

What's a Company For?

A Problem in Business Ethics

(or ... when Socrates met Milton Friedman)

Alexander Pepper



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About the author

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Preface

To study a corporation may be economics, or sociology, or law; to study its activities as resulting from the purposes of persons or as affecting the welfare of persons, and to judge its acts as good or bad from such a point of view, is ethics.¹

In an article published in *Harvard Business Review* in 2002, the venerable management scholar Charles Handy asked ‘What’s a business for?’² Handy, perhaps the greatest public intellectual among management academics – who sadly died while this book was being written – was often ahead of the times, most notably in the way that he anticipated the business process outsourcing phenomenon long before it became a standard part of the corporate play-book. The question about corporate purpose posed by Handy in 2002 has now become one of the current topics in business and management journals.

In 2002 I was a partner working for PricewaterhouseCoopers (PwC). Had you asked me ‘what’s a business for?’ I would probably have given the then standard answer ‘to create value for shareholders.’ I had heard of Charles Handy of course – my wife, then a management consultant with Coopers & Lybrand, had encouraged me to read *Understanding Organisations* in the late 1980s when she realised that I didn’t know what a stakeholder was – I previously had what might now be described as a rather financialised understanding of corporations. I became a fan of Handy and proceeded to read all his new books as they were published, from *The Age of Unreason* onwards. Perhaps I sensed some common ground as the son of the manse and an arts graduate who had ended up working in business. Perhaps I also tried, in a small way, to emulate him when I left PwC in the summer before my fiftieth birthday to become a Fellow at The London School of Economics and Political Science.

I arrived at LSE in 2008 after a prior career in accounting, tax, and human resource consulting with Coopers & Lybrand and PwC, latterly as global head of the human resource services consulting practice, a billion dollar by revenue business. Academically speaking, I had a bachelor’s degree in philosophy and English, a master’s degree in organisational change, and a partially complete doctorate in business administration. I had become an accountant partly by accident and partly as an act of rebellion. The careers officer at Durham University told me that he was aware of only one job outside academia for a professional philosopher and suggested that, with my degree in English and philosophy, I might instead consider becoming a teacher. I come from a family of preachers

and teachers. My father was a Methodist minister. My three sisters all trained as teachers, and two of them married teachers. One of my brothers-in-law, the one who was not a teacher (he was a solicitor), said that when I decided to study English and philosophy rather than economics, I was destined to become a teacher as well. In my last year at university, I thought about becoming a lawyer, but couldn't afford to go to law school, so I became an accountant instead. Hence my characterisation of this as an act of rebellion. However, my mother pointed out that my grandfather had been a City of London chartered accountant, so that my choice was hardly revolutionary. Eventually, of course, I did become a teacher when I went to LSE to teach master's students in the Department of Management. So perhaps it was my destiny after all.

One of the things I discovered early on at LSE is that academia is full of tribes (the full meaning of which I learnt from one of my new colleagues who was an anthropologist). I shouldn't really have been surprised I suppose, as I knew that organisations are full of silos, which *Financial Times* editor-at-large Gillian Tett, who has a PhD in anthropology, has explained are essentially the same thing.³ Tribalism seemed particularly true in management, which is, after all, a second-order discipline that draws on a number of first-order disciplines, notably economics, psychology, and sociology.

And so I had something of an identity crisis – with my heterodox background (someone once described me, rather unkindly I thought, as a 'prac-ademic' – I prefer 'professor of practice', or even 'clinical professor' as those of my particular tribe are sometimes called in the US). Who was I, what was I, and where did I fit in? Was I, as one of my friends from outside academia suggested (drawing a parallel with the relationship between Anglican priests and Methodist ministers), part of a 'tolerated anomaly' when it comes to academic tribes.

One of the specific problems I faced was where to publish my research work on my own special subject – executive compensation. My first article on senior executive pay was accepted by a human resources management journal. My second, a theory paper, was published in the *Journal of Management*, a general management journal, but they were not interested in the follow-up empirical paper, which I had to find another home for. Then I was invited by the American Psychology Association to write an article about my research for a psychology journal. I was also quite keen to publish in an economics journal, as there is extensive literature in economics on executive pay, but I'm not an economist and this proved to be a step too far. After a number of rejections, I eventually had an article published in an economic sociology journal. My most recent paper was rejected by an institutional economics journal (there are tribes within tribes in economics), a sociology journal (the one that had published my earlier article), and a political economy journal, before finally being accepted for publication by the journal *Business History*. However, it was when I did some research work with Dr Susanne Burri, a moral philosopher, in response to the spiralling inflation in executive pay that I dusted off my early training in philosophy. I wrote a book, *Agency Theory and Executive Pay*, which touched on the question of whether companies have ethical

responsibilities and moral agency. A further book, *If You're So Ethical Why Are You So Highly Paid?*, drawing on my research work with Susanne and Daniela Lup, a management scholar who trained as a sociologist, examined top pay and inequality from an ethical perspective. (A small aside here on academic tribalism – one reviewer, presumably a philosopher, recommended against publication, saying it couldn't be a philosophy book because it contained empirical work – fortunately LSE Press chose to think differently.)

Having discovered a new tribe, business ethicists, and in the belief that management students should all have some compulsory training in moral philosophy, I developed a course for the general management MSc programme, which I directed at LSE. It was this course, *Ethics, Governance, and Leadership*, which caused me to look again at the work of Charles Handy, in particular the question 'what's a business for?'

This is a book about large companies. I recognise that not all business is conducted through companies, and not all companies conduct business, but for the purposes of this book I shall treat the two as one and the same. I generally reserve the term 'corporations', predominately an Americanism equivalent to the English word 'companies', for companies (or, if you prefer, corporations) that are very large. I might have called the book *The Purpose of the Corporation*, but *What's a Company for?* seems more interesting.

There are, of course, many other types of companies, including start-ups, family companies, mutuals, public benefit corporations,⁴ social enterprise companies, and so on. This kind of diversity in corporate ecology is a strength.⁵ Ontologically (the philosophical study of the nature of existence, reality, being and becoming), these types of companies are different from both corporations and each other, so that an economic or philosophical analysis of them would identify many very distinct issues along with some common ground. In this book I focus on large companies with independent shareholders where there are diverse shareholdings and separation of ownership and control, sometimes known as 'modern corporations' or 'Berle–Means corporations'.⁶ I do so because Berle–Means corporations have been a dominant part of the UK and US economies for over 100 years. They have played a critically important role in raising and investing the very large amounts of capital that have fuelled enormous economic growth since the beginning of the 20th century and, at least for now, continue to be a major source of capital.

At around the time I was developing my new course at LSE, the American Business Roundtable, an association of the chief executive officers of major US corporations, voted to redefine the purpose of the corporation to 'promote an economy that serves all Americans'. Since 1978, the Business Roundtable have periodically issued a set of principles of corporate governance, and for at least 20 years have endorsed the principle of shareholder primacy – that corporations exist with the primary purposes of maximising value for shareholders. The new statement published in August 2019 instead affirmed 'the essential role corporations can play in improving our society when CEOs are truly committed to meeting the needs of all stakeholders'.⁷

The debate about corporate purpose is not confined to the US. In the UK, Professor Colin Mayer of Saïd Business School, Oxford University, has led a major research and engagement programme examining the purpose of business and its role in society at the British Academy, the national academy for the humanities and social sciences. Mayer proposes a new definition of the purpose of business – ‘to profitably solve the problems of people and planet, and not profit from creating problems.’⁸

As I reflected on the question of corporate purpose, I came across a letter in the *Financial Times*, published in June 2020, which caused me to buy a copy of Plato’s *Gorgias* and to learn that the question of occupational purpose dates back to ancient times.⁹ In the *Gorgias*, Plato’s interlocutor Socrates debates the purpose of rhetoric with three Rhetoricians, the Ancient Greek equivalent of advertising executives.¹⁰ Reading Plato led me to imagine a dialogue between Socrates and Milton Friedman, the American economist who perhaps more than anyone else has come to represent the shareholder primacy worldview. I thought that the discussion might have gone something like the dialogue between Socrates and Milton Friedman in first published in the online magazine *Board Agenda*.¹¹

This book has evolved into a continuation of the Socrates–Milton Friedman dialogue, along with a monograph based on the work I carried out preparing my course *Ethics, Governance, and Leadership*. Sandwiching the two together is not merely intended as a literary device – I believe that the ancient form of philosophical dialogue, made famous by Socrates and Plato, and the modern form of academic enquiry found, for example, in the social sciences, complement each other, and the juxtaposition has helped me to develop my thinking.

In September 2022, just before I retired from my full-time position at LSE, I hosted a conference at LSE on ‘The Purpose of the Corporation’, with attendees drawn from business, academia, the professions, and the media. The conference began with a play based on the first Socrates and Milton Friedman dialogue, performed by actors from RADA Business, the business arm of the Royal Academy of Dramatic Art.

One of Charles Handy’s early books, *Gods of Management*, uses Greek mythology to explore different styles of management and business culture. I would like to think that he would approve of the Socrates–Milton dialogue as a way of exploring the question about business which he posed in 2002.

Positioning

One of the questions raised while this book was being peer-reviewed was how precisely was it located in the context of different perspectives on business and management education? To answer this question, consider three possible positions.

Position 1. Business management teaching and research, which is predominantly rooted in neoclassical economics, takes shareholder

value maximisation as a given objective, and approaches teaching and learning with that goal in mind – let's call this 'the traditional business school position'.

Position 2. A critique of the traditional business school position that has its origins in a paper published in 2005 by eminent London Business School Professor Sumantra Ghosha entitled 'Bad Management Theories Are Destroying Good Management Practices'.¹² It argues that mainstream management theories, especially those inspired by economics, have had a damaging impact on actual business practices.

Position 3. A critique known as 'critical management studies', which is an approach within management and organisational studies that challenges the assumptions, practices, and ideologies of mainstream management theory and practice. It is rooted in Marxist critical theory and draws from disciplines such as sociology, political science, continental philosophy, and cultural studies.

This book, almost by definition if you think about it, is firmly located in Position 2, given that it draws heavily on philosophical thinking and argues in Chapters 5 and 6 for an approach to business that moves beyond the economic paradigm, embraces moral philosophy and human behaviour, and encourages managers to act as positive agents of change. For the avoidance of any doubt, this does not mean that the economic way of thinking does not have an important place in business and management education. Of course it does! But it is just one of a number of relevant disciplines, not the entire intellectual framework. This is, I believe, precisely what Sumantra Ghoshal was arguing for in his paper – business and management studies should be regarded as one of the liberal arts.

While I accept that there is merit in some aspects of Position 3, critical management studies, especially when it comes to questions about workplace alienation (very relevant, for example, to contemporary ideas about the future of work) and alternative ways of organising (such as workplace democracy and cooperatives), nevertheless, I'm afraid, I'm not a particular fan. Papers written in the critical management studies tradition are often highly abstract or overly negative, offering critiques without clear alternatives. Focusing too much on critical theory risks alienating managers and management students alike. The critical management studies tradition has little real-world impact and debates are largely confined to academic circles, which I shall leave for others to explore.

How to read this book

This book is by design an academic monograph interspersed with an imaginary dialogue between Socrates and Milton Friedman. The dialogue is intended to lead into the more conventional academic content. You could, if you wanted

to, just read the dialogue, which would (I hope) be quite fun, but might leave some gaps in your understanding. Alternatively, if you prefer, you could just read the chapters containing the monograph. These are self-contained and should make sense, but you might not find them as engaging. Or you could read both the monograph and the dialogue, which is really what is intended and should be most instructive. So I hope that that is what you will do.

Socratic dialogue, made famous in written form by Plato, has an illustrious history as a method of philosophical enquiry. The characters in Plato's dialogues are real historical figures, and the fictional views attributed to them largely consistent with what we know of their beliefs, even if the chronological gap in the Socrates–Milton Friedman dialogue between the actual chronology of the life of Socrates and the life of Milton Friedman is not something that you will find in Plato.

The objective of a Socratic dialogue as a method of inquiry is twofold: first, to tease out the issues involved in answering a particular question; and, secondly, to lead the reader to an answer that is consistent with the views of the writer. The question which the Socrates–Milton Friedman dialogue is designed to address is of course the one set out in the title of this book – what's the purpose of a company? But to add some further colour to this, more specifically we might ask – do companies have ethical or merely economic responsibilities? More prosaically we might ask – is the only job of a company's directors and managers to make as much money as possible for shareholders, and to do this in the short term, or do they have obligations to employees, other stakeholders, and society as a whole in both the short term and the long term? More contentiously, given that some of the most vociferous advocates of shareholder primacy are also deniers of anthropogenic climate change, do companies and institutional investors have any responsibility for the environment?

The objective of this book is to explore these questions in a thoughtful way, drawing on ideas from moral philosophy generally, business ethics specifically, economics, economic sociology, management, and related academic disciplines. As you might imagine, I have my own personal perspective on the various questions, which I will attempt to lead you towards in the final chapters. In the end, though, I would rather you disagree with my conclusion, provided that you have reflected deeply on the topic and have robust reasons for doing so, rather than blindly accepting my position.

And finally ...

A note on pronouns (specifically 'I' and 'we'): I was taught to write academic texts in the passive voice – 'this book proposes ...', 'this paper concludes ...', *etc.* But these days this feels increasingly heavy-handed. Therefore, in this book you will find both 'I' and 'we'. 'I' needs no further explanation. However, for the avoidance of doubt, when I use 'we' I do so not in the sense of the 'royal we', but in the sense of 'us', you and me, the author and the reader, who are undertaking this inquiry together. Philosophy at its best is a collaborative exercise.

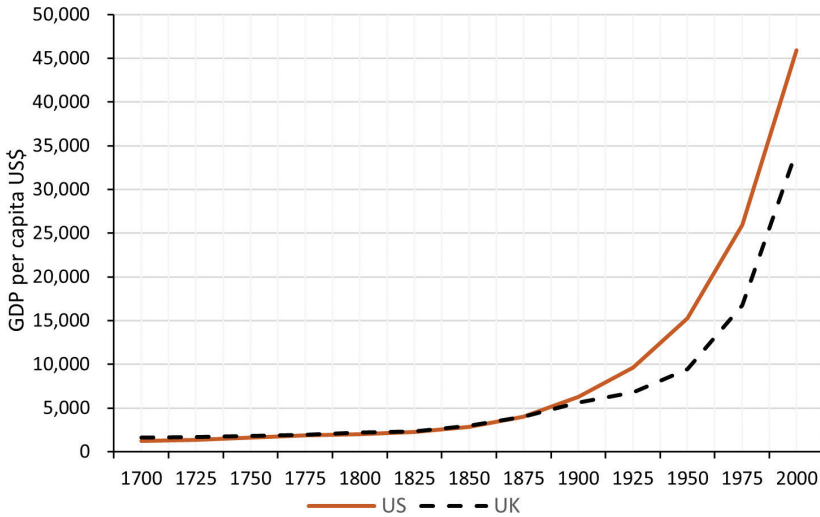
1. Introduction

This chapter introduces the question which this book seeks to answer, explains what is meant by business ethics, and briefly recounts the history of Western ethical thinking as background to what follows in the rest of the book.

In this book I address a critical question in business ethics, ‘what’s a company for?’ Famously, or perhaps notoriously, depending on your standpoint, the American economist Milton Friedman’s answer to this question is widely thought to have been – ‘the social responsibility of business is to increase its profits’ – except that this was not exactly what he said, as we will discover. My focus is on corporations, especially Berle–Means public companies where ownership is separate from control. The directors and managers of such corporations owe particular responsibilities to their shareholders, but also, I shall argue, to others who make specific investments in the firm, including, most importantly, the company’s employees. They also have moral obligations to society in general. Companies have been given certain privileges by governments, most notably the enormous benefit of limited liability. They should not take these privileges for granted, and have obligations to society as a whole as a result.

Capitalism has served the Western world well over the last 200 years. In the year 1700, gross domestic product (GDP) per capita in real terms amounted to around US\$1200 in the US and US\$1600 in the UK.¹³ By 1900, this had risen to around US\$6000 in both countries. In 2000, GDP per capita was nearly US\$46,000 in the US and US\$35,000 in the UK, a phenomenal increase if you think about it (see Figure 1.1).

However, since the start of the Global Financial Crisis in 2008, it has become apparent that the 21st century version of capitalism exhibits certain undesirable features. In 1942, William Beveridge famously identified five ‘giants’ that he saw as deeply destructive to society: idleness, ignorance, disease, squalor, and want. I believe that 21st century capitalism has come to exhibit three ‘monsters’ that are equally destructive: anthropogenic (i.e., man-made) climate change, extreme inequality, and the domination of certain markets by a small number of mega-corporations. While I believe that capitalism has a future and that the standard economic model of the firm (for which see Chapter 2) can be improved upon, this is only possible if an ethical perspective is incorporated into our business models.

Figure 1.1: Gross domestic product (GDP) per capita, 1700–2000

Source: Data from Maddison (2007).¹⁴

The three monsters

Climate change

Anthropogenic climate change is a negative externality, a term used by economists to describe how the production or consumption of a good has harmful consequences when the cost of this is not factored in. Some negative externalities can be addressed by government intervention, but climate change is a global issue that national governments acting alone cannot prevent. Some economists have argued that creating a market for carbon, thus embedding the costs of climate change in all goods and services, might solve the problem, but the world has so far been unable to agree on a price or system for trading carbon.

Extreme inequality

The French economist Thomas Piketty has carefully documented the steady rise in inequality over the seven decades since the end of the Second World War.¹⁵ Economists and philosophers who are ‘sufficientarians’ argue that the political focus should be on eliminating poverty rather than worrying about inequality.¹⁶ The now disgraced Labour peer Peter Mandelson was once quoted as saying that the then New Labour government was ‘intensely relaxed about people getting filthy rich as long as they pay their taxes’, although he later changed his mind

given rising inequality and stagnating middle incomes brought about by some of the downsides of 21st century global capitalism.¹⁷ However, many philosophers and economists over the ages, including Aristotle, Thomas Hobbes, Jean-Jacques Rousseau, Adam Smith, John Stuart Mill, and Karl Marx, have all argued that extreme inequality leads to political discord and eventually to societal breakdown. Poverty and extreme inequality should not be regarded, as sufficientarians think, as wholly disconnected issues.¹⁸

The domination of markets by mega-corporations

The downside of the domination of certain markets by mega-corporations such as Meta (Facebook), Apple, Microsoft, Amazon, and Alphabet (Google) is in one sense straightforward when it comes to conventional economic thinking. According to what is known as ‘the first fundamental theorem of welfare economics’, perfectly competitive markets are Pareto efficient – there is no reallocation of goods and services which will make one person better off without making somebody else worse off. In other words, to oversimplify somewhat, society’s total welfare and the common wealth are maximised when markets are efficient. In contrast, monopolies often lead to price gouging (producers setting high prices at the expense of consumers), a lack of incentive to innovate, a failure to maintain or improve product quality, lack of consumer choice, undue political influence by oligarchs, and ultimately to market failure, which is what happens when distorted market signals lead to an inefficient allocation of resources and a reduced level of overall economic welfare.

I do recognise, however, that a trade-off exists between the downsides of monopolistic competition and the benefits of platform economics, by which I mean the positive externalities and network effects that arise in the case of platforms such as Microsoft, Amazon, Google and Uber, where benefits result as more users sign up to the same platform, increasing economies of scale and convenience for consumers. Platforms can lead to increased general welfare, as long as policymakers and regulators ensure that benefits are shared with consumers as well as producers, anti-competitive behaviour is discouraged, and the value of the platform economies is not captured by a small number of mega-rich people.

Business ethics

This is not a standard text on business ethics. It does not cover, other than peripherally, ethics as it applies to individual consumers, suppliers, or employees, sometimes described by philosophers as ‘micro business ethics’. It deals instead with questions of broad business and social policy, sometimes described as ‘macro business ethics’.¹⁹ The focus is squarely on firms and the actions of their directors and managers.

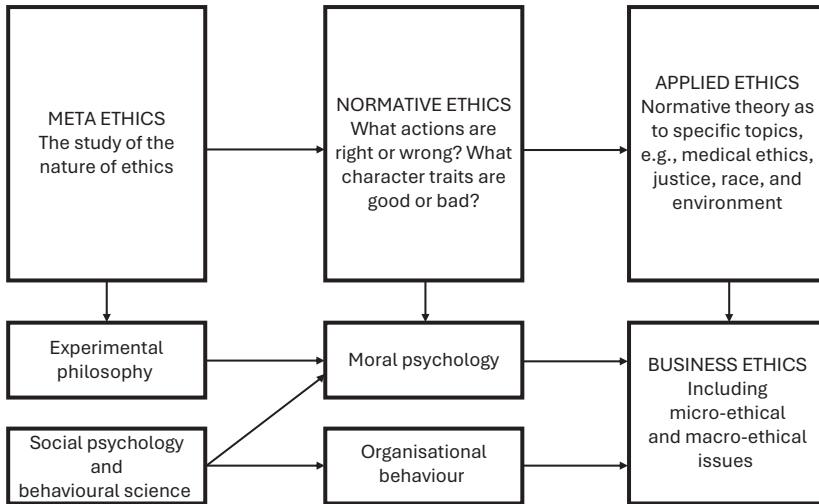
Chapters 2, 3, and 4 examine three philosophical approaches to macro business ethics. According to shareholder primacy, the interests of shareholders take priority over the interests of other stakeholders. According to stakeholder theory, managers are morally obliged to balance competing stakeholder interests in their decision-making. I discuss how both these approaches are importantly incomplete, and how two alternative ways of thinking, 'team production theory' and the 'market failures approach', may provide a viable alternative. In Chapter 5, I introduce a virtue ethics approach, which I hope helps to complete the picture.

The book is written primarily from an Anglo-Saxon business perspective, and its business ethics are essentially those of the Western ethical tradition. I recognise the limitations of this. Nevertheless, I hope that many of the lessons contained in the book will be of wider global application.

What do we mean when we talk about 'business ethics'? It has been suggested by a number of people that 'business ethics' is an oxymoron – 'any book on business ethics must be a very short book'. The subject matter is difficult to delineate, and business ethics has been defined as 'like nailing Jell-O to the wall'. It is said to be hard to teach – 'changing moral values in college students is difficult at best, impossible at worst'. At least one study has demonstrated that students who major in banking and finance are predisposed to act less ethically than other business students.²⁰

Ethics is itself a big subject. At one end of the spectrum is meta-ethics, which addresses highly theoretical questions such as 'are there such things as moral facts?', 'how might moral facts relate to other facts?', and 'what is the relationship between values, reasons for action, and human motivation'? Normative ethics examines the basis of moral standards that determine right and wrong behaviour: what actions are right or wrong, and what character traits are good or bad? Normative ethical systems include rights-based ethics, duty-based ethics (sometimes known as 'deontology'), utilitarianism, and virtue ethics. At a practical level, applied ethics looks at specific, potentially controversial moral issues such as abortion and euthanasia. Sub-disciplines include categories such as medical ethics and environmental ethics. Business ethics emerged as a separate sub-discipline in the 1970s and can be divided into two parts. Micro-ethical questions, for the most part, centre around potential conflicts that may arise between an individual's personal value system and the occupational demands of his or her work. Macro-ethical questions relate to potential conflicts between business, the law, and public policy.²¹ Moral psychology, a field of study in both philosophy and psychology, examines moral development from infancy through adulthood. Figure 1.2, based on the work of Arthur Brief, Professor of Business Ethics at the University of Utah, is a simplified map of the territory.

Western ethical thinking over the last 2000 years can be approximately segmented into four phases. Figure 1.3 provides a timeline. The Ancient Greek philosophers focused on character and virtue – just acts, they argued, are of a kind that a just person would perform. What, therefore, are the characteristics of a virtuous person, they asked?

Figure 1.2: Business ethics – a simplified map of the territory

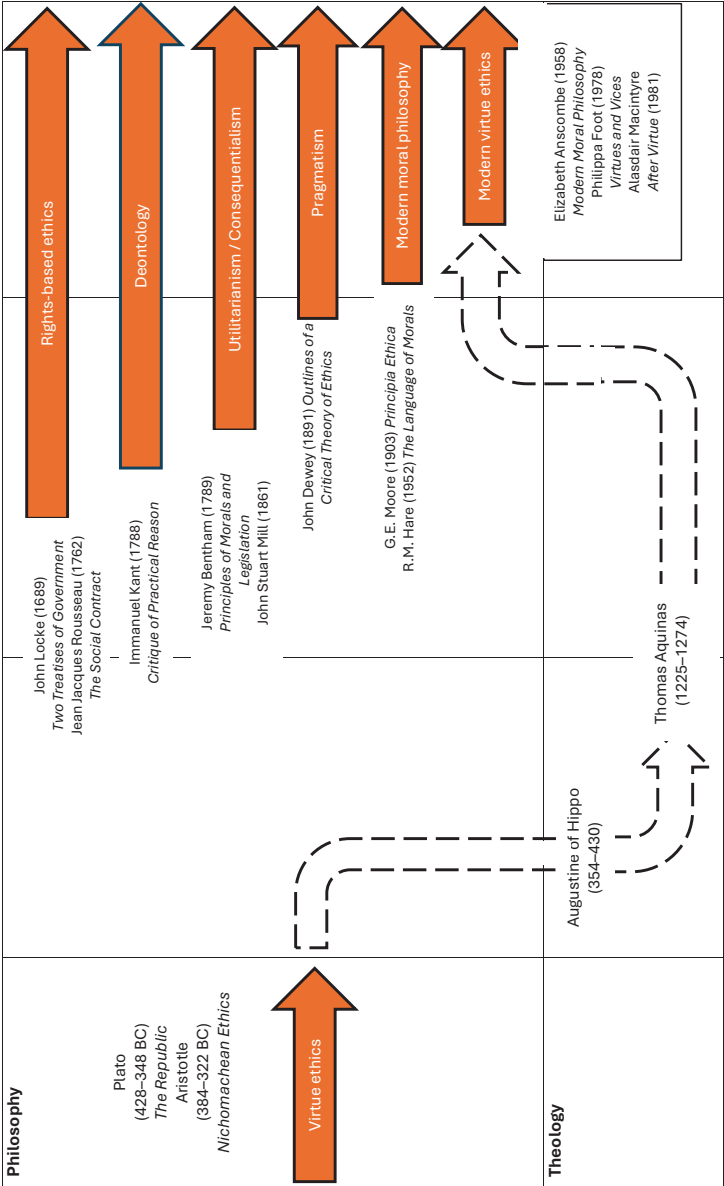
Source: Adapted from Brief (2012).²²

Medieval philosophy, extending roughly from the 5th to the 15th centuries, focused on reconciling ancient philosophical traditions, particularly those of Plato and Aristotle, with Christian, Islamic, and Jewish religious traditions. Ethics was largely the preserve of religious thinkers (hence it becomes ‘theology’ in my timeline), whose principal interest was in investigating the moral teaching of the Hebrew and Christian Bibles. Two leading scholars, Augustine of Hippo and Thomas Aquinas, linked morality to divine law, combining Christian teaching with Aristotelian moral philosophy.

It was not until the Enlightenment in the 17th and 18th centuries that there was a revival of interest in philosophical ethics from first principles with the development of rights-based ethics (John Locke and Jean-Jacques Rousseau), duty-based ethics (particularly Immanuel Kant), and utilitarianism (Jeremy Bentham and John Stuart Mill), of which more below. This was the beginning of the age of analytical philosophy, when philosophers believed the fundamental questions about existence, knowledge, morality, values, consciousness, and language could be answered by applying the full armoury of reason.

In the UK, the 20th century saw a focus on emotivism (‘good’ is like ‘beauty’, you know it when you see it), closely associated with the Cambridge philosopher G.E. Moore, and prescriptivism (moral statements are prescriptions or commands rather than references to moral facts) advanced by the Oxford philosopher R.M. Hare – together referred to as ‘modern moral philosophy’ in the timeline. Moore’s emotivism and Hare’s prescriptivism have their intellectual roots in the philosophy of the great 18th century Scottish philosopher

Figure 1.3: A brief history of Western moral philosophy



Source: Author.

David Hume. Hume argued that moral judgements are not determined by reason or fact – ‘you cannot get an ought from an is’, to paraphrase his famous statement. Instead, the primary reference of moral statements is to our passions. In the US, a school of philosophy led by William James (1842–1910) and John Dewey (1859–1952) that focused on practical consequences and real-world outcomes was known as ‘pragmatism’. In the UK in the aftermath of the Second World War there was increasing dissatisfaction with emotivism and prescriptivism. A searing critique of ‘modern moral philosophy’ by Elizabeth Anscombe, originally published in the journal *Philosophy* in 1958, led to a renewed interest in virtue ethics, notably in the work of Alasdair MacIntyre, of whom more will be said in Chapter 5.

To summarise, there are essentially four different ethical systems, all of which have been used as a basis for developing different codes of business ethics:

1. Rights-based ethics: an ethical system based on a number of natural rights, for example the rights to life, liberty, and property, which are regarded as self-evident.
2. Duty-based (rule-based, -obligation-based, or ‘deontological’) ethics: an ethical system constructed from a small number of moral obligations that are regarded as being axiomatic.
3. Utilitarianism: the idea of a moral calculus based on the maxim of ‘the greatest good for the greatest number’.
4. Virtue ethics: the belief that just acts are those that a just person would perform.

These four main ethical systems underpinning business are examined in more detail below.

Rights-based ethical systems

In his *Second Treatise of Government*, written in the late 1680s at the time of England’s ‘Glorious Revolution’, when William III and Mary II overthrew James II, the philosopher John Locke wrote that all individuals are born equal and with certain inalienable natural rights. These rights are God-given and cannot be removed. Among these fundamental rights, Locke said, are ‘life, liberty, and property’. Locke believed that the most basic natural law relates to the preservation of life. Individuals have the right to preserve their own lives, which Locke describes in terms of ‘self-ownership’. Because of self-ownership, we should be free to make choices about how we conduct our lives – in other words to ‘liberty’ – as long as in so doing we do not interfere with the liberty of others. Locke’s ideas about property are complex. He believed that property rights are obtained when a person mixes their labour with what is otherwise virgin territory or raw materials. Property rights are derived from the

principle of self-ownership – we have a fundamental right to the fruits of our own labour. To avoid exploitation, Locke recognises that this right must be subject to certain restrictions. First, one may only appropriate as much as one can use before it spoils. Second, one must leave enough for others.

Perhaps the most famous statement of rights-based ethics is the American Declaration of Independence, crafted by Thomas Jefferson, with the help of John Adams and Benjamin Franklin (see Figure 1.4). Jefferson's original draft, along with changes proposed by Adams and Franklin and Jefferson's response, is preserved at the Library of Congress in Washington DC. The authoritative version, signed by Congress on 2 August 1776, is held in the National Archives in Washington.

The influence of Locke can be seen in a number of places. Note how Jefferson regards certain truths as 'self-evident', based on natural law, and therefore axiomatic. Two of the three 'unalienable rights' that he identifies are 'life' and 'liberty'. Why Jefferson prefers 'happiness' to 'property' has been a cause of some debate. Some commentators attribute it to his interest in Epicureanism, a classical system of philosophy based on the teachings of Epicurus, who advocated a simple life, declared that modest pleasure is mankind's sole intrinsic goal, and that the avoidance of pain and fear is key to sustainable pleasure. Or perhaps Jefferson recognised some of the difficulties inherent in Locke's thinking about property.

Jefferson goes on to explain how a social contract between the government and the governed secures the people's unalienable rights, and that if a government breaches this covenant, then the governed have a right to replace their leaders.

Locke's theory of property rights made more sense in a world where land and raw materials were in relative abundance, especially in the New World of North America, than it does today. Nevertheless, it has had a significant impact on the subsequent development of laws and theories relating to property. For example, classical economists, including Adam Smith, David Ricardo and Karl Marx, argued that all value is ultimately derived from labour inputs (the 'labour theory of value'). Though the labour theory of value has now been

Figure 1.4: The beginning of the preamble to American Declaration of Independence

We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of Happiness. –That to secure these rights, Governments are instituted among Men, deriving their just powers from the consent of the governed, –That whenever any Form of Government becomes destructive of these ends, it is the Right of the People to alter or to abolish it, and to institute new Government, laying its foundation on such principles and organizing its powers in such form, as to them shall seem most likely to affect their Safety and Happiness.²³

largely debunked as a theory of how economic value is generated, in his essay ‘The requirements of a theory of value’, the Marxist economist Maurice Dobb (1900–1976) makes a sterling effort in its defence, arguing that in an ethical sense it is more important to attribute value to human effort and ingenuity than to anything else.²⁴

What constitutes a property right? While this might be an easy question to answer when it comes to tangible property (remember the phrase ‘possession is nine-tenths of the law’) it is much more difficult when it comes to intangible property such as shares in a company. One of the questions we will look at in Chapter 2 is whether shareholders own companies. Tony Honoré, formerly Regius Professor of Civil Law at Oxford University, identified 11 ‘badges of ownership’ (Figure 1.5).

