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THE CORPORATION AS MEDIATING INSTITUTION: AN EFFICACIOUS SYNTHESIS OF STAKEHOLDER THEORY AND CORPORATE CONSTITUENCY STATUTES*

Timothy L. Fort**

I. INTRODUCTION

A. *The Stakeholder/Constituency Debate*

No approach has been more prominent in contemporary business ethics than stakeholder theory. Led by the work of Edward Freeman, the theory has successfully played off the typical focus on corporate duties to "shareholders" to identify duties toward employees, suppliers, local communities, and perhaps many others besides.¹ More than half the states have enacted statutory forms of stakeholder theory known as "corporate constituency statutes."² These statutes,

* Copyright 1997 by Timothy L. Fort. All Rights Reserved. An earlier, but substantially similar, version of this paper was named "Outstanding Proceedings Paper" at the Annual Meeting of the Academy for Legal Studies in Business held in Quebec City, August, 1996.

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1 William M. Evan & R. Edward Freeman, *A Stakeholder Theory of the Modern Corporation: Kantian Capitalism*, in *ETHICAL THEORY & BUSINESS* 97, 101-105 (Tom L. Beauchamp & Norman E. Bowie eds., 3d ed. 1988). The authors specifically leave open the notion that the potential list of stakeholders could be quite broad.

2 See ARIZ. REV. STAT. ANN. § 10-2702 (West 1996); FLA. STAT. ANN. § 607.0830 (West 1993); GA. CODE ANN. § 14-2-830 (1994); HAW. REV. STAT. § 415-35(b) (1993); IDAHO CODE § 30-1702 (1996); 805 ILL. COMP. STAT. ANN. 5/8.85 (West 1993); IND. CODE ANN. § 23-1-35-1 (Michie 1995); IOWA CODE ANN. § 491.101B (West 1991); KY. REV. STAT. ANN. § 271B12-210(4) (Banks-Baldwin 1996); LA. REV. STAT. ANN. § 12:92(G) (West 1994); ME. REV. STAT. ANN. tit. 13-A, § 716 (West 1996); MASS. GEN. LAWS ANN. ch. 156B, § 65 (West 1996); MINN. STAT. ANN. § 302A.251(5) (West Supp. 1993); MISS. CODE ANN. § 79-4-8.30(d) (1996); MO. ANN. STAT. § 351.347 (West 1991); NEB. REV. STAT. § 21-2035(1)(c) (1991); N.J. STAT. ANN. § 14A:6.1 (West Supp. 1997); N.M. STAT. ANN. § 53-11-35(D) (Michie 1997); N.Y. BUS. CORP. LAW § 717(b) (McKin-

like stakeholder theory itself, are open-ended in two ways. First, they generally allow, but do not require, managers to take into account nonshareholder constituents in making corporate decisions. Second, it is unclear exactly what weight managers ought to give to the interests of various nonshareholders in the corporation.³

In addition to these philosophical ambiguities, the debate surrounding "corporate constituency statutes" has shed more heat than light on who is entitled to what:

It is surprising that in light of the significant amount of literature on constituency statutes, commentators have offered few specific answers to these questions [of how statutes should be interpreted and what principles ought to be used]. Instead, corresponding to the rhetorical temperature of the discussion, interpretations of the statutes have tended toward extremes.⁴

B. Business as Mediating Institution: A First Look

In this Article, I wish to suggest that criticisms of stakeholder theory do not fatally wound it when the corporation is viewed as a mediating institution.⁵ As a mediating institution, duties primarily flow to the internal members of the corporation. When corporate responsibilities are arranged so there is a mandatory requirement for management to be accountable to internal members of the corporation, such as shareholders and employees, but not legally accountable to external constituents, such as suppliers, the environment, and the host community, the corporation can do what it does best. Primarily, corporations should owe duties to internal constituents. Duties to external constituents are important, and specific legislation will be necessary to prevent corporate abuse of, for instance, the environment. Management may also find that "good business" dictates "good ethics" in how customers, suppliers, and host communities are treated. But as a matter of corporate governance, businesses ought to be mediating institutions.

ney Supp. 1997); OHIO REV. CODE ANN. § 1701.59(E) (Anderson 1992); OR. REV. STAT. § 60.357 (Supp. 1996); 15 PA. CONS. STAT. §§ 1715-1716 (1995); R.I. GEN. LAWS § 7-5.2-8 (1992); S.D. CODIFIED LAWS § 47-33-4 (Michie 1991); TENN. CODE ANN. § 48-103-204 (1995); WIS. STAT. ANN. § 180.0827 (West 1992); WYO. STAT. ANN. § 17-16-830(e) (Michie 1997).

3 See Timothy L. Fort, *Corporate Constituency Statutes: A Dialectical Interpretation*, 15 J.L. & COM. 257 (1995).

4 Eric W. Orts, *Beyond Shareholders: Interpreting Corporate Constituency Statutes*, 61 GEO. WASH. L. REV. 14, 71 (1992).

5 For the remainder of this paper, I use "stakeholder theory" and "corporate constituency statutes" interchangeably.

What is a mediating institution? According to a recent article, mediating institutions are communities which socialize their members.⁶ "Mediating" between the individual and society as a whole, they provide a community. They require individuals to grasp their responsibilities to others, at least within their group, so that a person's very identity is developed.⁷ Mediating institutions teach individuals that they are not autonomous beings accountable only to their own wants and desires. Instead, a series of relationships comprise personhood and therefore human beings obtain their identity by becoming accountable for their relationships.⁸ In short, mediating institutions teach us that we are relational, not autonomous beings. Because we are relational beings, our very "self" is dependent upon ethical responsibilities.⁹ In mediating institutions, we develop bonds of affection that motivate individuals to treat others well. Writing in a popular vein, Tom Chappell explains this educational process and relates it to business:

In the family, we learn love, patience, respect, nurturing, affirmation, and health. The family also teaches us about competition, domination, selfishness, and deceit. The family is thus a relatively efficient learning system for the development of mind, spirit, and body. . . . Substitute the word company for family . . . and you get an idea of what I envision a company to include. In my experience, employees will run through walls for a company that understands them, gives them some freedom, encourages their creativity, appreciates their work, and rewards it fairly. Treat an employee like a cog in a machine, and you'll get a cog's work. Treat that same person as a member of your family, and you'll get loyalty.¹⁰

6 Timothy L. Fort, *Business as Mediating Institution*, 6 BUS. ETHICS Q. 149 (1996).

7 See *id.* at 152.

8 In this regard, Business as Mediating Institutions theory is much like that of some contemporary feminist theories. The feminist version of stakeholder theory, in fact, develops this notion and will be described in Section II. I have definite affinities with some parts of feminist thought, and it may well be that a mediating institutions theory can be assisted by an integration of the two. That focus on relationality is not the source for mediating institutions in this paper nor in the sources cited in this paper, so that integration will not be done here.

9 For an even more sweeping statement of our relational sense, see ERROL E. HARRIS, *FORMAL, TRANSCENDENTAL & DIALECTICAL THINKING: LOGIC AND REALITY* (1987). Harris argues that the entire physical, biological, and even logical structure of the world is "dialectical" (Harris' philosophical term for what is essentially relationality). Thus, it is not simply that human beings are relational, but the entire physical and philosophical world is a series of complex interrelationships.

10 TOM CHAPPELL, *THE SOUL OF A BUSINESS: MANAGING FOR PROFIT AND THE COMMON GOOD* 61-62 (1993).

Although the process is traditionally associated with institutions such as family, church, and the local community,¹¹ businesses ought to be mediating institutions as well. That is, businesses ought to recognize that the very identities of those working in them are developed by work in the institution. When one realizes that relationships with others comprise one's identity, then one has a richer notion of responsibility. While one must be careful not to conflate mediating institutions like family with business, corporations can benefit from modeling at least some of its structure according to a mediating model.

A manager who "sees" that her person is affected by just relations with employees learns to inculcate responsibility just as a parent's identity is developed by being responsible for a child who has (at least sometimes) less power. Managers learn that their "selves" are tied up with those who are lower on the corporate hierarchy. In a dialectical sense, employees who have more power may also be more likely to empathize with the needs of managers.

