



Book China 2020

How Western Business Can – and Should – Influence Social and Political Change in the Coming Decade

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Recommendation

To what lengths will Western businesses travel in order to make profits in China? What morals and principles are they willing to sacrifice for a taste of success? Associate professor of business Michael A. Santoro investigates this subject by focusing on four salient issues: sweatshops, illegal drug manufacturing, Internet censorship and the rule of law. He offers a lucid, well-reasoned, though at times academic, analysis of how businesses are cashing in on corruption, weak regulation and the de facto absence of the rule of law instead of trying to improve conditions in China. Although some of Santoro's conclusions seem idealistic (for example, inject foreign firms operating in China with a sense of morality and you will fix China's problems), *BooksInShort* recommends his brief but excellent argument that Western corporations have a responsibility for human rights proportional to their ability to make a difference.

Take-Aways

- The 2008 Beijing Olympic Games offered China a platform to display its modernity.
- Yet, human rights violations, corruption and pollution are still pervasive in China, which finds itself at a crossroad between greater freedom or more despotism.
- Western companies generally have failed to exercise social responsibility in China.
- They have a moral duty to intervene in human rights abuses if they have ties with the victims, if they can make a difference and if they can withstand the repercussions.
- Sweatshops are still prevalent throughout China.
- American pharmaceutical companies abuse a loophole in drug safety laws by manufacturing cheaply in China.
- In 2007, U.S. Treasury Secretary Paulson traded away drug safety in exchange for greater access to China's financial market.
- Firms such as Google, Microsoft and Yahoo usually cooperate with Chinese censorship.
- Despite access to the best lawyers, Western firms have not litigated in China's courts.
- If they did, perhaps they could improve the judicial system and its ethics, but Westerners prefer to rely on *guanxi* – social capital – to settle disputes.

Summary

The Moral Compass

The opening of the Beijing Olympics on August 8, 2008 focused the world's attention on a modern, prosperity-driven China. On October 1, 1949, a short distance from where the new Olympic stadium now stands, Chairman Mao declared the foundation of a new Communist China – the People's Republic of China. Since then, the country has departed radically from its staunchly Communist creed, preferring to follow former leader Deng Xiaoping's assertion that "to get rich is glorious." If Chairman Mao's People's Republic was the new China, the China of the Olympics was the new, new China.

"Much of the criticism about China is warranted - in its rush to the future, corners have been cut, which have resulted in numerous catastrophes."

Yet, despite so many advances in the new, new China, many things have not changed at all. The Chinese government still does not function under the rule of law. Its human rights practices are questionable or even suspect. Corruption is endemic. Pollution is widespread. Western critics and Chinese citizens both find fault with the

new, new China, but a wide gulf divides them. Westerners focus on such issues as environmentalism, human rights, sweatshops, Tibet and unsafe products. The Chinese are more concerned about the rising cost of living, the unequal distribution of income, and corruption. They are quite sensitive to foreign criticism, and increasingly retort with anger and hostility. Resentful nationalism is on the rise. Since the late 1970s, foreign corporations have been pouring resources into China, now the world's factory. Corporate executives face criticism for willingly collaborating with a regime that flouts developed-world norms with respect to rights, freedoms and environmental protection. In response, they assert that economic progress will lead to reform on other fronts. In fact, although economic development has brought about some positive social changes, the Chinese Communist Party (CCP) is resolved to hold onto its solo political power.

“China has become the country that many in the West love to hate.”

Western businesses have done far less than they should to help advance human rights, freedom and justice. Corporations are legal “persons,” bound morally to accept social responsibility. Those operating in China face a clear choice: obey the government's rules or withdraw from the country. But can they find a middle ground? In apartheid-era South Africa, many foreign firms complied with the Sullivan Principles, which discouraged foreign-owned firms from implementing apartheid laws on their premises. The “fair share theory of corporate responsibility” states that a firm is obliged to intervene in human rights violations, depending on its relationship to the victims, its ability to make a positive change through intervention and its capacity to withstand “economic retaliation.” Corporations in China face a similar choice.

