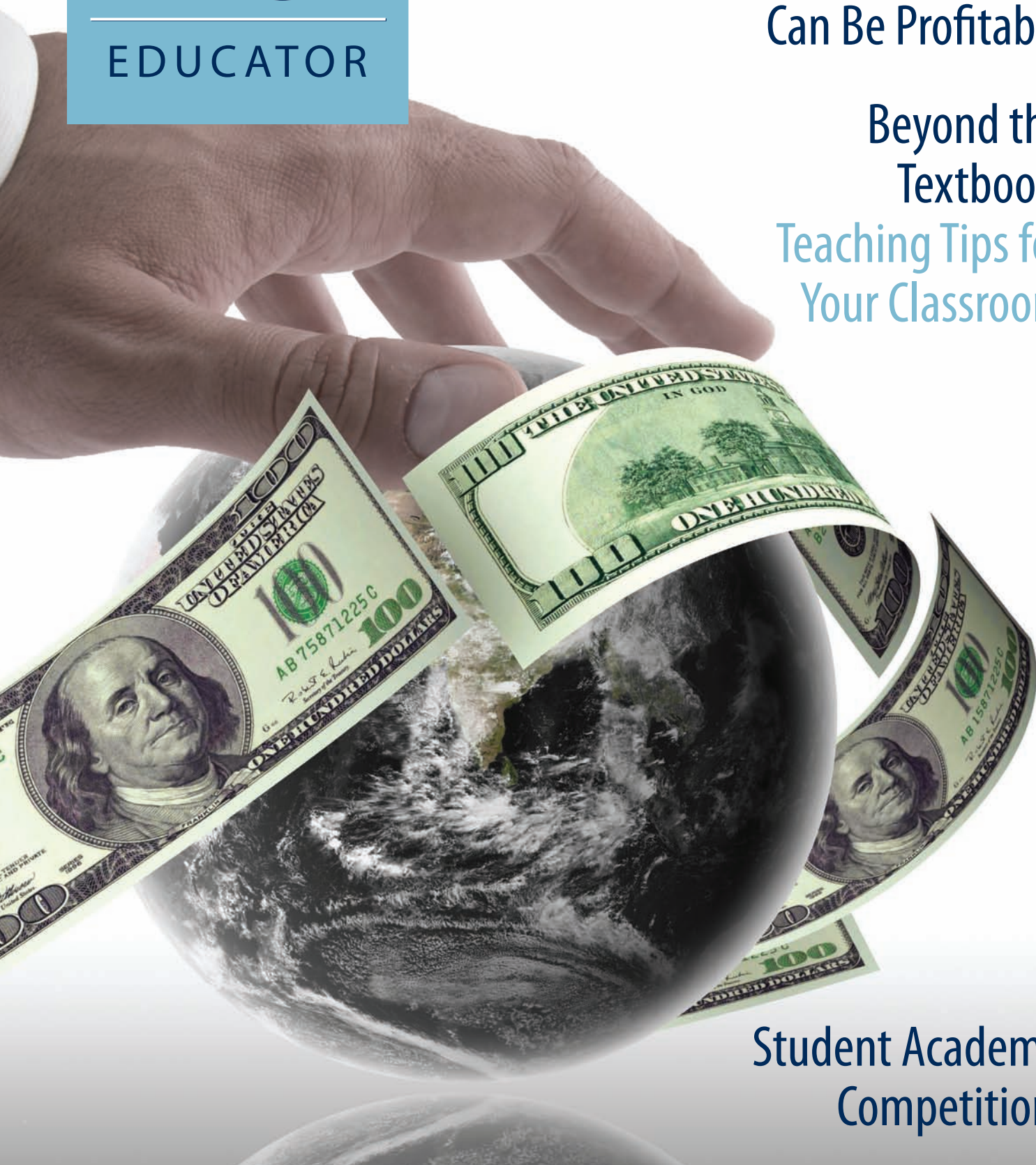


5E

EDUCATOR

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MISSION

The *5E Educator* provides K-12 teachers with content to enhance understanding of economics. It also offers lesson plans and Federal Reserve resources to reinforce state and local curriculum. We seek to enrich the learning experience for students and to highlight the importance of economics in the process of every day decision making.