Although a bit oversimplified, the connection between organizations structured as mediating institutions and ethics can be described as follows:

A company committed to ethics as well as profit needs to affirm that knowledge of ethics . . . comes not from a course in organizational behavior in a business school (or from a "business ethics" course) but from the bonds formed in the family, the church, the schools, the neighborhood, and self-help groups. As persons, we are in a web of beliefs, traditions, and religious and cultural values.¹²

Why should businesses be mediating institutions? In addition to the notion that they generally promote affections leading to ethical treatment of others, there are several other reasons as well. By being a mediating institution, the importance of the individual person is emphasized.¹³ Businesses accept the responsibility for the cost of its "takeover" of leisure time otherwise devoted to traditional mediating institutions.¹⁴ One creates a model for multicultural understanding through the assemblage of diverse workers within a single commu-

11 See Fort, *supra* note 6, at 156.

12 CHAPPELL, *supra* note 10, at 71.

13 See Fort, *supra* note 6, at 155-57.

14 See *id.* (noting JULIE B. SCHOR, *THE OVERWORKED AMERICAN: THE UNEXPECTED DECLINE OF LEISURE* (1991)) (Schor argues that contrary to expectations that technology leads to leisure, it leads to more time for workers working. Thus, capitalism has led to less time for family and other mediating institutions.).

nity.¹⁵ Individuals learn responsibilities as well as claiming rights.¹⁶ Contemporary management techniques such as Total Quality Management demonstrate the efficacy of participation of individuals towards a collective good.¹⁷ Such an organization raises the "stakes" of its members by more closely connecting individual and organizational ends¹⁸ so that ethics is not a separate activity of business, but a constitutive element of every day business life.¹⁹ Through these structures, the bonds of affections make ethics habitual.²⁰

While there will be a good deal of debate about whether constituents such as part-time employees are "internal" or "external," there ought to be a heightened ability for shareholders and employees to control the firm and, more particularly for employees, their work product. Other duties to external constituents (such as the welfare of a host community) may be represented by the concerns of employees themselves who are members of both the corporate and geographical community. The corporation ought to be structured so as to require both shareholders and employees to have significant control of the organization in which they work.

C. *Methodology of the Article*

This Article is neither descriptive nor interpretative. Rather than delineating the differences between the various state constituency statutes, or detailing the differences between the variations of stakeholder theory (except in brief), or analyzing the ways courts have interpreted the statutes, the Article argues that corporations ought to be operated for the primary benefit of all internal constituents. The Article leaves open the question of whether fiduciary duties or employee representation on the board is the better mechanism for actualizing the mediating organization. I do use employee participation in this Article for purposes of brevity (and because I suspect that I will eventually come

15 See *id.* (noting RONALD TAKAKI, *A DIFFERENT MIRROR: A HISTORY OF MULTICULTURAL AMERICA* (1993)) (Takaki argues that as diverse as Americans are, their common meeting ground has always been work. It is "on the job" that we become more multiculturally integrated.).

16 See *id.* It is one (important) thing to learn that everyone has certain rights. It is another to realize that those rights are not the totality of identity. If it were, a rights position would suggest that we are autonomous beings that should be left alone. If it is not, then in addition to rights, we understand our responsibilities in this complex web of relationality.

17 See *id.*

18 See Fort, *supra* note 3, at 284-85.

19 See Fort, *supra* note 6, at 159.

20 See *id.* (noting CHAPPELL, *supra* note 10, at 71).

down in favor of this mechanism instead of relying upon fiduciary duties). The Article is therefore normative. Other duties may be derivative of those mandatory duties or may be expressed in other specific legislation.

To make this argument, the Article makes the following moves: First, it briefly describes corporate constituency statutes and the debate concerning them. Next the debate is enriched by attempting an understanding of the normative positions taken in the debate concerning stakeholder theory. Finally, it proposes the concept of Business as Mediating Institution (also called Mediating Institutions approach) that provides a limited model of stakeholder management, but one grounded in prudential and normative rationales so as to make stakeholder theory a workable model for business ethics and corporate governance.

II. CORPORATE CONSTITUENCY STATUTES

A. *What They Are and Why They Were Enacted*

Corporate Constituency Statutes have been enacted in over half the states²¹ and have generated significant academic commentary.²² They are, however, only the latest round in a very old debate. While tracing their origin to the charter amendments of the 1970s²³ and to the opposition of the corporate takeovers of the 1980s,²⁴ the debate is probably best known in the Berle-Dodd debates of the 1930s.²⁵ In fact, the notion of what the corporation is has changed throughout American history so that it extends into history even further:

Over the past two hundred years, the prevailing conception of the nature and purpose of the corporation and, thus, of the nature of

21 See note 2.

22 In addition to other material cited in this paper, see, for example, Walter M. Cabot, *The Free Market Promotes Long-Term Efficiency That Benefits All Stakeholders*, 21 STETSON L. REV. 245 (1991); Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579 (1992); Edward D. Rodgers, *Striking the Wrong Balance: Constituency Statutes and Corporate Governance*, 21 PEPP. L. REV. 777 (1994); David A. Ruder, *Public Obligations of Private Corporations*, 114 U. PA. L. REV. 209 (1965); Steven M.H. Wallman, *The Proper Interpretation of Corporate Constituency Statutes and Formulation of Director Duties*, 21 STETSON L. REV. 163 (1991); Gary von Stange, *Corporate Social Responsibility Through Constituency Statutes: Legend or Lie?*, 11 HOFSTRA LAB. L.J. 461 (1994).

23 See Orts, *supra* note 4, at 20.

24 See *id.* at 23-26.

25 See A.A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931); E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees*, 45 HARV. L. REV. 1145 (1932).

the duties owed by corporate directors has changed dramatically. The notion that the directors' primary duty is to act on behalf of the interests of the share-holders—the putative “owners” of the corporation—represents but one approach. Over time, the law developed alternatives to this approach.²⁶

The judicial source for this malleability is Chief Justice John Marshall's *Dartmouth College* opinion in which he ruled that a corporation is an artificial creation of the state and thus subject to whatever duties the state imposes upon it.²⁷ This reason, along with other more philosophical rationales, prompts business ethicist John Boatright to declare that “except for the useful role they play in corporate governance, there is nothing special about shareholders.”²⁸ We, or at least a legislature, can alter corporate duties; they are not immutable laws of nature.²⁹

When the duties of corporations are viewed in the light of a public policy struggle,³⁰ the stage is set for the fierce polemic of politics, a fact that explains Eric Orts' conclusion that commentators have tended toward extremism.³¹ I do not wish to join that battle, but to suggest that there is a moderate (mediating) position that has prudential and moral advantages.

The rationale for the statutes is simply that corporate actions affect and have always affected (often significantly) nonshareholders. Whether the corporate decision is “downsizing” or discharging toxic waste, nonshareholders feel the impacts of this artificial creation of the state. In the wake of the takeovers of the past decades, those non-shareholder constituents have sought protection from their legisla-

26 Thomas J. Bamonte, *The Meaning of the “Corporate Constituency” Provision of the Illinois Business Corporation Act*, 27 LOY. U. CHI. L.J. 1, 14 (1995) (footnote omitted).

27 The seminal portion of Marshall's opinion reads:

A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly, or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created.

Trustees of Dartmouth College v. Woodward, 17 U.S. 518, 636, 4 Wheat. 250, 303 (1819).

28 John Boatright, *What's So Special About Shareholders?*, 4 BUS. ETHICS Q. 393, 405 (1994).

29 This is not to suggest, however, that there may not be recurring problems in business or recurring values in business that do take on the character of immutability. It simply acknowledges that we are culturally able to specify the particular things that corporations ought to do in our specific society.

30 See Boatright, *supra* note 28. Boatright concludes that there is no moral superiority of extending duties solely to shareholders. Instead, it is a matter of public policy.

31 Orts, *supra* note 4, at 71.

tures.³² Given the pain corporate decisions can cause in human lives and in communities, and given the legal precedent for the malleability of corporate duties, what could be wrong with requiring corporations to take into account the impact of their actions on nonshareholder constituents? One can summarize four key reasons.

