellow citizens by running or working for a good business.

I went on to point out that business has been the means of freeing many people from mindless toil. It is the wealth-creating institution of society. Over the past two hundred years it has transformed the way we live. It has produced marvellous products ranging from penicillin to Prozac, and gramophones to compact discs. It has expanded the opportunities for travel, learning, leisure and entertainment. Business is the vehicle through which countless individuals apply their talents to achieve their own aspirations and make a living by serving the needs of others.

Paul Johnson, the historian and journalist, who is visiting New Zealand next month, has developed this theme. He writes that business:

... is, in a curious sense, creative, and this is a point often missed about the capitalist system. We have been taught to see it, particularly by Marxists and their contemporary successors, purely in financial terms, 'shuffling bits of paper about' as they often say in the left-wing press. But capitalism also involves starting from nothing, building vast factories, digging mines and launching exciting new products on the market.

Johnson goes on to describe the efforts of the earliest entrepreneurs to build production lines, engines and bridges that were major artistic achievements. Bringing good wages to a family previously living at subsistence level was also to them creative. Of course they also took care to make their businesses pay, knowing full well that a business that can't meet the wage bill at the end of the week is no use to anyone.

The sheer creativity of capitalism - the product of the human mind or 'caput' - was a theme taken up by the Catholic theologian Michael Novak in his lectures in New Zealand earlier this year. The huge new University of Latin America now being established in Miami, which will partly relocate to Cuba when the Castro regime collapses, will have a special department named after Novak in which the creative aspects of capitalism will be explored and taught. Johnson writes that, by contrast, British academics tend to present the vocation of business as a horrible materialistic activity, characterised by greed and dishonesty. Some of them positively discourage bright students from going into industry - while simultaneously criticising British governments for "destroying Britain's manufacturing base". Johnson's conclusion is that countries today will only prosper into the next century if business is understood

as a high form of human endeavour, and if many of our brightest and most creative people are persuaded to work in it. If a culture of innuendo about the pursuit of business is allowed to flourish, we will end up with a community that can't create wealth. Who would want to be in business in such an environment?

Today I want to reflect a little further on perceptions of business and try to bring some current issues into clearer focus.

Attitudes have changed since the economy was mired in recession in the late 1980s and early 1990s. At that time many still doubted that the market reforms would work, and others argued that the gains would go to a favoured few and not be widely shared. The latter view had some validity when the labour market was highly regulated and outsiders were seriously disadvantaged in competing for jobs - ironically, it tended simultaneously to be held by those most strongly opposed to changes in labour laws. Since the second phase of reforms began in 1991, however, around 160,000 new jobs have been created, some \$2 billion of extra government spending is going into health, education and social welfare, and the forthcoming tax cuts will benefit low and middle income earners. It is no longer credible to argue that these are not widely shared gains, and polls show most people now believe New Zealand is going in the right direction.

With economic recovery, attitudes to business have also improved. The favourability rating of the corporate sector in general has lifted considerably. This year, for example, Telecom's favourability rating in an Insight poll has hit a record high of 74 percent, compared with 34 percent in 1993. New Zealand Post's rating was higher still at 85 percent and ECNZ's rating moved to 52 percent favourable and 25 percent unfavourable compared with a 20 percent favourable and 67 percent unfavourable rating during the 1992 power crisis.

Attitudes in education may also have changed. More of the best and brightest are looking to careers in commerce. Principals and teachers deny that their schools today impart negative views about business and competition. It's extraordinary to think that it could be otherwise, as four out of five New Zealanders find their employment in the private sector. And sections of the media are also doing more to feature human interest stories about business success and the callings in which most New Zealanders are engaged.

Yet attitudes generally in New Zealand are still far removed from those in many countries that are continuing to show the way ahead in today's world. I was struck recently by the findings of a Hong Kong poll that asked respondents to "name a Hong Kong person outstanding for creativity". The largest category of respondents, 23 percent, selected a business figure. Next most popular were fashion designers, with 15 percent, and politicians, with 12 percent. Artists, scientists and inventors picked up less than 2 percent, just ahead of one-off categories such as "my husband" and "my sex instructor". Other polls have reported that the most admired person in Hong Kong is Li Ka-shing, its richest man.