To sign up to receive the online *5E Educator*, visit: www.richmondfed.org/publications/education/5e_educator/

Dear Educators,



Welcome to the Winter Issue of the *5E Educator*! The Federal Reserve Bank of Richmond is committed to achieving the mission of the Federal Reserve System in a manner that supports our region. Volunteerism and environmental responsibility are just two of the ways that we demonstrate this commitment.

In this issue, we present articles that weigh the costs and benefits associated with Corporate Social Responsibility (CSR) and consider its desirability from a stakeholder perspective. Also included is an excerpt that debates the environmental impact and economic consequences associated with the cap and trade discussion. These topics introduce students to the nuances of thinking like an economist, and allow them the opportunity

to explore economic concepts such as markets, marginal analysis, tragedy of the commons, and positive and negative externalities. Articles featured include "Corporate Social Responsibility Can Be Profitable", from The Regional Economist, a Federal Reserve Bank of St. Louis publication and excerpts from our own Region Focus "Up In the Air".

Also provided are a number of useful links to lesson plans that give students the chance to examine these topics in an engaging and interesting way. As always, we welcome your comments and suggestions.

Jeffrey Lacker
President
Federal Reserve Bank of Richmond



Hallway Monitor

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Corporate Social Responsibility Can Be Profitable

This article is an excerpt from the *Regional Economist*, April 2009 issue, published by the Federal Reserve Bank of St. Louis.

By Rubén Hernández-Murillo and Christopher J. Martinek

Corporate social responsibility (CSR) is a doctrine that promotes expanded social stewardship by businesses and organizations. CSR suggests that corporations embrace responsibilities toward a broader group of stakeholders (customers, employees and the community at large) in addition to their customary financial obligations to stockholders. A few examples of CSR include charitable giving to community programs, commitment to environmental sustainability projects, and efforts to nurture a diverse and safe workplace.

As more attention is being paid by outsiders to the social impact of businesses, corporations have acknowledged the need for transparency regarding their social efforts. In a recent survey, 74 percent of the top 100 U.S. companies by revenue published CSR reports last year, up from 37 percent in 2005. Globally, 80 percent of the world's 250 largest companies issued CSR reports last year.

Is CSR Socially Desirable?

Despite the apparent acceptance of CSR by businesses, many economists have taken a skeptical view of CSR and its viability in a competitive environment. Milton Friedman, in particular, doubted that CSR was socially desirable at all. He maintained that the only social responsibility of a business is to maximize profits (conducting business in open and free

competition without fraud or deception).³ He argued that the corporate executive is the agent of the owners of the firm and said that any action by the executive toward a general social purpose amounts to spending someone else's money, be it reducing returns to the stockholders, increasing the price to consumers or lowering the wages of some employees. Friedman pointed out that the stockholders, the customers or the employees could separately spend their own money on social activities if they wished to do so.

Friedman, however, also noted that there are many circumstances in which a firm's manager may engage in actions that serve the long-run interest of the firms' owners and that also have indirectly a positive social impact. Examples are: investments in the community that can improve the quality of potential employees, or contributions to charitable organizations to take advantage of tax deductions. Such actions are justified in terms of the firm's self-interest, but they happen to generate corporate goodwill as a byproduct. Furthermore, this goodwill can serve to differentiate a company from its competitors, providing an opportunity to generate additional economic profits.