B. *Four Problems with the Statutes*

1. Too Many Masters

First, when one requires a corporation to take into account all the stakeholders affected by an action, one creates "too many masters" for management.³³ That is, having many bosses makes it difficult for management to effectively and fairly manage the firm. This could happen in two ways.

One way is that the statutes will allow managers to play constituencies against one another, thereby enhancing managerial discretion.³⁴ The second way is that multiple constituents, if actually powerful, could create corporate gridlock, allowing nothing to get done.³⁵ Either result does little to protect those that the statutes are presumably designed to protect. If either result is true, the statutes could even make things worse.

Is this criticism valid? Jonathan Macey argues that it is overstated.³⁶ Macey argues that managers typically have to deal with many conflicting goals and masters.³⁷ Balancing multiple forces, such as shareholders, bondholders, and other creditors, does not necessarily overburden management.

While this may be true, any organization's ability to respond to multiple demands is finite. Corporations may be able to process demands of some additional constituents, such as employees, but can they process the demands of community organizations, suppliers, cus-

32 See *id.* at 24. Orts argues that Rustbelt states such as Pennsylvania, Ohio, Wisconsin, Indiana, Minnesota, and Illinois were among the leaders in passing constituency statutes. (citing John C. Coffee, Jr., *The Uncertain Case for Takeover Reform: An Essay on Stockholders, Stakeholders and Bust-ups*, 1988 WIS. L. REV. 435, 436).

33 See, e.g., ROBERT CLARK, CORPORATE LAW § 1.2.4, at 21-22 (1986).

34 See Katherine Van Wezel Stone, *Employees as Stakeholders Under State Nonshareholder Constituency Statutes*, 21 STETSON L. REV. 45, 54-55, 70-71 (1991).

35 See, e.g., James J. Hanks, Jr., *Playing with Fire: Nonshareholder Constituency Statutes in the 1990s*, 21 STETSON L. REV. 97, 111 (1991).

36 Jonathan K. Macey, *An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties*, 21 STETSON L. REV. 23 (1991).

37 *Id.* at 33.

tomers, governments, and (in the case of environmental matters) constituents who may not be born for years to come?

While I am open to models that can make such a complex integration, it may well be true that if we wish corporations to be productive organizations, there may be limits to the number of constituents they can serve. One reason for a mediating model is that it limits the number of constituents to whom management is accountable; that limitation, however, may be sufficient for management to fulfill such responsibilities.

2. Slippery Slope to Socialism?

If a model can integrate these various constituencies contemplated by the states, is it still a corporation? This leads to the second problem for constituency statutes and the further development of a mediating notion of stakeholder theory. A corporation that fully engages all its affected constituents requires business to be an "unelected governmental entity."³⁸ As F.A. Hayek argued:

So long as the management has the one overriding duty of administering the resources under its control as trustees for the shareholders and for their benefit, its hands are largely tied; and it will have no arbitrary power to benefit this or that particular interest. But once the management of a big enterprise is regarded as not only entitled but even obliged to consider in its decisions whatever is regarded as the public or social interest, or to support good causes and generally to act for the public benefit, it gains indeed an uncontrollable power—a power which could not long be left in the hands of private managers but would inevitably be made the subject of increasing public control.³⁹

Implicit in this criticism is the fear of socialism. If private property of shareholders must be used for purposes other than what they desire, then their money has been, in some sense, confiscated.⁴⁰ Moreover, if corporations do become redistributive vehicles, society is not likely to allow such distribution to take place without giving those constituents a voice. Hayek's "slippery slope" argument states the public is not likely to entrust corporate executives with such power. The logical next step, then, is public control of corporations.

38 See Nell Minow, *Shareholders, Stakeholders, and Boards of Directors*, 21 STETSON L. REV. 197, 219 (1991).

39 3 F. A. HAYEK, *LAW, LEGISLATION, LIBERTY: THE POLITICAL ORDER OF A FREE PEOPLE* 82 (1979).

40 It is for this reason that, although unlikely to be upheld by the courts, a "takings" problem might exist.

As the statutes are currently written, these concerns seem overdrawn. Most statutes simply permit, but do not mandate, the consideration of nonshareholders. Even if such duties were mandated in part, such as through employee representation on the board of directors, one could argue that the corporation, like a state, becomes more autonomous, not less. That is, there may be less reason for the state to micromanage corporate affairs if the corporation itself is a more just organizational structure. The danger of socialist collectivism is not in making individuals accountable for their actions, but in undermining accountability itself. It may well be true that "too many masters" undermine accountability. But making management accountable to employees can make the corporation more independent from state control.

In limiting attention to employees, external stakeholders remain represented by forces that can have an impact on the corporation.⁴¹ The environment can be protected through a variety of legal mechanisms. Special protection of employees does not eliminate the fact that legal or economic incentives (economic in the sense that there can be good business reasons for being ethical in terms of goodwill and reputation)⁴² may foster corporate responsibility. Moreover, if employees have a say in corporate decisionmaking, then they are likely to consider concerns, such as community welfare, important for corporate action. Indirectly, they also represent the community of which they are a part. The effect on external constituents may not be as great as one might fear. The mediating approach allows for social accountability without socialism.

3. Adjudicatory versus Utilitarian Rationality

A third criticism of the statutes concerns the way in which corporations operate. Joseph Biancalana argues that corporations operate according to a "utilitarian rationality" maximizing preferences as opposed to "adjudicatory rationality" which depends upon normative reasoning.⁴³ Simply put, corporations are not designed to determine justice or fairness. They maximize preferences within the context of normative rules established by others. Because preferences are so fluid, a utilitarian rationality is not able to make normative judgments unless those judgments are imposed, such as in the traditional legal

41 See Macey, *supra* note 36, at 41-44.

42 "Market forces provide the strongest restraints on the discretion of corporate directors." Bamonte, *supra* note 26, at 17.

43 Joseph Biancalana, *Defining the Proper Corporate Constituency: Asking the Wrong Question*, 59 U. CIN. L. REV. 425, 429-30 (1990).

doctrine of *ultra vires* actions.⁴⁴ Without such specificity, vague notions of "fairness" supply no criteria for regulating corporate actions, and actually undermine notions of fiduciary duty.⁴⁵

This criticism, of course, begs the question of how corporations actually do operate. Are they economic preference maximizers or something else? For purposes of this argument, let us assume that they are preference maximizers. While Biancalana identifies one way to set limits to this utilitarianism—through specific legal constraints—the other way is to broaden the preferences that are maximized. This is exactly what stakeholder theory does. It expands relevant preferences. The problem with utilitarianism is the problem of determining whose preferences are, in fact, being maximized and at whose expense. For what "number" is a "greatest good" being sought? Corporate constituency statutes suggest that one must ask nonshareholders this question.

It is, however, practically impossible to ask all of one's suppliers or representatives of future generations (regarding environmental issues). But it is not so difficult to consult internal members of the organization. A mediating approach thus broadens the concern of a preference maximizing entity without making stakeholder theory impractical.

4. Do the Statutes Make a Difference?

Finally, William Carney has argued that corporate constituency statutes will not make a difference in a corporation's decision because an "enlightened board" will have already factored in the best interests of all parties.⁴⁶ This may well be true, but it begs the question of whether a board is enlightened. The fact that many boards are not enlightened suggests that they need a framework which will require them to become enlightened. In interpreting Illinois' corporate constituency statutes, for instance, Thomas Bamonte writes that the legislature was not convinced that boards were already enlightened. Thus directors needed direction toward the correct scope of their duties:

Illinois law already allowed directors to consider nonshareholder interests using a long-term perspective within a framework in which the directors are to serve "the best interests of the corporation and the stockholders." Thus, if all section 8.85 did was to codify the existing common law rules, it was hardly necessary. . . .

⁴⁴ See *id.* at 434–36.

⁴⁵ See *id.*

⁴⁶ William J. Carney, *Does Defining Constituencies Matter?*, 59 U. CIN. L. REV. 385 (1990).

Section 8.85 does, in fact, do more. . . . [It] establishes that the director's primary fiduciary duty is to the corporate entity. This, in turn, reduces the status of shareholders to a position of one among a set of corporate constituents. . . .

. . . The most popular formulation in Illinois case law, however, suggested that directors and officers owe a fiduciary duty to the corporation *and* to the shareholders.⁴⁷

If a board is already "enlightened," then the statutes should pose no particular burden on it. Such boards will continue to operate as they always have. If such boards are not "enlightened," then the statutes require them to become enlightened.