Of these, only five – the rights to income, capital, security, the absence of term, and the incidence of residuary – are satisfied by minority shareholders in a public company. Shareholders hold property in the form of shares, which provide various limited rights: to receive dividends (but only if declared by directors), to vote on certain matters of importance, including the appointment and reappointment of directors (but only from a slate of candidates proposed by the board), and to veto major transactions (but only if a coalition of shareholders representing the necessary proportion of total votes prescribed by law can be assembled). Shareholders are not automatically entitled to enter company premises, to use company assets, or to arrange transactions on the company’s behalf; they surely would be if they were genuinely a firm’s ‘owners’. They also have the right to receive residual assets in a winding-up, but this rule rarely operates in practice: public companies tend only to be wound-up when bankrupt, when there are often no residual assets.

Locke’s schedule of rights (life, liberty, and property) is of particular relevance to the issues we will examine in this book. Other schedules of fundamental rights have also been proposed. The Genevan philosopher, Jean-Jacques Rousseau (1712–1778), famously believed that basic human rights included liberty, equality, and fraternity. Liberty and equality are individualistic values, while fraternity focuses on the benefits of living in community. *Liberté, égalité, fraternité* were adopted by French revolutionary lawyer and political thinker Maximilien Robespierre, and became forever associated with the French Revolution. Though the specific list of rights was subsequently contested in France during the intervening years, the basic rights of liberty,

Figure 1.5: Honoré’s badges of ownership

The right to possess	The rights of transmissibility
The right to use	Absence of term
The right to manage	Prohibition of harmful use
The right to income	Liability to execution
The right to capital	Incidence of residuary
The right to security	

equality, and fraternity were eventually written into the French Constitution in 1958.

In 1948, the General Assembly of the United Nations adopted a Universal Declaration of Human Rights. This declaration sets out, in 30 articles, a set of universal basic human rights and fundamental freedoms that it argues are 'inherent, inalienable, and applicable to all human beings', and which are intended as a 'common standard of achievement for all peoples and all nations', perhaps indicating that they are aspirational rather than, as yet, globally accepted.

Duty-based ethical systems

Instead of focusing on natural rights, deontological, duty-, obligation- or rule-based ethics focuses on duties. Deontological ethics begin with a set of principles specifying things which we should or should not do. 'Deontological' in this context comes from the Greek word for duty, *déon*, and science, *logos*. Perhaps the most famous deontological principle, sometimes known as the 'golden rule', is 'do unto others as you would have them do unto you'. Variations of the Golden Rule can be found in Egyptian, Sanskrit, and Tamil traditions, as well as in texts from Ancient Greece and Rome.

The key question for any system of deontological ethics is: what is the source of the rule? This may be a matter of 'natural law', the belief that there are certain intrinsic ideas, common to all human beings, that can be derived from close observation of human nature. Alternatively, they may be religious rules, handed down to us by our Creator, as for example, in the case of the Ten Commandments in the Hebrew Bible, passed down to Moses by God. To the medieval philosopher and theologian Thomas Aquinas, the two were necessarily interconnected. In his discussion of natural law in the *Summa Theologica*, its two main features are that natural law is handed down by God, and that we as its recipients must focus on principles of practical rationality by which human action can be judged rational and reasonable.²⁵

The German philosopher Immanuel Kant (1724–1904) derives his ethics from two principles of practical rationality. These two principles, which Kant regards as being interdependent and axiomatic, are known as the 'categorical imperative' – for details see Figure 1.6.

The brilliance of Kant is his argument that an ethical system can be constructed from these two axiomatic principles, which are in themselves hard

Figure 1.6: The categorical imperative

1. 'Act in such a way that you treat humanity, whether in your own person or in the person of another, always at the same time as an end and never simply as a means'.
2. 'Act only according to that maxim whereby you can, at the same time, will that it should become a universal law'.²⁶

to deny or refute. Just as a logical or mathematical system can be constructed by starting with a small number of axioms – propositions which are regarded as established, accepted, and self-evidently true – so, Kant argued, the ethical system he develops in the *Groundwork of the Metaphysics of Morals* (1785) and the *Critique of Practical Reason* (1788) is equally robust and universal. ‘Ends’ and ‘means’ are primitive concepts that need no definition. Which of us would be prepared to accept that we can, in an ethical sense, be ‘used’ (treated as a means and not an end). If we are not prepared to be ‘used’ in any particular way, why should we allow others to be used in that way?

In terms of what can be universally willed, consider, for example, the following statements:

- ‘Torture is justified in some cases’
- ‘It is inevitable during a just war that some unarmed civilians will be killed’
- ‘There are certain circumstances in which slavery or servitude is legitimate’

If these principles are universalised, then they can equally apply to you, your family, and your friends. Would you want that to be an acceptable element of a system of ethics?

You might like to pause at this point to think about how the two elements of the categorical imperative might apply to the statements set out in Figure 1.7. True or false? What do you think? The problem with the first statement is that if bribery is regarded as inevitable and therefore morally acceptable, there is a risk that corruption in a country will become endemic. This means that legitimate business activity will become more or less impossible, with inevitable adverse consequences for the economy and the country as a whole. The second and third statements appear to licence treating junior employees and unskilled workers as a means and not an end. Who feels comfortable about this? Finally, if everyone lied most of the time, doing business of any kind would be impossible – hence statement 4 cannot rationally be universalised.

In Chapters 2 and 3, we will examine a question about duty in a business context. To whom do company directors and senior executives owe obligations? As we will see, the American economist Milton Friedman believes

Figure 1.7: Applying the categorical imperative

1. It is sometimes necessary to bribe public officials in developing countries in order to obtain important contracts.
2. The bullying behaviour of a trader towards junior employees should be tolerated if the trader personally generates a lot of business for the firm.
3. Paying very low wages to unskilled workers is acceptable if people are happy to work on this basis.
4. Lying is acceptable during a contract negotiation – everybody does it.

Figure 1.8: Section 172 duty to promote the success of the company

- 1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—
 - a) the likely consequences of any decision in the long term,
 - b) the interests of the company's employees,
 - c) the need to foster the company's business relationships with suppliers, customers and others,
 - d) the impact of the company's operations on the community and the environment,
 - e) the desirability of the company maintaining a reputation for high standards of business conduct, and
 - f) the need to act fairly as between members of the company.

that 'a corporate executive is an employee of the owners of the business,' and that 'he has direct responsibility to his employers.' But corporate executives are employed by the company, not by its shareholders, and companies have separate legal personality. In both common law and civil law jurisdictions, company directors have particular 'fiduciary duties'. In the case of public corporations, corporate law does not treat directors as the agents of shareholders, but as something quite different. They are not charged with serving shareholders' interests alone, but with serving the interests of the company. In the eyes of the law, corporate directors are a unique form of fiduciary who more closely resemble trustees than agents. They owe fiduciary duties of loyalty and care to the company, not to shareholders.²⁷

Section 172 of the UK Companies Act 2006 explains, somewhat elliptically, what this means in English law (see Figure 1.8).

We will explore the whys and wherefores of Section 172 in more detail in Chapter 3 and again in Chapter 6.

Utilitarianism

Utilitarianism is one of the most powerful and persuasive ethical systems, while at times provoking questions which are deeply problematic. The utilitarian is encouraged to act in the way that ensures the greatest good of the greatest number of people. 'Good' in this context is variously defined in terms of happiness, well-being, welfare, or more vaguely 'utility'. Act utilitarianism states that a person's act is morally right if it produces the best possible result (the highest level of well-being, the greatest amount of utility, *etc.*) in certain specific circumstances. Rule utilitarianism argues that an action is right if it confirms to a rule that generally leads to the greatest overall good.

The utilitarian systems of ethics were first articulated in the 18th century by Jeremy Bentham (1748–1832) and developed in the 19th century by John Stuart Mill (1806–1873) and Henry Sidgwick (1838–1900). Bentham was a

social reformer who wished to see corrupt laws overturned and social practices changed. He believed that humans were ruled by two sovereign masters: pleasure and the avoidance of pain. The ethics of an action should be evaluated on the basis of whether or not it causes more pleasure than pain and thus maximises human happiness – sometimes known as the ‘hedonic calculus’. Mill, while admiring Bentham’s work, believed that there are qualitative differences between pleasures (better or worse pleasures), not just quantitative differences (more or less); in particular, intellectual pleasures are more worthy than those pleasures which are merely sensual. In his book *The Methods of Ethics*, Sidgwick provided a sophisticated defence of classical utilitarianism and helped to prepare the ground for the assessment of utility in welfare economics.²⁸

Some of the problems of utilitarianism can be illustrated by the ‘trolley problem’, posed by the American philosopher Judith Thomson in 1976 in an essay entitled ‘Killing, letting die, and the trolley problem’. Thomson used the trolley problem thought experiment to illustrate a moral dilemma posed by the Oxford philosopher Philippa Foot in her 1967 essay ‘The problem of abortion and the doctrine of double effect’.²⁹ Foot argued that it is sometimes permissible to cause harm, if the harm, though foreseen, is not the primary intention, but is instead a by-product of an action which is intended to deliver a greater good. Thomson examines the doctrine of double effect by describing the following situation:

Edward is the driver of a trolley, whose brakes have just failed. On the track ahead of him are five people; the banks are so steep that they will not be able to get off the track in time. The track has a spur leading off to the right, and Edward can turn the trolley onto it. Unfortunately there is one person on the right-hand track. Edward can turn the trolley, killing the one; or he can refrain from turning the trolley, killing the five.³⁰

The utilitarian calculus for Edward seems straightforward: better to kill one person than to kill five. However, Thomson also describes another situation that appears to be equivalent to the trolley problem:

David is a great transplant surgeon. Five of his patients need new parts—one needs a heart, the others need, respectively, liver, stomach, spleen, and spinal cord—but all are of the same, relatively rare, blood-type. By chance, David learns of a healthy specimen with that very blood-type. David can take the healthy specimen’s parts, killing him, and install them in his patients, saving them. Or he can refrain from taking the healthy specimen’s parts, letting his patients die.³¹

Here our moral intuition is that it would be wrong for David to kill a healthy patient, even though by not doing so he is, in effect, allowing five other

patients to die. Foot’s solution to this inconsistency is that our negative responsibility to refrain from killing is weightier than our positive responsibility to save lives.

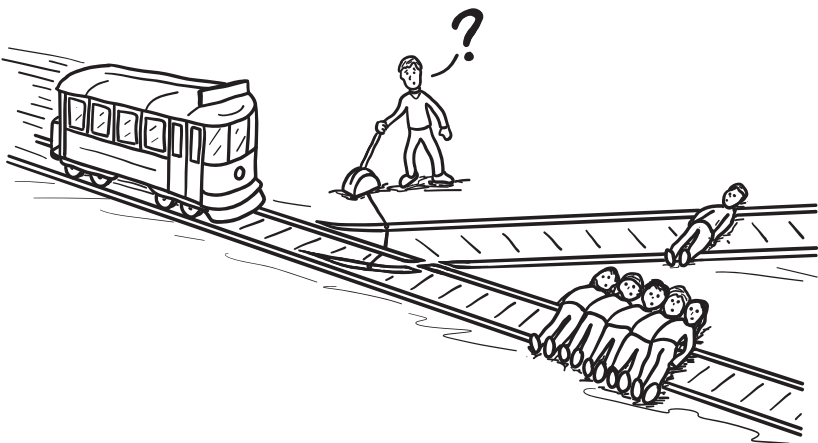
The trolley problem has generated substantial literature, written by academic philosophers, popular philosophers, and novelists.³² It has also generated many variations. In one popular example, the dilemma sits with a third-party bystander (it could be you!) who can pull a lever to cause the trolley to run into a siding, killing one person, rather than continuing on the main line and killing five people (see Figure 1.9). Here, ‘do nothing’ looks like a bad option, but is it ethical?

What happens when we introduce probability? Does the decision change if the probability of killing the one person is 4/5 ($p = 0.8$), whereas the probability of killing any one of the five people is 1/7 ($1/7 + 1/7 + 1/7 + 1/7 + 1/7 = 5/7$, $p = 0.7$)? In another variation, the person on the right-hand track is a healthy child of five with a life expectancy of at least 80 years, and the five people on the main track are all infirm and over 90? Here Foot’s distinction between positive and negative duties does not appear to solve the ethical dilemma.

Oxford philosopher Derek Parfit argues for a more nuanced version of utilitarianism.³³ Imagine a choice with two outcomes, 1 and 2, involving two persons, A and B:

1	A is at 20	B is at 10
2	A is at 25	B is at 9

Figure 1.9: The trolley problem



Source: Tim Wakeling.

At first sight, outcome 2 is better than outcome 1 as it satisfies the principle of the greatest good of the greatest number. But what if A is highly privileged and B is severely disadvantaged, such that 1 would make a much greater difference to their life than 5 would make to A? Therefore, Parfit proposes a version of utilitarianism called ‘prioritarianism’, which is based on three principles:

1. Diminishing marginal moral value: each person’s well-being has positive, but diminishing moral value.
2. Separability: the moral value of an increment in a person’s well-being does not depend on how anyone else fares.
3. Maximisation: we ought to maximise the sum-total of the moral value of each person’s priority-weighted well-being.

Notice also how in this example the focus has shifted from living or dying, a very binary decision, to the question of ‘well-being’, which is more difficult to measure, and would also seem to be conceptually different from ‘happiness’. Which brings us to four of the main problems for utilitarianism:

1. What are we measuring? Is it happiness, well-being, welfare, utility, or something else? And what do these different concepts really mean?
2. How do you measure it?
3. Can one person’s happiness, well-being, or welfare be weighed against another person’s, the interpersonal comparison of utility problem pointed out by LSE economist Lionel Robbins in his *Essay on the Nature and Significance of Economic Science*?³⁴
4. What about risk (known probabilities) and uncertainty (unknown probabilities)? How are these things taken into account in the ethical calculus?

Utilitarianism is a form of ‘consequentialism’ – the focus is on the rights and wrongs of outcomes, rather than intentions. It is sometimes regarded as of particular relevance for business ethics because of its close connection with economics, which also makes use of the concept of ‘utility’. However, it is certainly not the only important ethical system.

Virtue ethics

The virtue ethics approach is radically different from the other ethical systems we have considered so far in this chapter. Rather than assessing the ethical nature of actions or outcomes, virtue ethics proceeds on the basis that just acts are the kind that a just person would perform, thus requiring an assessment of the character of the person. Virtues are deep-seated dispositions, construed in such a way that actions, thoughts, and feelings are inextricably linked. We will

look in more details at virtue ethics and the question of character in Chapter 5, but a few preliminary comments are offered here.

Virtue ethics are actor centred – the key question is ‘what kind of a person do I want to be?’ rather than ‘what should I do?’. In the *Nicomachean Ethics*,³⁵ Aristotle argues that, although you can set out some ethical rules of thumb about right action, it is very hard to be precise, as the right thing to do will depend on the context:

The whole account of matters of conduct must be given in outline and not precisely ... matters concerned with conduct and questions of what is good for us have no fixity, any more than matters of health. The general account being of this nature, the account of particular cases is yet more lacking in exactness; for they do not fall under any art or precept but the agents themselves must in each case consider what is appropriate to the occasion, as happens also in the art of medicine or of navigation.³⁶

Hence the focus of virtue ethics is on judgement and character rather than hard-and-fast rules. Whereas much post-Enlightenment moral philosophy takes discrete human actions as its primary point of reference, the focus of both ancient and new virtue ethics is on the development of character.

The ancient moral philosophers reflected upon human actions in an attempt to determine what was essentially ethical or unethical. In this respect, the actions of the great Homeric kings and warriors were as important as the observations of philosophers such as Plato and Aristotle. Three important concepts were ‘virtue’ (*areté*), happiness or flourishing (*eudaimonía*), and purpose (*télos*). Leading a virtuous life is important as it is both a necessary and sufficient condition for human flourishing. The virtuous person is the one who is clear about his or her purpose in life. *Areté* also implies excellence (as in virtuosity), so there is a sense that human flourishing is associated with excellence as well as with virtue.

To Plato and Aristotle, the four cardinal virtues are those set out in Figure 1.10.

Later in this book, we will consider Aristotle’s thinking about temperance or moderation, and the doctrine of the ‘golden mean’. Ethical virtue involves a balance between two states, one involving a surplus, the other involving a deficiency. The courageous person, for example, believes that some dangers

Figure 1.10: The four cardinal virtues

- Temperance or moderation (*sophrosynē* or *enkratia*)
- Prudence or practical wisdom (*phronesis*)
- Courage (*andreia*)
- Justice (*dikaiosune*)³⁷

are worth facing – but to face certain other dangers would be reckless. True courage lies somewhere between two extremes.³⁸

Phronesis is a type of wisdom relevant to practical action. It can be contrasted with *epistêmê* (theoretical knowledge, from which we derive the modern word ‘epistemology’, the branch of philosophy dealing with knowledge) and *technê* (technical knowledge, which involves making or doing). *Phronesis* involves good judgement and excellent character. Plumbers have *technê*, academics have *epistêmê*, business-men and -women (hopefully) have *phronesis*.

Justice means the human characteristic of being just, rather than ‘justice’ as might be found, for example, in society as a whole. It is both ‘the virtue which regulates man in his dealing with others’ and ‘The quality of being fair and reasonable.’³⁹ Justice (‘being just’) might in turn be disaggregated into:

- Fairness (‘being fair’) and
- Trust (‘trustworthiness’)

Trustworthiness might itself be disaggregated into:

- Commitment and
- Competence

What do you think are the character traits of a good business leader? How many of the characteristics set out in Figure 1.11 would be included on your list?

No doubt you can think of other important character traits too, but I am sure you will agree that this is a pretty good list. Virtues, it seems, are as old as the hills.

Summary

In this chapter I have examined four different ethical systems. These four systems, associated tag lines, and names of philosophers who are associated with particular principles, are summarised in Figure 1.12.

Figure 1.11: The character traits of a good business leader

- Knowledgeable (about the business, the industry, and the economy as a whole)
- Well-balanced (not prone to anger or outbursts, calm under pressure)
- Courageous and risk-aware (prepared to take risks, but aware what actions are too risky)
- Competent (skilled in their particular area of expertise, good communicator, good general management skills)
- Committed (to the firm and the business)
- Fair
- Trustworthy

Figure 1.12: Four ethical systems – a summary

1. Right-based ethics
 - John Locke: 'Life, liberty and property'
 - Jean-Jacques Rousseau: 'Liberty, equality, fraternity'
2. Deontological ethics
 - Immanuel Kant: 'Act in such a way that you treat humanity ... always at the same time as an end and never simply as a means' and 'Act only according to that maxim whereby you can, at the same time, will that it should become a universal law'
3. Utilitarianism
 - Jeremy Bentham: 'The greatest good of the greatest number'
4. Virtue ethics
 - Aristotle: 'Just acts are the kind that a just person would perform'

The four-part typology I have used here is not the only way of categorising ethical systems. Ethical theories can also be labelled as consequentialist, deontological, or related to virtue ethics. Some philosophers include ethical egoism (based on the principle of maximising one's own good) and contractarianism (the idea that ethics is based upon a social contract). We have also touched on emotivism, which argues that moral statements do not convey objective facts but are simply expressions of emotion. In say 'lying is wrong', we are not stating a universal truth but simply expressing a feeling of disapproval. Prescriptivists argue that ethical statements function as prescriptions or commands rather than statements of moral fact. Thus to say, 'stealing is wrong' is simply to say, 'don't steal'. In two famous articles which she wrote in the 1950s, 'Does Oxford moral philosophy corrupt youth?' and 'Modern moral philosophy', the virtue ethicist Elizabeth Anscombe excoriated emotivism and prescriptivism as being worthless, both for resolving ethical dilemmas and as a general guide to practical action. As she says: '*de gustibus non est disputandum*': in matters of taste, there can be no dispute.⁴⁰ If ethics were merely a matter of taste, then rational argument would be futile.

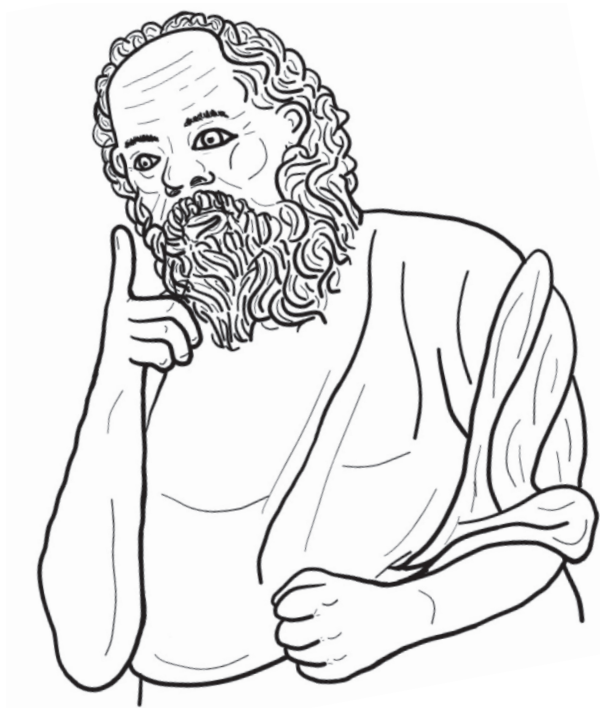
We will also come across pragmatism, only touched upon above, but made more use of in Chapter 3. Pragmatism is a philosophical tradition that views philosophical reasoning as a set of tools for problem solving and practical action, rather than dry theorising. John Dewey (1859–1952) believed that there was an empirical basis to ethics. Some societies, he believed, have made greater progress in terms of the development of their ethical understanding, in the same way that some societies have progressed further in terms of their scientific knowledge. Hence, moral principles can, he believed, be arrived at inductively by empirical enquiry – sometimes known as 'ethical pragmatism'.

While ethical systems might appear to be mutually exclusive or even contradictory, they often overlap. In his magnum opus, *On What Matters*, the great Oxford philosopher Derek Parfit argued that most ethicists see themselves as climbing the same mountain from different sides. When they reach the top, they recognise that other routes to the summit are equally legitimate.⁴¹ While not all philosophers would agree, it is nevertheless a beautifully imagined metaphor.

Dialogue I: Socrates and Milton

In which Socrates and Milton Friedman discuss the social responsibility of business and the concept of shareholder primacy

Figure I: Socrates



Source: Tim Wakeling.

Socrates was an Athenian philosopher who lived in 5th century BCE. Known through the writings of others, most notably Plato and Xenophon, Socrates himself wrote nothing, or if he did, nothing he wrote has survived. Famous as a

*debater and discussion partner, Socrates was, in the words of the ancient philosophy scholar Christopher Taylor, 'above all, an arguer and questioner, who went about challenging people's pretensions to expertise and revealing inconsistencies in their beliefs'. He was famously ugly, described as having a snub nose, wide nostrils, protruding eyes, thick lips, and a paunch.*⁴²

In the imagined dialogue which follows, Socrates discusses the social responsibility of business and the concept of shareholder primacy with the famous American economist, Milton Friedman (1912–2006) the leading proponent of the principle of shareholder primacy. More about Milton Friedman can be found at the start of Chapter 2.

Socrates and Milton Friedman meet at an awards ceremony held in Athens for 'Humanity's Greatest ever Public Intellectuals'. The event organisers have sat them next to each other at a gala dinner. They have been having a long conversation about each other's ideas.

SOCRATES: Well, Milton, I understand that you believe that the only social responsibility of business is to maximise profits for shareholders.

MILTON: That's right, Socrates. In a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of society.

SOCRATES: Thank you, Milton, for stating your position very clearly. Now would you mind if I ask you some questions about this proposition?

MILTON: Why not, Socrates, I would be happy to answer your questions. I am very certain of my position on the question of corporate purpose.

SOCRATES: Here we go then. Now, would you say that the purpose of a physician is to cure illnesses or make as much money as possible?

MILTON: Well, Socrates, I know some well-paid doctors, but if I asked them why they chose their profession I am sure that they would say it was to cure illnesses and to help their patients towards better health.

SOCRATES: And if one of your doctor friends answered the question the other way and said that they were trying to make as much money as possible, would you regard them as a good doctor?

- MILTON: Well, I certainly wouldn't like to have someone like that as my personal physician!
- SOCRATES: Good. So then, Milton, if the purpose of a physician is to cure illnesses and help patients towards better health, then what is the purpose of a hospital?
- MILTON: Obviously, it is to provide a location where doctors can carry out their duties.
- SOCRATES: Their duties to cure illnesses and help their patients towards better health?
- MILTON: That's right, Socrates.
- SOCRATES: And would it make any difference whether this was a private for-profit hospital or a public not-for-profit hospital do you think?
- MILTON
(cautiously): No, I don't think it would make any difference.
- SOCRATES: Then can I ask a follow-up question, Milton? If the purpose of a hospital is to cure illnesses and help patients towards better health, then what is the purpose of a pharmaceutical company which provides drugs for the hospital?
- MILTON
(even more cautiously): I suppose it is also to cure illnesses and help patients towards better health.
- SOCRATES: So the purpose of a company like AstraZeneca or GlaxoSmithKline is to cure illnesses and help patients towards better health?
- MILTON: Something like that, yes.
- SOCRATES: Not to maximise profits for shareholders?
- MILTON: Ah, I see where you are going now. Yes, I suppose that your argument is valid.
- SOCRATES: And is the purpose of a hospitality company to provide hospitality for their guests, and an airline to help passengers travel between different locations?
- MILTON
(now rather irritated): Yes, yes, I suppose so.
- SOCRATES: And the purpose of an oil and gas company is to provide oil and gas for their customers?

MILTON: Yes, as long as all these companies make sufficient profits to satisfy their shareholders.

SOCRATES: But would you agree that making sufficient profits to satisfy shareholders is a secondary objective rather than the primary purpose of these companies?

MILTON: Yes, Socrates, I have to accept that your argument is a very strong one. Now, I have just remembered that I have an urgent conference call with some economists in Chicago, please do excuse me. Our conversation has been most enlightening.

The next day Milton bumps into Socrates in the centre of Athens.

MILTON: Hey Socrates, it's Milton here.

SOCRATES: Milton, good to hear from you, I've been reading some of your poetry.

MILTON: What?

SOCRATES: You know, the one about the angel who fell out with God and became a Nietzschean superman.

MILTON: That's John Milton.

SOCRATES: Oh, sorry, so you're Milton, Milton Jones, the comedian?

MILTON: No, Friedman.

SOCRATES: Fridman, the Russian oligarch?

MILTON: No, Socrates, Milton Friedman, the American economist, you know we were talking at the dinner yesterday about business purpose, what's a company for, the purpose of the corporation, and all that jazz.

SOCRATES: Of course, sorry, I'm getting a bit forgetful in my old age. It must be this homeopathic medicine with wild hemlock in it that I've been taking recently.

MILTON: Anyway, Socrates, I've been reflecting on our discussion the other day, and I've got some further thoughts.

SOCRATES: I'd be interested to hear your ideas, Milton.

MILTON: Well, Socrates, you know you talked about the purpose of pharmaceutical companies being to cure illnesses and help patients towards better health?

SOCRATES: Yes.

- MILTON: So, I was thinking about AstraZeneca making that COVID vaccine in the UK and selling it at cost, that kind of fits the bill, doesn't it?
- SOCRATES: Yes, it does.
- MILTON: But Pfizer sold its vaccine at a profit, helped fix COVID in the United States and made a barrel load of money at the same time, so that's kind of interesting, isn't it?
- SOCRATES: Well, yes ... yes, it is.
- MILTON: Then there's that other pharmaceutical company that's been in the news a lot, Purdue Pharma, who according to Patrick Radden Keefe has made lots of money by getting millions of Americans addicted to opioids.⁴³ So how does that fit with the idea that the purpose of a pharmaceutical company is to cure illnesses and help patients towards better health?
- SOCRATES: I see what you mean, Milton.
- MILTON: And, you know, I was watching an old film on Netflix the other night, *The Constant Gardener* by that English guy with the funny French name, you know, Le Carré.
- SOCRATES: Yes, I've read the book.
- MILTON: Well, according to Le Carré, all pharmaceutical companies are run by a bunch of crooks.
- SOCRATES: I suppose you could say that that proves the point, Milton, if you think about it. Perhaps those companies have lost sight of their proper purpose and have become fixated on making money.
- MILTON: Okay, let's try something else. You know I've been doing lots of reading on this subject.
- SOCRATES: That's good, Milton. Reading is a thing to be admired.
- MILTON: So I've read some academic papers by a guy called Jerry Davis. He's a sociologist at the Michigan Ross School of Business. He's pretty sceptical about all this corporate purpose stuff. He says that if you want corporations to behave themselves, they need to be more democratic – greater worker control and more effective state regulation *etc.*⁴⁴
- SOCRATES: He's a sociologist, Milton. They sometimes have funny ideas.

- MILTON: Then there's Lucien Bebchuk at Harvard Law School, no wishy washy liberal he, he reckons that all this 'stakeholder capitalism' stuff is flawed and dangerous, that – and I quote – 'stakeholderism should be expected to produce only illusory benefits as well as serious detrimental effects'.⁴⁵ Strong stuff, eh, Socrates?
- SOCRATES: Yes, I suppose so, Milton.
- MILTON: You bet, I mean who are all these 'stakeholders' anyway and how do you adjudicate between them? If one thing is good for workers, and something else for customers, and something else again for shareholders – I mean, how do you decide between them?
- SOCRATES: That's a good question, Milton.
- MILTON: Mark Roe, he's another Harvard guy, he reckons that competitive firms in competitive industries can't afford expensive purpose costs. He reckons it's all about making sure markets are competitive and protecting stakeholders with rules, laws and widely shared norms.⁴⁶ Just like I said some time ago.
- SOCRATES: Well, he's an economist.
- MILTON: Actually he's a law professor. Anyway, what about Joseph Heath? He's a philosopher, so you should like him. He reckons that the best way to think about ethical business is where managers continue to owe fiduciary duties to shareholders and regard their interests as primary, but where they're constrained by laws and regulations which ensure that markets are competitive and healthy, and that companies don't exploit workers or consumers.
- SOCRATES: If you say so, Milton. You certainly have been doing a lot of research, haven't you?
- MILTON: Then there's some of those journos who write for that broadsheet in the UK, you know, the *Financial Times*. There's a guy called Stefan Stern, he reckons corporate purpose is all a load of bunkum – it's just greenwashing, 'the boardroom's futile pursuit of purpose' he calls it. Stern quotes from a book called *The Purpose Myth* by a lady called Charlotte Cramer. He thinks we need to get real about all this stuff.⁴⁷
- SOCRATES: I'm not quite sure which side of the argument you're on now, Milton.

- MILTON: I'm just trying to show how complex this question is. What about Geoffrey Owen, Sir Geoffrey Owen I should say, the guy who used to be the editor of the *Financial Times*? He points out that the world has done pretty well over the last 200 years from shareholder-based capitalism, and that having a proper purpose and maximising shareholder value can be done perfectly well within the present legal framework.⁴⁸
- SOCRATES: If you say so.
- MILTON: And what about Terry Smith, you know that superstar investor, who reckons Unilever should stick to its knitting rather than trying to save the world? He says that the company has become obsessed with virtue signalling instead of addressing the fundamentals of the business.⁴⁹
- SOCRATES: Well, he's an investor, and he has pretty strong views, Milton.
- MILTON: Okay, but back to my main argument. Didn't you say, Socrates, that 'a man with two masters serves only himself'? Isn't that the problem here, if we confuse the issue for those good people who run companies about who they're working for, either they'll get confused – or worse, they'll pull the wool over everyone's eyes and just look after themselves, feather their own nests, focus on numero uno, if you know what I mean.
- SOCRATES: When it comes to 'a man with two masters', I think you're getting muddled with the Bible, Milton. And I don't think Matthew was arguing that money comes first.⁵⁰
- MILTON: Okay, okay. But you get my point. Anyway, you philosophers don't have a monopoly on virtue, do you? Didn't you have some funny ideas about slavery?
- SOCRATES: That was Aristotle.
- MILTON: And didn't you say that countries are best run by dictators, like Vladimir Putin?
- SOCRATES: That was Plato.
- MILTON: But you and Plato are joined at the hip, aren't you? And I seem to remember that your mate Plato had some very dodgy ideas about banishing poets and playwrights from his ideal republic, didn't he? Are your ideas really as modern as you claim they are?

SOCRATES: Okay, Milton, it is my turn to acknowledge that you have advanced some very strong arguments. I will give all this some thought. Now, I have just remembered that I have a class to teach at the Academy, please do excuse me.

MILTON: The Academy? Aren't there a lot of arty types in your school, Oscar winners and all that?

SOCRATES: I think you must have the wrong Academy, Milton. I'll see you later.

2. Shareholder primacy

This chapter considers the shareholder primacy approach to the moral responsibilities of company managers. According to shareholder primacy, the overriding responsibility of corporate executives is to shareholders, who appoint the executives to run companies on their behalf in return for payment. I consider the strengths and weaknesses of shareholder primacy, but conclude that it is an incomplete approach.

In particle physics, the Standard Model is the theory describing three fundamental natural forces: electromagnetic force, weak nuclear force, and strong nuclear force. It was developed by a number of scientists working individually and in research teams during the second part of the 20th century. The Standard Model is widely accepted by physicists, although it still leaves some phenomena unexplained.

