

The Moral Market

The recession and its free-market-on-steroids causes provide progressives the opportunity to start a new culture war of our own.

The great financial crash, Bernie Madoff, predatory lenders, and easy credit—for all the pain, there is an upside: A long overdue conversation about how unchecked markets can distort and damage American society has begun. Part of that conversation is populist, about how Wall Street and the new Gilded Age bankrupted hard-working Americans. But it is also about how go-go values penetrated Main Street, leading these same hard-working Americans to over-consume and take too many risks.

While this conversation has been refreshing, history suggests that public doubts about laissez-faire economics may not linger. The 1980s produced scandals, greed, and record inequality, and ended with the recession of 1990-1991, along with a bailout of the savings-and-loan industry that cost taxpayers hundreds of billions of dollars. Yet just a few years later, with the economy bouncing back, talk of robust regulatory schemes was forgotten.

DAVID CALLAHAN *is a senior fellow at Demos and the author, most recently, of The Moral Center and The Cheating Culture.*

Something similar happened a decade later. In 2002, as Enron, WorldCom, and other scandals engulfed the business world and the Dow completed a 38 percent dive from its 2000 high, 38 percent of Americans thought that big business posed “the biggest threat to the country”—the highest point since Gallup started polling nearly 40 years ago. But by 2004, with the Dow back above 10,000, that number had fallen to 27 percent, and the corporate scandals barely registered that year as a campaign issue.

The current crisis is far bigger, and public anger at Wall Street and corporations is as hot as any time in memory. Yet assuming that we are not headed for another Great Depression, history will soon repeat itself; populist anger will cool and there will be less momentum behind efforts to curb Wall Street and corporations. Today, politicians voicing populist rage may sound like trumpeters for the common man; a year from now, if the Dow is surging along with employment rolls, they may sound like party poopers.

This reality should weigh heavily on Barack Obama and his advisers. After all, reversing 30 years of *laissez-faire* policies is hardly a short-term enterprise, accomplished with a few bursts of legislation. It will pit the president against some of the most powerful interest groups in Washington. That struggle will not get very far if public amnesia about the downsides of extreme capitalism sets in yet again.

The trick for Obama, and for progressives, is to keep up a sustained attack on free-market excesses even as—invariably—AIG bonuses fade from memory and nobody can quite remember why credit default swaps were such a bad idea. This requires going beyond the standard Democratic playbook, which stresses bread-and-butter economic appeals, and offering something different: a full accounting of the moral corruption spawned by contemporary American capitalism, along with plans to curb this spreading rot.

In addition to soaring inequality and insecurity, *laissez-faire* policies have produced a range of social poisons: rising greed and envy, rampant fraud and dishonesty, falling trust between Americans, and a crisis of ethics in nearly every institution in American life. A focus on these poisons can help not just to sustain the momentum for reform once good times return but also provide a new explanation of how America’s moral fabric came so unraveled.

The New Culture War

Pessimism about values has been a fixture of American life for decades. Polls since the 1970s have consistently found that a large majority of Americans in both parties are dissatisfied with the state of America’s values, and such feelings intensified during the Bush years. A May 2008 poll, for example, found that 81

percent of Americans said things were getting worse when it came to values, up from 66 percent in 2002. And this has held true despite much good news over recent years. Violent crime is way down compared with the early 1990s. Teen pregnancy has also fallen sharply over the past 15 years, by at least 30 percent, and the abortion rate has dropped by a similar degree. Drunk driving deaths are down by 38 percent since 1982. Even the divorce rate has fallen by 32 percent since the late 1970s.

Judging by these statistics, America is not in the middle of a broad-based moral decline. So why the rising moral anxiety? Here's where things get interesting. When pollsters for Harris Interactive asked Americans in January 2008, "What do you mean when you say that moral values are very important to you?"—an open-ended question—28 percent mentioned "honesty," 11 percent said "integrity," 9 percent said "family values/belief in family," 8 percent said "ethical/has character/has good values," and 8 percent said "someone who does the right thing/stands for what's right." In a 2005 poll by the Democracy Corps, even Catholics said that issues like abortion weren't the moral issues that concerned them most. When respondents to this poll were asked to define moral values in open-ended responses, issues of integrity led the list (24 percent), followed by family and culture (22 percent), and the golden rule/social compact (21 percent).

