TRANSPARENCY

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One objective of SFAS 141 and 142 is transparency in financial reporting, as is that of Sarbanes-Oxley. An essential concept, transparency is about much more than corporate disclosure of financial performance and its need appears to be spreading everywhere. It is causing thoughtful companies and other institutions to revise their values and behaviours for the better.

As a result two laws apply to today's businesses:

1. At some time you are going to be naked whether you like it or not.
2. If you're going to be naked, you'd better be fit.

Because of the trend to transparency, power is shifting from Managements of corporations to stakeholders such as customers, employees and shareholders. Companies are having to buff up their products as well as their behaviour, because outsiders are capable of finding out what they're really like, informing others, and even organizing to change them. It's good news for businesses too; when they are actively transparent they build trust and tend to perform better.

Transparency's opposites: opacity, lying and self-delusion remain robust, even in government. But despite reams of suspect news, the power of transparency continues to amaze. Why, for example, didn't someone in the government plant "weapons of mass destruction" for searchers to "find" in Iraq? Maybe the risk of being discovered was too great.

Transparency in business is now at a turning point, for three reasons:

1. The Rise of the Internet. Previous media, newspapers, TV, movies and radio, were one-way communicators, centrally controlled and easily subject to economic concentration; the Internet is the opposite. For the first time individuals and groups have a cheap, universal tool that lets them find out what organizations are doing, inform others and prepare a response. Music-swappers, anti-fast food campaigners, and workers in arms over offshore outsourcing are all evidence of how the Net delivers information and power.
2. Need for Above-Board Dealings. As market capitalism goes global, it imposes a performance discipline on the competitive success of firms and nations. The crises of 1998 in East Asia and 2002 in the United States exposed the costs of cronyism, corruption and false reporting. In addition to bankruptcies, job losses, and stock market crashes, opacity adds a risk premium "tax" to loans and investments. Banks charge higher interest and investors demand more equity or back off completely in the face of dubious business practices and obscure corporate governance.

3. Shift in Corporate Power. Since the start of shareholder capitalism in the sixteenth century, there has been a fundamental conflict in the separation of management from ownership. As long ago as 1933, when the SEC was not yet founded, US economists Adolf Berle and Gardiner Means wrote that a company's "controlling group can serve their own pockets better by profiting at the expense of the company than by making profits for it." In other words, executives do best when they line their own pockets at the expense of shareholders. Boards of Directors are supposed to counteract this tendency; in practice they too often prove to be members of the club.

However, now, for the first time, a new force is arising that represents shareholders and has clout: the pension funds. They now own a quarter of the share value of US publicly traded companies. They have the power to demand transparency as a first step to accountability and performance measurement. They have begun to draw blood; not only are they winning the proxy-disclosure battle, but the SEC recently announced a proposal that will allow shareholders to nominate directors, rather than simply having to ratify, Soviet-style, nominations from the incumbents.