Friedman's argument provoked economists to explore the conditions under which CSR can be economically justified. Economists Bryan Husted and José de Jesus Salazar, for example, recently examined an environment where it is possible for investment in CSR to be integrated into the operations of a profit-maximizing firm. The authors considered three types of motivation that firms consider before investing in social activities:

- **altruistic**, where the firm's objective is to produce a desired level of CSR with no regard for maximizing its social profits, i.e., the net private benefits captured by the firm as a consequence of its involvement in social activities;

- **egoistic**, where the firm is coerced into CSR by outside entities scrutinizing its social impact; and
- **strategic**, where the firm identifies social activities that consumers, employees or investors value and integrates those activities into its profit-maximizing objectives.

In agreement with Friedman, Husted and Salazar conclude that the potential benefits to both the firm and society are greater in the strategic case: when the firm's "socially responsible activities" are aligned with the firm's self-interest =

This article is co-authored by Rubén Hernández-Murillo, Economist and Christopher J. Martinek, Research Associate.

To access full article, click on the following link: www.stlouisfed.org/publications/re/2009/b/pages/socialresponsibility.cfm



Snacks

National Council on Economic Education Content Standard 16 & 17 High School Activity

Have students read and discuss the following article from *The Economist* to supplement the CSR discussion. This article examines the use of Pigouvian taxes to encourage healthier eating habits. www.economist.com/businessfinance/displaystory.cfm?story_id=14120903

As an alternative activity, consider having your students design their own "Pig Tales" and/or draw political cartoons that emphasize the pros and cons of implementing Pigouvian taxes to alter consumer and business behavior.



Class in Session II

Join The Club

Excerpted from *Region Focus*, Fall 2008 Issue “Up in the Air”; Carbon Policies Weigh Environmental and Economic Risks, a Federal Reserve Bank of Richmond Publication.

By Betty Joyce Nash

In the 1920s economist Arthur Pigou identified the concept of using taxes, now called “Pigovian” taxes, to compensate for negative side effects — externalities — of actions that harm third parties. Firms use the atmosphere as a depository for carbon but don’t pay for it the way trash haulers, for instance, pay to dump loads into a landfill, having already passed along that cost to customers.

That’s a kind of market failure, one of two that greenhouse gases represent. There’s also no incentive for firms to research and develop new technologies to improve the situation. So it’s necessary to price the privilege of sending pollutants into the atmosphere, says John Whitehead, an economist at Appalachian State University and co-author of an environmental economics blog. “When they see the cost, it creates an incentive to cut back pollution,” he says. And whether it’s a carbon tax or a permit generated by a cap-and-trade plan doesn’t matter. “In business terms, whether they’re paying in the form of a tax or paying another business to buy their permit, it doesn’t matter, \$100 is \$100.”

While a carbon tax or cap-and-trade plan may have similar outcomes, under certain conditions cap-and-trade plans aren’t considered “Pigovian.” The permits (either auctioned or handed out for free) are considered property in this created market. Along with the permit goes the right to buy or sell, and perhaps borrow or bank them. The theoretical frame-work for the cap and-trade plans

was conceived by Ronald Coase, a Nobel laureate, who suggested that if it doesn’t cost parties too much to bargain, then they’ll achieve an efficient distribution of ownership rights. So if a firm can make more money selling permits (“rights”) than by using them to emit pollution, it must be because that firm can better reduce pollution on its own at a lower cost than the permit buyer can.

Ideally a carbon price would be “harmonized” across sectors and countries. Yet the dynamic, gradual, and compounding effects of climate change make it tough to quantify the total costs to society, and the range of estimates is all over the map.

Based on 100 peer-reviewed estimates, the Intergovernmental Panel on Climate Change Working Group calculates that social costs in 2005 average \$12 per ton, but costs range from -\$3 per ton to \$95 per ton. Economist William Nordhaus of Yale University has developed models that suggest carbon taxes in 2010 could vary by policy scenario from \$2 per ton of carbon to \$200 per ton. Nordhaus favors an “internationally harmonized” carbon tax to achieve reductions or a well-designed universal cap-and-trade program. A regulatory approach, such as current policies that set emissions standards for vehicles and ban light bulbs, is inefficient.