So the sources of moral anxiety are broad and center heavily on issues of honesty. But thanks to the cultural right wing, our debate about values has been quite narrow, focused on issues like abortion and gay marriage most recently, crime and welfare in earlier periods—all leading to the same point: that permissive liberalism is to blame for America's moral decline. Yet for years now, this narrative has ignored a larger trend. Even as problems like drug use and teenage pregnancy have abated over the past decade, we have seen a growing tempo of news stories about fraud and deceit for financial gain: corporate leaders lying about earnings, traders using inside information, doctors taking money from drug-makers, politicians soliciting bribes, lawyers overbilling clients, and athletes taking steroids. These stories keep coming until nothing surprises us, even Bernie Madoff's \$65 billion Ponzi scheme.

This rising tide of bad behavior suggests that the great moral struggle of today is not between traditionalism and modernism, nor between faith and secularism, as the right would have it. Rather, it is between the relentless, amoral logic of

In one poll that asked people what values mattered to them, 28 percent said "honesty" while only 9 percent said "family values."

self-interest, profit, and the bottom line, a logic that has grown ever more dominant in this age of turbo-charged global capitalism and, against that, the fuzzier bonds of human connectivity—our integrity, our empathy, and our obligations to others. This divide, pitting market values against human values, is the real culture war of our time. And it is one progressivism is well-positioned to win.

Morals and Economics

The link between capitalism and moral turpitude is by no means a new idea. Since the days of Adam Smith, social critics have remarked on how the pursuit of profit, efficiency, and creature comforts can change people's values for the worse. More than thirty years ago, the sociologist Daniel Bell famously argued in *The Cultural Contradictions of Capitalism* that modern capitalism elevated the pursuit of short-term gain and pleasure over the more traditional values of self-restraint and obligation toward others. Bell was writing at a time when rising individualism and materialism, propelled by postwar affluence, seemed to be turning America into a more hedonistic and narcissistic society.

The picture turned much darker starting in the 1980s, as American capitalism went into overdrive and laissez-faire ideas came to dominate policymaking. In particular, ethical problems exploded as three features of contemporary U.S. capitalism took hold: high levels of inequality, widespread financial insecurity, and lax rules governing economic life.

Start with inequality. It makes sense that granting ever-larger rewards to economic winners might lead to bad behavior. Such fat carrots, which are endemic to what economist Robert Frank has called a "winner-take-all society," create obvious incentives to behave dishonestly or take excessive risks with other peoples' money. George Washington once said, "Few men have virtue enough to withstand the highest bidder." Very true it would seem, especially on Wall Street. While the issue of executive pay has received much attention lately, there is a clear if less discussed link between the recurrent wrongdoing of U.S. business elites and the outrageous amounts of money these people are paid.

Let's be clear: The criminality and extreme risk-taking by key actors in the mortgage meltdown were motivated by financial incentives of a magnitude that didn't exist a few decades ago, before inequality soared and norms changed around executive compensation. For instance, one of the central figures in the disaster—Angelo R. Mozilo, the founder and chief executive of Countrywide—earned up to \$470 million between 2001 and 2007, making him among the highest paid CEOs in America. One reason Countrywide was so successful, according to lawsuits filed by several state attorneys general, was that it engaged in widespread deceptive lending practices. The incentives on Wall Street for unethical or risky practices

were nearly as great. Richard Fuld made \$354 million as CEO of Lehman Brothers between 2002 and 2007, a period when the company earned vast profits from mortgage-backed securities. Joseph Cassano, who presided over AIG's credit-default-swap operation, made \$315 million during his time at the company.

Populist critics tend to demonize the executives and bankers who orchestrated the financial crisis. But upon closer scrutiny, many of the key figures in the crisis don't seem especially malevolent, or all that different than anyone else. For the most part, they are ordinary business leaders who were exposed to extraordinary temptation. And this is a key point: When people do bad things to make huge sums of money, the problem is usually not the moral failings of specific individuals as much as the distortions of an economy that offers outsized rewards to winners. As Alan Greenspan commented in 2002, about the dotcom era: "It is not that humans have become any more greedy than in generations past. It is that the avenues to express greed had grown so enormously."

This point was appreciated, briefly, when Greenspan made his comment, in the wake of the scandals that destroyed Enron, WorldCom, and other companies. Back then, there was much talk of how overly lavish stock options created huge incentives for CEOs to pump up, or prop up, stock values by reporting false earnings. The result was the 2002 Sarbanes-Oxley Act, which imposed stiffer penalties for earnings fraud and sought to ensure that the auditors of company books weren't compromised. But that reform did nothing to reduce the vast incentives that existed in other parts of the economy to cut corners, like the mortgage business. Thus, just a few years after the biggest corporate frauds in U.S. history, the business world has found itself roiled by a crisis of even larger proportions.

