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*Sub-Saharan Africa*

## FOR U.S. FIRMS IN SOUTH AFRICA, A DANGER OF COERCIVE SULLIVAN PRINCIPLES

### INTRODUCTION

"I'm not here to keep American companies in South Africa."

-- The Reverend Leon Sullivan<sup>1</sup>

A voluntary code of corporate conduct for American firms with South African investments has turned into a bureaucratic quagmire and created a controversial backlash with major foreign and domestic policy implications.

The code, known as the Sullivan Principles, was developed in 1977 to mute criticism from those who object to American economic activity in South Africa because of the government's apartheid policy of racial segregation and to channel American corporate resources into activities that are supposed to promote social and economic improvements for South Africa's non-white population. By 1983, some 146 U.S. companies had become Sullivan signatories, spending more than \$78 million in pursuit of the Principles' goals. Another five have joined in the past year. Despite this progress, significant problems developed.

Questions arose as to just how "voluntary" the program had become. Participants were saddled with a lengthy questionnaire on South African activities, required to submit to an annual audit, and pay a stiff fee for the privilege. Many did so, investing upward of \$100,000 on the in-house paperwork alone,<sup>2</sup> only to receive a questionable failing grade from the auditor, Arthur D. Little, Inc. Others could not justify spending that

<sup>1</sup> New York Times, November 6, 1983.

<sup>2</sup> Fortune, July 9, 1984.

kind of time and money and did not report. Some, calling it "low-grade blackmail," refused to pay.<sup>3</sup>

As a result, 30 of the 146 signatories were dropped from the Sullivan list in 1983. For them, and for the signatory companies that received failing grades, life has become unpleasant. Sullivan ratings are well-publicized and often cited by investment publications including News for Investors, published by the National Council of Churches' Investor Responsibility Research Center. News for Investors routinely prints Sullivan ratings. Companies receiving "failing grades" often find themselves deluged with inquiries concerning South African operations and Sullivan ratings. On occasion, universities, pension funds and other institutions use the ratings as rationale for divestiture. This threatens to depress the market value of these companies' stocks and securities and holds the promise for negative fiduciary impact for the institutions. A rash of state and local divestiture legislation compounds the problem. The media reflexively brand failing companies racist.

The problem for U.S. corporations is not the substance or intent of the Principles. They are laudable, pledging:

Nonsegregation of the races in all eating, comfort, locker room, and work facilities.

Equal and fair employment practices for all employees.

Equal pay for all employees doing equal or comparable work for the same period of time.

Initiation and development of training programs that will prepare blacks, coloreds and Asians in substantial numbers for supervisory, administrative, clerical and technical jobs.

Increasing the numbers of blacks, coloreds, and Asians in management and supervisory positions.

Improving the equality of employees' lives outside the work environment in such areas as housing, transportation, schooling, recreation, and health facilities.

While the substance of the Principles is not the problem, the compliance system and machinery are. The Principles' author, Leon Sullivan, a black Baptist minister from Philadelphia, has abandoned the voluntary nature of the procedure by publicly endorsing and testifying on behalf of the Solarz-Gray amendments to Title III of the Export Administration Act. Solarz-Gray would

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<sup>3</sup> From an interview, July 25, 1984.

transform into binding law major elements of the Sullivan Principles and would ban further investments by U.S. companies in South Africa. Violators would face fines up to \$1 million and stiff jail terms.

Solarz-Gray almost would assure U.S. disinvestment from South Africa. Faced with mounds of government paperwork and a prohibition on future capital improvements, American firms would quickly become non-competitive and eventually retreat from the South African market. A byproduct, of course, would be cessation of American social investment on behalf of South Africa's non-white population. More important, tens of thousands of non-white jobs would vanish. Fearful of the implications of Solarz-Gray, the State Department has begun pressuring those U.S. firms that refuse to sign the Sullivan Principles and pay the high audit fees to do so. The State Department apparently believes that universal voluntary compliance would make Solarz-Gray unnecessary. The potential pool of Sullivan participants is large. An estimated 350 U.S. companies operate in South Africa.

Codification of the Sullivan Principles is gaining popularity in state and local governments where legislators seek to head off complete disinvestment. Connecticut already has such a law. Recently, 24 states and localities were considering 66 separate pieces of disinvestment legislation. Such major cities as Washington and Philadelphia already have passed laws. New York City is considering it. The implication for \$200 billion worth of state and municipal pension funds looms large, for restrictions on how portfolio managers can invest the money entrusted to them significantly handicap potential performance of the funds. Those penalized, of course, will be pensioners or taxpayers.