None of us, I imagine, is drawn to admire people simply because they're rich. But in a healthy society I suggest we should value those who use their energy, initiative and mental capital, take risks with their money in worthwhile projects, find eager buyers for their products, and enjoy material success as a result. Surely that's what the

parable of the talents is all about. How people use the rewards of material success raises separate issues of morality and character.

Unlike Hong Kong, we seem to have difficulty accepting the case for rewards for people who are outstanding as leaders of businesses or other organisations which are important in our community. We don't have a problem with Jonah Lomu and Kiri Te Kanawa being paid handsome amounts, but we have a fixation about the salaries of high performers running companies, government departments, Crown Health Enterprises and the like.

Yet, by most countries' standards, top pay in New Zealand is modest. In a cross-country survey recently reported in the *National Business Review*, the ratio of New Zealand executive salaries to those of lower-skilled employees was the most equal. I suspect that Ted Turner and Tony O'Reilly earn more in a good year than all the chief executives of our top 50 companies put together.

Sir Ron Trotter is on record as saying that when Peter Troughton was head of Telecom, he added a billion dollars of value to the business. That achievement benefited all New Zealanders, through cheaper and better quality telecommunications services. The contribution top class people can make to any organisation is enormous, and their pay as a proportion of total costs is insignificant. We need to recognise that reality if we are to attract international talent and make progress as a country.

We also need to acknowledge, and take pride in, some other realities about New Zealand's business and political record. In the recent international survey by Transparency International, the worldwide lobby group against corruption, New Zealand came out the cleanest of the countries surveyed. The head of the Serious Fraud Office has said that, in his view, that ranking is deserved. Similarly, in the latest World Competitiveness Report, New Zealand picked up a squeaky clean award for the lack of bribery and corruption in the public sphere. The New Zealand government was ranked third, behind Singapore and Hong Kong, as being the least trammelled by lobbying in its decision making. And New Zealand was deemed to head the world in not having a stockmarket prone to insider trading.

These findings were deeply upsetting to journalists, politicians and other chatterers who have made a speciality of denigrating business and politics in this country. Yet they would have come as no surprise to anybody with relevant international experience. In nearly thirty years in government and the private sector, I have never been offered or heard of a bribe, and scores of New Zealand business people, lawyers and politicians would confirm their experience was the same. The last time a New Zealand politician was seriously accused of corruption was in 1961, and the accusation was not sustained in the resulting defamation case. One only has to cross the Tasman to encounter a different world in which the favours some business people have collected from their 'mates' in Canberra are legendary, and where politicians have no qualms about getting into the middle of business affairs. The corporatist environment, reminiscent of pre-1984 New Zealand, breeds such behaviour. Australia ranked around the middle in the Transparency International survey.

We must hope that a more balanced perspective is emerging. The claims made in the notorious 'For the Public Good' programme were found to be without substance, and the reputations of the journalists involved were severely tarnished. Martin Hames's

book on Winston Peters documents the fact that he has had a success rate of virtually zero in uncovering significant proven illegality. Moreover, it is ironic that the self-appointed champion of transparency has spent over two years trying to prevent his own allegations of bribery, of a person who turned out not to be a member of the Business Roundtable, being tested in court.

Needless to say, it is quite possible that some day one of Mr Peters's claims will turn out to be true. I am reminded of the character in Neville Shute's book *On the Beach* who said that given an infinite number of monkeys and an infinite number of typewriters, one of them will eventually write King Lear. But making random accusations about many law-abiding citizens in the hope of eventually hitting a target would be a contemptible practice, and taking them seriously would be a poor way of forming judgments about anything.

None of this is to deny for a moment that there have been events in business and politics in New Zealand in recent years that did no credit to those involved. There were examples of lamentable business behaviour in the 1980s, as people reacted to the environment they found themselves in. Most of them were cases of foolish so-called 'entrepreneurs' and small investors seeking to get rich quick rather than cases of wrongdoing, and they were swiftly punished by the markets. Similarly, foolish political promises were made and then broken, reducing confidence in the political process and the standing of politics as a profession.

An overhang of this era is still with us in the form of the so-called 'winebox' inquiry. I know little of the details of this affair but the following general points are perhaps worth mentioning.

First, the purpose of the inquiry is to determine if the Commissioner of Inland Revenue and the head of the Serious Fraud Office and their staffs acted lawfully and competently in dealing with the winebox transactions, and whether the tax or criminal laws need changing. Notwithstanding the slant of some of the reporting, it is not a trial of the business people, lawyers and others involved.