The cap-and-trade versus carbon tax debate has been discussed widely in economics literature, government reports, the popular press, and on the Internet. In 2006 Harvard University economist Greg Mankiw founded an informal group, the Pigou Club, composed of economists who say a carbon tax offers the most effective solution to limiting global warming effects. That’s especially true if the additional money the tax generates is used efficiently by cutting taxes that depress work effort. Club members include some pretty big names in economics as well as other big names, too, like Al Gore, who has endorsed a revenue-neutral carbon

Interested in exploring corporate social responsibility policies from a different angle? Consider introducing your students to the policy debate on cap and trade.

Defining Cap & Trade

Cap and Trade policies use economic incentives to motivate businesses to engage in more environmentally responsible behavior. For example, ceilings on emissions limit how much carbon businesses can emit into the atmosphere. Businesses that significantly reduce emissions can benefit by selling their excess pollution rights to other firms. A market is created where-by businesses buy and sell permits to emit carbon. Supporters of these types of policies argue that the Cap & Trade system incentivizes businesses to engage in research and development to find environmentally friendly methods to conduct business and that these policies lead to lower aggregate emissions.

tax. However if a carbon cap-and-trade program sells well as other big names, too, like Al Gore, who has endorsed are venue-neutral carbon tax. However if a carbon cap-and-trade program sells rather than gives allowances away, the differences all but disappear =

To access the full article “Up in the Air”, follow the link: www.richmondfed.org/publications/research/region_focus/2008/fall/pdf/up_in_the_air.pdf



Heard over the P.A.

Each issue of the 5E Educator features information on upcoming workshops, competitions, new resources from the fed and/or other topics of interest.

Staff Development Opportunities

The Fifth District offers a number of staff development opportunities for teachers. To find the workshop location nearest you, check out the following offerings opposite.

For additional workshop information and registration, follow the link: www.richmondfed.org/conferences_and_events/education/

Workshop	Date	Location
Nifty Fifty Presentation	November 6, 2009	SC Independent School Conference, South Carolina
Midsize Economics	November 12, 2009	Baltimore, Maryland
Kidsize Economics	November 13, 2009	Baltimore, Maryland
Teacher Presentation	November 19-20, 2009	Virginia Educational Media Association, Virginia
Kidsize Economics	January 27, 2010	Charlotte, North Carolina
Midsize Economics	January 28, 2010	Charlotte, North Carolina
Middle States Teacher Conference	February 25-26, 2010	Gettysburg, Pennsylvania
Great Depression Workshop	February 27, 2010	Baltimore, Maryland



Beyond the Textbook

Lesson Plan Ideas: Corporate Responsibility Lesson Plans

High School

“What Is CSR And How Should It Affect My Habits As A Consumer?”

This entire unit is designed to be taught over 7 class periods, but teachers may choose from a variety of engaging stand-alone activities that cover Corporate Social Responsibility through the lens of world history and “contemporary issues”. Economic concepts covered include economic decision making, positive and negative externalities, private property rights, and public policy. To specifically weigh the pros and cons of Corporate CSR policies, we recommend using Lesson #7. The lesson plans are published on the worldwide web courtesy of Keizai Koho Fellowship.

www.us-japan.org/programs/kkc/k2006/lessonplans/milligan.doc

High School and Middle School Explaining Cap & Trade

PBS Frontline features a video with an accompanying worksheet that discusses the costs and benefits of instituting a cap and trade program as well as both positive and negative externalities. Also attached is an entertaining and simple way to explain cap and trade by limiting the word, “dude”. NPR’s radio program features a funny and insightful way to demonstrate how creating a market for carbon offsets works. Also attached is a worksheet to accompany the video created by PBS.

www.pbs.org/newshour/extra/features/science/july-dec09/cap-trade_07-21.html

www.npr.org/blogs/thetwo-way/2009/06/dude.html

www.pbs.org/newshour/extra/teachers/lessonplans/science/july-dec09/captrade_07-21_printout.pdf