The Sullivan Principles regrettably have been evolving from well-intended voluntary guidelines for corporate behavior in South Africa to a coercive system in which the U.S. government now is being asked to participate. Such coercion, by driving progressive U.S. firms out of South Africa, could harm those whom the Sullivan Principles are supposed to help--South Africa's non-whites.

#### THE CRUSADER

Leon Sullivan's social activism began during the 1940s in New York City, when he worked with the colorful and controversial Adam Clayton Powell. He later moved to Philadelphia to become pastor of the Zion Baptist Church. From its pulpit he launched a number of initiatives that eventually spread across America and Africa and attracted hundreds of millions of federal, state, local and private sector dollars. Sullivan assembled an impressive matrix of supporters from both major political parties, from Wall Street to Main Street, from Ghana to Georgia.

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In 1962, along with several hundred other Philadelphia clergymen, Sullivan launched a consumer boycott that forced the Philadelphia Chamber of Commerce and 300 business owners to pledge to hire black unemployed and adopt what was called a fair employment policy. Two years later Sullivan founded a privately funded job training program called the Opportunities Industrialization Center. Several months later, Dr. Maurice Dawkins, a Sullivan associate, opened an OIC in Los Angeles. Dawkins subsequently left Los Angeles to join Lyndon Johnson's Administration. There he secured \$1 million from the Office of Economic Opportunity to open three more OIC facilities. In the following years, a national OIC structure took shape with Sullivan as chairman. The lion's share of the funding came from OEO, the Labor Department, and the Department of Health, Education and Welfare.

Sullivan's political clout subsequently multiplied. Amendments to the Manpower Act of 1970, the Comprehensive Employment and Training Act of 1973, and the Job Training Partnership Act all contained protective language specifically inserted for OIC's benefit. The code word for OIC in this legislation was "community-based organization" or CBO. "Whenever an amendment came up, we moved to make sure we were protected, so you'll find a whole lot of CBO amendments along with the other amendments," Dr. Dawkins told The Heritage Foundation.

This protection paid off. By the late 1970s, OIC operated 160 centers in 40 states, had 5,000 full-time employees and an annual budget of \$150 million, 90 percent coming from government. Boasts Dawkins: "Our guys would always get a fair share of whatever was available at any level of government."<sup>4</sup> OIC went global in 1969, launching OIC International. It operates in eight African countries and has interest groups in five others, including Zimbabwe, where a Marxist government recently rejected British-style democracy. Domestically, OIC claims to have trained 700,000 individuals, placing 75 percent in positions with an 85 percent on-the-job retention rate. In 1981, a series of Philadelphia Bulletin articles exposed significant OIC mismanagement. Sullivan admitted problems at a few centers.

The Reagan Administration has been reducing federal funding of OIC. As a result, the organization's operations have been cut back significantly, reducing its centers to 123 and its full-time staff to about 1,000. Nonetheless, Sullivan cannot complain about U.S. taxpayer generosity. Since 1970, his organizations have received over one-half billion dollars in federal, state and local grants.<sup>5</sup>

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<sup>4</sup> From an interview with Dr. Maurice Dawkins, August 1, 1984.

<sup>5</sup> Interview with Elton Jolly, Executive Director of OICs of America, Inc., September 6, 1984.

## BIRTH OF THE SULLIVAN PRINCIPLES

Sullivan's OIC activities brought him to the attention of American corporations. In 1971, he was invited to join the board of General Motors. He accepted. He then astounded his fellow directors when he called on GM to pull up stakes in South Africa. Operating profitably there since 1926, GM would do no such thing. After a dialogue with black South Africans, Sullivan drafted his Principles as an alternative to business divestment.

Twelve companies signed the Principles in 1977. The following year, Sullivan hired Arthur D. Little, Inc., the Cambridge, Massachusetts management consultancy, to establish a rating system for signatory performance. Executives from signatories were recruited to form an Industry Support Unit, responsible for participation in policy and administrative matters germane to the Principles. A formal administrative arm, the International Council for Equality of Opportunity Principles, Inc., handles day-to-day business and is located not far from Sullivan's Philadelphia church.