To take a very different example, it is probably no coincidence that steroid use spiked in Major League Baseball during the same period that the pay for top players rose dramatically. In 1993, Barry Bonds made \$4.5 million a year playing for the San Francisco Giants; by 2000, he made \$10.6 million; and by 2005, he made \$22 million. Although Bonds has yet to explain his alleged steroid use, one could imagine that his escalating compensation—and the expectations that went with such pay—provided incentives to boost his performance. Alex Rodriguez said as much when he cited "an enormous amount of pressure" in explaining why he used steroids between 2001 and 2003, a period when he was being paid \$22 million a year by the Texas Rangers.

When Obama was asked about Rodriguez's admission at his first White House press conference, he said it was "depressing news," but he missed an opportunity to explain how an obsession with fat paychecks has helped create a pernicious money culture in baseball and other sports that is pushing aside such quaint values of sportsmanship as fair play and self-restraint.

True, some inequality is necessary to make capitalism function. People who work harder or have better ideas deserve bigger rewards, and in this way, inequality can help nurture positive behavior. But when the gaps get too big and the winners get paid too much, bad things happen. This is a point that bears repeating by Obama and other progressives as they seek to make a deeper, more resonant case against laissez-faire ideas—and as they argue that America’s morals are under siege from a set of threats that have nothing to do with permissive liberalism.

The Pernicious Bottom Line

Growing bottom-line pressures and financial insecurity also have corrosive effects. It is not just that the carrots have been getting bigger for winners lately; it also that the sticks of economic life have been hitting harder for everyone, another trend that brings out the worst in people.

Well before the economy plunged into recession, the middle class—and even the upper middle class—was feeling squeezed by the high costs of housing, health care, child care, and college tuition. Meanwhile, corporations—their employers—are ever more focused on profit maximization as large investors look for growth in earnings every single quarter. Thanks to globalization and new technologies, competition is growing fiercer in many industries. The heat is on in the executive suite, and that heat is passed down through the entire corporation. Employees have come under greater pressures to perform than in the past, and even more so now amid the widespread layoffs of recent months.

People have incentives to behave badly when they’re pinched financially or when they perceive that their job—or their future—is at risk. You can see this motive at work in any number of areas where ethical misconduct is common. Take cheating by students, which has gone up since the early 1990s, with two-thirds to three-quarters of high school and college students now admitting to some recent cheating. Students are cheating more even as young people are less likely to drink and drive, use illicit drugs, engage in binge drinking, smoke cigarettes, get pregnant, or commit violent crimes. Why the dichotomy? One reason, cited by cheaters themselves, is the rising economic stakes of education. Getting into college is more competitive than ever, and the costs of college are higher than ever. Maintaining a high GPA while at college is increasingly essential as more students depend on scholarships, which are conditional on academic performance, to defray soaring tuition. And as the B.A. has become less valuable, good college transcripts matter more for getting into professional school, which is also more competitive than ever. In justifying her cheating, one student told a researcher investigating this problem that “good grades can make the difference between going to medical school and being a janitor.”

Many professionals are similarly tempted to trade personal integrity for financial security. A poll by Harris Interactive of 1,200 American workers in February 2009 found that 28 percent of respondents said they would act immorally—including lying or backstabbing—to keep their jobs. Take the widespread dishonesty around property appraisals. At the height of the real estate boom, surveys found that over half of all appraisers had felt pressure, typically from mortgage brokers, to overstate home values. While the appraisal process is meant as a key safeguard in the lending process, ensuring that borrowers and lenders alike are making sound judgments, it became commonplace for appraisers to take their marching orders from brokers and “hit the number” needed to close loans. This fraud made it easier for people to over-borrow against their homes, mainly through refinancing, and helps explain why so many homeowners now owe more than their homes are worth.

Appraisers were typically not the villains in this story. Rather, as I pointed out in a 2005 study for Demos, they felt they had no choice but to succumb to pressure from brokers and banks. In turn, former employees at lenders like Countrywide or WaMu have talked about the tremendous pressures they were under to close large numbers of loans—even if that meant cutting corners. Worse still, subprime lenders often tied compensation, in the form of “yield spread premiums,” to a broker’s success in steering borrowers to higher interest loans.