C. *Corporate Constituency Statutes: A Summary*

There are important truths to these criticisms of the statutes. They may create too many masters. Corporations may become unelected and unaccountable public bodies. The statutes may confuse the very ways in which corporations work. But a limited notion that requires managers to take into account internal constituents—shareholders and employees—dramatically simplifies these concerns. Business as Mediating Institution, which looks primarily to internal constituents, may allow corporate constituency statutes to avoid these typical critiques while significantly expanding the responsibilities of management.

In addition to the benefits of avoiding these criticisms, there are positive, normative reasons for the mediating institution approach. These can be better addressed within the context of the business ethics debate regarding stakeholder theory.

III. STAKEHOLDER THEORY

A. *The Theory and its Development*

As with the statutes, stakeholder theory argues that the corporation ought to be managed for the benefit of all affected by corporate actions, not simply the shareholders. The origins of the theory lay in a Kantian principle that all human beings should be treated as ends, not as means to ends.⁴⁸ This was extended to what is known as the stakeholder theory of the firm in which managers owe fiduciary duties to stakeholders as well as shareholders.⁴⁹

47 Bamonte, *supra* note 26, at 9–10 (quoting *Shlensky v. Wrigley*, 237 N.E.2d 776, 780 (Ill. App. Ct. 1968)) (footnotes omitted).

48 See Evan & Freeman, *supra* note 1, at 101–05.

49 See *id.*

Evan and Freeman summarize their theory first in terms of the "Principle of Corporate Legitimacy," in which the corporation should be managed for the benefit of all its stakeholders and that those stakeholders (customers, suppliers, owners, employees, and local communities) ought to participate in the decisions that substantially affect them.⁵⁰ Second, the "Stakeholder Fiduciary Principle" places a fiduciary duty on management toward the stakeholders of the corporation as an entity in safeguarding the long-term stakes of each constituent group.⁵¹

Who comprises the stakeholder group? Drawing on the previously mentioned Berle-Dodd debate (and demonstrating the linkage between corporate constituency statutes and stakeholder theory), Boatright says that "Dodd's position (and Freeman's, as well) is that the fiduciary duties of management should be extended now to include all other constituents."⁵²

Stakeholder theory has been amended in various ways by those who would retain fiduciary duties toward shareholders and extend important, but non-fiduciary, duties to other stakeholders.⁵³ Others, as we have seen, argue that there is nothing morally special about shareholders; our imposition of fiduciary duties is a choice of public policy that could just as easily be extended to various other stakeholders.⁵⁴ Recent stakeholder theory has gone beyond the Kantian commitment to persons to embrace a feminist theory of the firm. In this theory, our very "self" is understood as being relationally interconnected with others:

Persons are fundamentally connected with each other in a web of relationships which are themselves integral to any proper understanding of "the self," such that any talk of autonomy or search for personal identity must be qualified and located within this more organic and relational sense of the world. The stakeholder concept, understood in feminist terms, makes explicit how the boundaries of the self extend into areas far beyond what we can easily recognize and into areas clearly "outside" the corporation.⁵⁵

According to this approach, corporations should incorporate a variety of internal and stakeholder concerns. Thus, in responding to

50 See *id.*

51 See *id.*

52 Boatright, *supra* note 28, at 402.

53 See Kenneth E. Goodpaster, *Business Ethics and Stakeholder Analysis*, 1 BUS. ETHICS Q. 53 (1991).

54 See generally Boatright, *supra* note 28.

55 Andrew C. Wicks et al., *A Feminist Reinterpretation of the Stakeholder Concept*, 4 BUS. ETHICS Q. 459, 483 (1994).

the question of what managers should do, Wicks, Freeman, and Gilbert argue that "[w]e advocate that managers drop the quest for objectivity and embrace the quest for solidarity and communicatively shared understandings."⁵⁶

This feminist reinterpretation is subject to the same difficulties of "too many masters" and the other criticisms of the previous section. But it makes a significant advance in understanding the communal notion of the self. Human selfhood is not simply autonomous, if it is at all, but is stitched together through interaction with others in a community.⁵⁷

The question is, to what extent the self can cognitively embrace the myriad sets of relationships that comprise it. Beyond the notion of "bounded rationality,"⁵⁸ which suggests cognitive limitations in our ability to process such information, this is a question that I must in large part defer to psychologists. Nevertheless, there is a clue to our cognitive abilities to be relational beings when we examine our evolution. As Charles Taylor writes, contrary to the contemporary context in which "identity" is gained through the exchanges one makes in an anonymous market, "[i]n premodern times, people didn't speak of 'identity' . . . —not because people didn't have (what we call) identities, . . . but rather because these were then too unproblematic to be thematized as such."⁵⁹

While the evolutionary element will be addressed further in the naturalist critique of stakeholder theory, it is worth asking what it is about contemporary life that makes the anonymous market unable to create a mechanism for persons to achieve identity. Why do non-shareholder constituents have a claim to a greater role in corporate governance? These questions can be answered in a more systematic critique of stakeholder theory.

B. Four Critiques of Stakeholder Theory

1. The Agency Critique

The most direct critique of stakeholder theory comes from agency theory and is utilized in defense of a free market approach that directs fiduciary duties only toward shareholders. According to this theory, agents have moral duties to carry out the instructions of

⁵⁶ *Id.* at 490.

⁵⁷ See Fort, *supra* note 6, at 265–70.

⁵⁸ See generally 1 HERBERT A. SIMON, *MODELS OF BOUNDED RATIONALITY: ECONOMIC ANALYSIS AND PUBLIC POLICY* (1982).

⁵⁹ CHARLES TAYLOR, *MULTICULTURALISM AND "THE POLITICS OF RECOGNITION"* 35 (1992).

their principals. Anyone is free to establish a corporation and those who decide to take such a risk (shareholders) ought to have their instructions carried out by agents who have decided not to take the risk of investing in a business. Thus, according to Ian Maitland, corporations do not violate stakeholders' rights to self-determination, but are the result of stakeholders who choose to form or invest in a corporation rather than choosing to do something else.⁶⁰ If nonshareholders want to become shareholders, they can do so. If they do not, then they can choose to carry out the mandates of those who have become shareholders.

Rejecting the stakeholder position that current corporate structure defeats individual stakeholders' rights to self-determination, Maitland argues:

[W]hat on its face is a disagreement about the ethics of the internal constitutional arrangements of corporations is really an empirical disagreement about the efficacy of the competitive marketplace at protecting the right of stakeholders to self-determination. Both sides endorse the principle of self-determination—but they disagree about whether the corporation respects that principle.⁶¹

Thus, one argument against stakeholder theory is that it ignores the free choices that were made to establish corporations. Moreover, an agency approach does not harm self-determination according to Maitland, but as an empirical matter, better protects it.

As an empirical matter, Maitland offers evidence that employee-run firms and cooperatives do not seem to possess competitive advantages when, if it is true that participatory management is a preferable way of organizing corporations, it should. "Employee participation in firm governance should elicit greater commitment and work effort, so cooperative firms should have a competitive advantage over their hierarchical rivals But despite their supposed attractiveness to employees, such firms have repeatedly failed."⁶²

There are two difficulties with this argument. First, although Maitland also acknowledges that employees may be willing to sacrifice efficiency in a tradeoff to obtain governance input,⁶³ he leaves the criteria for determining how well employee-run companies protect rights to self-determination in terms of economic, competitive advantages. Of course, there is a truth to this position: without competitive

60 Ian Maitland, *The Morality of the Corporation: An Empirical or Normative Disagreement?*, 4 BUS. ETHICS Q. 445, 455 (1994).

61 *Id.*

62 *Id.* at 453.

63 *Id.*

advantages, there may not be a business organization in which anyone will have rights to self-determination. But to more accurately determine if such structures do better protect self-determination, one would need to evaluate other criteria supplied by those who work for the firm. Employees, for instance, may not make competitive advantages a high priority. This may make the companies less profitable, but better places to work.