Second, if the Commission finds evidence of possible wrongdoing the parties involved should be deemed innocent until proven guilty, if subsequently charged in a court of law. If found guilty, they should face the appropriate penalties.

Third, there is nothing illegal or indeed improper about tax minimisation. Court after court has reaffirmed judgments such as that of Justice Lord Tomlin that "Every man is entitled, if he can, to order his affairs so that the tax attaching under the appropriate Acts is less than it would otherwise be." Companies have a responsibility to their shareholders to minimise all costs, including tax, within the law.

Fourth, crossing the line into tax evasion is illegal and should be punished. Moreover, engaging in recklessly aggressive tax planning is not a prudent business practice. However, as in other areas of the law, the boundary line is often not easy to determine, and it would be surprising if directors took decisions in the grey area without the benefit of weighty legal advice. There is a difference between knowingly breaking the law and understanding that there is a risk that a court might deem you to be in breach. Clarity in law can help, but sometimes it is only when a law is tested in the courts that people can find out what it means.

Fifth, a large part of the story will almost certainly revolve around inadequacies in the tax laws and tax administration at the time. Developments in tax policy did not keep pace with other initiatives to open up the economy. However, New Zealand was not alone in experiencing this problem at a time of worldwide financial deregulation. Indeed many of the Cook Islands transactions appear to have been aimed at weaknesses in the Australian and Japanese tax bases. As it happens, New Zealand was faster than most in making changes. Our accrual rules were brought in less than two years after the removal of foreign exchange controls whereas Australia has still not got a comprehensive accruals regime. Our international tax regime came in two years ahead of Australia which liberalised two years before we did.

Sixth, and finally, what the last point brings out is that taxpayers - firms and individuals - respond to incentives. Indeed they are driven to do so. In old New Zealand, businesses could only survive with the aid of export incentives, investment allowances and a horror chamber of other props. For some years after liberalisation, punitive tax rates continued to apply - companies faced a tax rate of 45 percent and individuals a top rate of 66 percent - and the incentives to minimise tax were very strong. The moral of the story is that if you want businesses to focus on markets and consumers rather than the tax laws, you should get the incentives right.

What we can say with some confidence is that, by and large, the particular circumstances that brought about the winebox events are long since behind us. Further tax reforms have resulted in what the OECD has described as probably the least distorting tax system among OECD countries. A noted US academic has commented that the United States has been second only to New Zealand in attacking schemes for deflecting business income to tax havens, which is ironic given the backward focus that could emerge from the winebox inquiry. The claim by the Council of Trade Unions a couple of years ago that business was not paying its fair share of tax was ludicrous. As accumulated tax losses were run down and the economy picked up, company tax revenue has mushroomed: revenue for the year ended June 1995 was up by 65.7 percent on the year ended June 1993.

Having said all that, it is certainly the case that perceptions of business arising from the winebox inquiry are damaging, despite the distance from the events. As *The Evening Post* recently remarked, this is disappointing, especially when company reputations were improving after the 1980s excesses. However, no one in the business community is above the law. When the inquiry's findings are known, the lessons will need to be absorbed in a sober and rational way.

If wrongdoing is discovered, a few things should be borne in mind. One is that errors of judgment and lapses in morality are not confined to the corporate sector. By now, we should have given up on dreams of creating some 'new economic man': frailty is part of the human condition. Public officials can err, as events at Ohakea and in the auditor-general's office demonstrated last year. Robert Maxwell was not exactly an ornament to the media industry. Probably through incompetence rather than fraud, the Commissioners of the Anglican Church in England lost £500 - 800 million pounds in property investments in the early 1990s - an amount equal to several BNZ disasters. There have been notable recent cases of lawyers, teachers and sports administrators spending time as guests of Her Majesty. Let he who is without sin

Another form of selective morality should also be avoided. We rightly condemn business people for engaging in deceptive or misleading conduct. However, business people do not have a monopoly on loose statements and wild projections; indeed they typically go to great pains to avoid them. If we were to apply the standards of the Securities and Fair Trading Acts to, say, politicians, talkback hosts and Greenpeace, I venture to suggest many more people would be facing the judges.