Similar pressures to act unethically have become common in many parts of the economy—from discount retail stores to white-shoe law firms—amid a rising obsession with the bottom line. The rampant “wage theft” exposed in recent years at chains like Wal-Mart, Family Dollar, and Target offer another vivid illustration of the corrupting nature of such pressures. Managers at local stores were instructed to keep down payroll costs, with implicit or explicit threats to their compensation or job security. But because they had limited flexibility to reduce store hours or staffing, the managers turned to a variety of illegal tactics, like forcing employees to work off the clock, denying overtime, and manipulating time sheets so that workers were paid for fewer hours. In *Wage Theft in America*, Kim Bobo estimates that workers lose billions of dollars every year because of such illegal employer practices.

Rampant overbilling by lawyers shows a similar dynamic at work. Over the past few decades, as corporate firms have come to operate much more like businesses with a greater focus on profits, there has been an upsurge of accusations of overbilling by such firms. In early 2009, three tech companies sued Foley & Lardner, one of the largest corporate law firms in America, alleging overbilling. In 2002, a group of associates at Clifford Chance, then the largest firm in the world, wrote an extraordinary memo that condemned the firm’s requirement

that every associate bill 2,420 hours a year. The memo stated that “associates found the stress on billable hours dehumanizing and verging on an abdication of our professional responsibilities insofar as the requirement ignores pro bono work and encourages ‘padding’ of hours, inefficient work, repetition of tasks, and other problems.”

Regulatory Relativism

Finally, weak government and lax oversight have exacerbated the moral problems of extreme capitalism. Sleeping watchdogs create obvious temptations to lie and cheat for financial gain, but somehow progressives—despite all their passion for regulation—never fully capture the poisonous effects of this free-for-all. One problem is the narrow way that regulation is framed—as a means of protecting the little guy from big business—when, in truth, the need for stronger watchdogs extends far beyond Wall Street and corporate America.

Americans cite honesty as a top values concern in part because they confront its absence daily. Auto repair shops overbill consumers by billions annually. Insurance companies routinely refuse to pay out deserved claims, while the health care sector is notorious for padding bills or performing unnecessary work (like filling non-existent cavities, as recently happened to me). And, of course, the vast scope of predatory lending is by now well-known—as it was long before the crash. Across the country, government agencies and better business bureaus deal with an unending flood of complaints from consumers.

Conservatives have a ready explanation for all this bad behavior, which is that permissive liberalism and “moral relativism” have clouded the difference between right and wrong. Yet Americans are behaving better on many fronts, and there is no evidence of a broad-based decline of morality. Rather, behavior has worsened almost exclusively where there are financial gains to be had, and rampant dishonesty has been spurred on by weak watchdogs and lax rules.

The prosecution of consumer abuses and low-level frauds is a case in point. In many states and localities, law enforcement agencies do not investigate frauds where losses are under a certain amount, such as \$100,000, for lack of resources. Indeed, law enforcement agencies at all levels have generally given low priority to consumer fraud and white-collar crime, a reflection of both an under-investment in government and the tendency to focus its punitive powers on its poorest members.

Things are made worse by the abysmal state of professional ethics and the failure of key institutions to police themselves. Enforcement of the American Bar Association’s code of ethics is left to state bar associations, which are notoriously ineffective. A 2006 survey by the American Bar Association found that out of 123,927 complaints about lawyers, only 3.5 percent led to formal discipline

and less than one percent to disbarment. The American Medical Association has been sluggish in barring gifts to doctors from drug companies, and, anyway, the AMA's ethics code is enforced by state medical societies that—like their legal counterparts—are not known for their vigilance. Meanwhile, the epidemic of steroid use in Major League Baseball occurred because for many years MLB had no serious testing policy and players faced no negative consequences for juicing.

One particularly insidious effect of weak watchdogs is the pressure that otherwise honest people can feel to behave unethically. Come back to the example of wage theft. In 2007 the Labor Department's Wage and Hour Division oversaw 130 million workers with only 750 investigators, less than half the number it had 60 years earlier to police a vastly smaller labor force. What this hollowed out regulatory structure has meant, Kim Bobo writes, is that "ethical employers are placed at a competitive disadvantage by employers who steal wages from workers." The problem with lax oversight is not just that it makes Americans vulnerable to predation or undermines fair play; it is also that even the best among us can be drawn into immoral and illegal behavior. Our economic system, it turns out, routinely helps to turn ordinary people into criminals.

A side effect of all this is pervasive cynicism: When society's rules are routinely flouted or enforced selectively on those with little power, people lose faith in equal justice and feel license to make up their own rules. Add to that widespread feelings that the social contract is broken, and that hard work no longer assures economic security, and the result is a moral free-for-all.