Little will publish its Eighth Report on the Signatory Companies to the Sullivan Principles next month. Past reports, and the questionnaire and rating system on which they are based, have become controversial. The 55-page questionnaire asks over 100 questions. Eight pages of accountant's guidelines are also included, as answers detailing financial participation require independent audit, sometimes from more than one firm. Observed Fortune Magazine this summer: "The red tape is so daunting that William H. Magruder, head of Union Carbide in South Africa and an old hand, suggests that new signatories be assigned experienced 'buddies' in the manner of scuba divers facing the perils of the deep."<sup>6</sup>

As of last year, signatories not willing to pay the annual fee to the Industry Support Unit were dropped. The fee or "contribution," as S.G. Marzullo, manager of international government relations for Mobil and chairman of the Industry Support Unit, prefers to call it, is based on a company's worldwide sales and not on the scope of its South African operations. Says Marzullo: "You must pay and you must report."<sup>7</sup> Several signatories find this a curious form of voluntarism. "When it came time for the Seventh Report, we were informed that the fee would have to be paid before the report was graded. We saw this mandated fee as low-grade blackmail," says Rod Reck, vice president and general counsel for Loctite, the Connecticut-based fastener manufacturer and one of the signatories ejected from the 1983 Sullivan report. "This was being imposed by an outside source, not by the people

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<sup>6</sup> Fortune, July 9, 1984.

<sup>7</sup> From an interview August 7, 1984.

who share the common ideal,"<sup>8</sup> adds Reck. Loctite's annual fee was assessed by the Industry Support Unit, the official bill collector, at \$5,000. Individual fees range from \$1,000 to \$7,000 annually and are used to pay Little and the overhead for Sullivan's Philadelphia office and staff (International Council for Equality of Opportunity Principles, Inc.). Sullivan dismisses objections to mandatory fees as "jive,"<sup>9</sup> asserting that companies use it as a smokescreen to shield poor performance.

However, many signatories view the performance ratings as overly subjective and unrepresentative of corporate activity in South Africa. Even the Little executive in charge of the process, Reid Weedon, admits to major problems with the system. He told The Heritage Foundation: "I don't know any way to make [the ratings] foolproof. You're comparing apples and potatoes here."<sup>10</sup> Nevertheless, Weedon stands by the grading system. But Marzullo cautions, "The present questionnaire only partially reflects what companies are doing [in South Africa]. In effect, it's a shotgun approach to 'What do you do to help non-whites in South Africa?', with each company trying to make as many points as it can to get a good grade. We need a questionnaire that deals with how you address basic root problems."<sup>11</sup> Marzullo wants the grading system changed, for example, to award points for providing qualified teachers, not just new classrooms. Indeed, the Sullivan Principles have encouraged construction of housing, schools and clinics, but have not necessarily paid much attention to what goes inside.

Giant multinationals with great resources at their disposal receive better grades. Smaller companies encounter tougher sledding. "We have a very small operation and the cost did not warrant our involvement," said a spokesman for the Simplicity Pattern Company, one of 30 companies that either were ejected or withdrew as signatories in 1983.<sup>12</sup> According to Weedon, "The majority of companies who withdrew [as signatories] have no ownership in South Africa and no employees in South Africa."<sup>13</sup> Yet this contradicts the Seventh Report, which categorized at least 14 of the dropped companies as having 10 or more employees, a minimum of 5 having 10 or fewer employees and none owning less than 19 percent equity.<sup>14</sup>

Still, not even sheer size can insulate a signatory from swings in the South African economy, recently in recession, which

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<sup>8</sup> From an interview July 25, 1984.

<sup>9</sup> New York Times, November 6, 1983.

<sup>10</sup> From an interview July 27, 1984.

<sup>11</sup> From an interview August 7, 1984.

<sup>12</sup> New York Times, November 6, 1983.

<sup>13</sup> From an interview July 27, 1984.

<sup>14</sup> "Seventh Report on the Signatory Companies to the Sullivan Principles," October 25, 1983.

often dictate the level of its social spending there. "There's no way you can judge the success of a long-term program in one or two years," says Marzullo. "A company may fall back during a reporting period and then go back up again. It isn't fair to penalize them over the short-term for some temporary setbacks."<sup>15</sup>

And when Weedon does make a mistake, little time is provided for appeal before the error finds its way into print. Loctite received a failing grade in 1982, in part because it paid some employees \$10 below the minimum monthly wage (fixed at 30 percent above the local prevailing minimum wage) set by the Sullivan organization. "The employees concerned were two partially-disabled individuals, virtually unemployable, whom we acquired when we bought our South African subsidiary; but they're paid the acceptable wage level now. Reid Weedon visited our plant there and agreed with our handling of the matter, but there was no modification of the report."<sup>16</sup> After grades are issued, recipients have two and a half weeks to change Weedon's mind; otherwise, nothing can be done until the following year.