The second and more important point is that the determination to become an investor does not prescribe the totality of duties that result from such a decision. Deciding to become an investor is an important decision, the risk of which ought to be compensated (for instance in the form of capital growth). But a person may not have capital to invest and thus may not be able to choose. Even if an individual has made such a choice, the principal-agency relationship remains a relationship. As a relationship, one must at least hear the concerns of the other party in the relationship. Neither a principal alone nor a law can hear. Thus, Cohen is right to argue that:

The process of making a decision about what is to the advantage of a group or what advances *that group's* welfare should often (usually) involve considering *that group's* opinion. There are at least two reasons for this, the first (and maybe also the second) of which was advocated by John Stuart Mill. (1) That group is usually particularly well-placed to evaluate what is and what is not in its own interest. By itself, this concern has nothing to do with respect for agent-autonomy. (2) In many matters involving some decision procedure, there is no single exclusively rational decision. There can be a number of possibilities.⁶⁴

An example of the complexity of stakeholder voice and self-determination can be seen in another institution that can be a mediating organization: the military. When a soldier joins the military, there are clear rules he must follow. Even if one has voluntarily joined (as opposed to having been conscripted), there are very specific roles a soldier must carry out. As such, her position is very much like an agent/employee who has decided to join a corporation rather than set up her own company.

Being in such an organization, however, neither allows the agent/soldier to comply exclusively with the orders of superiors nor does it allow superiors to ignore the welfare of the soldiers. The Nuremberg Trials demonstrated that soldiers have a duty to question some orders of their superiors. The ancient Chinese general Sun-Tzu

64 Stephen Cohen, *Stakeholders and Consent*, BUS. & PROF. ETHICS J., Spring 1995, at 3, 13 (footnote omitted).

argued that a primary responsibility of a general is to treat soldiers with warmth and beneficence.⁶⁵ If an organization as hierarchical as the military requires "stakeholder" input, responsibility, and concern, then corporations ought to at least allow employees to have a voice in corporate governance.

There is no doubt that competition and contracting can protect many nonshareholder interests, as agency theory would suggest. But with less than twenty percent of the American workforce unionized,⁶⁶ this strength of contract may not be what it once was. In retirement years, employees are particularly vulnerable.⁶⁷ Traditional contracting and competition mechanisms may not be sufficient to give employees the voice that accurately reflects their "stake" in the organization.

Moreover, recent downsizing activities, such as AT&T's, may have evolved into a different form had employees had a greater voice. This is not to argue that workers cannot be fired, but it is to argue that employee participation is necessary for proper protection in today's economy.

In short, while Maitland may have a point that agency theory protects the right to self-determination, it only does so incompletely. Empirical evidence even shows that there may be advantages to including more employee control of the firm.⁶⁸

2. The Social Contract Critique

For Thomas Donaldson and Thomas Dunfee, stakeholder theory suffers from two problems. First, it does not consider the community standards in describing an account of business ethics, and second, it does not have any normative foundation to determine who counts as stakeholders and what weight ought to be given to particular stakeholders.⁶⁹ At least in part because of these weaknesses, Donaldson and Dunfee offer their Integrative Social Contracts Theory (ISCT),

65 SUN-TZU, *THE ART OF WAR* (Samuel B. Griffith trans., Oxford Univ. Press 1963). In the fourth paragraph of Sun-Tzu's work, he writes that leaders must have moral influence so that people are in harmony with their leaders. *Id.* at 64.

66 See Van Wezel Stone, *supra* note 34, at 54.

67 See *id.* at 49-51.

68 See, e.g., W. EDWARDS DEMING, *OUT OF THE CRISIS* 83-85 (1986); CHARLES HAMPDEN-TURNER, *CREATING CORPORATE CULTURE: FROM DISCORD TO HARMONY* 58-59 (1990).

69 See generally Thomas Donaldson & Thomas W. Dunfee, *Toward a Unified Conception of Business Ethics: Integrative Social Contracts Theory*, 19 *ACAD. MGMT. REV.* 252 (1994).

which attempts to specify weights and duties according to extant social contracts constrained by universal hypernorms.⁷⁰

Where do contracting relations take place? All over, of course, but in particular, the specification of rights and duties occurs within a community. In mediating institutions such as families, churches, and voluntary organizations, individuals learn the impact of their actions, and learn to internalize their responsibilities.⁷¹ Through community interaction, one learns to contract with others.

For instance, a person who wants to volunteer for her church's soup kitchen does not thereby become a minister in charge of the entire church. Instead, she learns the duties of a role specified through ongoing contracts between the church and the leaders of the soup kitchen, between the leaders of the kitchen and the volunteers, between volunteers and the recipients of the food, and a myriad of other agreements. Those contracts develop the character of the participants. In short, community life requires ongoing contracts between the various stakeholders of the institution. Mediating institutions require social contracting.

Ultimately, in fact, one learns to contract with one's self while internalizing the responsibilities one has to other members of the community. In negotiating what activities are acceptable and unacceptable, an individual gradually, although not inevitably, develops a character which internally regulates one's behavior. That is, one develops a conscience.⁷²

ISCT attempts to provide a specificity in terms of what duties ought to have more weight. In a mediating institution's framework, one's community—including a corporation—takes priority. Whatever the relationship may be among various external stakeholders, the internal stakeholders are a community.⁷³ The place where one is most likely to learn ethical duties toward others is, first, in one's community. The place where business is likely to develop ethical behavior is also internal.

⁷⁰ *Id.*

⁷¹ See generally RICHARD JOHN NEUHAUS, *DOING WELL & DOING GOOD: THE CHALLENGE TO THE CHRISTIAN CAPITALIST* (1992).

⁷² It may also be true that conscience is an inherent aspect of human nature. I would support that view in fact. But it is also at least in part the result of the internalization of the results of having been "caught" by others in a community. A child who is disciplined for hitting a sibling, for instance, may eventually internalize the notion that she should not hit her brother, regardless of whether or not she could get away with it.

⁷³ See EDWIN M. HARTMAN, *ORGANIZATIONAL ETHICS AND THE GOOD LIFE* (1996); ROBERT SOLMON, *ETHICS AND EXCELLENCE* (1992).

A common way of describing this today is as "corporate culture."⁷⁴ A company's culture can hold it together in the midst of turmoils such as decentralization, de-layering, and downsizing.⁷⁵ To be sure, individual companies have much different cultures; they are not identical.⁷⁶ Different as they may be, however, a corporate culture is important to the individuals who comprise it because a sense of community matters to people:

Culture, in a word, is community. It is an outcome of how people relate to one another. Communities exist at work just as they do outside the commercial arena. Like families, villages, schools, and clubs, businesses rest on patterns of social interaction that sustain them over time or are their undoing. They are built on shared interests and mutual obligations and thrive on cooperation and friendships.⁷⁷

At the heart of Donaldson and Dunfee's respect for community is an understanding of human nature which becomes particularly potent in an emerging naturalist approach to business ethics.

3. Naturalist Critique

In his recent book, *Values, Nature, and Culture in the American Corporation*, William Frederick somewhat whimsically summarizes contemporary business ethics in the formula: $EBB = f(R_k + J_r + U)$ where EBB stands for Ethical Business Behavior.⁷⁸ In this "Philosophers' Formula," ethical business is a function of Kantian rights (R_k), Rawlsian justice (J_r), and utilitarianism (U).⁷⁹ While the characterization has limits, it does roughly characterize the field. Most business ethics theories do not simply address one of these elements but emphasize certain elements within the formula.

Methodologically, Frederick uses the natural world of biology and physics as a resource for moral reflection. By experiencing the natural world, we reflect on it and better understand certain values that exist in all nature, including human beings who are part of nature.⁸⁰ These values include economizing, ecologizing, and power-aggrandiz-

74 See Rob Goffee & Gareth Jones, *What Holds the Modern Company Together?*, HARV. BUS. REV., Nov.-Dec. 1996, at 133.

75 See *id.*

76 See *id.* at 133-34.

77 *Id.* at 134.

78 WILLIAM C. FREDERICK, *VALUES, NATURE, AND CULTURE IN THE AMERICAN CORPORATION* 251 (1995).

79 *Id.*

80 See generally FREDERICK, *supra* note 78.

ing.⁸¹ Most ethicists concern themselves with ecologizing (community-building) values. But in addition to a broader conception of ecology, Frederick also stresses the natural importance of "economizing," the conversion of resources into materials that sustain our very lives.⁸² By recognizing economizing as a natural value, Frederick elevates its importance. This makes a big difference to his understanding of justice.