“Business Responsibility”

This lesson is a group exercise that allows students to research the Corporate Social Responsibility initiatives of five local corporations. Economic concepts covered include cost/benefit analysis, positive and negative externalities and private property rights. Lesson offering is posted on the worldwide web courtesy of the Unicef. www.unicef.ca/portal/Secure/Community/502/WCM/EDUCATION/assets/pdf/lessonplans_business-responsibility.pdf

(This lesson may be adapted to Middle School audiences by limiting research required. Suggest teachers provide research materials.)

(continued on page 5)

Beyond the Textbook (continued from page 3)

Lesson Plan Ideas: Corporate Responsibility Lesson Plans

High School and Middle School "The Polluted Lake"

Students will engage in marginal analysis to determine the costs and benefits associated with cleaning up a town lake. Students will be introduced to the decision making process of policy makers in trying to accomplish multiple initiatives on a limited budget. This lesson is published courtesy of the Powell Center for Economic Literacy.

www.powellcenter.org/uploads/Polluted%20Lake.pdf

Upper Elementary "Growing Food Problem: Economics, Resources, and Production"

Students will be immersed in data to analyze the effect of resources, production, and consumption on standard of living, especially as it relates to understanding the implications for poverty.

www.powellcenter.org/lesson_searchConcept2.asp?topic=17&grade_level=1&x=58&y=7

Upper Elementary "Hunting Elephants out of Extinction"

Students will be introduced to how incentives may generate both positive and negative externalities by learning how certain societal decisions may negatively impact animals.

www.powellcenter.org/lesson_searchConcept2.asp?topic=17&grade_level=1&x=58&y=7

The editors welcome comments and feedback on these lessons and your recommendations for future lesson plan topics.



Pep Rally

Academic Competitions

Interested in finding an interactive way to engage your students in the study of economics? The Federal Reserve Bank of Richmond offers two student competitions as reinforcement activities for the classroom toolbox.

The Creative Expression Contest

The relevance of small business and entrepreneurship to the American economy has been particularly newsworthy given the recent recession. Innovation is cited by many economists and policy makers as a key determinant of American economic progress. Given the recent signs of economic recovery, consider using the Creative Expression as a tool to spark student interest in innovation and entrepreneurship. The Creative Expression Contest is designed to channel students' imagination by asking them to correspond with a potential investor to request seed money to back an original

business start up. Contest entries are to be submitted to the branch nearest you by December 18th, 2009. For specific contest guidelines, click here: www.richmondfed.org/education/for_teachers/academic_competitions/index.cfm

High School Fed Challenge

Interested in offering your students a chance to become Fed policy makers? Consider registering a team of 3 to 5 students in the Fed Challenge. This competition asks students to analyze current economic conditions and offer a policy recommendation. Given current economic conditions, the Fed Challenge may prove to be an enlightening and engaging experience for your students. For more information, follow this link: www.richmondfed.org/education/for_teachers/academic_competitions/high_school_fed_challenge/index.cfm



Snacks

National Council on Economic Education Content Standard 16 & 17

High School Activity

Directions: After defining Corporate Social Responsibility, have students read the following linked articles or excerpts of these articles and discuss whether or not corporations should engage in CSR policies. Students may use the following questions to serve as a framework for article analysis.

1. Is it profitable for corporations to follow CSR policies? Why or why not?
2. Do investors in companies benefit financially from CSR policies?

3. Does management have the authority to implement CSR policies?
4. Should government be responsible for enacting socially responsible policies?
5. Is it up to individuals to consider whether or not they should engage in volunteerism or pursue environmental responsible behavior? Why or why not?

<http://www.colorado.edu/studentgroups/libertarians/issues/friedman-soc-resp-business.html>

<http://online.wsj.com/article/SB120491426245620011.html>



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