Companies that have never been signatories resent the pressure to comply formally with the Sullivan Principles, especially when they have their own anti-discrimination codes. "We do not need, nor do we wish a third party monitoring us," says Alan Mankoff, chief of Dun and Bradstreet in South Africa. "We integrated our operation long before Mr. Sullivan thought of putting it down in writing. There are people who say that the easy way out is to sign, but we think that's hypocrisy."<sup>17</sup>

Firms that have signed the Principles find that the requirements for a passing grade grow. Since 1977, Sullivan has written three "amplifications" to the Principles. "The Principles get tougher and more stringent all the time," he says.<sup>18</sup> "I keep saying to the companies, we must do more, more, more...we must move faster, faster, faster...."<sup>19</sup>

#### SIGNATORIES' SOCIAL INVESTMENT IN SOUTH AFRICA

Since 1977, Sullivan signatories have poured \$78 million into projects designed for the benefit of South Africa's non-white population. Marzullo thinks that this will top \$100 million by the end of 1984. Two years ago, reports the New York Times, American companies spent "more than five percent of operating earnings on housing developments, training and education programs, and community developments for their workers [in South Africa]--possibly more than they spend anywhere else in the world, including the United States."<sup>20</sup> According to the Seventh Sullivan

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15 From an interview August 7, 1984.

16 From an interview July 25, 1984.

17 New York Times, November 6, 1983.

18 Ibid.

19 From a speech to the Sullivan signatories, November 9, 1983, New York.

20 New York Times, November 6, 1983.

Report, significant progress in implementing the Principles has been made: all but one of the reporting signatories is desegregated; all have common medical, pension and insurance plans; blacks still receive higher wage increases than whites; and proportionate participation by non-whites in sales training programs has increased.

The number of South Africans employed by Sullivan signatories is down to approximately 66,000 from a high of 82,000, partially due to the recession and the withdrawal of a few U.S. firms. Non-Sullivan American firms employ about 33,000 South Africans.

Despite the flat economy, in 1983 reporting Sullivan signatories spent \$22.4 million on education and job training, entrepreneurial assistance, health and housing for non-whites. Over 35,000 blacks participated in scholarship and tuition refund programs, while 50,000 took part in job advancement training. More than 200 schools were "adopted" under the "adopt-a-school" program. The equivalent of 229 full-time employees contributed 57,072 employee days for instruction and consultation. The average employer spent more than \$225,000.<sup>21</sup> The irony is that this social investment may soon halt--in large part because of Leon Sullivan.

#### ANOTHER PUBLIC SECTOR SOLUTION SOUGHT

As with his Opportunity Industrialization Center job training program, Sullivan has turned to government for help when the marketplace did not satisfy him. The Principles were barely three years old when Sullivan endorsed the Solarz-Gray amendments to Title III of the Export Administration Act. Testifying before the House Subcommittee on Africa, Sullivan said, "The Government must require the adherence to the principles and there must be measurement and monitoring effectiveness....[A]t a minimum, I would like to see you pass legislation making the principles mandatory for American companies, including sanctions and penalties for those who do not comply....Companies have no social conscience; they have balance sheets; they want to see profits.

"I strongly support Congressman Solarz' bill which proposes: One, requiring that all U.S. companies sign the equal opportunity principles; two, onsite monitoring of all American companies in South Africa and three, tax penalties and sanctions imposed on companies that refuse to sign and do not comply with the standards set.