Frederick argues that justice within a naturalist context is not about decisions concerning distribution of particular goods. Instead, justice is about the ability of stakeholders to participate in the coordination of economic enterprise.⁸³ This approach recognizes the inherent and legitimate economizing drives of all stakeholders. It focuses on their involvement in an organizational process rather than a delineation of status according to which distributive processes flow.⁸⁴ Thus, rather than focusing on a Rawlsian theory of distributive justice that imposes duties on those well-off, Frederick concentrates on legitimizing the economizing participation of all members of nature. This at least suggests the legitimacy of a greater participation of employees in the decisions that affect them.

Frederick notes that his endorsement of the value of utility is the area of biggest disagreement between himself and other ethicists.⁸⁵ With economizing values central to survival in a naturalist theory, the utility of corporate actions is not only something to put up with, but the very justification for business. Without it, there would be no reason for us to have business. It provides "the vital link between business economizing and technologizing and the humanly vital needs and satisfactions pursued by the members of the society."⁸⁶ By endorsing utility and expanding it to include all persons by virtue of its "naturalness," Frederick expands the preferences that a corporation must maximize.⁸⁷

It is worth taking Frederick's naturalism further. Some in evolutionary psychology contend that human beings are not significantly different from what our ancestors were like in the days in which we lived in hunter-gatherer societies. As diverse as those societies may

81 *Id.* at 9.

82 *Id.* at 42-43.

83 *Id.* at 259-60.

84 *Id.* at 260-61.

85 *Id.* at 261.

86 *Id.* at 262.

87 *See id.* at 8.

have been, they were small groups.⁸⁸ For instance, hunting societies were larger than one or two families, but they remained small.⁸⁹ Perhaps human beings need small groups in order to learn responsibilities and duties rather than learning them through large anonymous organizations such as the market or the legal system.

More specifically, some have demonstrated a relationship between the size of the human brain and the optimal size of groups to which an individual can belong and process understandings of one's place in the relationships of the group. Psychologist Robin Dunbar found:

a correlation between the dimensions of the neocortex—the part of the brain engaged in conscious thought—and the size of different groupings of mammals. . . .

In humans, Dunbar found, the size of the neocortex predicts [optimal populations of] groups of about 150 people. This number happens to conform to the approximate membership of the clan within hunter-gatherer societies; the company unit within the military; and the aggregate of employees within a business that can be managed without an elaborate bureaucracy. The figure of 150, Dunbar writes, represents the maximum number of individuals with whom “we can have a genuinely social relationship, the kind of relationship that goes with knowing who they are and how they relate to us.”⁹⁰

Dunbar further noted the work of anthropologists in the last century who have found that hunter-gatherer societies did not simply live in small groups, but that their groups were related to larger social organizations. Thus, “overnight camps” of thirty to thirty-five people (comprising five or six families) collaborate with other such groups for hunting and foraging and ultimately belong to tribes of 1500 to 2000 people.⁹¹ This matrix ties together the already noted findings of Jaynes and Turnbull to suggest that individuals find their identity best in small organizations which can be linked to larger units.

Is this, however, a good idea? Anthropologist Lawrence Keeley has studied the degree of violence in these small hunter-gatherer com-

88 See ROBERT WRIGHT, *THE MORAL ANIMAL: EVOLUTIONARY PSYCHOLOGY AND EVERYDAY LIFE* 38 (1994).

89 See COLIN M. TURNBULL, *THE FOREST PEOPLE: A STUDY OF THE PYGMIES OF THE CONGO* 37 (1962); see also JULIAN JAYNES, *THE ORIGIN OF CONSCIOUSNESS IN THE BREAKDOWN OF THE BICAMERAL MIND* 129 (1976) (estimating the optimal number in such groups to be approximately thirty).

90 Gary Stix, *Different Strokes*, *SCI. AM.*, Nov. 1996, at 36 (reviewing Robin Dunbar's *GROOMING, GOSSIP, AND THE EVOLUTION OF LANGUAGE* (1996)).

91 ROBIN DUNBAR, *GROOMING, GOSSIP, AND THE EVOLUTION OF LANGUAGE* 70 (1996).

munities and has found the rate of deaths in warfare to be twenty times higher than during the (what we call a bloody) twentieth century.⁹² Clearly, the fostering of small groups in order to obtain a sense of moral identity has to be circumscribed or else one's moral identity can be gained through unacceptable behavior. Nevertheless, when James Wilson finds that children in rural, economically simple communities with strong kinship ties are more willing to help and comfort others—not only within their group, but outside the group as well⁹³—one can see that finding a place for small communities in order to encourage moral development is not a bad idea either.

Speaking in the business context, perhaps we best learn our moral responsibilities in small, mediating institutions in which there are face-to-face consequences of our actions rather than in large, abstract structures which are bound by rules that may seem to have little to do with the everyday life of the individual person affected by them.⁹⁴ Of course, one cannot simply turn back the clock so as to put

92 LAWRENCE H. KEELEY, *WAR BEFORE CIVILIZATION* 93 (1996).

93 JAMES Q. WILSON, *THE MORAL SENSE* 23, 41–42 (1993).

94 See Jacques Ellul, *The Theological Foundation of Law* 11–43 (1960). Ellul makes a complex argument in which he links the legitimacy of law to the ability of persons in the community to spontaneously identify with it.

He argues that in its origin, all law is religious. There is no separation between the lawgiver and the religious leader, such as perhaps a shaman, of the society. Gradually, however, the institutions of law and religion separate. There becomes a space between the religious and governmental institutions, but there is extensive homogeneity among the people so that they “naturally” or spontaneously understand what is right and wrong. Over time, however, scholars emerge who reflect upon the decisions that have been made about right and wrong. These persons develop “principles” and “laws” to encapsulate what previously was a spontaneously lived understanding of right and wrong. The problem with this scholarly distillation is that once articulated, the principles become malleable. In particular, those with money and power employ intelligent interpreters of the principles who interpret according to the interests of the rich and powerful. This causes laws to increasingly become divorced from the spontaneously understood “natural law” to become a set of rules that are understood and manipulated only by the rich and powerful. At that point, law ceases to be legitimate because the common people have no ability to connect with it nor to influence it.

Although Ellul's argument may prove too much, there is a wisdom of tying law's legitimacy to its meaning and to those who are affected by it. Without such a connection, law is indeed unjust and so viewed. A contemporary example of this is in the public's reaction to the Internal Revenue Code which does indeed seem to be a bewildering morass disconnected from the lives of everyday human beings.

In corporate terms, the same dynamic argues for rules and procedures that connect with the lives of stakeholders. While international treaties and accords are important to global business, there also need to be laws within the control of those affected by them if the laws themselves are to retain legitimacy.

human beings into small tribes roaming the countryside. The point is that within our large nation-states and corporations we need to foster the communities, the mediating institutions, in which individuals have some significant control over the rules of their community and learn to internalize moral responsibilities.

While evolutionary psychology is geared toward explaining reproduction,⁹⁵ our genetic similarity with our ancestors suggests that we do need small groups to form our identity and to learn our moral responsibilities. Evidence suggesting that the communication skills of such small groups are almost entirely internal to one's community⁹⁶ suggests that we may be similarly disposed. While this point requires far more consideration and expertise than I am able to provide here, I would like to hypothesize that it is part of our human nature that we need small groups to learn ethical duties. More abstract duties are derivative of these more intimate lessons.

Rather than attempting to grasp our responsibilities to far-flung stakeholder groups, perhaps our corporate responsibilities ought to focus on those things which we are best able to do: develop corporate communities with duties flowing primarily to internal members. This is exactly the position of Business as Mediating Institution.

4. The Mediating Critique

Stakeholder theory incorporates a good deal of the Philosophers' Formula. It attempts to protect Kantian commitments to the individual. It also incorporates utilitarianism. Evan and Freeman broaden the scope of utilitarian analysis to include nonshareholder interests. Evan and Freeman's approach, in other words, still operates under a utilitarian rationality, but it is one based on stakeholder rather than shareholder or managerial interests.