Sweatshops

Chinese factory workers, many of them migrants from desperately poor villages, know that factory jobs mean working long hours for low pay and having no real rights, yet they seek these jobs because they offer an escape from worse conditions back home. After suffering brand damage from bad press about exploiting workers in China, global manufacturers shifted their tactics and began to display a commitment to corporate social responsibility (CSR). Many large firms now hire consultants to assess their Chinese partners' operations or, like Wal-Mart, accept unionization. CSR programs are often PR exercises in which major corporations bribe nongovernmental organizations (NGOs) for clean reports to fend off criticism without improving their Chinese workforce's condition. Even firms that make a genuine effort to ensure that their suppliers comply with Chinese labor laws may fall far short. Meanwhile, enterprising instructors teach Chinese factory owners how to cheat on CSR audits and deceive their foreign customers.

“Rare is the company that doesn't have a ‘China Strategy’ for manufacturing or sales.”

In 2008, China enacted a new Labor Contract Law, which outlines workers' rights to work and social insurance entitlements – at least on paper. Enforcement could raise manufacturing costs by as much as 30%, killing China's comparative advantage. The big question is whether enforcement will happen. To dodge the law, some smaller firms have moved inland, where local authorities may be more lenient. The All China Federation of Trade Unions (ACFTU), “an arm of the state...controlled by the Communist Party,” has failed to improve working conditions because the Party is its main stakeholder. In fact, the ACFTU could even be hazardous to the embryonic, autonomous labor movement in China. It has been more diligent about discipline, productivity and “stability” than about workers' rights. Yet, it is now pushing to unionize migrant laborers working in foreign-owned firms, such as Wal-Mart, though the unions that the chain has joined do little more than provide recreation. They do not engage in substantive collective bargaining.

Dangerous Drugs

Chinese drugs are unsafe. In 2008, contaminated heparin from China killed up to 81 people in the U.S. An investigation revealed that no health inspectors – Chinese or American – had supervised the supplier. In fact, the pharmaceutical company's supply chain included remote family businesses that sold a cheap substitute chemical with enough similarities to heparin to pass basic quality screens. This is not an isolated incident. Hundreds of deaths and countless injuries have occurred globally due to counterfeit, contaminated, fraudulent and noxious Chinese drugs.

“The notion that one should ‘do in Rome as the Romans do’...is for the most part a sensible idea...In recent decades, however, multination corporations have been forced to consider the moral limits of this idea.”

China's drug regulatory system is so shoddy that China executed a former head of its State Food and Drug Administration when authorities discovered he had been taking bribes to approve fatally unsafe drugs. China's medical manufacturing regulations are much less stringent than U.S. laws. Basically, Chinese drugs are the products of an unregulated industry. The rules that do exist are often unpublished and unknown, and have wide loopholes. The judiciary is not empowered to draw boundaries and clarify accountability. For example, chemical companies are exempt from regulation by China's State Food and Drug Administration. Says one Chinese executive, “If you want to be regulated they will regulate you. If you don't want to be regulated, they don't.”

“Corporations have a primary duty to attempt to remedy human rights violations in which they are not to directly violate or assist others in violating human rights.”

This has not prevented U.S. and European pharmaceutical companies from sourcing “active pharmaceutical ingredients” in China. Although plants in the U.S. are subject to inspection by the Food and Drug Administration, the agency has inspected no more than a handful of Chinese manufacturing facilities. Moreover, China's supply chain for drugs and drug ingredients is so lengthy and complex that regulators may not even know some suppliers exist.

“Because so much of the world's low-wage production takes place in China, it has become a focal point for the anti-sweatshop movement.”

In 2007, American trade negotiators under the leadership of Bush administration Treasury Secretary Henry Paulson treated drug safety as a bargaining chip to gain access to China's financial services market. The World Trade Organization (WTO) and other trade agreements allow the U.S. to prohibit drug imports from China until it proves that it has a reliable, trustworthy regulatory system in place. Yet, the pharmaceutical industry opted to use China as a way to avoid costly compliance with American drug regulations. To demand higher safety regulations is to increase costs – a trade-off that U.S. pharmaceutical firms are unwilling to make.

“China's drug industry remains a significant danger to its own citizens and to the rest of the world.”

Thus, drug manufacturers outsourcing to China face even greater social responsibility than, say, clothes or toy manufacturers. Firms must ensure compliance to safety

standards on top of human rights and workers standards. The first small step to a solution should be a tracking and labeling system that clearly identifies drug sources and ingredients to provide some transparency to the supply chain. U.S. and European companies should help Chinese regulators design and implement world-class regulations. They should not ignore safety for the sake of low costs.