In much the same way, organisational economics has a standard theory of the firm. Firms are 'legal fictions' that serve as 'a nexus of contracts' among individuals.⁵¹ They exist primarily for three reasons:

1. To save transaction costs in circumstances where (external) market transaction costs exceed the equivalent (internal) governance costs.⁵²
2. To facilitate joint production where team surpluses could not otherwise be allocated by market mechanisms.⁵³
3. To provide a vehicle for defining property rights and solving contracting problems.⁵⁴

In the standard model of the firm, shareholders (*principals*) appoint professional managers (*agents*) to make both strategic and everyday tactical decisions on their behalf. The separation of ownership and control creates *agency costs* as a result of *information asymmetry* and because *self-interested managers* do not necessarily act in the interests of shareholders. The agency problem is solved by *monitoring* (corporate governance) and by constructing high-powered *incentive contracts* for managers.⁵⁵ Incentive contracts are designed to align the interests of shareholders and managers. Corporate governance structures are determined by the principle of *shareholder primacy*: shareholders, as residuary beneficiaries, are the firm's ultimate owners.⁵⁶ The overriding objective of company managers is to *maximise shareholder value* on behalf of the firm's owners.

As explained in the preface, one of the main objectives of this book is to embed business ethics into the theory of the firm, and hence into the standard model. In this chapter we will look in some detail at the final element of the standard model of the firm, the principle of shareholder primacy, a doctrine most closely associated with the American economist, Milton Friedman and his assertion in his book *Capitalism and Freedom* that 'the only social responsibility of business is to maximize profits for shareholders'.

While many political philosophers have argued that the profit motive and accumulation of capital have a deleterious impact upon society, the idea that commerce has a positive social impact has a long history. At a micro-ethics level, Thomas Paine, the English-American political theorist and revolutionary, argued that 'the invention of commerce ... is the greatest approach towards universal civilisation that has yet been made by any means not immediately flowing from moral principles'.⁵⁷ At a macro-ethics level, the French social commentator and political thinker Montesquieu said, 'two nations who traffic with each other become reciprocally dependent ... and thus their union is founded on their mutual necessities'.⁵⁸ The doctrine that commerce has a positive social impact is sometimes known, after Montesquieu, as the 'doux commerce' thesis.

In analytical terms the doux commerce thesis goes like this:

Commerce (C) promotes:

- Stable government (S) by promoting the virtues which make it possible – constancy, thrift, diligence, foresightedness, orderliness, reliability, hard work.
- Tolerant attitudes (T) that make liberalism and pluralism possible, especially to ignore religious differences and cooperate peaceably as citizens.
- Habits of reciprocity and fairness (H), the reputation for which has a definite cash value.⁵⁹

However, Edmund Burke argued that the doux commerce thesis confuses cause and effect. Where Montesquieu and Paine argued $C \rightarrow S, T, H$, Burke argued $S, T, H \rightarrow C$. In other words, a society which is characterised by stable government, tolerant attitudes, and habits of reciprocity and fairness is a society in which commerce can flourish, not that commerce leads to stable government, tolerant attitudes and habits of reciprocity and fairness.

Contemporary commentators with social democratic leanings would think that Burke had a point. Nevertheless, the doux commerce thesis has many modern articulations. See, for example, economist Albert Hirschman's *Rival Views of Market Society* and legal scholar Nathan Oman's *The Dignity of Commerce*.⁶⁰ Its most expansive modern expression comes in the work of economic historian and modern polymath Deirdre McCloskey. The main thesis of McCloskey's trilogy *The Bourgeois Era* (argued over three books and some 1900 pages) is that when business became virtuous in the eyes of the Western bourgeoisie sometime in the 17th and 18th centuries, thus began a

cycle of economic innovation, supported by bourgeois capital and affirmative rhetoric, which brought about the exponential growth in Western society's wealth after 1800 not found, for example, in China – although the exact cycle of causation (which came first, the bourgeois virtues, the innovation, or the rhetoric?) is not entirely clear.⁶¹

Economists have even found empirical evidence supporting the *doux commerce* thesis in a field experiment conducted in Greenland in 2020, one of those delightful natural experiments which occasionally illustrate economic principles apparently by chance.⁶²

Milton Friedman

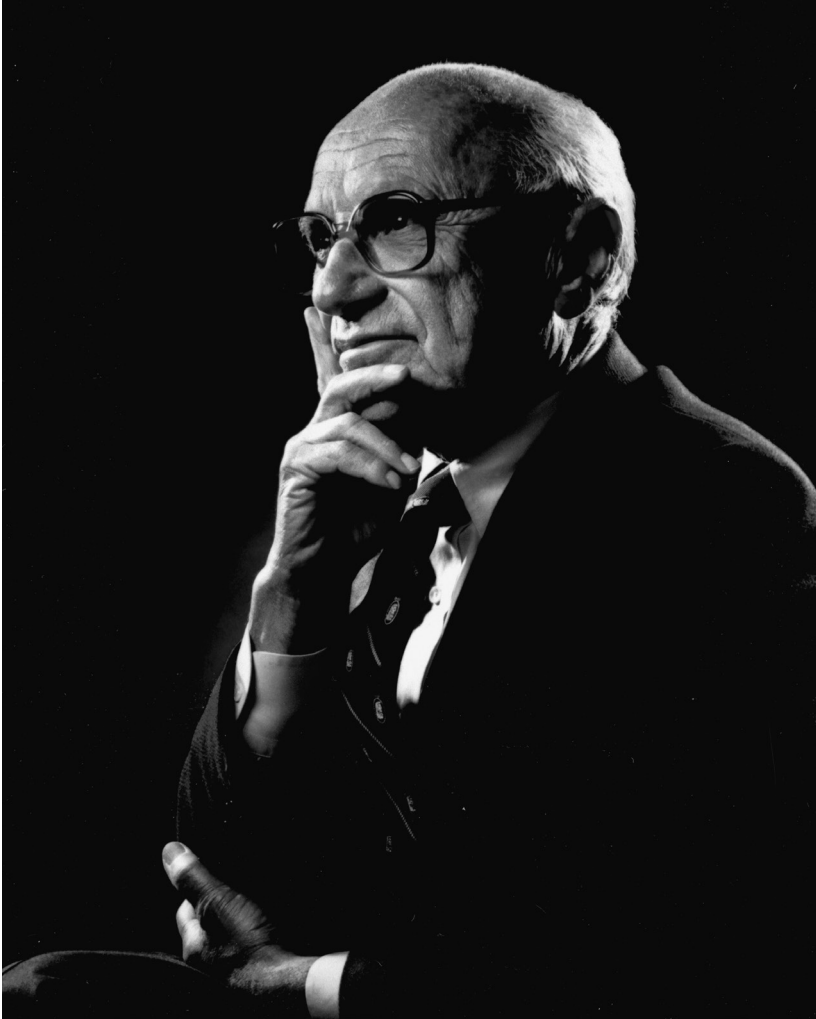
Milton Friedman (1912–2006) (see Figure 2.1) was the intellectual leader of the Chicago school of economics, a leading advocate of monetarism, and critic of Keynesian macroeconomic demand management. In 1963 he wrote *A Monetary History of the United States, 1867–1960* with co-author Anna Schwartz, although Friedman got most of the credit.⁶³ Based on his research, he developed a widely adopted policy response to 1970s problem of 'stagflation', arguing that 'inflation is always and everywhere a monetary phenomenon'. He was economic adviser to Ronald Reagan and Margaret Thatcher, and less illustriously to Chile's Augusto Pinochet. In 1962 he wrote *Capitalism and Freedom*, his manifesto concerning the relationship between economic freedom and political freedom, in which he advocated a limited role for government. In 1976 he won the Nobel Memorial Prize in Economic Sciences for his 'achievements in the field of consumption analysis, monetary history and theory, and for his demonstration of the complexity of stabilization policy'.

Among economists, Milton Friedman is known for his essay on the methodology of positive economics, in which he argued that economic theories should be judged by their predictive accuracy, not by the realism of their assumptions.⁶⁴ Among businessmen and -women he is probably best known for the Friedman doctrine: that the principal responsibility of corporate executives is to make as much money as possible for shareholders.

Friedman first set out the case for shareholder primacy in *Capitalism and Freedom*. In Chapter 8 he addresses the social responsibility of business and labour. Famously, he writes:

Few trends could so thoroughly undermine the very foundations of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for their stockholders as possible. This is a fundamentally subversive doctrine. If businessmen do have a social responsibility other than making maximum profits for stockholder, how are they to know what it is? Can self-selected private individuals decide what the social interest is? Can they decide how great a burden they are justified in placing on themselves or their stockholder as to serve that social interest?⁶⁵

Figure 2.1: Milton Friedman



Source: The Friedman Foundation for Educational Choice, public domain.⁶⁶

A few years later, in an article published in the *New York Times*, Milton Friedman repeated the argument for shareholder primacy.⁶⁷ Earlier that year, a group of campaigners had demanded that General Motors name three directors who should represent 'the public interest'. They had also demanded that the company set up a committee to consider General Motors' performance in areas of public concern such as safety and environmental pollution. While the campaigners' motion had been defeated at the company's annual general meeting, General Motors' management had subsequently set up a public-policy

sub-committee of the main board, apparently in response to the campaigners' second demand. Friedman, unimpressed, wrote an article responding to this, as well as other calls for businesses to exercise greater social responsibility. Shareholder primacy is known, after the title of his piece in the *New York Times*, as the 'Friedman doctrine'. For ease of reference, a copy of the article is included in an Appendix to this book.

Friedman criticises discussion of the social responsibilities of business for their 'analytical looseness and lack of rigor', thus inviting the type of detailed analytical critique which follows.

The first formulation of the Friedman doctrine

The first formulation of the Friedman doctrine goes like this:

There is one and only one social responsibility of business ... to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception and fraud ...⁶⁸

The intellectual roots of the Friedman doctrine can be found in the work of two 18th century Englishmen. John Locke (1632–1704) proposed that people have certain natural rights, in particular rights to life, liberty, and property. These rights provide the foundations of a broader ethical and political framework. Adam Smith (1723–1790) famously says of a merchant that:

By pursuing his own interest he frequently promotes that of society more effectually than when he intends to promote it. I have never known much good done by those who affected to trade for the public good.⁶⁹

The first formulation of the Friedman doctrine can be broken down into a number of separate arguments.

Friedman's first argument:

1. Only people [persons] have responsibilities.
2. A business is not a person.
3. Therefore a business cannot have responsibilities.

Comment: In the legal systems of most countries, a corporation is an 'artificial person'. As such, they have a great number of legal responsibilities. In English law, a company can even be found to have committed a criminal offence. Therefore, do you think Friedman is correct to argue that a business cannot have responsibilities?

Friedman's second argument:

1. Individual proprietors and corporate executives are persons [presumably he means 'natural persons' to distinguish them from artificial persons].
2. A [natural] person can have responsibilities.
3. Therefore, individual proprietors and corporate executives may have responsibilities.

At this point he focuses only on corporate executives.

Friedman's third argument:

1. A corporate executive is an employee [agent] of the owners of the business.
2. The owners of the business are the shareholders [principals].
3. Therefore, the corporate executive's primary responsibility is to conduct the business in accordance with the desire of the shareholders.
4. The desire of the shareholders is to make as much money as possible.

Comment: The last point is a question of fact which may or may not be true. While investors will typically wish to maximise their income and gains, they may not wish to do so in a way which, for example, causes long-term damage to the environment or involves mistreating employees or the societies in which the company operates.

Friedman's fourth argument:

1. A corporate executive is a person in their own right.
2. As a person, he/she may have other responsibilities, including 'social responsibilities'.
3. In respect of such responsibilities the corporate executive is the principal not the agent.
4. But when acting as agent, his/her first responsibility is to the principal(s).
5. The desire of the principals is to make as much money as possible.
6. Therefore, the 'social responsibilities' are those of the individual, not the business.

Comment: This argument rests on Friedman's assertions that: (1) a company is not a person and therefore cannot have its own moral responsibilities; (2) the primary responsibility corporate executives have is to stockholders; and (3) the sole desire of stockholders is to make as much money as possible.

Friedman's fifth argument:

1. 'Social responsibilities' might include acting to (a) keep prices down to prevent inflation, (b) incurring expenditure on reducing pollution

- in excess of legal requirements, or (c) employing the 'hardcore' unemployed.
- 2. If the corporate executive acts in such a way, he is spending 'someone else's money'.
- 3. This is in effect a tax.
- 4. Taxes can only be imposed by the government.

Friedman's sixth argument:

- 1. A corporate executive is an expert in running a company.
- 2. He/she is not an expert in managing inflation or of reducing pollution, or looking after the interests of the 'hardcore' unemployed.
- 3. Acting other than in the interests of shareholders may have unforeseen consequences (e.g., diverting spending power elsewhere or creating stock shortages).

Friedman's seventh argument:

- 1. It may be in the long-term interest of a corporation that is a major employer in a community to devote resources to providing amenities and making charitable contributions.
- 2. This is done in the interests of the business, not 'social responsibility' (the doctrine of 'social responsibility is a cloak').

Problems with the Friedman doctrine

There are several difficulties with Friedman's arguments. In what follows I identify three issues in particular.

Do shareholders own companies?

The American economist Margaret Blair contends that: 'The common assertion "shareholders are the owners" of large corporations is a highly misleading statement that often does more to obscure the important issues than to illuminate them.'⁷⁰ Shareholders own shares, not companies, and their property rights are limited to receiving dividends (but only if declared by directors), to vote on certain matters of importance, including the appointment and reappointments of directors (but only from a slate of candidates proposed by the board), and to veto major transactions (but only if a coalition of shareholders representing the necessary proportion of total votes prescribed by law can be assembled). They also have the right to receive residual assets in a winding-up, but this rule rarely operates in practice: public companies tend only to be wound-up when bankrupt, when there are often no residual assets. Shareholders are not automatically entitled to enter company premises, to

use company assets, or to arrange transactions on the company’s behalf; they surely would be if they were genuinely a firm’s ‘owners’. In all, only five of the ‘badges of ownership’ which we met in Chapter 1 are satisfied by minority shareholders of a public company: the rights to income, capital, security, the absence of term, and the incidence of residuary.

Consider also the balance sheet of ExxonMobil, one of the world’s largest publicly traded international oil and gas companies (see Figure 2.2). You will notice that, of 8 million shares in existence, 4 million have been repurchased and are owned by the company. If owning shares in ExxonMobil constitutes owning the company, then half the company is owned by itself. Legal scholar Meir Dan-Cohen illustrates the problem with a thought experiment: the story of the ‘personless corporation’. Imagine a company that is so highly profitable that its managers decide to repurchase all the shares, so that the company becomes an ‘ownerless’ corporation. (The laws of most countries would prevent this, but the story of the personless corporation is a thought experiment, so some philosophical licence is permitted.) Advances in technology eventually lead to automation of the manufacturing activity, a sharp reduction in staff levels, and computerisation of all management functions. Finally, the few remaining managers realise that there is nothing left for them to do and decide to retire, leaving a person-less, shareholder-less, corporation run by machines. Who owns the company then?

In philosophical terminology this is called an ‘ontological’ question. Ontology concerns the nature of being and existence. It seeks to classify and explain the nature of different entities. For the avoidance of any doubt, it is important at this stage to point out a difference between public and private companies. While a case can be made in a private company with a small number of shareholders that ownership of shares constitutes ownership of the company, the same cannot be said of a public company with widely dispersed shareholdings. A public company is an entirely different kind of entity from a private company with a small number of shareholders. The company and its shareholders are, in ontological terms, entirely distinct entities.

Figure 2.2: Extract from ExxonMobil’s 2023 financial review⁷¹

Summary balance sheet at year end	
Equity	US\$ billion
Common stock (8 million shares)	17.8
Earnings reinvested	453.9
Common stock held in treasury (4 million shares)	(254.9)
ExxonMobil share of equity	204.8

It has already been noted that, in law, companies are artificial persons which have certain legal rights and responsibilities. In the US, a landmark decision of the Supreme Court in the *Citizens United* case held that companies have a constitutional right to free speech. In *Burwell v Hobby Lobby Stores*, a private company was protected by the free exercise of religion clause of the First Amendment of the American Constitution. In the UK, companies may be found to have committed manslaughter either under common law or the Corporate Manslaughter and Corporate Homicide Act 2007.⁷²

Why does all this matter? If in the eyes of the law companies are persons with rights and responsibilities, then perhaps they have ethical rights and responsibilities as well. Michael Phillips says of corporate real entity theory – the theory that corporations are real persons:

Its acceptance would influence debates over certain legal questions and over certain issues involving the social control of corporations. In particular, if the theory is valid, the drives, interests, and obligations of the corporate group become factors that ought to be considered in some decisional contexts. More specifically, if the theory is true and if the corporate real entity assumes certain forms, corporations could have moral duties that sometimes might affect legal and policy deliberations.⁷³

Is the primary responsibility of corporate executives to stockholders?

To address this issue, we need to answer a question posed by political philosopher, David Ciepley. Where does the board of directors of a company get its authority from? Is it really delegated to them by stockholders?⁷⁴

Until the early part of the 19th century, business firms in the US and UK could, legally speaking, be organised in one of three separate ways: as a partnership, as an unincorporated company, or as a corporation (i.e., an incorporated company). Partnerships were organised under contract law and unincorporated companies were organised by vesting assets under the supervision of trustees by deeds of settlement. (Hence the common description, especially in the US, of unincorporated companies as ‘trusts’. Trusts were also used by the likes of John D. Rockefeller and J.P Morgan to consolidate power over groups of otherwise separate corporations.) Corporations were formed by Act of Parliament (State legislatures in the US) or through a legal charter granted by Parliament or the Crown. The earliest examples of large corporations were the great chartered trading companies, for example the Muscovy Company (which was given a Royal Charter by Mary I of England in 1555), the East India Company (founded in 1600), and the Hudson’s Bay Company (founded 1670). Provision of a charter was often accompanied by granting monopoly trading rights over a particular geographical region.⁷⁵ The state,

through a charter or Act of Parliament, granted a corporation's board the right to control property, hire and fire personnel, and manage the firm.

Thus, according to David Ciepley, the board derived its authority from the government rather than from stockholders. Ciepley argues that the same is true today. Corporations are incorporated under laws enacted by the state, even if nowadays they are only occasionally established by charter or Act of Parliament. The business corporation is, therefore, a way in which the state delegates authority to a group of people (the board of directors), which then undertakes activities of which the state approves.⁷⁶ If this argument is correct, then corporations also have important obligations to the state, not just to stockholders.

Perhaps employees have property rights in a firm as well. Just as shareholders provide financial capital, so arguably employees provide human capital. Margaret Blair and Lynn Stout argue that anyone making 'firm-specific investments in a firm obtains property rights in their joint production.'⁷⁷ We will explore this argument further in Chapter 4.

Is the only desire of stockholders to make as much money as possible?

For some investors, including certain pension funds and asset managers, climate change is rapidly becoming as relevant a factor in investment decisions as traditional financial considerations.⁷⁸ While it was reasonable for Milton Friedman to assume in 1970 that the only desire of stockholders was to make as much money as possible, it no longer seems safe to assume this. Many institutional investors now issue statements explaining how they incorporate climate change pledges into their investment decisions. Figure 2.3 is an extract from the Climate Impact Pledge of LGIM, one of the UK's largest institutional investors.

However, ESG investing (investing which takes account of environmental, social and governance considerations) has become a political issue in the US. Some Republican-led states, including Florida, Louisiana, and Missouri, have withdrawn funds managed by BlackRock because the investment firm's ESG investment policies. This is notwithstanding BlackRock's claim in 2024 that its 'role in the transition to a low-carbon economy is as a fiduciary. We seek the best risk-adjusted returns for clients, and we rely on a research-based view of economic developments, including how the low-carbon transition is likely to unfold in practice over time.'⁷⁹

The second formulation of the Friedman doctrine

We now turn to the second formulation of the Friedman doctrine, in which a more significant logical flaw will become apparent. The second formulation of the doctrine is subtly different from the first.

Figure 2.3: Extract from LGIM's climate change pledge⁸⁰**LGIM Climate Impact Pledge**

Climate change is one of the defining issues of our time. In recognition of its potentially catastrophic outcomes for the world – and our clients' assets – we support efforts to limit carbon emissions to net zero by 2050. Under our Climate Impact Pledge, we commit to helping companies to reach this objective.

Assessment criteria

From LGIM's total corporate holdings of around 11,000 companies worldwide, we have mapped over 5,000, in climate-critical sectors, against key indicators. Using quantitative and qualitative measures, we assess them under a 'traffic light' system, drawing on independent data providers and our pioneering climate modelling.

These metrics inform our direct engagements. We will take action against companies that fail to demonstrate adequate climate commitments, through our voting rights across our entire book and investment decisions within some of our funds. We will celebrate successes, too.

An urgent challenge

As a collective problem, climate change requires collective solutions – urgently. On behalf of our clients, we are taking decisive action to meet the goal of net zero, from our investment processes and solutions to our engagement with companies and our collaboration with other investors.

A corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the *basic rules of the society, both those embodied in law and those embodied in ethical custom* [my emphasis].⁸¹

In this second formulation, Friedman makes shareholder value maximisation contingent on 'conforming to the basic rules of society', taking into account 'both law and ethical custom'. It should be apparent that Friedman has committed the fallacy of assuming the truth of the proposition he is trying to prove – an example of 'begging the question', a logical fallacy first identified by Aristotle in the *Prior Analytics*.

If it is ethical custom that shareholder value should be maximised without regard to any other factors, then Friedman's argument is correct, but unnecessary, since the principle has been established already. If, on the other hand, it is widely accepted that company managers should have regard to social factors such as employment levels and reducing anthropogenic climate change, then Friedman's argument fails.

That 'ethical custom' has perhaps changed since 1970 is evidenced by a statement issued by the American Business Roundtable in 2019. The Business

Roundtable is an association of chief executive officers of major US companies. It addresses issues relating to corporate governance, economic policy, and business practices. In August 2019 the Business Roundtable published a statement in which it renounced its long-standing principle that ‘corporations exist principally to serve shareholders’. The revised statement of purpose is set out in Figure 2.4.

In August 2024, the Business Roundtable published an update on the August 2019 statement with the title ‘Five years on: corporate purpose and profit’. This cites: ‘countless undertakings by America’s most successful companies

Figure 2.4: Business Roundtable redefines the purpose of the corporation

Statement on the Purpose of a Corporation

Americans deserve an economy that allows each person to succeed through hard work and creativity and to lead a life of meaning and dignity. We believe the free-market system is the best means of generating good jobs, a strong and sustainable economy, innovation, a healthy environment and economic opportunity for all.

Businesses play a vital role in the economy by creating jobs, fostering innovation and providing essential goods and services. Businesses make and sell consumer products; manufacture equipment and vehicles; support the national defense; grow and produce food; provide health care; generate and deliver energy; and offer financial, communications and other services that underpin economic growth.

While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:

- Delivering value to our customers. We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
- Investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.
- Dealing fairly and ethically with our suppliers. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.
- Supporting the communities in which we work. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.
- Generating long-term value for shareholders, who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.

Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country.

Business Roundtable August 19, 2019⁸²

[which] demonstrate that a company's commitment to stakeholders and profit go hand in hand'.⁸³ The paper concludes that 'when the Business Roundtable statement was announced in 2019, *Fortune* ran a headline, "Profits and purpose: can big business have it both ways?" The answer is yes – companies can and must'.⁸⁴ While not all investors agree, and the empirical evidence on the topic is far from conclusive, the August 2024 paper shows that the Business Roundtable is very committed to the August 2019 statement on the purpose of the corporation.

Rescuing shareholder primacy

The doctrine of shareholder primacy has been found wanting. Nevertheless, a number of arguments can be made in its defence. Michael Jensen has pointed out that a single value objective is a prerequisite for purposeful or rational behaviour. As he puts it, 'it is logically impossible to maximize in more than one dimension at the same time unless the dimensions are monotonic transformations of one another'.⁸⁵ In economics, monotonic transformations of functions are those which are order-preserving, involve one-to-one mapping, and do not give rise to a change in relative ranking. What Jensen means is that any attempt to maximise two or more objectives at the same time is only possible if the two functions are very strongly aligned. The implication of what he is saying is that, when it comes to a company with multiple objectives, this is unlikely to be the case except in very rare circumstances. Ample empirical evidence in support of this claim can be found in the financial performance of many state-owned enterprises; see, for example, the cases discussed in Andrei Shleifer and Robert W. Vishny's book *The Grabbing Hand*.⁸⁶ State-owned enterprises have often encountered financial difficulties because they had multiple objectives – political and social objectives, as well as financial ones. For example, in the UK, British Coal (formerly the National Coal Board) and British Steel (formerly the Iron and Steel Corporation of Great Britain) were perennial loss-makers after they were nationalised in 1947 and 1967, respectively.⁸⁷

Furthermore, stakeholder theory, the main alternative to shareholder primacy, which argues corporations have multiple constituencies to whom they owe social and ethical as well as financial responsibilities, has problems of its own, as we will find out in Chapter 3.

Dialogue II: Socrates and Milton

In which Socrates and Milton Friedman discuss the purpose of the corporation and stakeholder theory

Figure II: When Socrates met Milton Friedman



Source: Tim Wakeling.

Socrates has been on the lookout for Milton for a few days. He finds him reading the Wall Street Journal at a cafe by the Agora in Athens Archaeological Park.

SOCRATES: Milton, how nice to see you.

MILTON: Hello, Socrates, I'm Milton Friedman, the economist.

SOCRATES: I know, that's why I said 'hello, Milton'.

MILTON: It's just that last time you confused me with a poet.

SOCRATES: You? Milton, that seems most unlikely. Anyway, I've been wanting to talk to you.

MILTON: Really?

SOCRATES: Yes, I've been thinking about what you said in our last conversation. I have also been reading some of your stuff. You have written a lot haven't you – academic papers, books, *etcetera*? Strange that the thing everybody talks about is an article that you wrote in a newspaper.

MILTON: It was based on solid research. Anyway, my recollection is that you didn't write anything. You just talked a lot.

SOCRATES: Different era, Milton. Anyway, to the point. We were talking about the purpose of the corporation, and you raised some interesting issues. I was able to pick out two arguments in particular.

MILTON: If you say so.

SOCRATES: The first argument was about the exact meaning of the word 'purpose'.

MILTON: Okay.

SOCRATES: The second was about the people who can affect or are affected by the achievement of the organisation's objectives. I gather that they are known as 'stakeholders'.

MILTON: That old chestnut. And the way you have expressed it sounds suspiciously like a quote.

SOCRATES: It is, but in any case, I think the stakeholder question is for another day. What I would like to do first is focus on the word 'purpose'. You will be interested to hear that there is a specific branch of philosophy which examines questions of purpose. It's called 'teleology', from the Greek word *télos*, which means 'purpose' or 'final cause'. Aristotle used the term *télos*, as he explored the ultimate causes of things, be they entities, or organisms, or human works of art. So teleology is the study of ends or final causes.

MILTON
(yawning): Okay, I'm with you so far.

SOCRATES: Let's consider two extreme positions. First, everything has a purpose. Second, nothing has a purpose. In Western philosophy the first position is, you won't be surprised to hear, most closely associated with Aristotle. He believed that everything has a purpose. This includes inorganic

things, like chairs and tables, but also organic things, like eyes and arms. The idea that everything has a purpose was key to Aristotle's understanding of the nature of reality, his ontology, in philosophical terms. It is also a key part of his theory of knowledge, his epistemology. To understand something we have to understand its purpose. Critically, for Aristotle it was also a key part of his ethics – all deliberate human action is, or should, be believed, be aimed at the good.

MILTON: Hmm, I'm not so sure about all this. For example, what is the purpose of a tree, or a cow? To argue that they provide sustenance for humans seems to be self-evidently unduly people-centred.

SOCRATES: Well, I could perhaps try to construct a case out of biological systems theory – 'everything has its place in the circle of life', and so on – but I might be stretching the point. In any case, I think you're probably right: modern science is on the whole hostile to teleological explanation. Francis Bacon, one of the founders of modern scientific method in the 17th century, put it rather nicely like this: 'enquiry into purposes is sterile, and, like a virgin consecrated to God, produces nothing'.

MILTON: Strong stuff. I bet he said it in Latin too.

SOCRATES: He did. Anyway, contemporary scientists are of much the same mind. For example, chaos theory postulates that complex phenomena can be the result of apparently random small acts.

MILTON: The flapping of a butterfly's wings altering the path of a tornado?

SOCRATES: Exactly.

MILTON: Aren't we drifting off the point? We were talking about the purpose of the corporation.

SOCRATES: Okay, I'm sorry, I do tend to get carried away. Let's get back to the main argument. Whatever the position of natural phenomena, would you accept that it is reasonable to assume that the majority of things made by humans do have, or should have, a purpose?

MILTON
(cautiously): Yes.

SOCRATES: So a company, which is a human construct, has, or should have, a purpose?

MILTON: I suppose so, and as I think about it, it would be true to say that the charter companies of the 16th, 17th and 18th centuries were all established for a particular purpose. For example, the purpose of the British East India Company was: 'to venture in the pretended voyage to the East Indies, the which it may please the Lord to prosper'.

SOCRATES: You've just looked that up on your 'phone.

MILTON: And in the Anglo-Saxon legal tradition companies have to state their purpose in the objects clauses of their constitutions or articles of association, although I think that principle has become rather watered down in recent years. And modern companies have mission statements, of variable quality it has to be said, which are designed to explain their purpose.

SOCRATES: Before you go any further, don't you think we need to define what is meant by 'purpose'?

MILTON: If we must.

SOCRATES: A dictionary definition of purpose would be something like this: One, the reason why something is done, created or exists. Two, an idea or outcome which is the object of action or effort. Three, fixed intention, as in 'a man of purpose'. Four, practical advantage or use, as in 'to work to good purpose'. Five, that which is relevant, as in 'to the purpose'.

MILTON: Okay.

SOCRATES: To simplify, we might say that purpose means either, first, 'the reason why something exists', picking up one above, and/or secondly, 'a call to action', which picks up two, three, four, and five.

MILTON: I agree.

SOCRATES: Actually, I think there is a third possible meaning, which is associated with Aristotle's idea that all deliberate human action is, or should be, aimed at the good. This might summarised as 'a call to virtuous action'. Whether the call to action needs to be good is a separate question, which I suggest we come back to.

- MILTON: If we must.
- SOCRATES: The word 'good' is quite interesting actually. What do you think of when people talk about 'a good'?
- MILTON: Well, to an economist, a good is a noun meaning a thing of value – any physical object, natural or manmade, or service rendered, that could command a price in a market.
- SOCRATES: Interesting. Can I ask what you mean by 'value'?
- MILTON: In economics, 'value' means something of worth. This is sometimes further subdivided into either 'value in use', being the pleasure or welfare that a commodity generates for its owner, or 'value in exchange', being the quantity of other commodities (or more usually money) for which something can be exchanged.
- SOCRATES: Good – oh, sorry, for the avoidance of confusion, I should of course say 'thank you' rather than 'good'.
- MILTON: Very funny.
- SOCRATES: Now in ethics, on the other hand, the *good* is a normative concept, meaning 'that which conforms to the moral ideal'. For example, Plato defines 'the good' in his theory of forms as 'a perfect, eternal, and changeless entity existing outside space and time, in which particular good things share'. The philosopher John Rawls also talks about 'social goods', such as freedom and equal opportunities, which he saw as more fundamental to leading a good life. And in ethics, value(s), more often discussed in the plural, are the basic and fundamental beliefs that guide or motivate attitudes or actions. Values help to determine what is important to us. They are personal qualities that we choose to embody to guide our actions.
- MILTON: Where is all this going?
- SOCRATES: What I am trying to explain is that, just as economists and philosophers use 'good' and 'value' in a completely different way, so in the debate about 'corporate purpose', people have confounded, one, 'the reason why something exists' and two, 'a call to action', with three 'a call to virtuous action'.
- MILTON
(cautiously): So when I say, 'the purpose of a company is to maximise shareholder value', I suppose that this ticks the box for the first part of our definition of purpose.

SOCRATES: Yes, but it's hardly a call to action, is it? Employees are hardly likely to rally round a CEO who says: 'our job as a company is to make shareholders rich!' And customers are unlikely to be sympathetic to a company with the mission statement: 'We exist to make investors lots of money'. It seems to me that a statement of purpose like that would inevitably be self-defeating. By telling employees and customers that your purpose is to make shareholders richer, you're likely to fail to do so.

MILTON: Yes, I think I follow your line of thought.

SOCRATES: So I want to distinguish between the meaning of purpose in the sense of one and two on the one hand, and three on the other hand. There is a guy at Oxford University called Jonathan Trevor who calls the first 'mastery' and the second 'virtue'. I think that's quite a helpful distinction. Trevor talks about companies being 'aligned' when shareholders, directors, employees, suppliers, customers, and so forth are all pulling in the same direction, which is consistent with 'mastery'. You might call purpose 'super-aligned', or something like that, when it is also consistent with the good of society, social purpose, saving the planet, and so on. Hey, Milton, you're looking a bit confused.

MILTON: I guess I am a bit. Anyway, you said we needed to talk about stakeholders.

SOCRATES: We do! But I'm getting a bit tired of this discussion about corporations. I need to go and immerse myself in questions about truth, beauty, and the meaning of life for a bit of light relief. Meet tomorrow – shall we say two o'clock?