What kinds of needs would be raised by stakeholders? The specific needs, of course, would vary from company to company. But there are certain basic human needs likely to be raised by stakeholders if given the opportunity. Sociologist Robert Nisbet, for instance, has written about the basic human social needs of affection, friendship, prestige, and recognition.⁹⁷ These kinds of cooperative goods have been traditionally met by mediating institutions such as families, churches, and guilds,⁹⁸ and in non-industrial societies within small

95 See WRIGHT, *supra* note 88.

96 See J. BRONOWSKI, *THE ASCENT OF MAN* 45 (1973).

97 ROBERT A. NISBET, *THE QUEST FOR COMMUNITY: A STUDY IN THE ETHICS OF ORDER AND FREEDOM* 50 (2d ed. 1990).

98 *Id.* at 237.

groups such as hunting groups.⁹⁹ Modern psychologists have documented the non-economic needs of individuals in the workplace as well.¹⁰⁰

These associational needs, primarily and best met in small, mediating institutions are consistent with the Kantian approach taken in stakeholder theory. The point is that corporations ought to be managed so that individuals are treated as "ends" instead of as "means." A mediating institutions approach, however, does question the extent to which large organizations can meet associational needs unless the organization is structured in such a way so that sub-units of the organizations are themselves capable of meeting associational needs. A mediating institutions approach would also question the extent of duties one has. Rather than a set of open-ended duties to all stakeholders affected by corporate action, it would place primary duties on meeting the associational needs of internal constituents such as employees and shareholders.¹⁰¹

IV. BUSINESS AS MEDIATING INSTITUTION

A. *Mediating Institutions*

To this point, I have argued that mediating institutions are communities in which individuals have direct contact with others. They witness the impact of one's actions on others. They provide a person with a sense of identity and probably a common purpose.¹⁰² Duties are primarily directed toward internal constituents, an aspect which can lead, it must be admitted, to problematic tribalism.

I do not wish to specify too precisely what mediating institutions must look like structurally. Different communities, churches, and families structure themselves in quite different ways. Just as Donaldson and Dunfee propose "moral free space"¹⁰³ for communities to develop norms appropriate for themselves, so Business as Mediating Institution proposes likewise.

99 See, e.g., JAYNES, *supra* note 89, at 129; TURNBULL, *supra* note 89, at 37; WRIGHT, *supra* note 88, at 38-39.

100 See, e.g., FREDERICK HERZBERG, *WORK AND THE NATURE OF MAN* (1966); DAVID C. MCCLELLAND & DAVID G. WINTER, *MOTIVATING ECONOMIC ACHIEVEMENT* (1971); CHARLES R. WALKER & ROBERT H. GUEST, *THE MAN ON THE ASSEMBLY LINE* (1952).

101 See generally Fort, *supra* note 3.

102 A traditional mediating institution, such as a church, has a common purpose for its members. Voluntary organizations do also and, insofar as childrearing and family affection is concerned, so do families. Corporations may also have a common purpose of economic viability, if not profitability.

103 Donaldson & Dunfee, *supra* note 69, at 259-60.

There are central elements, however, that apply to all mediating institutions. Perhaps these are the same or closely related to Donaldson and Dunfee's "hypernorms."¹⁰⁴ I do not wish to tackle that extensive question here, but I do wish to suggest at least one such norm: participation.

As natural law theorist John Finnis writes, "one who is never more than a cog in big wheels turned by others is denied participation in one important aspect of human well-being."¹⁰⁵ This "natural law" combined with Frederick's naturalist recognition that we are all entitled to our economizing drives and the further naturalist notion that we are best able to direct our moral duties toward internal members suggests that Business as Mediating Institution may be a workable conception of stakeholder theory. It also suggests that the right to participate in the decisions affecting one's life is a basic natural law that ought to apply to corporations. In particular, it recognizes all constituents who are members of a business community and stresses their right to participate, particularly in the day-to-day work that will have the most impact on a person. However, it keeps the number of constituents at a more manageable level than full-blown stakeholder responsibility.

B. Justifying Business as Mediating Institution

1. Justification Through Business Ethics Convergence

Business as Mediating Institution represents a convergence of contemporary business ethics theories. It draws upon a limited notion

104 *Id.* at 265-66.

105 JOHN FINNIS, *NATURAL LAW AND NATURAL RIGHTS* 147 (1980). Finnis goes on to write:

It is therefore a fundamental aspect of general justice that common enterprises should be regarded, and practically conducted, not as ends in themselves but as means of assistance, as ways of helping individuals to "help themselves" or, more precisely, to constitute themselves. And in all those fields of activity, including economic activity, where individuals, or families, or other relatively small groups, can help themselves by their own private efforts and initiatives without thereby injuring (either by act or omission) the common good, they are entitled to justice to be allowed to do so, and it is unjust to require them to sacrifice their private initiative by demanding that they participate instead in a public enterprise; it remains unjust even if the material dividend they receive from the public enterprise is as great as or even somewhat greater than the material product of their own private efforts would have been. The principle of subsidiarity [which includes participation] is a principle of justice.

Id. at 169.

of stakeholder theory. Like social contract theory and virtue theory,¹⁰⁶ it recognizes the importance of community determination of proper behavior and the community's role at inculcating moral identity. It draws upon a human nature that requires small groups in order to develop that identity and to stress the importance of participation. There are other convergences worth noting that substantiate the validity of viewing businesses as mediating institutions.¹⁰⁷

2. Justification Through Religion, Nature, and Philosophy

When one looks at world religions, sociology, and philosophy, one can see a repeated emphasis on duty toward those with whom one is closest. Japanese and Aristotelian notions are worth noting.

Aristotle notes concentric circles of duties first to oneself, then to one's friends and family, then to fellow citizens, and then to all other human beings.¹⁰⁸ Iwao Taka has written of similar notions in Japanese ethics.¹⁰⁹

While a great deal of ink could be spilled analyzing these notions, it is important to recognize that human beings intuitively tend to think, for the most part, that our duties to our families, for instance, supersede our duties to our fellow citizens. Given the previously noted findings of anthropologists and psychologists, this should not surprise us. While the approach of Business as Mediating Institution should not give a license to ignore any responsibility to those outside of the firm, a corporation is more likely to find that moral behavior can be accomplished by considering the needs of internal constituents.

3. Justification Through Management Theory

The understandable fear of any broadening of corporate duties is that doing so undermines the role corporations play in society which is to efficiently produce goods and services for consumers. Raising the notion of duties to any stakeholder can trigger a reaction like those seen in Part II.

There is a significant stream of managerial theory, however, indicating that a mediating institutions approach is efficacious. Total Quality Management (TQM) is based on carefully understanding and

106 See, e.g., Solomon, *supra* note 73.

107 See generally Timothy L. Fort, *Goldilocks and Business Ethics: A Paradigm that Fits "Just Right"*, 23 J. CORP. L. (forthcoming Jan. 1998).

108 See JEFFREY WATTLES, *THE GOLDEN RULE* (1996).

109 Iwao Taka, *Business Ethics: A Japanese View*, 4 BUS. ETHICS Q. 53 (1994).

meeting the needs of customers.¹¹⁰ But in the midst of the sophisticated statistical processes necessary to assure that products and services will be free of defects,¹¹¹ an important notion of TQM is to recognize that a co-worker is a customer whose needs must be met.¹¹² When the workplace becomes one in which there is a shared concern for individual fulfillment and empowerment, which is what mediating institutions do,¹¹³ it produces pride, meaningful work, and a reduction of sloppiness. This is why W. Edwards Deming wrote:

He [the worker] will feel important to the job if he can take pride in his work and may have a part in the improvement of the system. Absenteeism and mobility of the work force are largely the result of poor supervision and poor management. . . . The possibility of pride or workmanship means more to the production worker than gymnasiums, tennis courts, and recreation areas.¹¹⁴

Other popular, contemporary theories such as "Open-Book Management"¹¹⁵ offer similar notions, but the theme of empowered workers championed by Business as Mediating Institution is not the same as a full-fledged workplace democracy. Gary Hamel and C.K. Prahalad, probably the most influential management strategists today, argue that while "bureaucracy can strangle initiative and progress, so too can a large number of empowered but unaligned individuals who are working at cross-purposes."¹¹⁶ Instead, they argue that employees also want a sense of direction set by management, a notion of what they call "strategic intent."¹¹⁷ So too, Business as Mediating Institution does not call for worker plebiscites in order to operate a company. It does, however, call for corporations to recognize that they are communities and that in communities interpersonal relationships are important. Because they are important, so are ethical duties, because relationships are sustained by ethical rules and principles. Creating such organizations, however, is not only possible, but has already

110 See MARY WALTON, *THE DEMING MANAGEMENT METHOD* (1986).

111 See JOHN S. OAKLAND, *TOTAL QUALITY MANAGEMENT* (1989), for a good example of the individual steps and statistical processes necessary to establish a TQM system.