Progressive Ethics

This argument isn't new to Obama. He has already spoken eloquently about "the failed theories of the last eight years that got us into this fix in the first place." But Obama, along with other Democrats, has resisted opening a full-fledged moral attack on the economic and regulatory policies of the past thirty years. In some of his speeches on the financial crisis, for instance, the president mentions the central role of predatory practices and deceptive subprime lending in creating the crisis; in other speeches, he does not. More often, he has deployed familiar Democratic language about salvaging the American Dream and ensuring middle-class security. That helps in a recession, but it will provide little guidance once the economy picks up.

People have incentives to behave badly when they're pinched financially or when they perceive that their job—or their future—is at risk.

A tough moral critique of unchecked markets will find a receptive audience among Americans who often already understand the ethical risks that arise in such a system. Many intuitively know that bigger temptations can lead more people to lie and cheat in a society where winners live like kings. They know that financial anxiety can tempt even those with integrity. And they know that more bad things happen when nobody is watching. The basic dynamic is not very complicated, and with the right push from up high, this story can become central to the national conversation about why and how to temper capitalism.

The Obama Administration is already advocating many of the needed policy changes. Its tax plan, along with its economic and education policies, aim to reduce inequality, while its push for health care reform and other social protections would help alleviate insecurity. The administration is also promoting greater regulation along a wide front, not just in the financial sphere.

But the Administration still needs to think bigger. What is needed is a targeted, high-profile presidential initiative that can serve as a focal point for a new and distinctively progressive push to strengthen America's values. Why not create a White House Office of Ethics, Integrity, and Character that would work with federal agencies, state and local governments, and nonprofit organizations to address serious ethical problems in different sectors of American society?

The "to do" list of the new office would be long. For instance, it might mount a sweeping effort to reduce the rampant fraud and conflicts-of-interest found in the healthcare sector. In recent years, the Justice Department has gone after many large pharmaceutical companies for corrupting doctors, promoting the "off label" use of drugs, and overbilling government programs. These efforts should be ongoing, but also linked to a softer campaign to raise the ethical standards among doctors and healthcare administrators, encouraging better self-policing by these professionals. A similar campaign could target the decrepit state of ethics among lawyers and look at how the federal government could either push the legal profession to better police itself or take on some of these oversight functions directly. The government could additionally play a useful role in pushing for strong codes of ethics in industries where no such infrastructure now exists, such as construction.

Or, to take another example, the White House might work with the Internal Revenue Service to change American attitudes about tax avoidance. Despite a strong majority of Americans who say tax evasion is wrong, the IRS estimates that \$350 billion is lost annually to tax avoidance. One common excuse of tax cheats is that the rich don't pay their fair share, thanks to various loopholes, and so it's okay for the little guy to level the playing field. As the Obama Administration moves to change the tax code, including closing the loophole on "carried interest"

that allows hedge-fund managers to pay lower taxes than their secretaries, there should be an opening to encourage better tax compliance. Such a soft campaign to instill ethical citizenship would go hand-in-hand with long overdue efforts to bolster IRS resources, especially so that it can go after wealthy tax cheats.

A White House push on ethics should also focus on character building among young people. Recent decades have seen any number of efforts to change the behavior of young people when it comes to drugs, smoking, alcohol, and sexuality. These campaigns reflect America's narrow values conversation since the 1970s. What young people haven't heard is another set of messages about how to be a good person in a culture and economic climate that is so much about self-interest. Young people need to hear why it's important to help others, how to resist getting caught up in materialistic pressures, what to do when the heat is on to cut corners, and why it's important to value integrity over financial gains.

There is already a growing universe of service programs that help young people look beyond their own self-interest and feel a sense of obligation to others. That universe is about to get much larger thanks to a new law that triples the size of AmeriCorps. As well, there are national initiatives to teach character, such as Character Counts, a resource program for educators, that could be revamped and greatly expanded. A White House office would work to fit these efforts into a broader national strategy to raise up America's ethics.

But the window of opportunity won't stay open forever. The worst of the recession may already be over and recent polls show a glimmer of returning economic optimism among Americans, which is very good news. Now is the time to explore the moral wreckage all too frequently left behind by American capitalism. We won't like what we find, but we need to prepare for the day when the malls are packed once again, and the economy has more or less resumed its normal rate of growth. If Obama can get ahead of the curve and reinvent how America talks about both values and the economy, there is a good chance that this nation's politics will never be the same. **■**