The following morning Socrates and Milton meet at the Agora as arranged to continue their dialogue.

MILTON: You wanted to talk about stakeholders?

SOCRATES: I do. You see I met a really interesting man the other day.

MILTON: Really?

SOCRATES: Well, he seemed real enough, but let's not get metaphysical. He had long beard, and looked like an ancient philosopher, though he called himself a 'pragmatist'. He had a surname like yours, you know, 'Friedman'. I wondered if he was a relative? Anyway, we were chatting about

shareholder primacy and what's a business for, as you do, and he said he'd sorted all that out a long time ago. He told me all about it – called it 'stakeholder theory'. Tried to get me to buy his book on strategic management.

MILTON: That'll be Ed Freeman.

SOCRATES: A relative?

MILTON: It's 'Freeman', not 'Friedman'. He's a professor of business administration at Darden Business School.

SOCRATES: Really?

MILTON: Now who's being metaphysical? Anyway, let's explore this stakeholder theory stuff a bit further. Let me see if I can turn the tables on you.

SOCRATES: What tables?

MILTON: It's a metaphor, Socrates. Think backgammon in the Middle Ages. I'm going to try using your technique to make you think again.

SOCRATES: I'm mildly flattered. Do give it a go.

MILTON: First of all, we need to define our terms. What do you mean by 'stakeholders'?

SOCRATES: Well, Freeman defines a stakeholder in an organisation as 'any group or individual who can affect or is affected by the achievement of the organization's objectives'.

MILTON: Is that organization with a 'z' or with an 's'.

SOCRATES: A 'z' obviously. He's American.

MILTON: Just checking. So that would include employees, right?

SOCRATES: Certainly.

MILTON: And suppliers?

SOCRATES: Yes.

MILTON: And customers?

SOCRATES: If it was a commercial organisation, yes it would.

MILTON: So a stakeholder is anyone with a financial interest in a company?

SOCRATES I suppose so.
(cautiously):

- MILTON: Now would you agree that an employee's financial interest is satisfied through payment of a fair wage, a supplier's financial interest through receiving a fair price for the goods or services they are providing, and a customer's financial interest through paying a fair price for the goods or services they are receiving?
- SOCRATES: It depends on what you mean by 'fair', but in principle, yes, I suppose so.
- MILTON: Now in a market economy we know that prices are determined by the law of supply and demand. This is true of labour markets as well as markets for products and services. According to general equilibrium theory markets are interconnected, so that a change in one market, like the labour market, impacts on other markets, such as the market for goods. Also in general equilibrium, resources are allocated in a way such that no one can be made better off without making someone else worse off. This principle, which is called Pareto efficiency after the Italian economist Vilfredo Pareto, is a core principle of general equilibrium theory. It means that in an efficient market economy everyone gets their fair share.
- SOCRATES: Whoa, hold on a minute. There you're making a lot of assumptions here. We need to think about this a bit more.
- MILTON: Maybe, but it's good economics. Anyway, let's try something else. According to your definition of 'stakeholders' there is a bunch of other people who might fit under this heading. Competitors can also affect or be affected by the achievement of a company's objectives, as can the state, the media, and the general public, in fact practically everybody.
- SOCRATES: It's a very broad definition.
- MILTON: And they all have an interest in the company?
- SOCRATES: Yes.
- MILTON: So everyone has an interest in every company?
- SOCRATES: I suppose so.
- MILTON: This is all getting a bit absurd isn't it. How are the managers of a company to choose between all these competing interests, especially when the interests aren't mediated by the price mechanism. A man with two

masters serves only himself, and all that stuff we talked about the other day. Economists call this the agency problem.

SOCRATES: I see.

MILTON: And, for the avoidance of doubt, I recognise that what an economist calls a fair allocation might not be deemed as such by a moral philosopher.

SOCRATES: Indeed

MILTON: So there we have it, a *reductio ad absurdum*. Stakeholder theory gets us nowhere, so we had better stick with shareholder primacy, albeit it revised for Jonathan Trevor's concepts of 'mastery' and 'alignment'. Full stop. End of story.

SOCRATES: I don't think so, Milton, but you've certainly learnt some good debating techniques. I'd like to mull this over. Let's meet again tomorrow.

MILTON: Shall we say two o'clock?⁸⁸

3. Stakeholder theory

The stakeholder approach to the moral responsibilities of managers underlies most ESG (environmental, social, and governance) approaches as practised by corporations around the world. According to the stakeholder theory, managers have moral responsibilities towards all the stakeholders of their business, and the interests of different stakeholders need to be carefully assessed and balanced against each other. In this chapter I examine stakeholder theory, discuss why the stakeholder approach is importantly incomplete, and consider how it might be rescued.

Stakeholder theory is a view of capitalism that stresses the importance of the relationships between a company and its employees, customers, suppliers, investors, communities, and others who share an interest in the business. Its main thesis is that a firm should create value for all stakeholders, not just for shareholders. A subsidiary thesis is that ethical as well as economic considerations have a part to play in determining what constitutes business success.

I begin this chapter with the black and white photographs of three famously bearded men (Figure 3.1). The first photograph is of the great Russian writer Leo Tolstoy (1828–1910). In his novels, short stories, and essays, Tolstoy directly

Figure 3.1: Three bearded men



Sources: Left by Karl Bulla, public domain; centre: permission courtesy Stephanie Gross Photography; right; Houghton Library, Harvard University, public domain.⁸⁹

and indirectly poses the question 'how shall we live?' A notable example is in the short story *Three Questions*, published in 1885, in which Tolstoy recounts the tale of a king who is convinced that he will succeed in any endeavour if he knows the answer to three questions: (1) When is the right time for action? (2) Who are the right people to listen to? (3) What is the most important thing to do? The king learns the answers from a hermit and by saving an injured man who had, in fact, intended to harm him. The time to act is now. The most important people are those you are with at the moment. The most important thing to do is good.

The second picture is of R. Edward Freeman, an American philosopher and professor of business administration at Darden School of Business, University of Virginia. Freeman is the source of many of the ideas set out in this chapter. In 1984 he advanced the stakeholder theory of business management in his book *Strategic Management: A Stakeholder Approach*. He identifies the people who are key stakeholders in any organisation and argues that managers must give proper regard to the diverse interests of all them.

The identity and relevance of the person in the third photograph will be revealed in due course.

Freeman argues that Tolstoy's question 'how shall we live' must be answered by every businessperson. He also believes, like Tolstoy, that there is an important ethical component to the question. Freeman puts it like this: 'We need to dissolve the distinction between [management] science and ethics, keeping what is best and most useful about each'. Freeman believes that adhering to a rigorous fact-value dichotomy, a distinction favoured by neo-classical economists and advocated, most notably, by the economist Lionel Robbins in his influential *Essay on the Nature and Significance of Economic Science*, makes no sense. Answers to the question 'what is a company for', he says, inevitably involve an ethical component.

Freeman's thesis is that businesses have a responsibility to help solve the world's problems. They cannot just leave it all to governments. Resource allocation efficiency is only one desirable societal objective; others include liberty, equality of opportunity, fair distribution of benefits and burdens, protection of individual rights, and preservation of common pool resources. The responsibility of executives is to create as much value as possible for everyone, but to do so in a socially responsible way. In the long run, that is how you create the most value for shareholders. In the short run, the interests of different stakeholders may come into conflict. There may be trade-offs. The job of the manager is to find ways of resolving trade-offs and conflicts that, in the long run, serve the best interests of everyone.⁹⁰

This is Freeman's answer to Tolstoy's question 'how shall I live?'. In his book on strategic management, he goes on to address Tolstoy's question 'what is the most important thing to do?' In a sense, he is much more interested in this question, which he sees as about solving society's problems, than in dry philosophical discussions about who has a legitimate interest in defining a company's objectives and benefitting from the goods (in the broadest sense) that a company creates.

Nevertheless, he recognises the need to be rigorous in the way he develops his argument. To this end, he identifies four specific principles that underpin stakeholder theory.⁹¹

1. *The separation fallacy.* Is it useful to believe that 'X is a business decision' has no ethical content or implied ethical point of view and that 'Y is an ethical decision, the best thing to do all things considered' has no content or implicit view about value creation? Stakeholder theorists believe that this type of argument is inherently fallacious.
2. *The integration thesis.* Stakeholder theorists believe that most business decisions have some ethical content and that many ethical statements have an implied view about business.
3. *The responsibility principle.* This is the belief that most people, most of the time, want to do the right thing and accept responsibility for their actions.
4. *The open question argument.* For whom is value created, and for whom is it destroyed? Who benefits and who is harmed? Whose rights are enabled and valued realised – and whose are not? The principle that shareholder value must be maximised at all costs and that shareholder rights take priority over all others is disputed by stakeholder theorists.

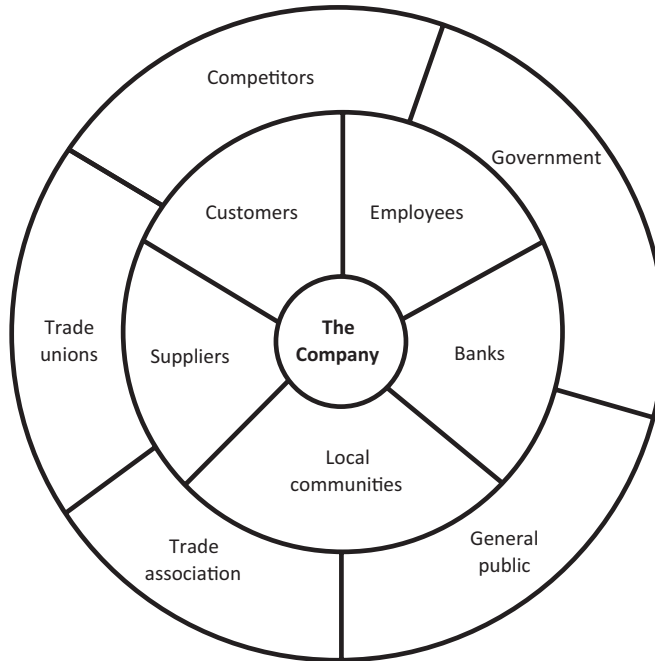
The four points build on one another: the integration thesis is a response to the separation fallacy; out of this comes the responsibility principle, which in turn provides an answer to the open question argument. In short, executives have a responsibility to create value for all stakeholders.

Who are the stakeholders?

Freeman defines stakeholders in the following terms: 'A stakeholder in an organization is (by definition) any group or individual who can affect or is affected by the achievement of the organization's objectives.'⁹² A later book by Freeman and a number of his associates provides a useful figure which distinguishes between primary and secondary stakeholders (see Figure 3.2).

Applications

Stakeholder theory has applications in almost all aspects of managerial activity. Corporate finance theory developed at a time when firms were asset-intensive and the boundaries of the firm were relatively clear-cut. This may not be a sensible approach to take in human capital-intensive firms, or when changing business models and funding arrangements can affect what constitutes the boundaries of the firm. How should company accounts reflect environmental impact? Is it right to account for people as a cost rather than an asset? Should

Figure 3.2: Stakeholder model

Source: Based on Freeman (2012).⁹³

employees be described as ‘partners’ or ‘colleagues’ rather than ‘human capital’ or ‘units of labour’? Is marketing about building relationships with co-creators of services rather than selling products to consumers? Do managers need to understand their own internal ‘stakeholders of the mind’, given the deep-seated human propensity to split, repress, and project parts of ourselves in ways that come into conflict in a changing social world? Managers may themselves have competing or changing preferences, some of which may be buried in the subconscious and may not be consistent with the principle of maximising shareholder value.⁹⁴

Problems

Stakeholder theory, like shareholder primacy, is not without its shortcomings. Thomas Donaldson, professor of legal studies and business ethics at the Wharton School, University of Pennsylvania, puts it like this:

Despite its important insights, the stakeholder model has serious problems. The two most obvious are its inability to provide standards for assigning relative weights to the interests of various constituencies, and its failure to contain within itself, or make reference to, a normative, justificatory foundation.⁹⁵

A third problem is what exactly is meant by the term 'stakeholder' which, unlike 'shareholder' or 'stockholder', has no direct reference point in company law. Hence we need to address three questions:

1. Philosophical foundations – what type of theory is stakeholder theory?
2. The problem of stakeholder identification – who are the stakeholders?
3. The problem of adjudication between stakeholders – how do we determine who gets what?

Philosophical foundations

It is time to reveal the identity of the person in the third photograph. It is the American philosopher William James (1842–1910) who, with Charles Sanders Peirce (1839–1914) and John Dewey (1859–1952), founded the philosophical school known as pragmatism. Peirce (pronounced 'purss') also sported a fine beard, although it wasn't a requirement, as John Dewey was clean-shaven. Whereas the majority of Anglo-Saxon philosophers of the late modern era believed that philosophy involved the systematic study of fundamental topics such as existence, reason, knowledge, values, mind, and language, the American pragmatists viewed language and thought as tools for problem solving, prediction, and action. A later pragmatist philosopher, Richard Rorty (1931–2007), put it like this:

Pragmatists ... ask the practical question, 'Are our ways of describing things, or relating them to other things as to make them fulfil our needs more adequately, as good as possible? Or can we do better? Can our future be made better than our present?'⁹⁶

Freeman and his various supporters and associates are management scholars operating within the pragmatist tradition. About stakeholder theory, they write:

Some have argued that it is not a 'theory' because theories are connected sets of testable propositions. Others have suggested that there is just too much ambiguity in the definition of the central term for it ever to be admitted to the status of theory. Still others have suggested that it is an alternative 'theory of the firm', contra the

shareholder theory of the firm ... As philosophical pragmatists we do not have much to say about these debates. We see 'stakeholder theory' as a 'framework', a set of ideas from which a number of theories can be derived.⁹⁷

This position has provoked much debate. In 1995, Thomas Donaldson and Lee Preston were the first to acknowledge that stakeholder theory has three distinction perspectives:

1. Descriptive – research that makes factual claims about what companies and managers actually do.
2. Instrumental – what should companies and managers do in a strategic sense.
3. Normative – research that asks what companies and managers should do in an ethical sense.⁹⁸

In an article in the *Journal of Business Ethics* entitled 'The moral basis of stakeholder theory', Kevin Gibson calls these three perspectives 'agency', 'prudential', and 'deontological', respectively.⁹⁹ The first perspective, descriptive or agency stakeholder theory, is consistent with the perspective taken by positive economics – it deals with factual statements and objective analysis without making value judgements. Instrumental or prudential stakeholder theory is about what is the best thing to do in terms of business strategy, but discounting any ethical questions. Normative or deontological stakeholder theory incorporates an ethical perspective in addressing questions of what ought to be done.

Freeman objects to this typology. In his own words:

I have suggested ... that relying heavily on a fact-value, or descriptive-normative, distinction is a form of separation thesis ... The overwhelming logic to drop this distinction is pretty simple. By choosing to call groups 'stakeholders' rather than 'interest groups' ... we have already mixed up 'fact' and 'value' ... The very idea of a purely descriptive, value-free, or value-neutral stakeholder theory is a contradiction in terms. Why, then, ... claim that the Donaldson–Preston tripartite typology is useful, when plainly it relies on an outmoded, non-pragmatist method? ... The debate between deontologists and consequentialists is long, historical, and tedious, and it depends on more philosophical dualisms that are not terribly useful.¹⁰⁰

Stakeholder identification

The problem with Freeman's definition of stakeholder is that, because of the way it is framed, it is difficult to know where the boundaries are. For a category to be useful, the criteria for determining who is in and who is out must

be clear. In particular, Freeman's inclusion of those who are 'affected by' as well as 'can affect' ... 'the achievement of the organization's objectives' has troubled some commentators. Freeman rather lays himself open to challenge when he writes:

For instance, some corporations must count 'terrorist groups' as stakeholders. As unsavory as it is to admit that such 'illegitimate groups' have a stake in our business, from the standpoint of strategic management, it must be done.¹⁰¹

Robert Phillips questions this in two ways, posing what is sometimes called 'the terrorist objection' when he writes:

Stakeholder theory ... has no means of determining who are and who are not stakeholders in the moral sense ... It has been suggested that groups as disparate as terrorists, competitors, and the natural environment be considered stakeholders. In fact it would seem that current theory is unable to rule out any group from stakeholder status ... if everyone is a stakeholder of everyone else, how useful is the term 'stakeholder' itself?¹⁰²

Freeman's point is that the strategies of business leaders need to take account of any person who has the potential to affect business outcomes. While this is undoubtedly true, does it necessarily make them 'stakeholders'. The first problem is: where do you draw the line? If anyone who is 'affected by' an organisation is a stakeholder, then the category 'stakeholder' is very wide indeed. Hence, is the stakeholder concept really of any use? Secondly, there is an ethical objection: surely stakeholders must have some moral standing and legitimacy if they are to be regarded as having a genuine 'stake' in an organisation?

To explore this problem further, let's have a look at two case studies: the 'Janesville dilemma' (Figure 3.3) and 'Just Stop Oil' (Figure 3.4).

The Janesville dilemma is an example of an all-too-common problem. If a company's directors have to choose, in the teeth of a recession, between protecting employment, maintaining the company's presence in all the communities in which it currently operates, and paying a dividend, then they are expressing a preference between the utility of employees, the utility of other residents in local communities, and the utility of shareholders. This has been described as 'the multi-principal problem', of which it has been said: 'a manager told to serve two masters has been freed from both and is answerable to neither.'¹⁰³ Freeman has suggested that managers must 'act like King Solomon' in adjudicating among the claims of various stakeholder groups. The risk is that giving managers such freedom to balance rival claims would create extraordinary agency risks. Too much freedom of choice might allow managers to act in their own interests, rather than in the best interests of shareholders.

Figure 3.3: The Janesville dilemma

In 2008 Janesville, Wisconsin, about 100 miles north-west of Chicago, had a population of around 60,000 in 25,000 households. From 1919 to 2009 it was home to the Janesville Assembly Plant, an automobile factory owned by General Motors. At its peak, the GM plant had employed 7,000 people, although by 2008 the number had fallen to 3,000. Secondary employment, in shops, schools, and other service industries, meant that thousands of other jobs were dependent on the GM factory which was, according to Amy Goldstein 'the heart and economic soul of this small southern Wisconsin city'.

In 2008 the Board of General Motors faced a major problem. Over-capacity in the US automobile industry, combined with high fuel prices meant, that sales of SUVs, such as the Chevy Tahoe assembled in Janesville, were particularly slow. At GM's annual shareholder meeting in June 2008, chief executive officer Rick Wagoner announced that the Janesville assembly plant would close, along with three other GM factories. By 2009, after the last Chevy Tahoe had rolled off the assembly line, unemployment in Janesville had risen to 13% of the population.

The closure of the GM assembly line and its impact on the community became the subject of an award-winning study by journalist Amy Goldstein.¹⁰⁴

Figure 3.4: Just Stop Oil

Just Stop Oil is a British environmental activist group focusing on anthropogenic climate change. Founded in 2022, the group launched a series of protests targeting oil companies and the British government. These included blockades of critical oil facilities in the south-east England, stopping and surrounding oil tankers to cause motorway congestion, sabotaging petrol pumps at M25 motorway service stations, and attempting a track invasion at the 2022 British Grand Prix. In October 2022, supporters of Just Stop Oil climbed the Dartford Crossing, bringing the M25 between Essex and Kent to a standstill. In November of that year, demonstrations at multiple junctions on the M25 led to further road closures. The group have also carried out a series of protests in art galleries around London. Citing the sponsorship of the arts by BP and other major oil companies, supporters glued themselves to the frames of Vincent van Gogh's *Peach Trees in Blossom* at the Courtauld Institute of Art, John Constable's *The Hay Wain* at the National Gallery, and Leonardo da Vinci's *The Last Supper* at the Royal Academy of Arts. In 2023, protesters representing Just Stop Oil turned their attention to sporting events, including the second cricket test match of The Ashes between England and Australia, the tennis Wimbledon Championships, and the Open Championship at the Royal Liverpool golf club in Hoylake.

Just Stop Oil is a non-violent, direct action and civil resistance group opposed to the development, exploration, and production of fossil fuels. They believe, many would argue quite justifiably, that state-sponsored action to tackle climate change is proceeding too slowly, and that the kind of radical interventions they favour are therefore justified.

What is your analysis of these two cases? If employees are stakeholders, as many would argue, was the GM board right to close the Janesville assembly plant, given the predictable highly devastating impact on the local economy?

If not, what was the alternative? If citizens are stakeholders in major companies, then shouldn't boards of directors recognise their legitimate concerns about climate change? Does this justify the actions of Just Stop Oil, particularly those directed at oil and gas companies?

The adjudication problem

One of the advantages of shareholder primacy is clarity when it comes to the allocation of resources. Under perfect competition, factors of production receive a return which is determined by market forces. Labour is paid the rate for the job determined by the relevant labour markets. Suppliers are paid for the goods and services they provide according to the prices determined in competitive goods and services markets. Product markets determine the prices that companies can charge to their customers. Lenders are paid a market interest rate. Shareholders take whatever residual profit is left over. If this is out of tune with equity markets, then some of them will sell their shares until the share price and dividend yield comes into line with market rates. What could be simpler than that?

But a problem arises when we muddy the rights of different factors of production. Employees might be entitled to share in residual profits. Suppliers might be entitled to favourable terms of trade. How then are surpluses to be shared in an appropriate way between different stakeholders? Who decides on the method of allocation? And these problems are compounded given that, in the real world, companies operate under imperfect competition in markets that do not necessarily work efficiently. This is the 'adjudication problem'.

Conclusion

Even if we have made some progress in solving the foundational problem (i.e., what are the underlying philosophical foundations of shareholder theory), we have not solved the problem of stakeholder identity or the adjudication problem – how are we to adjudicate between the legitimate interests of different stakeholders? I turn to these two questions in Chapter 4.

Dialogue III: Socrates and Milton

In which Socrates and Milton Friedman meet in the Agora to discuss the concepts of 'mastery' and 'virtue'

SOCRATES: Hey, Milton, good to see you.

MILTON: Excuse me?

SOCRATES: It's me, Socrates.

MILTON: Sócrates, Sócrates, oh, you mean the Brazilian footballer with a medical degree, South American footballer of the year in 1983?

SOCRATES: No, Socrates the Greek philosopher. We've been having discussions about corporate purpose. We saw each other yesterday.

MILTON: It's alright, I'm just kidding, I know who you are. You don't look anything like a Brazilian footballer.

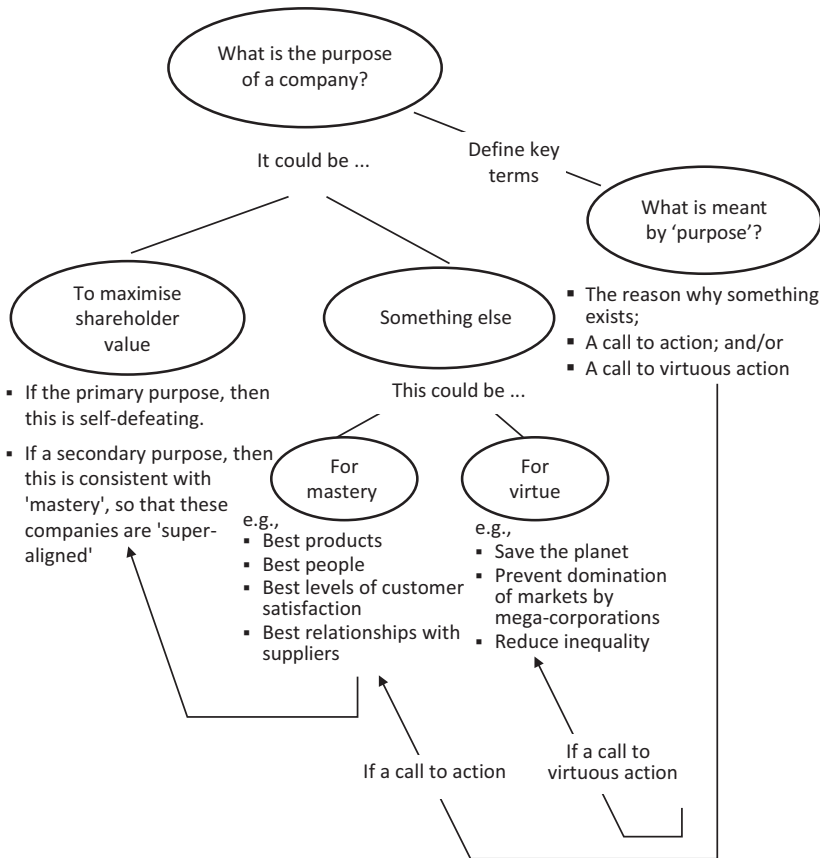
SOCRATES: I will take that as a compliment. Anyway, Milton, in I've been thinking a lot about our interesting conversation yesterday. Shall we begin by taking stock – would you like me to draw a picture to illustrate the position for you?

MILTON: A picture is worth a thousand words, and all that. How modern of you, Socrates. You'll be doing a TED talk next.

SOCRATES
(*looking
puzzled*):

MILTON: A TED talk is a recorded public-speaking presentation which was originally given at a Technology, Entertainment and Design conference, hence 'TED' ... Actually, don't worry about it – just draw your picture.

Socrates kneels and draws a picture in the sand.

Figure III: Socrates's picture about the meaning of corporate purpose

Source: Author.

MILTON: So I guess what you are saying is that there might be two alternative answers to the question about what a company's main objective should be. Either it's 'for mastery', as you describe it – a kind of souped-up shareholder primacy which embraces ideas about having the best products, best people, best levels of customer satisfaction, best relationships with suppliers, and all that jazz. Or it's 'for virtue' which incorporates ideas about saving the planet, preventing certain markets from being dominated by a small number of mega-corporations, and reducing inequality. No doubt you could also add a whole bunch of other virtuous objectives too.

SOCRATES: Let me give you another example. The Japanese have a concept which they call *ikigai*, which means 'a reason for

being' – something which gives a person a sense of purpose, a reason for living. It's derived from two Japanese words: *iki*, which means 'life' or 'alive', and *kai*, which means an effect, a result, fruit, something of worth or benefit.¹⁰⁵

MILTON: Hold on, this is anthropomorphism, isn't it? Companies aren't people.

SOCRATES: Well, that opens up an entirely new question. There is a perfectly respectable argument that says companies are persons. When we think of a natural person, we think of someone: first, located in time, with a past, a future, and a memory things gone by; second, with an identity, such that their persona is in some way recognisable to themselves and others; third, with a personality, which, barring calamitous accidents will remain fundamentally unaltered over the course of a lifetime; and fourth, with a physical presence which is observable and recognisable, although of course it changes gradually over time. I would contend that, of these features, the first and second are equally true of public corporations, which have identities (we are able to distinguish BP from Shell, and Apple from Microsoft), corporate memories (both in the sense of what is held in corporate archives as well as in the minds of long-standing employees). Some people may find it difficult to think of a corporation as having a personality, but will nevertheless be able to accept that a company has a corporate culture. As the famous organisational scholar Edgar Schein says: 'culture is to a group what personality or character is to an individual'. Schein defines culture in terms of shared beliefs, values, mental models, rituals, symbols, and history, all of which have close analogues in individual personality. Like personality, organisational culture will evolve over time, but will only rarely alter fundamentally. In terms of the fourth point, it is true to say that public corporations typically have some kind of physical presence, in terms of buildings, plants, construction sites, representative people, websites, *etc.*, even if this is rather different from what is observable when it comes to natural persons. Ian Clarke has explored at length the relationship between place and identity in multinational corporations, focusing particularly on the case of ICI. We can see the Microsoft campus in Redmond, Washington; ICI used to be identified with its Millbank Head Office in London and industrial complex on Teesside; Ford will

forever be associated with the River Rouge Complex in Dearborn, Michigan.¹⁰⁶

MILTON: Is this really relevant?

SOCRATES: In any case, the Japanese concept of self is very different from American individualism.

MILTON: Okay, but let's get back to the main point, shall we? The question we are trying to answer is, if you remember: 'what's the purpose of a company'?

SOCRATES: How about 'the purpose of a company is to maximise shareholder value'?

MILTON: Hey, I said that!

SOCRATES: You did.

MILTON: Well, I suppose that this ticks the box for the first part of our definition of purpose.

SOCRATES: But it's hardly a call to action, is it? Employees are hardly likely to rally round a CEO who says: 'our job as a company is to make shareholders rich'. And customers are unlikely to be sympathetic to a company with the mission statement: 'we exist to make investors lots of money'. It seems to me that a statement of purpose like that would inevitably be self-defeating. By telling employees and customers that your purpose is to make shareholders richer, you're likely to fail to do so. Interestingly, the American Business Roundtable changed their tune on this in August 2019, after years of focusing on shareholder value maximisation, when they redefined the purpose of a corporation as being: 'to promote an economy that serves all Americans'. And, in November 2019, The British Academy said in their report on the future of the corporation that 'the purpose of business is to profitably solve the problems of people and planet, and not to profit from creating problems'.

MILTON: Hmm. I'm reminded of an article in *Harvard Business Review* on 'The business case for purpose', which talks about purpose in terms of 'An aspirational reason for being which inspires and provides a call to action for an organization and its partners and stakeholders and provides benefit to local and global society'.¹⁰⁷ But I wonder if we are running ahead of ourselves here. This is all rather extravagant stuff, 30,000 feet and all that. We seem to

have jumped straight to ‘a call to virtuous action’, in terms of our definition of purpose. What about looking at some actual mission statements?

SOCRATES: A bit of empirical research, in other words. Not my normal approach, I can tell you, but I’m happy to go along with it.

MILTON: How about this one as a starter for 10? ‘Being the world’s premier petroleum and chemical manufacturing company’.

SOCRATES: An American oil company. Exxon?

MILTON: Quite right. And this one: ‘We strive to offer our customers the lowest possible prices, the best available selection, and the utmost convenience’.

SOCRATES: That sounds like Amazon.

MILTON: Exactly. So the stated purpose of these two companies is about as close to the classic Porterian business mission as possible – dominate the industry you’re in and thereby make as much money for shareholders as possible.

SOCRATES: Sorry, ‘Porterian’?

MILTON: Michael Porter, Harvard Business School professor who made a barrel load of money out of his books on business strategy.

SOCRATES: Oh, okay. Of course, none of these ‘mission statements’, as you call them, say that the ultimate purpose is to maximise shareholder value, do they?

MILTON: No, but don’t you agree that it’s implied that shareholder value maximisation is the outcome they are aiming for?

SOCRATES: Yes, I think that’s right. But Amazon’s mission statement also specifically mentions customers.

MILTON: It does, but in terms of offering them low prices, choice, and convenience – I would argue that this is a stereotypical neoclassical economic argument about efficiency and effectiveness.

SOCRATES: Do you know, a couple of days ago late at night I ordered a book on Amazon by a fairly obscure Orcadian poet. It arrived the following day at 4pm. Impressive, eh? But I have to tell you another story. A few months ago I bought a book called *The Curse of Bigness – How Corporate Giants Came to Rule the World*, by a guy called Tim Wu. It cost

£9.79 on Amazon, guaranteed delivery the following day by 5pm. On Bookshop.org (*buy books online to support independent bookshops*) it cost £12.08, delivery in 3 days time.

MILTON: Twenty-three percent more expensive and three times as long to deliver? You're an Amazon junkie, aren't you? I bet you bought it on Amazon.

SOCRATES: Actually it is one of the few times I used Bookshop.org instead. It seemed too paradoxical to buy a book about the curse of bigness from Amazon.

MILTON: Ha ha. Anyway, what have we learnt so far?

SOCRATES: That there are some companies who focus on scale and customer satisfaction with the tacit purpose of maximising shareholder value. So lesson one is that maximising shareholder value is an outcome not a purpose. If you focus on it first and foremost it is potentially self-defeating. If it is a tacit objective, with a stated primary purpose of satisfying customers and achieving economic scale, then it is more likely to be achieved. Let's try another one. This is Deloitte's mission statement.

MILTON: They're not strictly a company of course, but I guess that more or less the same considerations apply.

SOCRATES: Deloitte says: 'Our mission is to help our clients and people excel'.

MILTON: Interesting, so now we have a reference to customers and employees. Which makes sense if you think about it. The business model of a professional services firm, like Deloitte, is all about having really good people who do really good work, thereby making customers happy, and thus maximising profits. Now, here's an interesting one. This is Alibaba's mission statement: 'To make it easy to do business anywhere – we enable businesses to transform the way they market, sell and operate and improve their efficiencies'.

SOCRATES: So there the focus seems to be on partners and suppliers?

MILTON: But still with the ultimate aim of making money for shareholders. Here's another one: 'to be the catalyst in communities of customers, contributors, and partners creating better technology the open source way'.

SOCRATES: Who's that?