112 See *id.* at 29-42, 145.

113 See PETER BERGER & RICHARD JOHN NEUHAUS, *TO EMPOWER PEOPLE: THE ROLE OF MEDIATING STRUCTURES IN PUBLIC POLICY* 7 (1977).

114 DEMING, *supra* note 68, at 83-85.

115 See JOHN CASE, *OPEN-BOOK MANAGEMENT: THE COMING BUSINESS REVOLUTION* (1995).

116 GARY HAMEL & C.K. PRAHALAD, *COMPETING FOR THE FUTURE* 290 (1994).

117 *Id.* at 129.

been done. Business as Mediating Institution is a way to build on those successes on a wider scale.

C. A Proposal for Implementation

In many ways, the notion that we should place less weight on important ethical issues such as the environment or the relationship between a host community's well-being and the corporation seems troublesome. I do not wish to deny that such responsibilities are important, nor to suggest that they not be addressed. It also can be argued that by focusing our duties on what our nature predisposes us toward (internal members) I fall prey to the so-called "naturalistic fallacy" because I confuse "what is" with "what ought to be." Moreover, if all human beings are important, why draw the line at internal members? To take a biblical example, do we not risk being on the wrong side of the story of the Good Samaritan?

To briefly and preemptively respond to such possible criticisms, it is important to note that the mediating institutions position does not claim to offer a complete solution to ethical dilemmas in business. The mediating approach is essentially a theory of the firm proposing a new model of corporate governance. Even in this regard, such a theory has many additional questions to answer, but for the purpose of normative thought, the approach does not argue that businesses should not be "Good Samaritans," but that we will never learn to be "Good Samaritans" until we learn that we are responsible for others. Learning that lesson is hard to do if one has not been socialized to see it. This is exactly what mediating institutions do.

Relatedly, noting that we may be naturally adapted (or designed) to look first to members of our communities is not to confuse "what is" and "what ought to be," but to note that we will never understand "what ought to be" if we demand duties beyond our ability to absorb. Simply making corporations into mediating institutions would dramatically change the way they operate. It might be worth working out the kinds of mediating approaches before trying the more complex work of full-blown stakeholder theory.

A mediating institutions approach requires that individuals have the opportunity to participate in the decisions affecting their lives. This is a central theme of stakeholder theory as well. In practice, it is impossible in all but the smallest of organizations for individual employees and shareholders to have such a role, which is why agency theory is a necessary theoretical component of stakeholder management. But a mediating institutions approach suggests two levels of participatory control in corporate decisions.

First, there ought to be employee representation on the board of directors in some form. I leave open the question of what the best form would be. It could follow a German model of employee representation on a board overseeing the work of a board of directors or it could follow the lines of an employee-owned company in which employees have direct representation on the board itself.¹¹⁸ The point is that there ought to be a voice of internal, nonshareholder stakeholders on the board.

Second, employees ought to have the ability to be a part of the processes of the work in which they are engaged. It is through this kind of work that identity is formed and individuals learn that they are members of a community with both rights and responsibilities. Contemporary management models, such as TQM, provide a ready storehouse of the economic efficacy of such an approach. Thus, even if employees do not control the firm, they ought to be able to have a say in how work they do is performed.

The first recommendation is statutory. The second is not. Both are necessary, but it is hard to see how a statute could be drafted so as to require specific levels of participation in the work employees do. While I would certainly be open to suggestions of how that might be done, it does not seem to me that law can successfully mandate the second approach. It becomes one of managerial and moral integration.

IV. CONCLUSION

Corporations that are structured as mediating institutions owe primary duties to internal constituents. Those include shareholders and employees. Because of the difficulties in articulating a voice other than that on the board, it is important for employees to have some kind of representation on the board itself. Moreover, if a corporation is a community—that is, a mediating institution in which individuals learn both rights and responsibilities—particular work must be structured so as to provide some type of effective meaning.¹¹⁹ While board representation may be statutory, work details are not.

118 See Edward B. Rock, *America's Shifting Fascination with Comparative Corporate Governance*, 74 WASH. U. L.Q. 367 (1996), for a good review of German and other comparative corporate governance models.

119 See Timothy L. Fort, *The Spirituality of Solidarity and Total Quality Management*, 14 BUS. & PROF. ETHICS J. 12 (1995), in which I argue that TQM's efficacy is based on an affective connection between the person and her work that is similar to the solidarity that is prominent in Roman Catholic Social Thought.

The rationale for this approach is that it takes advantage of the valuable aspects of stakeholder theory, manifested legal by corporate constituency statutes, as well as other business ethics theories. It does not, however, ask of corporations more than they are capable of doing. By proposing a "mediating" position between full-blown stakeholder theory and traditional shareholder responsibility, corporations may be able to be more like communities in which moral identity as well as economic efficiency is fostered.

I do not wish to suggest that this theory is complete. There are many other questions that require attention. For instance, one important question is determining exactly who is an internal constituent. Is a part-time employee an internal constituent or is that person more in the realm of an independent contractor?

A second question is what other elements are necessary for an organization to be one in which individuals find meaning and identity. In addition to the psychological issues inherent in this question, there is also a role for issues such as dispute resolution. Do mediating institutions need mediation structures within them to be a community that resolves its own disputes?

A third question, or set of questions, concerns corporate governance. One encounters a host of questions as to what this model would mean in terms of election of directors and their responsibilities, mechanisms for complaints, and liability issues.

A fourth question extends the second one by asking how self-standing institutions avoid tribalism.¹²⁰ While mediating structures provide identity, they also have a darker side. How does one provide for some kind of a "corporate federalism" so as to allow "moral free space" to corporations that do not violate basic standards of conduct? This is a question that has a significant opportunity for integration with Donaldson and Dunfee's work, particularly on hypernorms.¹²¹

What about the sources relied upon in this article? While I would contend there is great promise in seriously incorporating naturalist findings into moral theory, there is danger in confusing "what is" with "what ought to be." Thus, there is justificatory work to be done in

120 See, e.g., W. Jethro Brown, *The Personality of the Corporation and the State*, 21 LAW Q. REV. 365, 368 (1905). Brown wrote that people act differently in groups than they do individually so that "[u]nder the inspiration of *esprit de corps*, the humane will give a cruel decision, the cruel a humane." This is a potential problem requiring serious attention.

121 Although I have not seen formal work making the connection between traditional theories of natural law and hypernorms in business ethics, this strikes me as a worthy integration to make.

order to more fully ground the legitimacy of this source as it relates to ethical and legal conduct of business.

Extending this idea further, how does a mediating institutions paradigm help us in global business? It may well be that it does not help us at all in questions such as environment because the corporate focus is primarily internal (although internal members may well have an interest in the environment that they can voice with board representation). If mediating institutions do not help with this, it suggests that they are helpful in business ethics in some ways, but that they must be supplemented in other ways as well. My hunch is that they require supplementation—I do not think that Business as Mediating Institution is a “silver bullet.” I do conclude, however, that structuring corporations as mediating institutions provides a mechanism for institutionalizing ethical behavior in business in a way that has pragmatic and moral desirability.

IN MEMORIAM
JOHN J. BRODERICK



The Broderick legend is made of stern stuff. His dramatic, ebullient personality is fed by deep springs. He lives an intense spiritual life. With what Aquinas called magnanimity, he manages to make it seem easy to give abundantly.*

* From a faculty resolution upon Professor Broderick's retirement, 50 NOTRE DAME LAW. 569 (1975).