"I strongly support Congressman William Gray's bill which calls for a halt to all new investments except for essential

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<sup>21</sup> "Meeting the Mandate for Change," Sullivan Principles Industry Support Unit, 1984.



retooling; and I urge, in addition, that there be no further expansion of operating already in South Africa until changes are made in the prevailing conditions."<sup>22</sup>

Earlier, Sullivan had issued a joint statement with Rev. William Howard, president of the National Council of Churches, pledging acceleration of a campaign aimed at ending U.S. bank loans to South Africa.<sup>23</sup>

Signatories have greeted Solarz-Gray with horror. "What Solarz has proposed is a bureaucratic monstrosity," says William Broderick, director of intergovernmental relations at Ford.<sup>24</sup> General Motors, whose six-year old education and training program for non-whites predates the Principles, voiced early opposition to Solarz-Gray. "...We firmly believe that mandating these principles would act as a negative--not positive--force. The Sullivan Principles are all the more impressive because of their voluntary nature....We also believe that the South African government would consider mandated principles an extraterritorial application of U.S. law."

A prohibition on new South African investment, according to GM, "would make it impossible for us to remain competitive. If we can't be competitive, we would not be able to provide new jobs, as we did this year and last" as well as providing other social and economic assistance to non-whites in South Africa.<sup>25</sup> Complains Mobil's Marzullo, "The danger of that legislation is that it is punitive. There's a lot involved here. In the long run they're hurting the people they want to help."<sup>26</sup> Atlanta Mayor Andrew Young, in fact, several years ago warned that South African blacks would suffer most from reduced economic activity of U.S. firms.<sup>27</sup>

Analyzing labor provisions of the Solarz bill, Senator Orrin Hatch, the Utah Republican, concludes, "Five of the codified Sullivan Principles are inconsistent with Federal labor law," as they dramatically exceed domestic standards for U.S. companies.<sup>28</sup>

Title III to the Export Administration Act, of which Solarz-Gray would be part, currently awaits action from a House-Senate conference committee. The Senate version of EAA contains no South Africa language. To keep such language out of the bill's final version, the State Department has begun twisting arms to recruit more signatories for the voluntary Sullivan Principles. Said Secretary of State George Shultz to a group of corporate executives this March: "Ladies and gentlemen, we must face the

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<sup>22</sup> Hearings before the House Subcommittee on Africa, September 24, 1981.

<sup>23</sup> From a joint statement, March 19, 1981.

<sup>24</sup> New York Times, November 6, 1983.

<sup>25</sup> From a 1981 statement.

<sup>26</sup> From an interview August 7, 1984.

<sup>27</sup> Chicago Tribune, February 6, 1978.

<sup>28</sup> Congressional Record, February 29, 1984, p. S1932.

fact that we are dealing with perception as well as reality.... Many Americans believe some form of governmental action is required to address the issue of apartheid and to punish South Africa. They seek to suspend a normal economic relationship, cut off investments and credits, embargo South African gold coins, block non-sensitive nuclear trade, and force American companies to accept modified Sullivan principles....I strongly urge those companies that have not adopted the principles, as for example those basically defined by the Sullivan code, to do so without delay."<sup>29</sup> Yet since the 1983 Sullivan Report, only five new companies have become signatories.

#### FUTURE OF THE SULLIVAN PRINCIPLES

Complaining of the probable consequences of Solarz-Gray, Sullivan Industry Support Unit Chairman Marzullo says, "If you start imposing bureaucratic control over this thing, you're going to ruin it."<sup>30</sup> But the damage may already have been done. Annual paperwork for reporting signatories has mushroomed. Much of the voluntary spirit of the endeavor has been lost. The prime mover, Leon Sullivan, has not only disparaged voluntarism, but the morality of the free enterprise system. Warned Secretary Shultz, "No outside power can or should try to impose its vision on South Africa."<sup>31</sup> While the South African government remains officially neutral with regard to the Principles, it has done nothing to stop their implementation by American businesses or their subsidiaries.

Meanwhile, signatories and non-signatories alike await promised reforms slated for the ninth questionnaire in 1985, among them the intention to make the procedure less cumbersome and bureaucratic, more representative and fair. Above all, the Principles again should be completely voluntary--free of the implicit coercion of recent years. Much is at stake. Says Gatsha Buthelezi, chief minister of the black national state of Kwa Zulu: "Some...in America have got the whole issue exactly upside down. They seem to think it is immoral for American companies to invest here but irresistably profitable. The truth is the opposite. It is morally imperative that American firms remain active here."<sup>32</sup>

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<sup>29</sup> From a speech at Blair House, March 29, 1984.

<sup>30</sup> From an interview August 7, 1984.

<sup>31</sup> From a speech at Blair House, March 29, 1984.

<sup>32</sup> Congressional Record, October 27, 1983, p. H8753.

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