- MILTON: Red Hat Industries, an IBM subsidiary. They call themselves 'the world's leading provider of enterprise open source solutions'.
- SOCRATES: This all sounds like the mantra – best people, best clients, best partners, best profits.
- MILTON: Exactly, Socrates, you've got it.
- SOCRATES: That's very interesting, Milton, but would you mind if I took a philosophical turn again?
- MILTON: If you must.
- SOCRATES: I'm still interested in the notion of purpose which I described above as 'a call to virtuous action'. I wonder if we could explore that further. For example, here's Tesla's mission statement: 'accelerate the world's transition to sustainable energy'.
- MILTON: Tesla, that's Elon Musk's company. Now there's a real capitalist!
- SOCRATES: How about this one: 'make sustainable living commonplace – we believe this is the best long-term way for our business to grow'.
- MILTON: That's Unilever
- SOCRATES: What about: 'bring health through food to as many people as possible'.
- MILTON: Who's that?
- SOCRATES: Danone. Here's another one which is quite interesting. This company's mission statement used to be: 'build the best product, cause no unnecessary harm, use business to inspire and implement solutions to the environmental crisis', but now they've change it to simply: 'we're in business to save our home planet'.
- MILTON: That will be Patagonia, but you've got to be careful. Patagonia is a privately owned Benefit Corporation. It is not under any obligation to maximise shareholder value. Let me try this one out on you instead: 'Our purpose is reimagining energy for people and our planet. We want to help the world reach net zero and improve people's lives'.
- SOCRATES: Don't tell me.
- MILTON: It's BP.

- SOCRATES: Hmm, I wonder about that one.¹⁰⁸ Anyway, let's try to analyse what's going on here. We seem to have four categories. First, companies who aim to do well financially by doing good. You might say that this is consistent with The British Academy's definition of business purpose as being 'to profitably solve the problems of people and planet, and not to profit from creating problems'. Perhaps Tesla is an example of this.
- MILTON: Perhaps, but remember it's run by Elon Musk. Moving on, we have companies like Unilever and Danone who claim that they are doing well by doing good, but have been criticised by investors like Terry Smith, who say that management should stick to the business of making money for shareholders rather than, to paraphrase what he said in a letter to investors: 'responding to poor performance by uttering meaningless platitudes'.
- SOCRATES: Strong stuff. And I know that Danone's shareholders sacked their long-standing chief executive, Emmanuel Faber, because they thought he was focusing too much on sustainability and not enough on financial performance. Thirdly, we have companies like Patagonia, who have positioned themselves as B Corporations, so that maximising shareholder value is no longer explicitly a primary objective.
- MILTON: I think that Danone is moving in that direction too. But we also have a fourth category, companies who talk a lot about mission purpose, doing good, saving the planet, and so on, but are still really solely in the business of making money for shareholders.
- SOCRATES: Are you talking about BP?
- MILTON: I'll let you decide.
- SOCRATES: Fair enough. In summary, we have got a group of companies whose purpose is focused on what I think you call, simply, 'virtue'. Some of these, like Patagonia, have, as it were, made a virtue of 'virtue', and are also, it seems, able to make lots of money for their shareholders as well. In Jonathan Trevor's nomenclature, we might call these 'super-aligned'.
- MILTON: Okay.
- SOCRATES: I would also argue that a super-aligned company is a good example of Aristotle's golden mean. The best outcome for

everyone is obtained when the interests of shareholders, customers, employees, business partners, the planet, and society as a whole are all taken into account in determining what constitutes purpose.

MILTON: We've also got other companies who focus on virtue, but at the expense of financial performance. I suppose that's okay if it's part of the implied contract with shareholders, as it is with B Corporations, but not otherwise.

SOCRATES: We also have a group of companies who are guilty of 'greenwashing' – they claim to be virtuous, but really, they are still in the same old business of maximising value for shareholders.

MILTON: Okay so far. Now I've got to run. Meet again tomorrow?

SOCRATES: Shall we say two o'clock?

The following day.

MILTON: So let me summarise. You postulated, I like that word by the way, that the purpose of a company might be either (*with emphasis*) to maximise shareholder value or (*with greater emphasis*) for something else.

SOCRATES: That's right.

MILTON: And you divided 'something else' into two further categories: 'for mastery' or 'for virtue'.

SOCRATES: I did indeed.

MILTON: Well, the first point I want to make is that there is no difference between the first category 'to maximise shareholder value', and the second category 'for mastery'.

SOCRATES: Why is that?

MILTON: Well, if you think about it, a company which aims to have the best products, produced by the best people, with the best levels of customer satisfaction, and the best relationships with suppliers, is likely to be very profitable.

SOCRATES: You keep saying 'well'.

MILTON: Oh, give me a break.

SOCRATES: Okay. Yes, you make a reasonable inference. A company which focuses on the best products, people, customer

satisfaction, and relationships with suppliers is likely, *ceteris paribus*, to be very profitable

MILTON: *Ceteris paribus*, I thought you were Greek?

SOCRATES: It's a philosophical term. It means 'all other things being equal'.

MILTON: I know what it means – economists use it too. Anyway, as you were saying, a company which focuses on the best products, people, customer satisfaction, and relationships with suppliers is likely, *ceteris paribus*, is likely to be very profitable.

SOCRATES: Yes.

MILTON: And therefore would be maximising shareholder value.

SOCRATES: I suppose to be precise it would be maximising the value of the company. The value isn't necessarily all attributable to shareholders.

MILTON: Oh, come on, you're splitting hairs.

SOCRATES: I don't think so. I think one of your economists wrote a paper about this. He talked about 'enlightened value maximization' which he says, 'utilizes much of the structure of stakeholder theory but accepts maximization of the long-run value of the firm as the criterion for making the requisite tradeoffs among its stakeholders'.

MILTON: You're beginning to sound like an economist. Wait a minute, what's that paper you're reading from?

SOCRATES: It's an article by a man called Michael Jensen, called 'Value maximization, stakeholder theory, and the corporate objective function'.¹⁰⁹

MILTON: Okay, I know Jensen. Good guy. But it remains the case that we have one category of company whose primary purpose is to make a barrel load of money, and a second category of company whose focus is on 'virtue', whatever that means.

SOCRATES: Well perhaps. I might draw a distinction between primary purpose and secondary purpose, between intrinsic motivation to produce the best goods and develop the best people, and extrinsic motivation to make lots of money, but for the purposes of discussion, let's say that I accept what your argument up to this point.

MILTON: Thank you. So here's my question. How do we decide between these two categories of corporate purpose? What criterion do we use to determine which is better?

SOCRATES: That, Milton, is the 64,000 dollar question.¹¹⁰

MILTON: 64,000 dollars, that's not much. Shall we meet for a coffee sometime and continue our conversation?

SOCRATES: What's coffee?

MILTON: It's a drink, Socrates. I'm away for a while. Let's meet a week today at The Philosophers' Cafe. Shall we say two o'clock?



4. On ‘mastery’ – reconciling shareholder primacy and stakeholder theory

To what extent can the problems which have been identified with shareholder primacy and stakeholder theory be resolved and the two perspectives on the question ‘what’s a company for?’ be integrated? To explore this question we examine the ideas of the philosopher Joseph Heath, the legal scholar Margaret Blair and the economist Lynn Stout.

Let’s begin with a brief rehearsal of the argument so far.

1. In Chapter 2, I explained that shareholder primacy, which privileges financial capital, is flawed in at least three respects:
 - a. First, the property rights problem – shareholders own shares in a company, not the company itself, as shareholder primacy takes for granted.
 - b. Second, the ontological question – shareholder primacy fails to recognise the differences between a public corporation and a private company.
 - c. Third, begging the question – shareholder primacy assumes ‘the basic rules of society’, which it is trying, in part, to establish.
2. In Chapter 3, I argued that stakeholder theory is also flawed. In particular, this is because of:
 - a. The problem of stakeholder identification.
 - b. The logical impossibility of maximising in many dimensions.
 - c. The problem of adjudicating between stakeholders.

In this chapter I look at how some of these problems with both perspectives can be addressed.

Joseph Heath on shareholder primacy

In his 2014 book *Morality, Competition, and the Firm*, the Canadian philosopher Joseph Heath (see Figure 4.1) attempts to help Milton Friedman by

Figure 4.1: Joseph Heath

Source: Photo by Jenna Muirhead, courtesy of University of Toronto.

developing an ethical system called the ‘market failure approach,’ which integrates business ethics into a larger project of working out how best to organise economic activity in society.¹¹¹

Heath argues that the primary reason for introducing the profit motive is to secure the operation of the price mechanism – the mechanism whereby the forces of supply and demand determine the allocation of resources in society. The price mechanism is in turn valued for its efficiency effects. The formal proof of this is the first fundamental theory of welfare economics, which states that the outcome of a perfectly competitive market economy will be Pareto optimal. This means that it will not be possible to improve

any one person's condition without worsening someone else's. In this way, Heath argues that efficiency is an ethical concept – it is in the best interests of society as a whole to allocate resources efficiently. Hence, a robust moral code can be developed out of the idea that the fundamental obligation of managers is to maximise total firm value. It has always been accepted that managers must do so within the framework of the law. However, Heath goes on to say: 'An ethical manager is one who does so while respecting not only the letter of the law, but also its spirit – which is to create the conditions necessary for private enterprise to generate an efficient allocation of goods and services in the economy'.¹¹²

The market failures approach therefore regards the deliberate fostering of market failures as morally unacceptable. This includes rent-seeking (profits in excess of normal profits), monopolies, oligopolies, and incumbent co-operation; imperfect competition in general; externalities, particularly negative externalities (for example, pollution), but possibly also some positive externalities (for example, benefitting from large network effects, as in the case of social media companies); information asymmetry (for example, misleading advertising); and labour market failures (for example, excessive executive pay).

That the market failure approach has real teeth can be seen from the fact that neoclassical economics postulates the benefits of perfectly competitive markets, with many buyers and sellers, free market entry and exit, homogenous products (or ready substitutes), complete contracts, readily available prices, and plentiful information. Yet classical business strategy, and much actual business practice, involves positioning – how to avoid competition – implying rent seeking, imperfect competition, cartels, monopolies, oligopolies, and incumbent co-operation.

The version of capitalism that the market failures approach extols is the free-market perfect-competition version of capitalism found in economic textbooks, not the version based on imperfect competition found in some books on business strategy, and certainly not the 'red-in-tooth-and-claw' version in which unscrupulous operators seek to create and exploit market imperfections ('competition is for losers', as one American CEO once said).¹¹³ It is legitimate for a business to lower its prices or improve its product quality in order to increase its market share in a competitive market. It is immoral to construct barriers to entry, use deceptive advertising, pollute the environment at no cost, or exploit other kinds of market failure. Fraud, false accounting, certain kinds of negligence, and other types of corporate malfeasance are all immoral and typically also illegal.

Following the logic of the market failures approach, a number of ethical imperatives can be derived. These include minimising negative externalities, reducing information asymmetries between firms and customers, not exploiting dispersion of share ownership, avoiding erecting barriers to entry, and not opposing regulations aimed at correcting market imperfections.¹¹⁴

Margaret Blair and Lynn Stout on stakeholder theory

While the market failures approach helps to address some of the problems with shareholder primacy, some of the ideas of Margaret M. Blair, an economist, and Lynn A. Stout, a legal scholar, can help to remedy some of the shortcomings of stakeholder theory (see Figure 4.2). To understand what Blair and Stout call ‘team production theory’ we need to do two things.

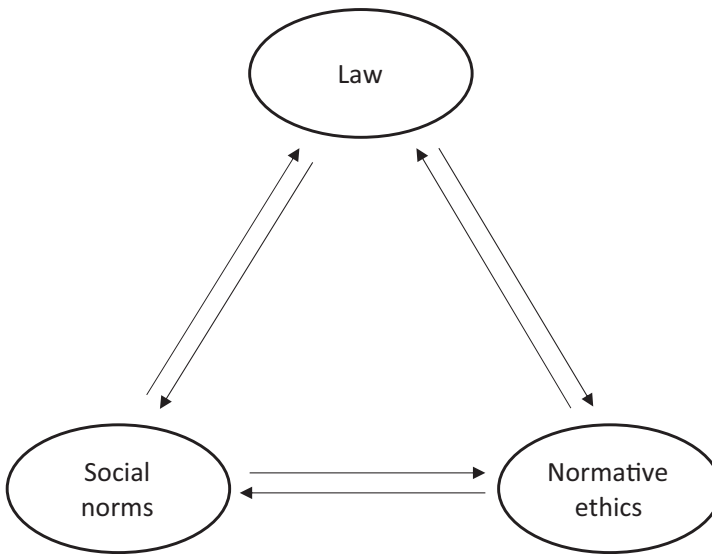
First, we need to understand something about ‘social ontology’, the systematic study of the nature and basic structure of social reality. The primary motivation of social ontology is a shared belief that social research has much to gain from a better understanding of the nature of the underlying reality. Scientific ontology focusing on the social domain is concerned with the nature of things such as money, gender, markets, technology, the corporation, community, power, authority, trust, cooperation, institutions, norms, rules, customs, conventions, collective practice, profit, output, income, wealth, identity, society, economy, and so on. Leading figures and associates include Tony Lawson (Emeritus Professor of Economics and Philosophy, University of Cambridge), Simon Deakin (Professor of Law, University of Cambridge), and John Searle (Philosopher, UC Berkeley). They are all members of the Cambridge Social Ontology Group.

Figure 4.2: Lynn Stout and Margaret Blair



Sources: Lynn A. Stout (left) at the Cornell Law Library, by Heather Ainsworth, CC BY-SA 3.0 licence; Margaret Blair (right), photo courtesy of Vanderbilt Law School.¹¹⁵

Figure 4.3: Interaction between social norms, normative ethics, and the law



Source: Author.

One of the things that interests social ontologists is the relationship between social norms, normative ethics, and the law (see Figure 4.3).

Studying legal concepts can tell us something about the social world beyond the legal realm. Studying juridical concepts using the techniques of legal analysis can inform us about the nature of social practices beyond the legal text. As Simon Deakin says:

Legal concepts form a bridge between facts and norms. Law is partly endogenous to economic and political change ... regularities which begin in a transactional or organizational context can find their way into the legal system ... Conversely, the law may trigger social change by altering the basis of conventional.¹¹⁶

Second, we must look again at the typologies of stakeholder theories. Joseph Heath, Professor of Philosophy at the University of Toronto, proposes a more fine-grained typology of stakeholder theories than the tripartite classifications put forward by Thomas Donaldson and Lee Preston on the one hand, and Kevin Gibson on the other (see Figure 4.4).

Figure 4.4: Typologies of stakeholder theory

Donaldson and Preston (1995)	Gibson (2000)	Heath (2014)	
Descriptive	Agency	Ontological Explanatory	A theory about the fundamental nature of reality of the corporation A positive theory of how companies and managers actually behave
Instrumental	Prudential	Strategic Branding and culture Managerial Governance Regulatory	Explains how resources should be allocated between stakeholders for competitive advantage How extraordinary attention to stakeholders can become part of the value proposition Catch-all for how managers realise the benefits of stakeholder theory Explains how different stakeholder groups should exercise control and oversight of managers Defines which interests of stakeholder groups ought to be protected by government regulation
Normative	Deonto-logical	Deontic Corporate law	Says that stakeholder theory helps to determine the rights and duties of stakeholders and managers from an ethical perspective Argues that stakeholder theory accurately describes the legal nature of corporations.

Source: Donaldson, T.; and Preston, L. (1995) ‘The stakeholder theory of the corporation: concepts, evidence, and implications’, *The Academy of Management Review*, vol. 20, no. 1. pp. 65–91; Gibson, K. (2000) ‘The moral basis of stakeholder theory’, *Journal of Business Ethics*, vol. 26, no. 3, pp. 245–57; Heath, J. (2014) *Morality, Competition, and the Firm – The Market Failures Approach to Business Ethics*, Oxford: Oxford University Press.

Our particular interest at this point is what Heath calls 'corporate law stakeholder theory', a theory about the relationship between corporate law and the principles and practices favoured by ontological, deontic, and governance approaches to stakeholder theory. Can a systematic analysis of corporate law help us to understand who the stakeholders in a company are?

Margaret Blair and Lynn Stout argue that, while agency theory may be important in understanding the private business firm, it does not necessarily provide the same insights into our understanding of public corporations. In the case of public corporations, corporate law does not treat directors as the agents of shareholders, but as something quite different. They are not charged with serving shareholders' interests alone, but with serving the interests of the company. In the eyes of the law, corporate directors are a unique form of fiduciary who more closely resemble trustees than agents. They owe fiduciary duties of loyalty and care to the company, not to shareholders. The primary job of the directors of a public corporation is to act, in effect, as trustees for the corporation itself. The directors are thus *not* merely the agents of shareholders, pursuing shareholders' interests at the expense of employees, creditors, and other team members. Blair and Stout propose that public corporations comprise teams of people making 'specific investments' in the form of both financial and human capital. They enter into a complex agreement to work together for mutual gain under a 'mediating hierarchy'. Blair and Stout call this the 'team production theory of corporate law'.¹¹⁷

So far so good. Now we need a definition of 'specific investments'. Here Blair and Stout draw on the work of economists Raghuram Rajan and Luigi Zingales, who list examples of the kinds of things that constitute specific investments. They include physical capital (for example, plant and machinery that are specific to the production process), which is funded by financial capital provided by shareholders; human capital (for example, education, training, and expertise), which is specific to the production process and of limited value to another employer; suppliers' physical and human capital (see, for example, Susan Helper and Mari Sako's work on supplier relationships in the Japanese automotive industry¹¹⁸); and communities' physical and social capital (for example, local infrastructure and roads, and business and social networks supporting the main corporation, as illustrated by the Janesville example in Chapter 3).¹¹⁹

A somewhat toned-down version of team production theory is in fact what we find in English company law. Section 172 of the Companies Act 2006 confirms the view that companies are run for the benefit of their members (i.e., shareholders). However, it requires directors to have regard to the interests of employees, relationships with suppliers and customers, the impact of a company's operations on communities and the environment, and the desirability of maintaining a reputation for high standards of business conduct. It also requires directors to consider the long-term consequences of their decisions and the need to act fairly between members of the company. Andrew Keay, an English law scholar, calls this 'the enlightened shareholder value principle'.¹²⁰

The adjudication problem

Perhaps most difficult of all to deal with is the adjudication problem: how are the relative contributions of different stakeholders to be evaluated? Shareholder primacy solves this problem by letting the market fix the amounts paid to employees and suppliers, and the price paid by customers, and attributing all residual profits to shareholders. Stakeholder theorists recognise that markets are imperfect and believe that the price mechanism under-rewards stakeholders who make specific investments. A better approach, they argue, can be reached by drawing on the principle of fairness, which many philosophers regard as being of critical importance when it comes to justice and ethics. One business ethics scholar, drawing on the ideas of the political philosopher John Rawls, puts it like this:

Whenever persons or groups of persons voluntarily accept the benefit of a mutually beneficial scheme of cooperation requiring sacrifice or contribution on the parts of the participants and there exists the possibility of free-riding, obligations of fairness are created among the participants in the co-operative scheme in proportion to the benefits accepted.¹²¹

A modern corporation fits the bill. It is, if you think about it, 'a mutually beneficial scheme of co-operation'. Benefits accrue only if everyone, or nearly everyone, co-operates. Co-operation requires sacrifice and some restrictions on the liberty of participants; employees, for example, forgo some freedoms in return for their wages. Last but not least, the possibility for free-riding exists – the limited bargaining power of certain stakeholders may be exploited by others with more power. Under these conditions, according to Rawls, any person who accepts the benefits of the cooperative scheme is bound by a duty of fair play to do their part in ensuring that there are fair outcomes.¹²²

There is an economic theory of fairness. One version of it has been articulated by Hal Varian, Chief Economist at Google, Emeritus Professor of Economics at the University of California, Berkeley, and the author of a best-selling textbook on microeconomics. In an article entitled 'Distributive justice, welfare economics and the theory of fairness' that was published, interestingly, in *Philosophy and Public Affairs*, a well-known philosophy journal, Varian articulates the economic theory of fairness like this:

A distribution of goods is called fair if X prefers his own bundle of goods x to the bundle of goods y obtained by Y, that is, if X does not envy y, AND if Y prefers her own bundle of goods y to the bundle of goods x obtained by X, that is, if Y does not envy x. A distribution of goods is said to involve envy by X of the bundle of goods y obtained by Y if X would rather have y than the bundle of goods x obtained by X AND to involve envy by Y of the bundle of goods

x obtained by X if Y would rather have x than the bundle of goods y obtained by Y.¹²³

These definitions are essentially mirror images. They are typically sparse definitions of the kind favoured by economists.¹²⁴ Two other economists, Ernst Fehr and Klaus M. Schmidt, propose a model of fairness that follows the structure of these definitions and has become a standard in the economic literature.¹²⁵ For simplicity, like Varian, their model assumes two persons (or 'players' in game-theory terminology). However, the model is perfectly capable of being extended (but with much more complex mathematics!) to any number of participants (an '*n*-person game').

We must allow for the possibility that X and Y may make differential contributions (for example, in terms of their ability and effort) prior to receiving x and y, and that his perception of these differential contributions might be taken into account by X as he weighs the extent to which he envies or does not envy the bundle of goods y obtained by Y. To allow for this, we can incorporate the psychologist John Stacy Adams's equity theory.¹²⁶ Adams explains equity in the context of social exchange in terms of X's perception of the costs of his inputs (i.e., what X must do to obtain x) and the value of his outputs (i.e., the bundle of goods x obtained by X as a reward) versus the perceived cost of Y's inputs (i.e., what she must do to obtain y) and Y's perceived outputs (i.e., her bundle of goods y). Incorporating Adams's ratio into Fehr and Schmidt's utility function enables us to generate a new version of the fairness model. For the mathematically minded reader this is set out in Figure 4.5. Equation [1] is the Fehr and Schmidt economic theory of fairness. Equation [2] is Adams equity theory. Equation [3] is what we get when equations [1] and [2] are combined.¹²⁷

Limitations of the principle of fairness

The big problem here, as you may have already spotted, is that, while this is all very well in theory, and the mathematics of fairness theory is all very elegant, it is extraordinarily difficult to operationalise the theory in practice. It assumes that X and Y evaluate greed and envy similarly. It also assumes that X and Y both know about, and assess in the same way, the inputs and outputs of X and Y. While this may be true in rational choice theory, as favoured by economists, it is all rather questionable in real life. It is even harder to apply when X is a shareholder, Y is an employee, and their inputs and outputs are both conceptually different. The key point, nevertheless, is simply this: there is a strong deductive argument for saying that equity is necessary in teams in order to maximise team utility and motivation.

The well-known American moral philosopher, Michael J. Sandel, and Debra Satz, Dean of the School of Humanities at Stanford University and Professor of Ethics in Society, have both written about the things that money can't buy

Figure 4.5: An economic theory of fairness

$$U_x(v) = v_x - \underbrace{\alpha_x \max[(v_y - v_x), 0]}_{\text{Factor for envy}} - \underbrace{\beta_x \max[(v_x - v_y), 0]}_{\text{Factor for guilt}} \quad [1]$$

v_x and v_y can in turn be thought about in terms of the ratio of outputs to inputs, what an economic agent gets out compared with what he or she puts in.

$$\left\{ \frac{O_x}{I_x} \right\} : \left\{ \frac{O_y}{I_y} \right\} \quad [2]$$

where O_x are the outputs of the first agent, X, e.g., his compensation, I_x is the first agent's inputs e.g., his ability and effort, O_y are the outputs of the second agent, Y, and I_y is her inputs.

$$U_x(v) = v_x - \underbrace{\alpha_x \max[(\frac{V_y}{C_y} - \frac{V_x}{C_x}), 0]}_{\text{Envy}} - \underbrace{\beta_x \max[(\frac{V_x}{C_x} - \frac{V_y}{C_y}), 0]}_{\text{Guilt}} \quad [3]$$

Value Envy Guilt

where $U_x(v)$ is the utility of the payment to X, v_x is the value of the good as perceived by X, v_y is X's perception of the value of the good to Y, c_x is the contribution made by X in return for v_x , and c_y is X's perception of the contribution made by Y in return for v_y , α_x is the coefficient for envy such that $\alpha_x \geq 0$, β_x is the coefficient for guilt such that $\beta_x \leq 1$.

Sources: Adapted by the author from [1] Fehr and Schmidt (1999), [2] Adams (1965), and [3] Pepper, Gosling, and Gore (2015).¹²⁸

and the things that shouldn't be for sale. Both argue forcefully that there are moral limits to markets. The spectrum of goods and services which, arguably, should not be for sale is sketched out in Figure 4.6.

There is a further problem with both shareholder primacy and stakeholder theory that none of the things we have dealt with in this chapter really addresses. This is the problem of 'telos' (purpose). Is efficiency really the best objective when it comes to the question 'what's a company for?'. Is financial performance the only thing that matters? 'Is that all there is?', the lady wondered.¹²⁹ If so, it would seem to be a rather dismal conclusion. This is particularly relevant when it comes to potentially cataclysmic issues such as climate change, at a macro-political level, or the Janesville dilemma, at a micro-political level. When are the benefits of better financial performance outweighed by more critical social objectives?

Figure 4.6: The limits of markets – what should not be for sale

Legitimate	Morally ambiguous	Immoral	Unlawful
	Healthcare		Human organs
	Blood	College admissions	Narcotics
	Education		
Higher education	Nuclear waste disposal		
	Political lobbying		Political favours
		Child labour	
	Gambling	Markets in sexual labour	

Source: Author.

Conclusion

This chapter has gone some way towards addressing the problems of shareholder primacy and stakeholder theory, and to combine the two perspectives into a single view – which has been called ‘for mastery’,¹³⁰ although it might alternatively be called ‘enlightened shareholder primacy’ or ‘real stakeholder theory’. This is a more narrowly focused version of stakeholder theory which also draws on some elements of shareholder primacy. Rather than maximising value for shareholders, it focuses instead on ‘total firm value maximisation’ (to use Michael Jensen’s terminology), which embraces ideas about having the best products, best people, best levels of customer satisfaction, and the best relationships with suppliers – for the benefit of all stakeholders who make specific investments in a company. However, the either (mastery)/or (virtue) duality remains unresolved. That is the topic of Chapter 5.

Dialogue IV: Socrates and Milton

In which Socrates and Milton Friedman discuss the question of either/or at The Philosophers' Café

Figure IV: The Philosophers' Café



Source: Tim Wakeling.

***Dramatis Personae* in order of appearance**

- Elizabeth Anscombe** British analytical philosopher famous among other things for two articles she wrote in the 1950s. 'Does Oxford moral philosophy corrupt youth?' was deeply critical of linguistic analysis and prescriptivism. 'Modern moral philosophy' called for a return to virtue ethics.
- Alasdair MacIntyre** Scottish-born, British-educated, American-based moral philosopher. His best-known book *After Virtue* has been a major contributor to the development of modern virtue ethics.
- Philippa Foot** English philosopher who, with Elizabeth Anscombe and Alasdair MacIntyre, was one of the founding figures of modern virtue ethics.
- Karl Popper** 20th-century Austrian-British philosopher who rejected the scientific method of induction, citing as an example how the statement 'all swans are white' was believed to be a universal truth until black swans were found in Australia by explorers in the 17th century.
- G.E. Moore** Professor of Philosophy at Cambridge University from 1925 to 1939, best known for his theory of ethical non-naturalism, also known as emotivism.
- R.M. Hare** Professor of Moral Philosophy at Oxford University from 1966–1983, an 'ordinary language' philosopher best known for his meta-ethical theory of prescriptivism.
- Ludwig Wittgenstein** Austrian philosopher who worked primarily in the philosophy of language, mind, mathematics, and logic; widely regarded as a genius.
- Bertrand Russell** Mathematician, philosopher, and public intellectual, who had a bit of a reputation as a ladies' man.
- Søren Kierkegaard** Danish theologian, philosopher and social critic, author of *Either/Or* (1843).
- Jean-Paul Sartre** 20th-century French existential philosopher and public intellectual whose works include *L'Age de Raison*, *Les Mains Sale*, and *La Nausée*.
- Georg Wilhelm Friedrich Hegel** A German philosopher who lived between 1770 and 1831. One of the most influential figures of post-Kantian Idealism and 19th century school of continental European philosophy.
- Roger Scruton** English philosopher, writer, and social critic, who had a dim view of continental philosophy.

György Lukács	Hungarian Marxist philosopher, the pre-eminent Marxist intellectual of the Stalin era. The only continental philosopher who Roger Scruton judged to be downright wicked.
John Locke	17th-century British philosopher who advocated rights-based ethics, epitomised by the opening words of the American Declaration on Independence of 4 July 1776: 'We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of happiness'.
Immanuel Kant	18th-century German philosopher, a central figure in modern philosophy, advocate of deontology (duty-based ethics) and famous for articulating the categorical imperative as a way of evaluating motivations for action.
Plato	A pupil of Socrates and founder of the Academy.
Aristotle	A pupil of Plato and founder of the Lyceum.
Heraclitus	A pre-Socratic Greek philosopher who believed that the world was in a constant state of flux, epitomised by the epigram 'no man ever steps in the same river twice'.

It was a busy morning at the Philosophers' Cafe. At one table Alasdair MacIntyre, Elizabeth Anscombe and Philippa Foot were talking about the virtues of good coffee. At another table a waiter asked Karl Popper if he wanted a cappuccino, a flat white or a long black.

'Most probably a flat white', said Popper. 'Don't you know that you only find long blacks in Australia? You know, like swans'.

'This coffee is so good', said G.E. Moore, at another table where he was chatting to the Oxford ordinary language philosopher R. M. Hare. 'Its quality is indefinable'.

'What you mean is that people must drink it', said R.M. Hare, emphatically. 'By the way, why do we always refer to each other by our initials, rather than our first names?'

Their discussion was overheard by Ludwig Wittgenstein, who was sitting nearby by himself. 'Your discussion is completely meaningless', he shouted angrily. 'It's all a matter of taste. Whereof one cannot speak, thereof one must be silent'.

'Calm down, Wittgenstein', said Bertrand Russell, who was busy chatting up one of the waitresses.

Nearby, another waitress was asking customers what they would like to drink. 'EITHER' (said with emphasis) 'a hot chocolate with whipped cream and marshmallows', said Søren Kierkegaard, 'OR' (said with equal emphasis) 'a filter coffee,

black, no sugar'. 'I'm afraid I drank so much coffee in my youth the mere smell of it now gives me nausea', said Jean-Paul Sartre. 'I'll just have a glass of water, or a drop of red wine if you have it. Now I see my hands are rather dirty, I'd better pop along to the bathroom and wash them'. Georg Wilhelm Friedrich Hegel (Georgy to his friends) said he would like a single source Colombian coffee: 'It is dense, idiosyncratic, and complex – just how I like it. The essence, the history, the tradition of fine Colombian coffee is the very substance of its being, its presence, its immediacy'.

'What nonsense' said Roger Scruton, who was sitting nearby. 'You're all fools or frauds. I've never understood you continental philosophers and your obsession with coffee. I prefer English breakfast tea myself'.¹³¹

'That's wicked', said György Lukács.¹³²

Elsewhere, John Locke and Immanuel Kant were, not unreasonably given the location, having a deep philosophical discussion. 'Do you think that a man's right to good coffee is self-evident?', John Locke asked.

'I don't know about that', said Kant, 'but it is certainly true that cafes have a duty to provide good coffee'.

In a corner by the window, away from the shadows, another waiter was having difficulty with three older men, who all had long white beards. 'This coffee is well-balanced but decidedly average', said Aristotle'.

'What do you mean?', asked the waiter.

'Exactly', said Aristotle.

'I think you misheard him', said Plato. 'Anyway, I disagree. This coffee is a mere shadow of the ideal'.

'I'm so sorry', said the waiter.

'No, no', said Plato, 'that is the best that can be expected in an imperfect world of ephemeral objects'. Heraclitus added helpfully, 'did you realise that you can never drink the same cup of coffee twice?'

MILTON: Interesting place, I thought you'd like it here, it's packed out with your mates.

SOCRATES I am not friendly with all of them, you know (*scowling at Aristotle*). We disagree on many things.
(*nodding to Plato as he sat down*):

MILTON: Just like economists.

SOCRATES: I gather that you've been away.

MILTON: Yes, I've been at a conference in Europe, Scandinavia actually. Nice place. They've produced some good economists, Knut Wicksell, Berthil Ohlin, Gunnar Myrdal, Ragnar Frisch, Trygve Haavelmo, Bengt Holmström. Lots of Nobel Prize winners.

SOCRATES Really? How fascinating.
(acerbically):

MILTON: Yes, anyway, I had some really interesting discussions about the matter we've been discussing, you know 'what's a company for?'. I explained our dilemma. You know you drew that picture in the sand, which shows that we've come up with two different answers to the question. Either what you called 'for mastery', though I might prefer to call it Shareholder Primacy 2.0., or what you called 'for virtue'. But we can't find a way of deciding between these two different paradigms. That's a fair summary of where we are, isn't it?

SOCRATES: For the purposes of discussion, let's say that it is.

MILTON: Well I was talking to one guy at the conference and he said I should read a book called *Either/Or*. It's by Søren Kierkegaard. He's a philosopher, you'd like him. He's Danish.

SOCRATES: Danish?

MILTON: Yes, like the pastry.

SOCRATES: What?

MILTON: Danish. He comes from Denmark. *(Pause)* Look, don't worry about the pastry. The point is this: *Either/Or* is a really interesting book. Actually, it's really two books. It's very long, so I made some notes. Can I read them to you?