The Chinese Internet

A Chinese journalist is serving a 10-year prison sentence because Yahoo, his e-mail service provider, turned his name over to Chinese authorities. Microsoft removed the blog of an advocate for Chinese democracy, even though the server hosting the blog was based in the U.S. Cisco sold China the technology it needs to censor information and spy on its citizens. Google launched a censored Chinese search engine that prevents users in China from finding information that the Chinese government does not want them to see.

“Every year in China thousands of people die or fall ill, many suffering permanent disabilities such as brain damage, from tainted pharmaceuticals.”

Hopes had been high that the Internet would bring information, transparency and freedom to China. However, American technology companies’ numerous cooperations with China have dashed those hopes. As a result, the government is very much in control of what Chinese netizens, or citizens of the Internet, see and don’t see. Censors block access to Web sites such as YouTube when they carry politically objectionable content, like videos of the crackdown in Tibet. Chinese authorities rely on individuals to spy on their peers. For example, students can earn money for ratting out others who e-mail, blog or chat about forbidden subjects.

“Article 19 of the Universal Declaration of Human Rights [imposes] a duty on the Chinese government not to censor the Internet. Private companies operating in China have a duty not to assist the government in censoring the Internet.”

This official censorship has a chilling effect, leading to self-censorship. Chinese Internet users know that they must be cautious about what they search for or say online. However, they now have power and freedom that they could only dream about before the dawn of the Internet. Netizens are using the Internet to publicize egregious injustices. The story of the graphic designer who died following a brutal police beating, or that of the husband who, under torture, confessed to killing his wife – even though she was still very much alive in another province – received lots of Web publicity.

“The stark reality facing Internet companies in China is that they will unavoidably have ‘dirty hands.’ There is no way to operate in China without compromising and violating basic human rights principles.”

Western companies such as Google, Yahoo and Microsoft make a trade-off between corporate social responsibility to Chinese citizens and responsibility to their shareholders. Access to information is a human right. Thus, Internet companies are violating human rights by blocking access to information, cooperating with the Chinese government and putting profits before principles. Of the three Internet giants, Yahoo has demonstrated the most deplorable behavior. It censors even more diligently than Chinese companies. In 2002, Yahoo signed a “Public Pledge of Self Discipline” to enter the Chinese market.

“After nearly three decades of explosive economic growth and accompanying tectonic social changes, China’s future remains highly uncertain.”

Internet companies must decide whether they will do business morally, legally or not at all. So far, Western Internet companies have preferred to operate legally but immorally in China. There is some hope for change. In 2008, the Global Network Initiative brought American and European companies together to agree upon a code of principles for operating in countries that, like China, violate the human right to information. By working together and involving academic and NGO stakeholders, these companies can reduce their collective and individual vulnerability to economic retaliation by China, and perhaps manage to do more good than evil in the long run.

Rule of Law

The rule of law is embryonic in China. Corruption is rampant, as is *guanxi*, a Chinese form of social capital or cronyism. It’s a radically new and not widely accepted idea that the law, courts and judges, of which only about half have law degrees, can protect individual rights and property. The judiciary is not independent, but an agency among others. Moreover, the CCP has made it clear that the judiciary’s duty is to serve the Party and advance its policies.

“In the coming decade and beyond, only a Pax China that protects civil and political rights will respect the economic rights of Western business.”

China’s entry into the WTO required it to implement legal reforms, including the Administrative Litigation Law (ALL), which “allows individuals to sue public agencies and officials.” Foreign businesses have the right to resolve their disputes in the same courts as Chinese citizens. However, no foreign company has ever filed a suit under the ALL. Why? Multinational firms hire the best lawyers, who advise extreme caution in challenging China’s government in court. First, there is no reason to believe that Chinese courts are fair. Second, there is every reason to expect retaliation from the Chinese government.

Western businesses know that if they cultivate *guanxi* they don’t need to worry about the law. They see corruption as just another way of doing business, and have been willing to participate. This insults the argument that Western businesses can help to change China for the better. In fact, in some cases they may be changing it for the worse. If foreign businesses would insist on enforcing their legal rights in court, rather than merely abiding by Chinese law, they could make a positive difference. Their example could encourage other companies and individuals to use the courts. Of course, they run the risk of an economic and political backlash, but foreign businesses are collectively strong enough to withstand retaliation – especially when they act in concert. A call for foreign businesses to contribute to the rule of law in China by stepping back from corruption and fighting their battles in court is not sheer idealism. Billions of dollars in foreign direct investment have now flowed into a lawless country with questionable property rights.

About the Author

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