The dangers of irrational reactions should also be borne in mind. Former Australian Prime Minister Bob Hawke expressed the view that, in voting for MMP, New Zealanders thought they were punishing politicians but they ended up punishing themselves. It would be folly to turn our back on an open economy, and most of the relevant tax loopholes have been closed. It has been reported that tax professionals and the government's own advisers believe national superannuitants are now collectively dodging more tax than was involved in the Cook Islands transactions. This might be a new area to which Mr Peters could apply his talents. Perhaps he might agree that, as well as pursuing those who are guilty, one of the best solutions would be to lower the tax rates which create incentives for such behaviour. It is no accident that rorts are endemic in welfare and accident compensation programmes where there are strong incentives to break the rules.

Finally, we need to think more broadly about the conditions most likely to breed corruption or dubious business and political behaviour. Nobel laureate Gary Becker has put it bluntly : "To root out corruption, boot out big government." Most scandals arise, he observes, whenever big government infiltrates all facets of economic life. This observation is as true of Italy and Brazil as it was of Eastern Europe and the Soviet Union. If politicians are willing to grant favours through subsidies, protection or favourable tax arrangements, businesses will demand them. We should also be wary of things like resource management legislation, Treaty of Waitangi processes and welfare policies which involve wide administrative discretion. The only way to reduce undesirable influence over the political and bureaucratic process, Becker argues, is to reduce the role of government through privatisation, deregulation and the introduction of competitive markets in as many parts of the economy as possible.

That has been the approach advocated by many in the New Zealand business community in recent years. The Muldoon era, which Mr Peters invokes when he argues that governments should back winners, was a breeding ground for political favouritism; we were lucky to escape worse forms of corruption. Politicians who want to be serious and constructive about the issues, as opposed to those who are only concerned with self-aggrandisement and a destructive agenda, should get behind those who understand Becker's point and are continuing to push for the depoliticisation of economic life in this country.

In the new New Zealand, we are starting to build businesses and a business environment of which New Zealanders can feel justly proud. Businesses are doing a far better job of providing consumers with value and quality. There is more trust and cooperation in our workplaces. Businesses are more environmentally conscious, and conscious of the need for high ethical standards. They are getting actively involved in supporting education. More women are entering business and moving up the corporate ladder. The overall balance sheet is a very positive one. Mario Vargas Llosa, a person more familiar than most with Latin American cronyism and economic stagnation, remarked on his visit to New Zealand that he had never encountered a

country where the business community had done so much to help eliminate privilege and support competition and openness. There is no basis for generalised, destructive criticism of New Zealand's record. A country that accentuates the negative, that mindlessly denigrates achievement and tall poppies, is unlikely to be a prosperous and happy place.

What form should more constructive responses to the issues take? I would argue:

- first, that we need to recognise there are opportunists, charlatans, fraudsters and corruptible people in business and every other walk of life; we must try to minimise the damage they can do, but, given human nature, there is no way we can eliminate the problem entirely. To try to do so would bring social and economic life to a standstill;
- second, that people respond to incentives everywhere, and if we want to change their behaviour we must change the incentives they face. Creating more open and competitive markets, and avoiding a 'rent-seeking' and 'entitlement' culture, which is conducive to patronage and abuse, are powerful means of improving incentives;
- third, that we need fair and effective laws, and laws that are strongly enforced. If some people are seen to get away with wrongdoing, others will be tempted to 'join the game'. Law enforcement agencies let the scrupulous majority down when wrongdoing goes unpunished; and
- fourth, that laws are not enough. We cannot rely on laws to cover all contingencies; a civil society also depends on a strong moral culture. Business can only operate on the basis of honesty and fair dealing in contracts, because trust is all that is left when contracts are incomplete. We have to be worried about signs of 'culture decay' around us, such as conflicts of interest in local government employment, moonlighting in the police, and clergy who condone stealing and regard the Ten Commandments more as optional suggestions. We all need to think about these problems and take responsibility for them.

It is regrettable, but hardly surprising, that some of our institutions were found wanting and fell in public esteem given the wrenching changes that had to be made to escape from the pre-1984 economic museum. But the constructive response must be to strive to remedy the weaknesses and to restore confidence in the institutions - such as politics, business, the law, education and the media - that are fundamental to a healthy, democratic society.

I believe the business sector for its part knows it must earn community respect not just demand it; must accept criticism where warranted and put its own house in order; and must play a role in debating issues and developing sound perspectives on them. I hope I have made a small contribution to that task today.