SOCRATES: If you must.

MILTON: Okay, here goes *(reading from a paper)*.

Either/Or by Søren Kierkegaard is a philosophical work that explores two contrasting ways of life: the aesthetic and the ethical. Written in 1843, it presents these ideas in a two-part structure, each representing a different perspective. The aesthetic life is explored in the first part and the ethical in the second, with each side written by different fictional authors, making it feel like a debate between two ways of existing.

Part One, about the aesthetic life, is written by a character called 'A', who represents a hedonistic, pleasure-seeking, and often nihilistic viewpoint. He values beauty, art, personal enjoyment, and experiences, often disregarding the long-term consequences of his actions. He believes in living for the moment, finding fulfilment in

transient pleasures, and keeping his life free of commitments. A's perspective showcases the dangers of a life that lacks deeper purpose or responsibility, as his pursuit of pleasure leads to a sense of emptiness.

Part two, about the ethical life, is supposedly written by someone called Judge Vilhelm who represents a more structured, morally committed viewpoint. He argues for the ethical life, which involves personal responsibility, commitment, and finding meaning through marriage, duty, and moral integrity. The judge emphasises that true happiness arises not from fleeting pleasures but from making responsible choices and developing a stable character. The ethical life, he argues, has the power to overcome the despair that can arise in the purely aesthetic pursuit of pleasure.

SOCRATES: Thank you, that's a clear summary. Did you do it yourself?

MILTON: No, I used ChatGPT.

SOCRATES: Who's she?

MILTON: It's an app, not a person.

SOCRATES: What's an app?

MILTON: A computer application. A computer is a machine which can process a vast amount of information, and a computer application is a thing which runs on a computer. ChatGPT is what's called a 'large language model', a form of artificial intelligence.

SOCRATES: How interesting. Can it think? Is it conscious?

MILTON: Those are philosophical questions. I'm an economist.

SOCRATES: Is it cheating to use ChatGPT?

MILTON: That's an ethical question, and I'm still an economist. But no, I don't think using Chat GPT is cheating. It's a rather long book and very complicated – a bit outside my comfort zone. I've been completely transparent, haven't I? It's just like having a research assistant. I recognise that you've got to take great care with the accuracy of the output. Anyway, what's originality? Shakespeare never wrote a plot.¹³³

SOCRATES: Who's Shakespeare?

MILTON: Look, if you know who John Milton is, then you must have heard of William Shakespeare.

SOCRATES: Of course, just kidding. By the way originality and creativity are fascinating areas of philosophical enquiry. But look, Milton, while this is all very interesting, what's it got to do with the question of 'what's a company for?'

MILTON: It's obvious, isn't it. The either/or dilemma is essentially the same. Either you could say the answer to the question is Shareholder Primacy 2.0., or 'for mastery' as you call it. Or you could say it's 'for virtue'. There's no one right answer. It's a choice. We Americans could choose 'for mastery' and make barrel loads of money. You left-leaning Europeans could choose 'for virtue' and not do so well, but still feel good about yourselves.

SOCRATES I'm not sure it's so simple.
(thoughtfully):

MILTON: Why not? Works for me.

SOCRATES: Don't you think it is possible, rather than presenting the aesthetic life and ethical life as a choice which cannot be decided upon by rational criteria, that in his description of the aesthetic life, especially its more distasteful aspects, Kierkegaard is encouraging us to lean towards the ethical life, and that this might even have been as preparation for a religious life?

MILTON: So you have come across *Either/Or*?

SOCRATES: I'm very well read.

MILTON: Anyway, that's not the way I see it.

SOCRATES: I think perhaps a period of reflection is required. Let's sleep on it and meet for a further discussion tomorrow.

MILTON: Shall we say two o'clock?

The following day.

SOCRATES: Dear Milton, let me begin. The proposition which I think you have advanced is this. There are two possible answers to the question 'what's a company for?' The first is a modified version of your thesis 'the social responsibility of business is to increase its profits'. Let's call this 'the Friedman doctrine'.

MILTON: I like that.

SOCRATES: The modification we have made to your original formulation is that you have agreed it is necessary to construct a 'call to action' in order to ensure that a company has the best products, the best people, the best levels of customer satisfaction, and the best relationships with suppliers. We incorporate into this way of thinking the idea that at some people, for example certain employees and suppliers, make specific investments in the company, which must be considered alongside the financial investments of stockholders, and Michael Jensen's concept of 'total firm value maximisation'. I called this modified version of shareholder value maximisation 'for mastery' and you called it Shareholder Primacy 2.0.

MILTON: Agreed.

SOCRATES: I have also sketched out an alternative answer to the question 'what's the purpose of a company?' which involves what I have described as 'a call to virtuous action'. As well as achieving financial sustainability, this takes account of other objectives, such as saving the planet, reducing poverty and inequality, and so on. I have called this 'for virtue'.

MILTON: I agree.

SOCRATES: Your thesis is that, while 'for mastery' and 'for virtue' are both potentially valid answers to the question, there is no ethical decision-making process that allows us to choose between them. It is, to borrow from Kierkegaard, an either/or situation.

MILTON: Exactly.

SOCRATES: Let's discuss 'for mastery'. The first thing I'd like to talk about is anthropogenic climate change.

MILTON: Anthro what?

SOCRATES: Anthropogenic. It means 'man-made'.

MILTON: Well of course that's highly debatable.

SOCRATES: Oh dear. Are you a climate change denier?

MILTON: No, I'm just saying it's debatable.

SOCRATES: Well can we make a working assumption for the purpose of our discussion that man-made climate change is a real phenomenon.

MILTON: Sure, if we must.

SOCRATES: Now, Milton, I would like to know what tools you have to help evaluate the economics of climate change.

MILTON: Okay, well the first thing I would do is to evaluate the costs of taking action to prevent the further degradation of the planet compared with the future benefits that would be obtained. Then I would discount the future benefits using a discount rate. Now, the actual rate is a matter of some contention among economists. Some argue 5% or more, equivalent to the rate that a country can borrow in the international capital markets. Others say it is unethical to discount the welfare of future generations at such high rates, and advocate a much lower discount rate, say 1%. Let's pick a low rate, say, 2%, which is fairly prudent. We will also assume zero population growth. This way I can work out what it's worth spending now to obtain benefits in the future.¹³⁴

SOCRATES: Interesting. Now can I ask you some questions about this.

MILTON: Of course.

SOCRATES: The costs incurred now fall on the current generation. The benefits accrue to future generations. So there is a question about, let's call it 'inter-generational equity'.

MILTON: Sure. People do worry about the world that their children and their grandchildren will live in, though interest in later generations tends to fall away.

SOCRATES: What about people who live in other countries?

MILTON: Sure, we need to take them into account.

SOCRATES: What about those who live a long way in the future, say 2000 years?

MILTON: Well, that starts to get a bit more nebulous. Who are these hypothetical people? Anyway, the discount rate should take care of that. A million dollars 200 years in the future is worth nothing much today.

SOCRATES: Milton, are you a hypothetical person?

MILTON: No, certainly not, how rude.

SOCRATES: But if you think about it carefully, you are to me.

Milton is quiet for a while.

SOCRATES: You see, Milton, if I had used the approach to the future which you advocate during my lifetime, I would have overlooked you altogether. (*Socrates pauses*) Let me ask you another question. What tools do you economists have to deal with man-made climate change?

MILTON: Ah, now you're talking. The economics of that are relatively simply. The problem is that carbon in the atmosphere is what we call a 'negative externality'. Companies benefit from industrial activities without having to address the carbon costs or the cost of cleaning up afterwards. So we have to put a price on carbon. There are two ways to do this. The first way is a carbon levy – heavy taxes on the people who would otherwise be big polluters. We call these Pigouvian taxes after an English guy called Arthur Pigou. Funny name, but a good economist. The other way is called 'cap and trade'. You place limits on the amount of carbon a business can create, but allow companies to trade carbon credits to make sure that carbon is only created where it's really necessary.

SOCRATES: Thank you, Milton, that's very helpful. But can I ask who would levy carbon taxes and establish a cap on carbon emissions.

MILTON: Why the government of course.

SOCRATES: But you don't like government intervention much do you?

Milton is again quiet for a moment.

SOCRATES: Also, wouldn't these arrangements require cooperation between governments? I mean the benefits of industrialisation might accrue in one jurisdiction and while the costs of climate change are experienced elsewhere. And taxes would have to be levied at equivalent rates to prevent big companies arbitraging between different fiscal systems. The same is presumably true of carbon caps. Would different countries really all agree to this?

Milton hums quietly to himself.

SOCRATES: Let's try another topic, Milton. I'd like to talk about big corporations. I understand that in your time there are some companies which are bigger than some countries?

- MILTON: *(Recovering his composure)* Yes, that's true, Socrates. Walmart's sales are over US\$600 billion, which is more than the gross domestic product of Belgium. Amazon's annual revenue is more than the GDP of Ireland and Norway. Apple is bigger than Denmark and Malaysia.
- SOCRATES: I also understand that some companies dominate their markets, especially in what I think you call 'tech'.
- MILTON: That's right, Socrates. Amazon and Apple would fall in that category. Big tech companies benefit from scale economies and network effects. It makes economic sense for a lot of consumers to use only one computer system.
- SOCRATES: So they're monopolies?
- MILTON: Well, I wouldn't put it like that. But there are certainly constraints on competition. Joan Robinson, another Cambridge economist like Pigou, – but hey a woman! – in economics in the 1960s and 1970s, what about that? Excuse me, where was I? Yes, Joan Robinson called this 'monopolistic competition'.
- SOCRATES: Milton, didn't you write somewhere that competition was key to effective working of the price mechanism? Perfect competition, many buyers and sellers, lots of information, minimal information asymmetry, and all that? If these big companies dominate their industries, can't they set their own prices and make super-profits?
- MILTON: You're beginning to sound like an economist. Yes, I guess you've got a point.
- SOCRATES: There's one more thing I'd like to discuss. In my day, we used to say that the four cardinal virtues are courage, justice, temperance, and practical wisdom.
- MILTON: Temperance? What, no drinking?
- SOCRATES: By 'temperance' I mean self-control and moderation. Temperance promotes balance and restraint in both actions and desires.
- MILTON: Ooh. And what is 'practical wisdom' supposed to mean?
- SOCRATES: What is says. Practical wisdom is the ability to choose wisely in different situations. It involves foresight, prudence, good judgement, and the ability to make sound decisions based on reason.

- MILTON: Okay. But what's this all about?
- SOCRATES: What would you say are the most important virtues under, what did you call it? – Capitalism.
- MILTON: Hmm, well I suppose truthfulness – we need people reasonably honest if the economy is going to work problem. Justice. Wisdom – I quite like your description of what you call practical wisdom. Resilience – that's a bit like courage I suppose, the strength to overcome adversity, resist temptation, and keep going in the face of challenges. I might also add compassion, if I'm allowed to have five cardinal virtues – I think we need compassion in the modern world.
- SOCRATES: Well, that list sounds as good as any. Now, I would like you to think about the leaders of some of the very big companies we were talking about. How would you describe them?
- MILTON: Charismatic. Visionary. Risk-takers. Determined. Independent-minded. Ambitious.¹³⁵
- SOCRATES: Or manipulative, grandiose, reckless, stubborn, resistant to feedback, and self-centred.
- MILTON: Hey, wait a minute ...
- SOCRATES: I'm just suggesting that the character traits which you describe in a positive light might also be viewed in a more negative light.
- MILTON: Maybe.
- SOCRATES: You haven't talked about being truthful, acting justly, foresight, prudence, good judgement.
- MILTON: Wait a minute.
- SOCRATES: And you certainly haven't talked about being compassionate.
- MILTON: Okay, I see where this is going now. Look, being a business leader isn't a popularity contest. Their job is to make as much money as possible for shareholders.
- SOCRATES (quietly): Aren't you begging the question again, Milton?
- MILTON: Okay, okay, okay, I get it ... but you still haven't won.
- SOCRATES: I wasn't aware it was a competition.

MILTON: The argument I mean. You've highlighted some of the shortcomings of 'for mastery' for sure, but you haven't really developed an alternative 'for virtue' proposition. Are these virtuous companies really going to be financially sustainable? And can you really point to a coherent ethical code that says we must choose 'for virtue' over 'for mastery'. As far as I can see we're still in an either/or situation. Anyway, look, I'm done. I need a break from all this philosophising. Thanks for the coffee and it's been interesting to meet your friends. Now I need to run. I've got a drinks reception at the Athen's branch of the Heritage Foundation to talk about some policy ideas. See you tomorrow, Socrates. It's been interesting meeting some of your philosopher friends. You guys have got some interesting ideas.

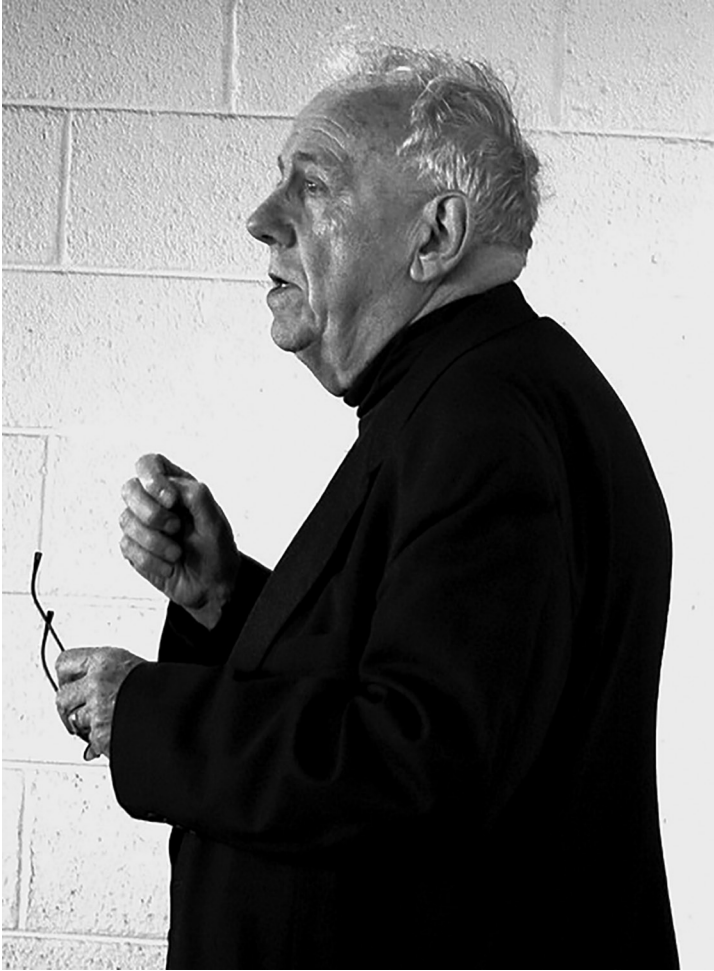
5. On ‘virtue’ – business ethics after ‘mastery’

In this chapter I explore the moral philosophy of the Scottish philosopher Alasdair MacIntyre and show how it has been used to develop an approach to business ethics that might, in turn, be applied in helping to resolve the question of corporate purpose.

In Chapter 1 I explained how virtue ethics made a comeback in the 20th century after World War II. This was heralded by Elizabeth Anscombe with her critique of modern moral philosophy, notably in a talk given on the BBC Third Programme with the provocative title ‘Does Oxford moral philosophy corrupt the young?’, which was subsequently published in *The Listener* on 14 February 1957. The new interest in virtue ethics is exemplified in the work of a number of scholars, including Anscombe herself, her husband Peter Geach, who was also an academic philosopher, and Anscombe’s Oxford colleague, Philippa Foot – but perhaps most notably by Alasdair MacIntyre, who developed a systematic moral framework based on Aristotelian virtue ethics.

Alasdair MacIntyre (see Figure 5.1) was born in Glasgow in 1929. He studied classics at Queen Mary’s University of London, Manchester University, and Oxford University. Thereafter he became something of an ‘intellectual nomad’ – he has taught widely in the UK at Manchester, Leeds, Essex, and Oxford, and in the US at Brandeis, Boston University, Wellesley College, Duke, and Vanderbilt, before eventually settling at the University of Notre Dame, a private Catholic research-intensive university located in Indiana. He died in 2025, not long before this book was published.

MacIntyre first gained attention for his Marxist critiques of liberalism in the 1950s. He was a member of the Communist Party of Great Britain, leaving in 1956, like many other left-wing intellectuals, when Soviet Union troops invaded Hungary to put down the Hungarian uprising. His thought evolved significantly in the 1960s and 1970s, moving away from his Marxist roots and culminating in the publication of *After Virtue* (1981), his most influential book, in which he argued that modern moral discourse had become badly fragmented after the Enlightenment. In *After Virtue*, he argues instead for a return to Aristotelian virtue ethics, advocating a teleological (purpose-based)

Figure 5.1: Alasdair MacIntyre

Source: Photograph by Sean O. Connor/Flickr, CC BY 2.0 licence.¹³⁶

framework rooted in virtue, community, and tradition. An interest in religion coexisted with his early Marxist beliefs, and in *Marxism and Christianity* (1968) he explored the complex relationship between Marxist theory and Christian thought. While critiquing both traditions, he saw potential for dialogue, suggesting that each can learn from the other in addressing human alienation and the importance of fostering genuine community. So perhaps it was not entirely surprising that he converted to Roman Catholicism in the 1980s. Throughout his life, MacIntyre was a prolific writer. In addition to *After Virtue*, his major works include *Whose Justice? Which Rationality?*

(1988), *Three Rival Versions of Moral Enquiry* (1990), *Dependent Rational Animals: Why Human Beings Need the Virtues* (1999), and *Ethics in the Conflicts of Modernity* (2016). These books develop his system of Aristotelian virtue ethics.

MacIntyre's phenomenal research output measured in terms of academic journal articles, essays, books and book chapters, is estimated at over 100 publications. These works span a wide array of topics, including religion, political philosophy, and critiques of modernity, as well as moral philosophy. He was himself extraordinarily widely read, and wrote expansively, often beginning his articles and books with an analysis of what classical literature and ancient philosophy has to say on a topic before constructing his own distinctive viewpoint through his fresh lines of reasoning. The richness of his writing, which it must also be said is at times of byzantine complexity, is in turn extraordinarily generative of new ways of thinking.

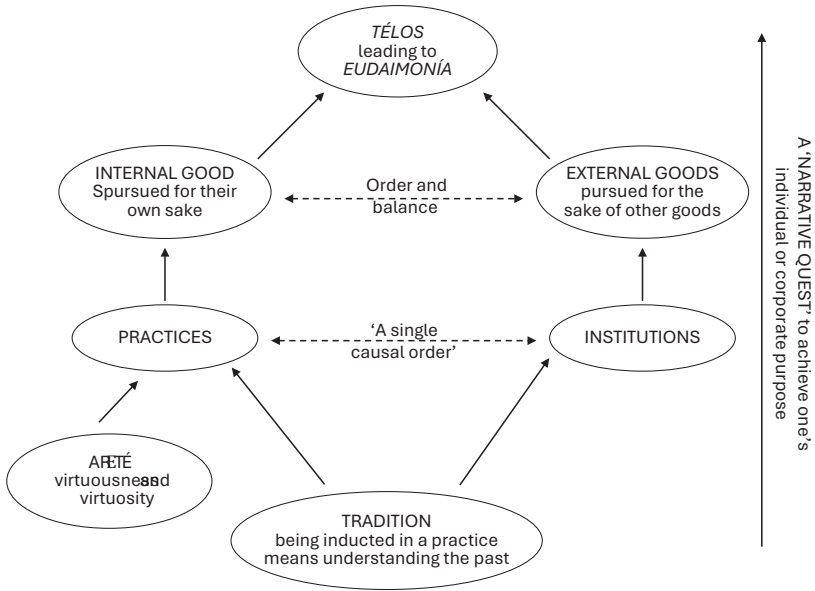
It must be acknowledged at this point that MacIntyre is no apologist for capitalism. In particular, he is a staunch critic of managerialism, which he associates (negatively) with concepts of hierarchy, bureaucracy, efficiency, and effectiveness. Managers are, for MacIntyre, along with aesthetes (like Kierkegaard's 'A') and therapists, three of the principal villains of modernity. To paraphrase what he says about bureaucratic managers in *After Virtue*:

Managers, and most writers about managers, claim to be morally neutral characters whose skill is to devise the most efficient means of achieving whatever end is proposed. Whether a given manager is effective or not is a quite different question from the morality, or otherwise, of the ends which their effectiveness serves. Efficiency and effectiveness should not be regarded as morally neutral. In particular, managerialism involves the manipulation of human beings into compliant patterns of behaviour.¹³⁷

Prior to 2002, most business ethics articles that referenced MacIntyre regarded him as a critic of business. In 2002 a notable shift occurred when a paper by Geoff Moore of Durham University was published in *Business Ethics Quarterly* that showed how MacIntyre's work could be interpreted in a way which was more favourable to business.¹³⁸ Since then, Moore, along with a number of other management scholars, have demonstrated that the complete, ordered, and holistic nature of MacIntyre's ethical system makes it particularly helpful as a basis for constructing a framework for evaluating company purpose and strategy from a socio-economic and ethical perspective¹³⁹. Hence, the application of MacIntyre's work to business ethics should be regarded as 'MacIntyrean', rather than being 'of MacIntyre' – a technical distinction perhaps, but a necessary one in order to show due respect to the author of *After Virtue*.

Figure 5.2 provides a schematic of MacIntyre's 'virtues–goods–practices–institutions' framework of ethics. The framework can be applied to both

Figure 5.2: The ‘virtues–goods–practices–institutions’ framework



Source: Author, after MacIntyre (1981).

individuals and organisations. As Thomas D. D’Andrea puts it in his painstaking study of Alasdair MacIntyre’s thought:

MacIntyre endows virtue with a social locus as opposed to the personal locus more common in the Aristotelian tradition. Social teleology, the sustaining and furthering of some collective undertaking, is to replace biological teleology or the sustaining and the development of the self.¹⁴⁰

Organisations are communities. In communities, both personal goods and the common good are inextricably intertwined.

Purpose and a ‘narrative quest’

The starting point in MacIntyre’s ethical framework is the critical importance of purpose or *télos* in Greek – both primary and secondary purpose. Following Aristotle, an individual’s primary purpose is *eudaimonía*, normally translated as ‘flourishing’, but also incorporating the contemporary notion of ‘wellbeing’. Secondary purposes are more specific – they might include, for example, being an excellent scholar, engineer, or athlete. By setting out to

achieve excellence in a particular profession, career, or sport, we hope thereby to achieve, or at least contribute to, our overall sense of wellbeing.

In his book *The Corporation in the 21st Century*, the economist John Kay argues that the purpose of a company is 'the flourishing of the multiple stakeholders of the corporation: employees, investors, suppliers and customers, the communities in which it operates and the corporation itself'.¹⁴¹ Another economist, Colin Mayer, argues that the corporate equivalent of *eudaimonía* is 'prosperity'. As health is to medicine and justice is to law, so, Mayer argues, prosperity is to business.¹⁴² This is not just prosperity for the few, for current shareholders and executives, but prosperity for the many, including employees, communities, and not-yet-born future generations. The secondary purpose of a business is the kind of thing found in a company's mission statement; for example, 'to provide customers with the energy they need for today and tomorrow' (Shell) or simply 'to find, produce, refine, and distribute oil and gas'.

The teleological nature of virtue ethics means that individuals and organisations are on a 'narrative quest'. MacIntyre notes how, in the Homeric tradition, the chief means of moral education was by telling stories.¹⁴³ Human beings are 'story-telling animals'.¹⁴⁴ Our life stories help us to explain our past and future selves.¹⁴⁵ In much the same way, business strategies can be thought of as 'strategic quests' – imagined futures that help companies to navigate what lies ahead. Scenario planning, the approach to strategic planning made famous by Shell in the 1970s, exemplifies this.¹⁴⁶ Thus, the narrative quest is both individual and joint. Within an organisation there is a shared sense of *télos*. Individual goods and the commonwealth are interrelated.

Goods

In pursuit of purpose we produce *goods*, things of value, both tangible and intangible. *Internal goods* are things of value that are pursued for their own sake – excellent work, fine art, beautiful music, the ideal golf swing, and the perfect cover drive. Internal goods are things to which we aspire – achievements, accomplishments, and things associated with intrinsic motivation that make us feel fulfilled. In a business context, internal goods include the best products, best staff, and best customer relationships. *External goods* are goods pursued for the sake of other goods. These include money, power, and status. They are enablers, things that help us to achieve the internal goods to which we aspire. There is a risk in pursuing external goods for their own sake. They provide extrinsic motivation, but in themselves leave us unfulfilled, always wanting more.

The relationship between internal goods and external goods is an important one. There is an order – internal goods take priority over external goods – but also an important sense of balance, Aristotle's mean. In this way of thinking, the pursuit of wealth, or 'shareholder value maximisation' if you like, makes no sense in its own right, but good financial performance is necessary for financial

sustainability and for enabling the creation of internal goods. In a corporate context, this means that businesses must generate sufficient profits to satisfy shareholders, bankers, executives, and employees – indeed all stakeholders who are in any way dependent upon the financial resources produced by the company.

Practices and institutions

A *practice* is a particular kind of skill, specifically defined by MacIntyre as: ‘any coherent form of socially established cooperative human activity through which internal goods are realized’. *Institutions*, on the other hand, are:

characteristically and necessarily concerned with external goods ... they distribute money and other material power and status as rewards ... no practice can survive for any length of time unsustained by institutions.

One often quoted example that MacIntyre gives to illustrate the distinction is chess, a practice, and a chess club, an institution where chess is played. Chess is a higher-order skill that has to be learnt and commonly requires years of practice in order to become proficient. Other examples might include playing a musical instrument (a practice) and a music college (an institution), or medicine, a practice, and a medical school or medical royal college (a professional body responsible for training and development of a specific medical speciality), both of which are institutions. In a business context, professions like engineering or accountancy are practices, and their respective professional bodies, such as the Institution of Mechanical Engineers and Institute of Chartered Accountants in England and Wales, are institutions.

Curiously, MacIntyre denies that business management is a practice, probably because managers, along with aesthetes and therapists, are one of his ‘villains of modernity’. He writes:

I am not of course questioning the existence of genuine experts in many areas: the biochemistry of insulin, historical scholarship, the study of antique furniture. It is specifically and only managerial and bureaucratic expertise that I’m going to put into question. And the conclusion to which I shall finally move is that expertise does indeed turn out to be one more moral fiction: because the kind of knowledge which would be required to sustain it does not exist.¹⁴⁷

I would contend that MacIntyre is jumping the gun here. Because of his dislike of capitalism and distrust of business and management, he assumes that capitalism’s practitioners play no part in creating moral ‘goods’. But that is to prejudge the issue. Part of the thesis of this book is that there is such a thing as ‘good business’ and values-driven business leadership.

Virtues

Virtue ethics are person-centred. At an individual level, the focus of ethics is on character. Virtuous acts are those carried out by virtuous people. What then makes someone a virtuous person? What behaviours do they exhibit? At a corporate level, virtuous organisations are those in which good behaviour is encouraged, affirmed, and even mandated. They are typically led by virtuous people, people of character, 'great men' (sic), as Thomas Carlyle would have it, although today we would contest Carlyle's use of gender-specific terminology and question whether all his 'great men' were in fact models of virtue.¹⁴⁸

According to Philippa Foot, one of the Oxford philosophers who was instrumental in the revival of virtue ethics after Second World War, there are three essential features of a virtue. First, a virtue is a disposition of the will, a 'hexis' in Aristotle's terminology, something induced by habit which leads to a person having appropriate feelings. Second, a virtue is beneficial to others, or to its possessor as well as to others. Third, it is corrective of some bad general human tendency.¹⁴⁹ Business ethicist Robert C. Solomon defines a virtue as: 'a pervasive trait of character that allows one to "fit into" a particular society and to excel in it'.¹⁵⁰ Alasdair MacIntyre himself says:

The virtues are precisely those qualities, the possession of which will enable an individual to achieve *eudaimonía* [flourishing], and the lack of which will frustrate [their] movement towards that *télos* [purpose].¹⁵¹

Elsewhere he describes a virtue as 'an acquired human quality the possession and exercise of which tends to enable us to achieve those goods which are internal to practices'. Virtue ethics involves the pursuit of excellence – 'virtuousness' and 'virtuosity' are both involved. The Greek word *areté* means both 'virtue' and 'excellence'. Virtues are, however, not the same as knowledge or technical skills. All of these are needed in order to be excellent.

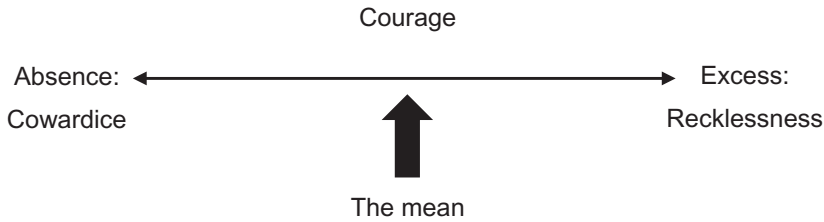
That much is clear. What is much less clear is what the most important virtues actually are. You might like at this point to look back at your own answer to the question of what the character traits of a good business leader are (see Figure 1.11 in Chapter 1). Figure 5.3 provides a number of other possible classifications.

The cardinal virtues, temperance (*sophrosynē* or *enkratia*), prudence (*phronesis*), sometimes translated as 'practical wisdom', courage (*andreia*), and justice (*dikaiosune*) have their roots in ancient philosophy and have been central to ethical thinking in the Western tradition.¹⁵³ In *Republic*, Plato explains how the cardinal virtues are essential to the harmony of the soul and the *polis* (the city-state). He associates each virtue with a part of the soul. Prudence governs reason, courage governs spirit, and temperance governs desires, while justice harmonises the other three virtues. Aristotle emphasises similar qualities in the *Nicomachean Ethics*, linking virtues to the development of moral

Figure 5.3: Typologies of virtue¹⁵²

Cardinal virtues ^a	MacIntyre ^b	Solomon ^c	Moore ^d	Peterson and Seligman ^e
Temperance or moderation (<i>Sophrosynē</i> or <i>enkrateia</i>)	Justice	Community	Integrity	Wisdom (<i>Curiosity</i> , <i>creativity</i> etc.)
Prudence or practical wisdom (<i>Phronesis</i>)	Courage	Excellence	Honesty	Courage (<i>Persistence</i> , <i>Integrity</i> , etc.)
Courage (<i>Andreia</i>)	Truthfulness	Role identity	Fairness	Humanity (<i>Kindness</i> , <i>emotional intelligence</i> , etc.)
Justice (<i>Dikaiosune</i>)	Integrity	Integrity	Courage	Justice (<i>Fairness</i> , <i>citizenship</i> , etc.)
		Judgement	Compassion	Temperance (<i>Forgiveness</i> , <i>humility</i> , <i>self-control</i> , etc.)
		Holism	Humility	Transcendence (<i>Gratitude</i> , <i>humour</i> , <i>appreciation</i> , etc.)
			Practical wisdom	

Sources: ^aPlato, *The Republic*, Book IV, pp. 426–435; Aristotle, *Rhetoric*, 1366b1; Cicero, *De Inventione*, II 53. D’Andrea, T. (2006) *Tradition, Rationality, and Virtue: The Thought of Alasdair MacIntyre*, London: Routledge, p. 272–3. ^cSolomon, R. (1992) *Ethics and Excellence*, Oxford: Oxford University Press, and Solomon, R. (1992) ‘Corporate roles, personal virtues: an Aristotelean approach to business ethics’, *Business Ethics Quarterly*, vol. 2, no. 3, pp. 317–19. <https://doi.org/10.2307/3857536>. ^dMoore, G. (2016) *Virtue at Work – Ethics for Individuals, Managers, and Organizations*, Oxford: Oxford University Press. ^ePeterson, C.; and Seligman, M. (2004) *Character Strengths and Virtues: A Handbook and Classification*, Oxford: American Psychological Association and Oxford University Press.

Figure 5.4: Aristotle's conception of the virtue of courage

Source: Author.

character through habit. However, whereas for Plato virtues were absolutes, associated with his theory of the forms, Aristotle links virtues with his concept of the 'golden mean'. For example, courage is the point of balance between two vices, cowardice and recklessness (see Figure 5.4).

Cicero popularised the cardinal virtues for a Roman audience, emphasising their importance for personal and civic life. He viewed them as an essential part of moral and political leadership. Augustine integrated the cardinal virtues into Christian theology, aligning them with the theological virtues (faith, hope, and charity). For Augustine, the cardinal virtues reflect the natural order, but require divine grace for perfection. In *Summa Theologica*, Thomas Aquinas systemised the virtues, presenting them as habits that perfect human actions: prudence guides practice reason, justice directs relationships with others, temperance moderates desires, and courage strengthens the will in adversity. Aquinas sees the cardinal virtues as complementary to the three theological virtues, necessary for living an ethical and rational life.

The cardinal virtues continued to influence medieval and early modern ethical thinking. The scholastics (Anselm, Peter Abelard, Duns Scotus, and William of Ockham) continued to refine Aquinas's synthesis of the cardinal and theological virtues. Renaissance humanists re-examined classical sources, reviving a secular emphasis on the virtues in public and private life. During the Enlightenment, as we have seen, scholars moved away from the cardinal virtues, focusing on rights, duties, utility, and universal principles, rather than virtue ethics.

In reviving virtue ethics in the 20th century, MacIntyre sees three key strands in past thinking about the virtues in the Western tradition, represented by the moral theories of, respectively, Homer, Aristotle, and Benjamin Franklin. In *After Virtue*, he puts it like this:

We have at least three very different conceptions of a virtue to confront: a virtue is a quality which enables an individual to discharge his or her social role (Homer); a virtue is a quality which enables an individual to move towards the achievement of their specifically

human *télos*, whether natural or supernatural (Aristotle, the New Testament and Aquinas); a virtue is a quality which has utility in achieving earthly and heavenly success (Franklin).¹⁵⁴

In drawing up his own list of the most important virtues, MacIntyre takes justice and courage of the cardinal virtues as a starting point, but emphasises the importance of truthfulness, in order to ensure that we are reliable in our communications with others, as well as integrity – the habit of character, which maintains through time a coherence, wholeness, and unity of purpose.¹⁵⁵

Robert Solomon, a business ethicist, argues that there are six dimensions of (business) virtue ethics. *Phronesis* (which Solomon describes as ‘good judgement’) we would recognise from the cardinal virtues, and Solomon, like Geoff Moore, picks integrity as an important corporate virtue. To these he adds ‘community’ (or perhaps more precisely the ability to live in community and foster good community relations), ‘role identity’ (understanding and carrying out one’s role in an organisation effectively), and ‘holism’ (having the same values in all aspects of one’s life, and not one set of values at work and another at home). He also adds ‘excellence’ (pursuing excellence in all things), although in many ways that is double counting, as *areté* means both excellence and virtue.

Geoff Moore chooses integrity, honesty (truthfulness and transparency), fairness (which is closely related to the cardinal virtue of justice), courage (another of the cardinal virtues), compassion (concern for the well-being of others, particularly employees, customers, and society at large), humility (acknowledging one’s limitations and being open to learning from others), and practical wisdom, the cardinal virtue of *phronesis*, the ability to make sound decisions that balance competing interests, as well as short and long-term goals).

Christopher Peterson and Martin Seligman are psychologists working in the field of positive psychology, rather than philosophers, and so take a different approach. In their 2004 handbook called *Character Strengths and Virtues*, they identify 24 specific character strengths classified under six broad categories of virtues. This classification was developed after an extended period of research. They began by examining the history of religion, politics, education, and ancient philosophy, for information about how virtues were classified across cultures and over time. Six core virtues emerged from this analysis. They continued by carrying out an exhaustive literature search across a number of domains, including philosophy, psychology, psychiatry, and child development, in the process identifying a large number of possible character strengths, which they eventually refined into 24 types, categorised under the six core virtue headings. Having done this, they developed a questionnaire, the VIA Inventory of Strengths (VIA-IS), which they have tested extensively in over 40 countries. Their classification provides an interesting counterpoint derived using social science research methods, compared with the typologies constructed by moral philosophers and business ethicists.

Rationality and tradition

In *Three Rival Versions of Moral Enquiry*, Alasdair MacIntyre discusses three competing frameworks for understanding and justifying moral reasoning.

1. The 'encyclopaedic' tradition, as MacIntyre calls it, is rooted in the Enlightenment. It aims to construct an objective body of knowledge through scientific method and empirical evidence, presenting itself as neutral and universally valid. Encyclopaedists emphasise detachment from tradition and aim to offer explanations free from metaphysical or theological commitments.
2. The 'genealogical' tradition, influenced by Friedrich Nietzsche and the Existentialists, and later developed by postmodern thinkers, critiques claims of universality and objectivity in the encyclopaedic tradition. It argues that all claims to knowledge and morality are expressions of power, historical contingencies, or social constructions. Rationality in this view is fragmented. There is scepticism about grand narratives or claims of absolute truth.
3. The Thomist tradition emphasises tradition. Based on the work of Thomas Aquinas and extended by MacIntyre, this method grounds rational enquiry in a tradition-based framework of knowledge. Rationality is embedded with a historical and cultural context. Thomism seeks to reconcile faith and reason, arguing for a teleological view of human life where rationality is directed towards the realisation of human flourishing and the ultimate good.

Traditions evolve and change over time, with certain notable breakpoints. If we take the Western ethical tradition as dating back to Homeric times, evolving through 5th century BCE Athens and Imperial Rome to the Byzantine Empire, then a major breakpoint occurred when Constantine converted to Christianity. The next major breakpoint was the Enlightenment, which sought to break from the Christian tradition of Augustine and Aquinas that had prevailed throughout the medieval period.

While there is much in the Enlightenment project, especially the Scottish Enlightenment, that MacIntyre admires, he is critical of the attempts of Enlightenment thinkers such as Locke and Kant to justify moral principles without recourse to any historical tradition. Enlightenment philosophers sought to construct moral theories from first principles. They justify claims made within those theories on the basis of their deduction from these first principles. But the only thing that justifies the first principles themselves, and hence the theories on which they are based, is the particular tradition of which they are part. Modern liberalism, born out of the Enlightenment and in many ways antagonistic to all traditions, has transformed itself gradually into what is now clearly recognisable even by some of its adherents as one more tradition. Yet it seeks to separate out questions of fact and value in

a way that leads inexorably to the poverty of modern moral philosophy of which Elizabeth Anscombe was so critical. Christianity and Marxism, both of which MacIntyre has subscribed to at different times, oppose the liberal fact-value dichotomy by espousing metaphysical and ethical systems in which an understanding of the world and how we should act within it are integrally connected. But it is the Enlightenment project that is the basis of the modern liberal tradition. The premises of moral arguments today are described by MacIntyre as 'incommensurable' because they are deployed in a piecemeal fashion in settings that are no longer structured by any coherent, shared, moral framework. MacIntyre's argument, with which many would agree, is that we are now in a time of crisis over what should constitute the 21st century moral tradition.

A tradition is a shared set of background beliefs. In MacIntyre's words: 'a tradition is an argument extended through time in which certain fundamental agreements are defined and redefined in terms of two kinds of conflict'. One conflict is with those critics who sit outside the tradition and reject key parts of the fundamental agreements. The other is with people inside the tradition who engage in 'internal debates through which the meaning and rationale of the tradition come to be expressed'. Progress comes from dialogue and dialectic.¹⁵⁶

One of the ways in which MacIntyre departs from the genealogical critics of the Enlightenment is in his belief that it is possible to make rational choices between traditions. Not for him the point/counterpoint of Kierkegaard's *Either/Or* where, on at least one interpretation of the text, there is no right answer, but only a choice between two traditions without any adequate criteria to determine which is right. Practical wisdom, or *phronesis*, means that we should be prepared to adopt whichever statement or set of statements about any given subject matter that best withstands critical argument. As MacIntyre puts it:

that thesis which most successfully withstands all attempts to refute it – characteristically, of course, such a thesis will have had to be modified and reformulated in the course of its encounters with a variety of objections – is that which claims our rational allegiance.¹⁵⁷

Every tradition has its own *logos*, a Greek word that broadly encompasses notions of language, reason, and order, and functions as a bridge between thought, expression, and the structure of reality. Rational resolution between traditions is possible by pitting one *logos* against another and determining which of the two better stands up to argument. For philosophers of science, this bears comparison with Karl Popper's thesis of epistemological fallibilism – while it is not possible to prove a proposition is correct by finding an increasing amount of positive evidence, it is possible to disprove a proposition by finding negative evidence; hence, for Popper, falsifiability rather than verifiability is the true measure of scientific thinking.¹⁵⁸

Traditions can be cut and classified in different ways, depending on whether the primary focus is on politics, economics, culture, or religion, and at various levels of analysis. For current purposes we need only focus on two: American neoliberalism, which is closely associated with shareholder primacy, and European social democracy, which is closely associated with stakeholder theory.

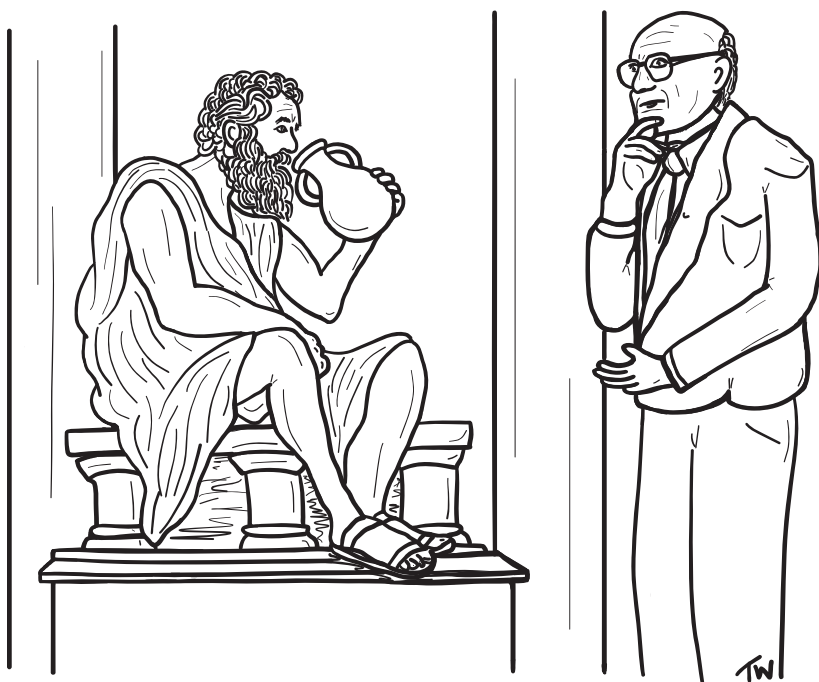
Business ethics after MacIntyre

Alasdair MacIntyre's philosophy, emphasising as it does the role of character, virtue, internal as well as external goods, the importance of community, and the significance of tradition, provides an important counterpoint to the individualistic and utilitarian approaches often found in business ethics. In conjunction with the thinking of Blair and Stout's theory of team production, and Joseph Heath's market failures approach to business ethics, it helps us to move to a possible answer to the question 'what's a company for'? In the same way that virtue ethics advances the thesis 'just acts are the kind that a just person would perform', in Chapter 6 I shall argue that in business ethics virtuous acts are of a kind that are associated with virtuous corporations, and that virtuous corporations must be led by virtuous people. Before you dismiss this as corporate gobbledegook or an unwelcome distraction from a focus on company performance, I will also argue that financial sustainability is a fundamental component of 'for virtue' corporate purpose.¹⁵⁹

Dialogue V: Socrates and Milton

In which we say goodbye to Socrates and Milton Friedman

Figure V: Socrates and Milton



Source: Tim Wakeling.

Socrates is sitting on a plinth in the Agora drinking from a clay flask.

MILTON: Socrates, my friend, how are you?

SOCRATES: Not so great, to be honest, Milton. I'm in a bit of trouble with the polity, the city-state. I've been indicted.

- MILTON: Oh dear, I'm sorry to hear that. Is it serious?
- SOCRATES: Well it could be, I'm afraid, existential even. I'm currently studying eschatology.
- MILTON: What's that, insects?
- SOCRATES: No, Milton, 'last things'. Anyway, let's change the subject – I don't want to talk about it anymore, too depressing. *(He takes a swig from his clay flask.)*
- MILTON: What's that you're drinking?
- SOCRATES: Dandelion and burdock. Very refreshing. Better than some of the other things I've been offered recently. Look, I ask the questions. I want to talk to you again about corporate purpose. Everything that's going on at the moment makes me think that it's important that we bring our dialogue to a conclusion.
- MILTON: Okay, old boy. Where shall we start?
- SOCRATES: Let me summarise. We have reached the point where we are discussing two propositions. The first proposition is that the purpose of a company is to achieve 'mastery', a modified version of shareholder primacy that incorporates ideas about having the best products, best people, best levels of customer satisfaction, and the best relationships with suppliers – all with a view to maximising efficiency and effectiveness and realising the greatest profit, the capitalist's dream scenario.
- MILTON: I like it.
- SOCRATES: Alternatively, the purpose of a company is 'for virtue', a modified version of stakeholder theory in which the focus is on creating firm value over the long term for the benefits of all those who make specific investments in a company, investors, employees, and some suppliers who are, in effect, in partnership with the company, and that also incorporates ideas about saving the planet, preventing some markets from being dominated by a small number of mega-corporations, and reducing inequality.
- MILTON: A bit fluffy for me.
- SOCRATES: You argue, based on your reading of Kierkegaard's book *Either/Or*, that while 'for mastery' and 'for virtue' are both potentially valid answers to the question of what's a company for, there is no ethical decision-making process

which allows us to choose between them. It is an either/or situation.

MILTON: You've got it.

SOCRATES: My thesis is that that conclusion is not good enough, that it must be possible for a rational person to develop an argument that determines which one or other of 'for mastery' or 'for virtue' is a better answer to the question.

MILTON: Well good luck with that.

SOCRATES: In our last conversation I demonstrated some of the limits of shareholder primacy, in particular that there is an inexorable trend towards the domination of certain markets by very large imperialistic companies, and that capitalism is unable by itself to solve the problem of anthropogenic climate change. You've also got to acknowledge that 21st-century capitalism seems to involve some extremes of inequality – the top 1% of the population own nearly half the world's wealth and Elon Musk's net worth is greater than Denmark's gross domestic product.¹⁶⁰ I also put forward the case for developing a new consensus around our understanding of what constitute 'corporate virtues' – the characteristics which we would expect to see exhibited by good corporate leaders, which would be mirrored in the cultures of the companies which they managed. You argued, not unreasonably, that I had not really developed an alternative 'for virtue' proposition. In particular, you asked whether virtuous companies were going to be financially sustainable. And you said I had not been able to point to a coherent ethical code that says we must choose 'for virtue' over 'for mastery'.

MILTON: Thanks for the 'not unreasonably' qualifier.

SOCRATES: Credit where credit is due – your counter argument is a reasonable one. I recognise that I need to do two things. First, I need to articulate a more complete version of the 'for virtue' thesis. Second, I must explain how, when it comes to rational enquiry, we can distinguish between a better answer and a worse answer.

MILTON: Sounds good to me.

SOCRATES: A 'for virtue' company is one which has the objective of ensuring that everyone who actively participates in its success prospers in an equitable fashion, be they

investors, employees, supplier partners, or the community. In other words, a company's *télos* is prosperity for everyone involved.

MILTON: What's *télos* again?

SOCRATES: A company's purpose.

MILTON: Ah yes, well keep going.

SOCRATES: Value should be shared according to the principle of fairness, taking into account the contributions made by each party. Excellence should be pursued in all things, including products, people, customer relationships, and supplier relations – remember that *areté*, the Greek word for virtue, also means 'excellence'. Attempts to exploit what you have described as negative externalities, or to create monopolies, or to deliberately take actions that increase income inequality, should be regarded by the company as unethical. A company should actively promote the virtues, which include practical wisdom, courage, justice, and temperance.

MILTON: What's 'temperance' again?

SCORATES: By temperance, I mean a humility, self-control, and a capacity for forgiveness. The Greek word is quite hard to translate.

MILTON: Okay, sounds great. But is this company going to make any money?

SOCRATES: It won't make anyone prosperous if it doesn't, so yes absolutely – financial sustainability, generating sufficient profits to satisfy all those who make investments, whether in cash or in kind, is certainly a key part of its *télos*.

MILTON: Amen to that.

SOCRATES: I have set out what I hope you will agree is a well-articulated theory as to what 'for virtue' as answer the question of corporate purpose in fact comprises. Now I want to explain why it is rational in the light of this theory to subordinate the 'for mastery' thesis to the 'for virtue thesis. So the second argument goes like this. I imagine that you will be familiar with the problem of induction – past experiences cannot reliably predict future events; no amount of observations of the form 'that X is Y' can logically lead to the conclusion 'all Xs are Y'. You may also know

about Karl Popper's solution to the problem of induction – that falsifiability rather than verifiability should be the distinguishing characteristic of what is, and what is not, a scientific statement.

MILTON: Yes, I know about all that stuff.

SOCRATES: Well, in much the same way my argument is that the thesis which most successfully withstands all attempts to refute it – characteristically, of course, after having been modified and reformulated in the course of its encounters with a variety of objections – is the one which claims our rational allegiance

MILTON: That sounds suspiciously like a quote.¹⁶¹

SOCRATES: A paraphrase perhaps, but you're right – I've been reading some of the work of a philosopher called Alasdair MacIntyre. He's a good chap, one of the new generation of virtue ethicists, a big believer in the things that can be learnt from ancient philosophers. I'm hoping that he will carry forward the flame of the best ethical thinking.

MILTON: Socrates, my old mate, that's very eloquently and elegantly put – well-argued and entirely rational. I am almost convinced.

SOCRATES: So, to summarise. Shareholder primacy has served the world pretty well for many years, but it has now been found wanting. It is unable to deal with the challenges facing 21st-century capitalism – anthropogenic climate change, extreme inequality, and the domination of certain markets by very large companies. From a macro-ethics perspective, holes can be picked in the 'for mastery' thesis. It is time for a new consensus of what should constitute the purpose of the corporation in the 21st century. The best thing available is the 'for virtue' thesis, recognising that financial sustainability has to be an integral part of that thesis. Successful companies are the bedrock of a successful economy, and a successful economy is key to a stable and prosperous society. But profits aren't everything, shareholder value maximisation isn't the only game in town and shareholder primacy is a myth. It's time for a new paradigm, a new consensus, a new tradition of 'good business', articulated by corporate leaders, accepted by investors, and enshrined in laws by governments. In that way capitalism might have a future. Now Milton, I trust you are enlightened. There are some difficult days ahead.

I'm convinced that the future of humankind is bright. I may not get there with you, but I want you to know that that you can prosper and that the planet can be saved.¹⁶² Humanity just has to do the right thing, to make some good choices, and quite quickly.

MILTON: I hear you. I have to admit that you have made a strong case. Now I'm sorry to butt in, but there are a couple of chaps here who want to talk to you, military types, they want you to go with them.

SOCRATES: I was expecting them. Fortunately I have said all that I wanted to say to you. Farewell and good luck. You might need it.

6. What's a company for? A call for responsible business

We concluded that the purpose of business is to solve the problems of people and planet profitably, and not profit from causing problems. We proposed a framework for 21st century business based on corporate purposes, commitments to trustworthiness, and ethical corporate cultures.

Principles for Purposeful Business
A report by The British Academy, 2019.

As well as Milton Friedman, corporate leaders still invoke Adam Smith, the 18th-century Scottish intellectual who pioneered free-market economics, when they talk about the merits of capitalism. Smith, like Friedman, believed in profit-maximisation, strong incentives and that the pursuit of self-interest, which he saw as being key to economic growth and the development of the common wealth. He shared many businessmen and -women's distaste for government regulation and high taxes. But Smith favoured owner-managed businesses – the dominant business vehicle at the time he was writing – rather than joint-stock companies. He was certainly not a fan of large corporations:

The directors of such companies, however, being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honour, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company.¹⁶³

Modern economists call this the agency problem, and believe it can be fixed with correct incentives and proper governance. Smith was not so sure. He particularly disliked how concentrated market power and the desire to construct monopolies can lead large corporations to act in ways that harm consumers and undermine the public good.

Adam Smith was a philosopher as well as an economist. In *The Theory of Moral Sentiments* he discusses the moral consequences of individuals' decisions, aware that unbridled self-interest can sometimes be damaging for

society as a whole.¹⁶⁴ There is a growing body of literature arguing that Smith was among the most powerful critics of poverty and inequality, and an advocate of the importance of responsible business.¹⁶⁵ Smith wrote at a time when there was only a limited understanding of the unintended harmful side-effects of certain business activities. The economic theory of externalities, with its specific focus on policy responses including taxes and regulation, was developed in the early 20th century by scholars such as the Cambridge economist Arthur Pigou. Man-made climate change was not considered to be a problem in the 18th century.

Responsible business

The concept of responsible business is not a new thing. We need only look back to some of the examples of philanthropic businessmen in the 19th century. Robert Owen, a Welsh industrialist and social reformer, is famous for his work at New Lanark, a village built around his textile-factory in Scotland that became a kind of social experiment in humane industrial management during the early part of the Industrial Revolution. Quaker families, such as the Cadburys, Rowntrees, and Frys, promoted cocoa and chocolate drinks in the belief that chocolate was a wholesome, health-giving alternative to alcohol. Titus Salt, the textile manufacturer, built the model village of Saltaire for his workers at Salts Mill. David James writes in the *Oxford Dictionary of National Biography*:

Salt's motives in building Saltaire remain obscure. They seem to have been a mixture of sound economics, Christian duty, and a desire to have effective control over his workforce. There were economic reasons for moving out of Bradford, and the village did provide him with an amenable, handpicked workforce. Yet Salt was deeply religious and sincerely believed that, by creating an environment where people could lead healthy, virtuous, godly lives, he was doing God's work.¹⁶⁶

In much the same way, William Hesketh Lever, like Titus Salt a member of the Congregational church, designed Port Sunlight, a model village in Merseyside, to provide housing and community activities for men and women working at the Lever Brothers' factory making Sunlight soap. Lever was, like Salt, no doubt somewhat autocratic and paternalistic, and his business practices in Africa did not replicate his fair dealings in England, but infant mortality in Port Sunlight at the turn of the 19th and 20th centuries was half what it was across the Mersey in Liverpool, and many of the employees of Lever Brothers prospered while they worked for the company, along with their wives and husbands and adult children, for the whole of their lives.

The Lever Brothers story is interesting for another reason. In 1929, Lever Brothers merged with the Dutch company Margarine Unie to become

Unilever, eventually becoming one of the world's largest fast-moving consumer goods companies. Between 2009 and 2019, Unilever was run by Paul Polman, a champion of socially responsible business. Under the headline 'The parable of St Paul', *The Economist* newspaper described his corporate philosophy in the following terms:

PAUL POLMAN runs Europe's seventh-most valuable company, Unilever, worth \$176bn, but he is not a typical big cheese. A Dutchman who once considered becoming a priest, he believes that selling shampoo around the world can be a higher calling and detests the Anglo-Saxon doctrine of shareholder primacy, which holds that a firm's chief purpose is to enrich its owners. Instead Mr Polman preaches that companies should be run 'sustainably'—by investing, paying staff fairly, and by making healthy products with as little damage as possible to the environment. This is actually better for profits in the long run, he argues: society and shareholders need not be in conflict.¹⁶⁷

In February 2017, Kraft Heinz Company launched an ultimately unsuccessful hostile takeover bid for Unilever. Kraft Heinz's bid was characterised by some commentators as pitting red-in-tooth-and-claw capitalism against green purposeful business. Kraft had form. In 2010, Kraft acquired Cadbury in a controversial takeover. Following the acquisition of Cadbury, Kraft reneged on a number of its promises, including to stick with Cadbury's commitment to using Fairtrade cocoa beans to produce its chocolate, confirming the suspicions of many UK-based business commentators that the American company was 'only in it for the money'. One journalist described the controversial takeover as 'how one of Britain's best-loved brands went from a force for social good to the worst example of corporate capitalism'.¹⁶⁸

Paul Polman stepped down as CEO of Unilever at the end of 2018. He has continued to work on sustainability, climate change, and inequality, and is a leading proponent of 'net positive' business, the subject of a book co-authored with Andrew Winston called *Net Positive: How Courageous Companies Thrive By Giving More Than They Take*, published in October 2021. He was succeeded by Alan Jope, an internal candidate, who continued Polman's strategy. Jope was replaced in 2023 following widespread investor discontent over the misconceived bid for GSK's consumer pharmaceutical business and the company's perceived lacklustre financial performance. His replacement, Hein Schumacher, announced a radical change in Unilever's strategy with a renewed focus on financial performance. While Schumacher believed that for some brands purpose was central to marketing and positioning to consumers, this was not true for others, for whom it had become an 'unwelcome distraction'. He added that the time and investment the company had put into sustainability had had a negative impact on its financial performance.¹⁶⁹ In this respect, Schumacher's strategy was playing to the gallery of a number of

Unilever investors, such as Terry Smith, CEO of the London-based investment management company Fundsmith, who once described Unilever management's focus on 'net positive business' under CEOs Paul Polman and Alan Jope as 'corporate goobledegook'.¹⁷⁰

The Unilever story, and the story of the takeover of Cadbury by Kraft, are stark reminders of how difficult it is for large listed companies to maintain a 'for virtue' corporate strategy in the face of activist investors solely focused on financial returns. Therein lies the problem. If investors continue to believe that the sole responsibility of directors and managers is to maximise financial returns, then shareholder primacy will continue to be the dominant paradigm – the capital markets and market for corporate control will ensure that that is the case. But markets are not ethical wastelands and investment funds should not be moral vacuums. Investment managers act on behalf of investors – that is all of us, the general populace, as it is our pension fund monies and other savings that they are investing. They should take our long-term financial and ethical preferences into account. And the directors and managers of investment funds have moral responsibilities themselves, which they should not put aside simply on the specious grounds that 'business is business'. The field of business is not a morality-free zone. Nor is investment management. Surely no truly rational person really believes that it is?

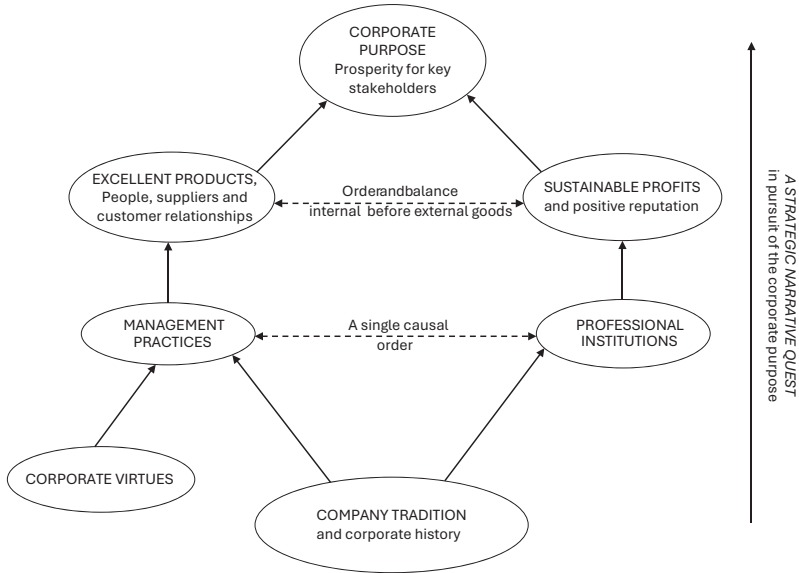
What a company really is, and what it should be

I hope by now it is clear that, while the stripped down, nexus of contracts, shareholder primacy, standard model of the firm is a useful analytical tool, it does not properly represent what a company really is. To say that it is, is like arguing that a musculoskeletal diagram is a complete representation of a person. It isn't. We need a richer model.

My thesis is that Blair and Stout's theory of team production, Joseph Heath's market failures approach, and MacIntyrean virtue ethics, can together be combined to provide a better answer to the question 'what's a company for'? So now we have a possible answer. In many ways, Socrates has put it better than I can. But on the basis that a picture is worth a thousand words, as Milton said in the third dialogue, here goes.

The schematic in Figure 6.1 depicts how what constitutes a 'for virtue' business can be summed up in eight principles:

1. The purpose of the company is to pursue prosperity for all investors, executives, employees and other stakeholders who make specific investments in the company.
2. Stakeholders are those who make specific investments in the company. This includes those who invest in physical capital (e.g., plant and machinery that are specific to the production process), which is funded by financial capital provided by shareholders; human capital

Figure 6.1: A new framework for evaluating company performance

Source: Author.

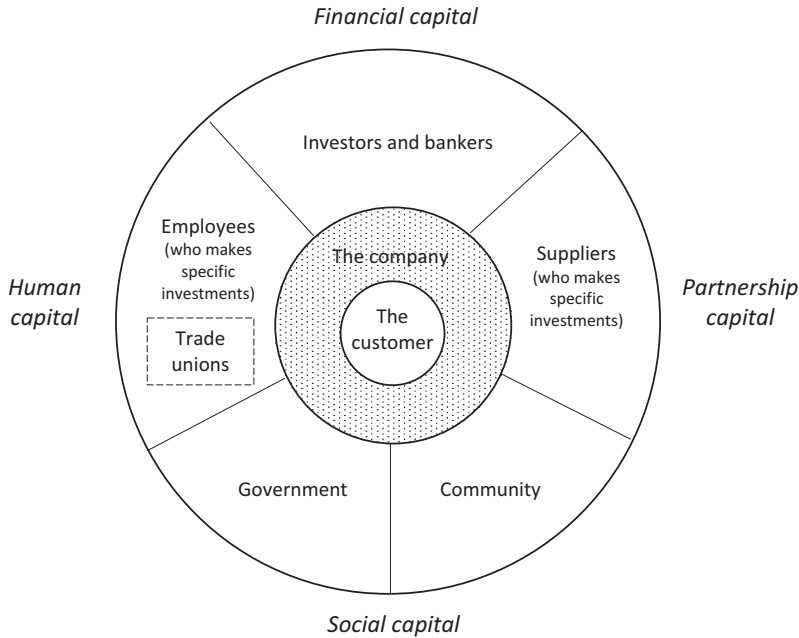
(e.g., education, training, and expertise), which is specific to the production process and of limited value to another employer; suppliers' physical and human capital; and communities' physical and social capital (e.g., local infrastructure and roads, as well as business and social networks supporting the main corporation).

3. Excellence should be pursued in all things, including products, people, customer relationships, and supplier relationships. These are, in MacIntyrean terms, 'internal goods'. Attempts to exploit negative externalities, create monopolies, or take actions which increase income inequality are unethical according to the market failures approach to business ethics.
4. Profits matter if a company is to survive and be sustainable, but maximising profit is not the sole purpose of a company. Reputation matters too for if a company is to survive and flourish. In MacIntyrean terms these are 'external goods'.
5. When it comes to products and profits, both order (internal goods before external goods) and balance matter. Value is to be shared according to the economic principle of fairness, considering the contribution made by different stakeholders.
6. Management disciplines (including strategic management, operations management, marketing, financial management, human

resource management, information technology management, project management, supply chain management, engineering, and research and development) should be regarded as MacIntyrean 'practices' – 'coherent and complex forms of socially established cooperative human activity through which internal goods are realised'. They thus take on many of the characteristics of a profession: specialised knowledge and training, ethical standards and codes of conduct, a service orientation, a degree of autonomy and self-regulation, accountability, and a responsibility to ensure continuing development. The institutions that support these practices, including professional bodies, networks, universities, and business schools, should be encouraged to recognise their place in what is an ethical, as well as economic, system. Management practices and professional institutions are connected, in MacIntyrean terminology, through 'a single causal order' – professional bodies are formed by practitioners of the management disciplines in order to encourage development of the professions.

7. Virtues of wisdom (curiosity and creativity), courage (persistence and integrity), humanity (kindness and emotional intelligence), justice (fairness and citizenship), temperance (forgiveness, humility, and self-control), and transcendence (gratitude, humour, and appreciation), are to be developed, encouraged, and celebrated.
8. Strategy development can be thought about as like writing the future story of a company. Business strategists sometimes talk about future scenarios as 'memories of an expected future' – imagining what it would be like to look back 10 or 20 years from now and thinking about how the company might have progressed in the intervening years. And the future strategy must be written in such a way as to take into account the company's past history. Today's company is part of a tradition. Karl Marx said that history matters – the past determines the future. Karl Popper argued that it doesn't – the emergence of new scientific ideas means that we are not determined by the past. The economic historian Douglass North maintained that history matters to some extent, though not in a way which is deterministic – there are path dependencies which mean that the past has an impact on the future. This is closest to the MacIntyrean perspective. A company is a living, evolving community, with shared stories, practices, and goals. While changes occur over time they occur within the context of a historical tradition.

The second picture (Figure 6.2) is a refinement of the stakeholder map shown in Chapter 3. It now focuses on those who make specific investments in companies, whether in cash or in kind. Note the role of trade unions in this revised stakeholder map has been relegated to supporting employees, which should be their primary role. Trade unions play an important role in society,

Figure 6.2: New stakeholder model

Source: Author, after Freeman (2012).

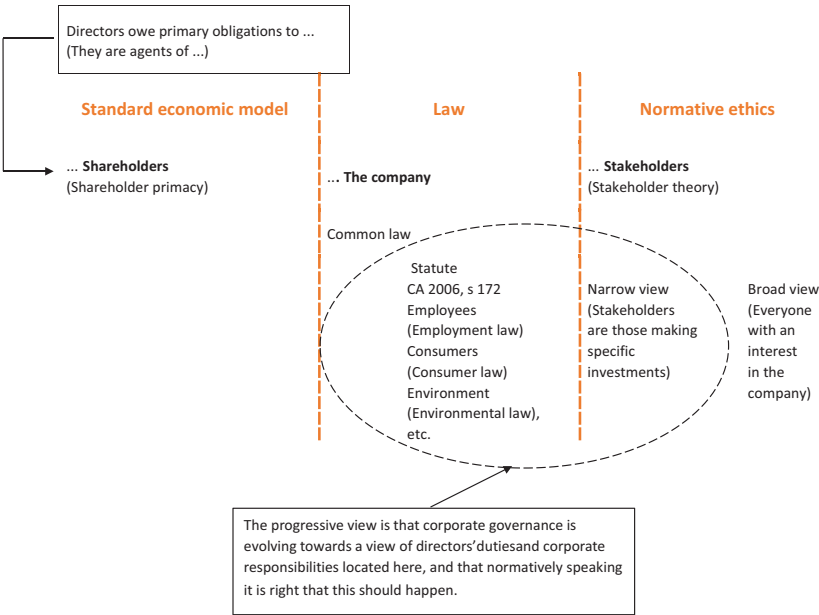
but they must recognise that they are servants of the individuals who they represent, rather than primary stakeholders in companies.

Note also the inclusion of an important stakeholder absent from the earlier model, namely the customer, who I have placed at the centre of the diagram.¹⁷¹ In a sense, the most important determinant of corporate purpose should be the customer. Companies exist to provide goods and services for their customers. Companies that fail to satisfy their customers soon cease to exist. Rather than shareholder primacy, it might be wiser to think about 'customer primacy'. All other stakeholders are, in a sense, secondary.

The third picture (Figure 6.3) illustrates the dynamic relationship between the standard economic model of shareholder primacy, the law in England, and normative ethics.

This is a picture of a changing tradition. While the standard model of the firm asserts the primary importance of shareholders, in English law (as well as the law in many US states and other common law countries) directors owe their fiduciary duty to the company, not to shareholders. In legal terms managers are not, and never have been, agents of shareholders, notwithstanding the dominant logic of agency theory in economics.¹⁷² Law and practice appear to be evolving towards a view of director's duties and corporate responsibilities

Figure 6.3: The role of law and regulation



Source: Author.

that takes account of a wider group of stakeholders. Two examples of this are: first, in the US the Business Roundtable's revised statement on the purpose of the corporation referred to in Chapter 2 (see Figure 2.4); and, second, in the UK new reporting requirements introduced in 2019 that strengthen the responsibility of directors to take account of the interests of a range of stakeholders while promoting the success of the company – specifically the mandating of a requirement that large companies should produce a Section 172 statement explaining how directors have addressed stakeholder considerations and long-term decision-making as part of their governance reports.

The positive view is that an evolution in law and corporate governance practice from 'for mastery' to 'for virtue' is already happening. The normative view is that this is necessary if we want to have more responsible business. The evolution of the tradition that underpins Western capitalism needs to continue and at speed. An extension of the fiduciary duty of directors to a wider group of stakeholders must be incorporated into law. In the UK, this would require further amendments to Section 172, strengthening the requirement that the directors consider the likely consequences of any decision in the long term, the interests of the company's employees, the need to foster the company's business relationships with suppliers, customers, and others, the impact of the

company's operations on the community and the environment, and the desirability of the company maintaining a reputation for high standards of business conduct (items (a)–(e) in Figure 1.8). It should also be made mandatory that directors act fairly as between all stakeholders (that is, not just among members), and that all these considerations be weighted equally.

Equally importantly, the fiduciary duty of investment managers needs to be clarified to permit them to incorporate environmental, social, and governance factors into their investment choices. A legal requirement broadly corresponding to Section 172 should make it mandatory for investment managers to consider the likely consequences of their decision in the long term, the impact of their decisions on employees, suppliers, the community, and the environment, and the desirability of maintaining a reputation for high standards of business conduct. Investment managers who uncritically advocate shareholder primacy appear to believe that a company's objectives can be encapsulated in one financial metric – maximising shareholder value, of which, of course, they are the main beneficiaries. But this is unrealistic. Investors who disclaim ESG investment standards either believe that anthropogenic climate change is a myth (there is a mountain of empirical evidence that shows that it isn't) or that it is somebody else's problem (presumably the government's). It is everybody's problem, theirs included. To think otherwise is irresponsible.

Postscript

I have presented the combination of ideas in this book as if they are entirely new. In some ways they are. But in some ways the plea for business leaders to act responsibly and to recognise their obligations to all stakeholders, including society as a whole, is much older. Consider, for example, the words of Owen D. Young, who was President and Chairman of General Electric from 1922 to 1939:

It makes a great difference in my attitude toward my job as an executive officer of the General Electric Company whether I am a trustee of the institution or an attorney for the investor. If I am a trustee, who are the beneficiaries of the trust? To whom do I owe my obligations?

Now, I conceive my trust first to be to see to it that the capital which is put into my concern is safe, honestly, and wisely used, and paid a fair rate of return. Otherwise we cannot get capital. The worker will have no tools. Second, that the people who put their labor and lives into this concern get fair wages, continuity of employment, and a recognition of their right to their jobs where they have educated themselves to highly skilled and specialized work. Third, that the customers get a product which is as represented and that the price is

such as is consistent with the obligations to the people who put their capital and labor in. Last, that the public has a concern functioning in the public interest and performing its duties as a great and good citizen should.

I think what is right in business is influenced very largely by the growing sense of trusteeship which have described. One no longer feels the obligation to take from labor for the benefit of capital, nor to take from the public for the benefit of both, but rather to administer wisely and fairly in the interest of all.¹⁷³

One needs only add something about the impact of decisions in the long-term, and the responsibility of business for the planet as whole, in order to give an admirable statement of what the responsibility of a CEO should be in the 21st century.

Afterword: A letter from Socrates

After being found guilty of impiety and corrupting the youth of Athens in 399BCE, Socrates remained in prison awaiting execution until the return of the Athenian ceremonial vessel from the island of Delos. During Delia, a religious festival which took place each year to honour the god Apollo, a ship was sent from Athens to Delos, the mythological birthplace of Apollo. Athenian law prohibited executions during this period to maintain the city's ritual purity.

Let's imagine that, while in prison, Sophocles dictated a letter to Milton Friedman.¹⁷⁴

Dear Milton

I've been thinking a lot recently about our discussion.

There is one rather important point which I want to make sure that you understand what I was saying. The 'for mastery' or 'for virtue' argument that I have advanced in our discussion is not the same as pitting capitalism against some other kind of economic system. I imagine you have all the economic data at your fingertips and would argue that capitalism – which you would presumably describe as the economic system in which companies and wealthy individuals accumulate capital, invest in production, and trade in competitive markets, incentivised at all times by the profit motive – has greatly benefitted mankind over the last three or four hundred years. Of your era, not mine, that is.

I would probably agree with you that it has.

However, that does not mean that more is better – if what is meant by that is bigger companies, bigger profits, and greater accumulation of wealth. Sometimes a better answer than 'more' is 'enough'.

To illustrate this, I want to take you back to the discussion we had when we first met. You will remember that I asked you what the purpose of a pharmaceutical company was? I argued that it was to cure illness and help patients towards better health, not to maximise profits for shareholders.

Did you know that the Greek word for medicine, *phármakon* – hence the English word 'pharmaceutical' by the way – also means 'poison'? If that surprises you, then think about aspirins. 300 mg of aspirin will help to cure a headache. 600 mg will probably do it quicker. 6000 mg of aspirin will cause severe gastrointestinal distress. 60,000 mg would probably kill you. Most drugs are very harmful if taken to excess.

This shows that more is not necessarily better. Most biochemical functions in nature are curves, not straight lines. Some level off and then turn downwards. Others accelerate so fast they eventually run out of control. The same is true of functions in economics.

This is what I have been trying to tell you about capitalism and corporate purpose. 'For mastery' is fine up to a point, but to excess can lead to enormous damage – to the planet, to society, and even to the economy. Ultimately, 'for virtue' companies – or 'responsible capitalism' as some might call – is much better.

Think on this. And remember that the unexamined life is not worth living.¹⁷⁵

With very best wishes

Your old friend Socrates.

Appendix: 'A Friedman doctrine – the social responsibility of business is to increase its profits'

*Milton Friedman*¹⁷⁶

New York Times, 13 September 1970

WHEN I hear businessmen speak eloquently about the 'social responsibilities of business in a free-enterprise system', I am reminded of the wonderful line about the Frenchman who discovered at the age of 70 that he had been speaking prose all his life. The businessmen believe that they are defending free enterprise when they declaim that business is not concerned 'merely' with profit but also with promoting desirable 'social' ends; that business has a 'social conscience' and takes seriously its responsibilities for providing employment, eliminating discrimination, avoiding pollution and whatever else may be the catchwords of the contemporary crop of reformers. In fact they are—or would be if they or anyone else took them seriously—preaching pure and unadulterated socialism. Businessmen who talk this way are unwitting puppets of the intellectual forces that have been undermining the basis of a free society these past decades.

The discussions of the 'social responsibilities of business' are notable for their analytical looseness and lack of rigor. What does it mean to say that 'business' has responsibilities? Only people can have responsibilities. A corporation is an artificial person and, in this sense, may have artificial responsibilities, but 'business' as a whole cannot be said to have responsibilities, even in this vague sense. The first step toward clarity in examining the doctrine of the social responsibility of business is to ask precisely what it implies for whom.

Presumably, the individuals who are to be responsible are businessmen, which means individual proprietors or corporate executives. Most of the discussion of social responsibility is directed at corporations, so in what follows I shall mostly neglect the individual proprietor and speak of corporate executives.

IN a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom. Of course, in some cases his employers

may have a different objective. A group of persons might establish a corporation for an eleemosynary purpose—for example, a hospital or school. The manager of such a corporation will not have money profit as his objective but the rendering of certain services.

In either case, the key point is that, in his capacity as a corporate executive, the manager is the agent of the individuals who own the corporation or establish the eleemosynary institution, and his primary responsibility is to them.

Needless to say, this does not mean that it is easy to judge how well he is performing his task. But at least the criterion of performance is straightforward, and the persons among whom a voluntary contractual arrangement exists are clearly defined.

Of course, the corporate executive is also a person in his own right. As a person, he may have many other responsibilities that he recognizes or assumes voluntarily—to his family, his conscience, his feelings of charity, his church, his clubs, his city, his country. He may feel impelled by these responsibilities to devote part of his income to causes he regards as worthy, to refuse to work for particular corporations, even to leave his job, for example, to join his country's armed forces. If we wish, we may refer to some of these responsibilities as 'social responsibilities.' But in these respects he is acting as a principal, not an agent; he is spending his own money or time or energy, not the money of his employers or the time or energy he has contracted to devote to their purposes. If these are 'social responsibilities,' they are the social responsibilities of individuals, not of business.

What does it mean to say that the corporate executive has a 'social responsibility' in his capacity as businessman? If this statement is not pure rhetoric, it must mean that he is to act in some way that is not in the interest of his employers. For example, that he is to refrain from increasing the price of the product in order to contribute to the social objective of preventing inflation, even though a price increase would be in the best interests of the corporation. Or that he is to make expenditures on reducing pollution beyond the amount that is in the best interests of the corporation or that is required by law in order to contribute to the social objective of improving the environment. Or that, at the expense of corporate profits, he is to hire 'hard core' unemployed instead of better qualified available workmen to contribute to the social objective of reducing poverty.

In each of these cases, the corporate executive would be spending someone else's money for a general social interest. Insofar as his actions in accord with his 'social responsibility' reduce returns to stockholders, he is spending their money. Insofar as his actions raise the price to customers, he is spending the customers' money. Insofar as his actions lower the wages of some employees, he is spending their money.

The stockholders or the customers or the employees could separately spend their own money on the particular action if they wished to do so. The executive is exercising a distinct 'social responsibility,' rather than serving as an agent of the stockholders or the customers or the employees, only if he spends the money in a different way than they would have spent it.

But if he does this, he is in effect imposing taxes, on the one hand, and expending how the tax proceeds shall be spent, on the other.

This process raises political questions on two levels: principle and consequences. On the level of political principle, the imposition of taxes and the expenditure of tax proceeds are governmental functions. We have established elaborate constitutional, parliamentary and judicial provisions to control these functions, to assure that taxes are imposed so far as possible in accordance with the preferences and desires of the public—after all, ‘taxation without representation’ was one of the battle cries of the American Revolution. We have a system of checks and balances to separate the legislative function of imposing taxes and enacting expenditures from the executive function of collecting taxes and administering expenditure programs and from the judicial function of mediating disputes and interpreting the law.

Here the businessman—self-selected or appointed directly or indirectly by stockholders—is to be simultaneously legislator, executive and jurist. He is to decide whom to tax by how much and for what purpose, and he is to spend the proceeds—all this guided only by general exhortations from on high to restrain inflation, improve the environment, fight poverty and so on and on.

The whole justification for permitting the corporate executive to be selected by the stockholders is that the executive is an agent serving the interests of his principal. This justification disappears when the corporate executive imposes taxes and spends the proceeds for ‘social’ purposes. He becomes in effect a public employee, a civil servant, even though he remains in name an employee of private enterprise. On grounds of political principle, it is intolerable that such civil servants—insofar as their actions in the name of social responsibility are real and not just window-dressing—should be selected as they are now. If they are to be civil servants, then they must be selected through a political process. If they are to impose taxes and make expenditures to foster ‘social’ objectives, then political machinery must be set up to guide the assessment of taxes and to determine through a political process the objectives to be served.

This is the basic reason why the doctrine of ‘social responsibility’ involves the acceptance of the socialist view that political mechanisms, not market mechanisms, are the appropriate way to determine the allocation of scarce resources to alternative uses.

ON the grounds of consequences, can the corporate executive in fact discharge his alleged ‘social responsibilities’? On the one hand, suppose he could get away with spending the stockholders’ or customers’ or employees’ money. How is he to know how to spend it? He is told that he must contribute to fighting inflation. How is he to know what action of his will contribute to that end? He is presumably an expert in running his company—in producing a product or selling it or financing it. But nothing about his selection makes him an expert on inflation. Will his holding down the price of his product reduce inflationary pressure? Or, by leaving more spending power in the hands of his customers, simply divert it elsewhere? Or, by forcing him to produce less

because of the lower price, will it simply contribute to shortages? Even if he could answer these questions, how much cost is he justified in imposing on his stockholders, customers and employees for this social purpose? What is his appropriate share and what is the appropriate share of others?

And, whether he wants to or not, can he get away with spending his stockholders, customers' or employees' money? Will not the stockholders fire him? (Either the present ones or those who take over when his actions in the name of social responsibility have reduced the corporation's profits and the price of its stock.) His customers and his employees can desert him for other producers and employers less scrupulous in exercising their social responsibilities.

This facet of 'social responsibility' doctrine is brought into sharp relief when the doctrine is used to justify wage restraint by trade unions. The conflict of interest is naked and clear when union officials are asked to subordinate the interest of their members to some more general social purpose. If the union officials try to enforce wage restraint, the consequence is likely to be wildcat strikes, rank-and-file revolts and the emergence of strong competitors for their jobs. We thus have the ironic phenomenon that union leaders—at least in the U.S.—have objected to Government interference with the market far more consistently and courageously than have business leaders.

The difficulty of exercising 'social responsibility' illustrates, of course, the great virtue of private competitive enterprise—it forces people to be responsible for their own actions and makes it difficult for them to 'exploit' other people for either selfish or unselfish purposes. They can do good—but only at their own expense.

Many a reader who has followed the argument this far may be tempted to remonstrate that it is all well and good to speak of government's having the responsibility to impose taxes and determine expenditures for such 'social' purposes as controlling pollution or training the hard-core unemployed, but that the problems are too urgent to wait on the slow course of political processes, that the exercise of social responsibility by businessmen is a quicker and surer way to solve pressing current problems.

Aside from the question of fact—I share Adam Smith's scepticism about the benefits that can be expected from 'those who affected to trade for the public good'—this argument must be rejected on grounds of principle. What it amounts to is an assertion that those who favour the taxes and expenditures in question have failed to persuade a majority of their fellow citizens to be of like mind and that they are seeking to attain by undemocratic procedures what they cannot attain by democratic procedures. In a free society, it is hard for 'good' people to do 'good,' but that is a small price to pay for making it hard for 'evil' people to do 'evil,' especially since one man's good is another's evil.

I HAVE, for simplicity, concentrated on the special case of the corporate executive, except only for the brief digression on trade unions. But precisely

the same argument applies to the newer phenomenon of calling upon stockholders to require corporations to exercise social responsibility (the recent G.M. crusade, for example). In most of these cases, what is in effect involved is some stockholders trying to get other stockholders (or customers or employees) to contribute against their will to 'social' causes favoured by the activists. Insofar as they succeed, they are again imposing taxes and spending the proceeds.

The situation of the individual proprietor is somewhat different. If he acts to reduce the returns of his enterprise in order to exercise his 'social responsibility,' he is spending his own money, not someone else's. If he wishes to spend his money on such purposes, that is his right, and I cannot see that there is any objection to his doing so. In the process, he, too, may impose costs on employees and customers. However, because he is far less likely than a large corporation or union to have monopolistic power, any such side effects will tend to be minor.

Of course, in practice the doctrine of social responsibility is frequently a cloak for actions that are justified on other grounds rather than a reason for those actions.

To illustrate, it may well be in the long-run interest of a corporation that is a major employer in a small community to devote resources to providing amenities to that community or to improving its government. That may make it easier to attract desirable employees, it may reduce the wage bill or lessen losses from pilferage and sabotage or have other worthwhile effects. Or it may be that, given the laws about the deductibility of corporate charitable contributions, the stockholders can contribute more to charities they favour by having the corporation make the gift than by doing it themselves, since they can in that way contribute an amount that would otherwise have been paid as corporate taxes.

In each of these—and many similar—cases, there is a strong temptation to rationalize these actions as an exercise of 'social responsibility.' In the present climate of opinion, with its widespread aversion to 'capitalism,' 'profits,' the 'soulless corporation' and so on, this is one way for a corporation to generate goodwill as a by-product of expenditures that are entirely justified in its own self-interest.

It would be inconsistent of me to call on corporate executives to refrain from this hypocritical window dressing because it harms the foundations of a free society. That would be to call on them to exercise 'social responsibility'! If our institutions, and the attitudes of the public make it in their self-interest to cloak their actions in this way, cannot summon much indignation to denounce them. At the same time, can express admiration for those individual proprietors or owners of closely held corporations or stockholders of more broadly held corporations who disdain such tactics as approaching fraud.

WHETHER blameworthy or not, the use of the cloak of social responsibility, and the nonsense spoken in its name by influential and prestigious

businessmen, does clearly harm the foundations of a free society. I have been impressed time and again by the schizophrenic character of many businessmen. They are capable of being extremely far-sighted and clear-headed in matters that are internal to their businesses. They are incredibly short sighted and muddle-headed in matters that are outside their businesses but affect the possible survival of business in general. This short sightedness is strikingly exemplified in the calls from many businessmen for wage and price guidelines or controls or incomes policies. There is nothing that could do more in a brief period to destroy a market system and replace it by a centrally controlled system than effective governmental control of prices and wages.

The short-sightedness is also exemplified in speeches by businessmen on social responsibility. This may gain them kudos in the short run. But it helps to strengthen the already too prevalent view that the pursuit of profits is wicked and immoral and must be curbed and controlled by external forces. Once this view is adopted, the external forces that curb the market will not be the social consciences, however highly developed, of the pontificating executives; it will be the iron fist of Government bureaucrats. Here, as with price and wage controls, businessmen seem to me to reveal a suicidal impulse.

The political principle that under lies the market mechanism is unanimity. In an ideal free market resting on private property, no individual can coerce any other, all cooperation is voluntary, all parties to such cooperation benefit or they need not participate. There are no 'social' values, no 'social' responsibilities in any sense other than the shared values and responsibilities of individuals. Society is a collection of individuals and of the various groups they voluntarily form.

The political principle that under lies the political mechanism is conformity. The individual must serve more general social interest—whether that be determined by church or a dictator or a majority. The individual may have a vote and a say in what is to be done, but if he is overruled, he must conform. It is appropriate for some to require others to contribute to a general social purpose whether they wish to or not.

Unfortunately, unanimity is not always feasible. There are some respects in which conformity appears unavoidable, so I do not see how one can avoid the use of the political Mechanism altogether.

But the doctrine of 'social responsibility' taken seriously would extend the scope of the political mechanism to every human activity. It does not differ in philosophy from the most explicitly collectivist doctrine. It differs only by professing to believe that collectivist ends can be attained without collectivist means. That is why, in my book 'Capitalism and Freedom,' I have called it a 'fundamentally subversive doctrine' in a free society, and have said that in such a society, 'there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud.'

Figure VI: The Philosophers' café (with names)



Source: Tim Wakeling.

Notes

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- ³ Tett, G. (2021) *Anthro-Vision. How Anthropology Can Explain Business and Life*, London: Penguin Random House.
- ⁴ It is important to note the difference between a Benefit Corporation, which is a type of legal entity available in some jurisdictions (especially certain states in the US), and B Corp, which is a company that has been certified by B Lab, an independent non-profit organisation. Certification as a B Corp does not confer separate legal status. This means that, for example in the UK, certified B Corps must still comply with all the relevant requirements of the Companies Acts.
- ⁵ For the merits of a diverse corporate ecology see Davies, W. (2009) *Reinventing the Firm*, London: Demos. https://demos.co.uk/wp-content/uploads/2023/03/Reinventing_the_firm.pdf.
- ⁶ For Berle–Means corporations see Berle, A.; and Means, G. (1932) *The Modern Corporation and Private Property*, New York: The MacMillan Company.
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- ⁹ Dixon, W. (2020) 'Letter: A Socratic reading casts doubt on Cummings' "effectiveness"', *Financial Times*, 5 June. <https://www.ft.com/content/397223ee-fa35-46db-b87f-bd183360cad>.
- ¹⁰ The *Gorgias* follows the logical pattern of many of Plato's dialogues: the Rhetoricians put forward a proposition, *p*; Socrates gains the assent of the Rhetoricians to an alternative proposition, *q*; Socrates demonstrates.
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- ¹³ Calculated at year 2000 average exchange rates and purchasing power parity.
- ¹⁴ Maddison, A. (2007) *Contours of the World Economy, 1–2030 AD. Essays in Macro-Economic History*, Oxford: Oxford University Press.
- ¹⁵ Piketty, T. (2014) *Capital in the Twenty-First Century*, Cambridge, MA: Harvard University Press.
- ¹⁶ Sufficiency is mostly closely associated with the philosopher Harry G. Frankfurt. See his slim monograph entitled *On Inequality* published by Princeton University Press in 2015.
- ¹⁷ Malik, S. (2012) 'Peter Mandelson gets nervous about people getting "filthy rich"', *The Guardian*, 26 January. <https://www.theguardian.com/politics/2012/jan/26/mandelson-people-getting-filthy-rich>.
- ¹⁸ Williams, D. (2024) *The Greatest of All Plagues – How Economic Inequality Shaped Political Thought from Plato to Marx*, Princeton, NJ: Princeton University Press.
- ¹⁹ See Brummer, J. (1985) 'Business ethics: micro and macro', *Journal of Business Ethics*, vol. 4, pp. 81–91. <https://doi.org/10.1007/BF00383560>.
- ²⁰ Lewis, P. (1985) 'Defining "business ethics": like nailing jello to a wall', *Journal of Business Ethics*, vol. 4, no. 5, pp. 377–83. <https://doi.org/10.1007/BF02388590>; Ritter, B. (2006) 'Can business ethics be trained? A study the ethical decision-making process in business students', *Journal of Business Ethics*, vol. 68, no. 2, pp. 153–64. <https://doi.org/10.1007/s10551-006-9062-0>. O'Leary, C.; and Hannah, F. (2008) 'Are students from different business majors predisposed to different ethical sensitivities', *Corporate Ownership and Control*, vol. 6, no. 1, pp. 254–62. <https://doi.org/10.22495/cocv6i1c2p1>.
- ²¹ Joseph Heath offers an alternative duality based on a parallel with just war theory. On the one hand, what Heath calls *jus ad mercatum* addresses questions about whether a free-market economy is justifiable or whether the economy should be organised on alternative principles. On the other hand, *jus in mercatu* addresses questions about how economic actors should conduct themselves in the context of a free-market economy. Heath, J. (2023) *Ethics for Capitalists – A Systematic Approach to Business Ethics, Competition, and Market Failure*, Victoria, BC: FriesenPress.
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- ²³ US National Archives (1776) 'Declaration of Independence: a transcription.' <https://www.archives.gov/founding-docs/declaration-transcript>.
- ²⁴ Dobb, M. (2012) *Political Economy and Capitalism – Some Essays in Economic Tradition*. London: Routledge.
- ²⁵ See the entry for 'The natural law tradition in ethics' in the Stanford Encyclopedia of Philosophy, 30 April 2025. <https://plato.stanford.edu/entries/natural-law-ethics/>.
- ²⁶ Kant, I. (1785) *Groundwork of the Metaphysics of Morals*.
- ²⁷ I explore this topic in more detail in Pepper, A. (2018) *Agency Theory and Executive Pay*, London: Palgrave Macmillan.
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- ²⁹ Foot, P. (1967) 'The problem of abortion and the doctrine of double effect,' *The Oxford Review*, vol. 5, pp. 5–15.
- ³⁰ Thomson, J. (1976) 'Killing, letting die, and the trolley problem,' *The Monist*, vol. 59, no. 2, pp. 204–17. <https://doi.org/10.5840/monist197659224>.
- ³¹ Thomson (1976), p. 205.
- ³² The American philosopher Frances Kamm is the academic in question: see Kamm, F. (2016) *The Trolley Problem Mysteries*, Oxford: Oxford University Press. Popular philosopher David Edmonds wrote on the topic in Edmonds, D. (2013) *Would You Kill the Fat Man? The Trolley Problem and What Your Answer Tells Us about Right and Wrong*, Princeton, NJ: Princeton University Press. Alasdair MacCall Smith created the character of Isobel Dalhouse, a philosopher who reflects on the trolley problem in MacCall Smith, A. (2004) *The Sunday Philosophy Club*, New York, NY: Little, Brown and Company.
- ³³ Parfit, D. (1991) 'Equality or priority,' The Lindley Lecture, University of Kansas.
- ³⁴ Robbins, L. (2007 | 1932) *An Essay on the Nature and Significance of Economic Science*, Auburn, AL: Ludwig von Mises Institute.
- ³⁵ The Nicomachean Ethics was named either after Nicomachus, Aristotle's father and first teacher, or after Aristotle's son, also called Nicomachus, who edited the work after Aristotle's death.
- ³⁶ Aristotle, *Nicomachean Ethics*, Book II, Chapter 2, Paragraph 1.
- ³⁷ Plato, *The Republic*, Book IV, pp. 426–35; Aristotle, *Rhetoric*, 1366b1; Cicero, *De Inventione*, II.53.

- ³⁸ See the entry for 'Aristotle's ethics, the doctrine of the mean' in the Stanford Encyclopedia of Philosophy, 2 July 2022. <https://plato.stanford.edu/entries/aristotle-ethics/#DoctMean>.
- ³⁹ Hawley, K. (2014) 'Trust, distrust and commitment', *Nous*, vol. 48, no. 1, 1–20. <https://doi.org/10.1111/nous.12000>.
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- ⁴¹ Parfit, D. (2011) *On What Matters*, volumes 1 and 2, Oxford: Oxford University Press. To be precise, Parfit was talking about the coming together of Kantian deontological ethics (focusing on duty and the universalisation of moral principles), rule utilitarianism (a set of societal rules which produce the greatest good for the greatest number), and contractualism (principles that no one could reasonably reject as part of a fair social contract). This is sometimes referred to as Parfit's 'triple theory', but I see no reason why the 'all moral philosophers are climbing the same mountain' metaphor cannot be extended to embrace other ethical theories.
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- ⁵⁰ Bible, Matthew 6:24.
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- ⁵⁸ Montesquieu (1748) *The Spirit of Laws*, Book XX, Chapter 2.
- ⁵⁹ Movsesian, M. (2018) 'Markets and moral: the limits of *doux commerce*', *William and Mary Business Law Review*, vol. 9, no. 2, p. 449. <https://scholarship.law.wm.edu/wmblr/vol9/iss2/7>.
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- ⁶⁵ Friedman, M. (2004) The Friedman Foundation for Educational Choice, CC0 licence (public domain). Available from https://commons.wikimedia.org/wiki/File:Portrait_of_Milton_Friedman.jpg.
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- ¹¹⁵ Lynn A. Stout (left) at the Cornell Law Library, by Heather Ainsworth, republished under a CC BY-SA 3.0 licence. Available from https://commons.wikimedia.org/wiki/File:Lynn_Stout_by_Heather_Ainsworth.jpg; Margaret Blair (right), photo courtesy of Vanderbilt Law School
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- ¹²⁹ The song 'Is that all there is?' was written by Jerry Leiber and Mike Stoller, based on a short story by Thomas Mann called *Disillusionment*, written in 1896. The song became a hit for American singer Peggy Lee in 1969.
- ¹³⁰ Not least by Socrates in the imagined dialogue with Milton Friedman!
- ¹³¹ Roger Scruton had a dim view of continental philosophy: see Scruton, R.V. (2015) *Fools, Frauds and Firebrands: Thinkers of the New Left*, London: Bloomsbury Continuum.
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- ¹³³ According to ChatGPT (answer downloaded on 10 February 2025), in 'A Defence of Poetry' (1821), Percy Bysshe Shelley explains that Shakespeare's genius is in transforming existing stories rather than inventing new ones. In a similar vein, T.S. Eliot wrote 'Shakespeare acquired more essential history from Plutarch than most men could from the whole British Museum'. Eliot, T.S. (1919) 'Tradition and the Individual Talent'.

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- ¹³⁵ The description of business leaders is based on the work of Michael Maccoby, whose 2003 book *The Productive Narcissist – The Promise and Peril of Visionary Leadership* (New York, NY: Broadway Books) describes the character traits of visionary and capable leaders, but explains how the same character traits can sometimes lead to destructive behaviours and negative organisational outcomes.
- ¹³⁶ Alasdair MacIntyre at The International Society for MacIntyrean Enquiry conference, University College Dublin, 2009. Photograph Sean O'Connor/ Flickr, reproduced under a CC-BY-2.0 licence. Available from <https://www.flickr.com/photos/seanoconnor365/3351618688/in/set-72157615114247195/>.
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- ¹³⁹ Geoff Moore, Ron Beadle, and Gregory Beabout have in particular written extensively on the subject of MacIntyrean business ethics. Their published work includes Moore, G. (2017) *Virtue at Work: Ethics for Individuals, Managers, and Organisations*, Oxford: Oxford University Press; Beadle, R. (2017) 'MacIntyre's Influence on Business Ethics', in: Sison, A. (ed) *Handbook of Virtue Ethics in Business and Management*, Heidelberg: Springer, pp. 59–67; Beabout, G. (2013) *The Character of the Manager: From Office Executive to Wise Steward*, London: Palgrave MacMillan; and Beadle, R. and Moore, G. (eds) (2020) *Learning from MacIntyre*, Eugene, OR: Pickwick Publications; as well as a large number of academic journal articles.
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- ¹⁴¹ Kay, J. (2024) *The Corporation in the 21st Century – Why (Almost) Everything we are Told About Business is Wrong*, London: Profile Books.
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define the term 'prosperity', as an economist he may have been influenced by bodies such as the OECD (Organisation for Economic Co-operation and Development), World Bank, and IMF (International Monetary Fund), who explain prosperity in terms of sustained economic growth, characterised by high levels of income and employment, rising productivity, low inflation, economic stability, access to education, healthcare and good infrastructure, and an improving standard of living in general. The word 'prosperity' comes from the Latin root *prosperitas*, which implies thriving, success, and good fortune. *Prosperitas* itself is a combination of the Latin words *pro* (forward) and *sperare* (hope), suggesting moving towards favourable future outcomes. The environmental economist Tim Jackson makes this point in his 2017 book *Prosperity Without Growth – Foundations for the Economy of Tomorrow* (Milton Park: Routledge), which was originally published as a report by the Sustainable Development Commission, and focuses on the environmental aspects of economic prosperity.

¹⁴³ MacIntyre (1981), p. 142.

¹⁴⁴ MacIntyre (1981), p. 219.

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¹⁴⁷ MacIntyre (1981), p. 90.

¹⁴⁸ See Carlyle, T. (1840) *On Heroes, Hero-Worship, & the Heroic in History*, Cambridge, MA: Yale University Press.

¹⁴⁹ See the entry on Philippa Foot in the Stanford Encyclopedia of Philosophy, 9 December 2021, <https://plato.stanford.edu/entries/philippa-foot/#PrimSour>.

¹⁵⁰ Solomon, R. (1992) *Ethics and Excellence*, Oxford: Oxford University Press.

¹⁵¹ MacIntyre (1981), p. 148.

¹⁵² The cardinal virtues can be found in Plato, *The Republic*, Book IV, pp. 426–35; Aristotle, *Rhetoric*, 1366b1; Cicero, *De Inventione*, II.53. Other references are to Peterson, C.; and Seligman, M. (2004) *Character Strengths and Virtues: A Handbook and Classification*, Oxford: American Psychological Association and Oxford University Press; Solomon, R. (1992) 'Corporate roles, personal virtues: an Aristotelean approach to

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¹⁵³ *Sophrosynē* and *enkratia* are both virtues in ancient Greek thought, especially in the ethical frameworks of Plato and Aristotle. However, they have distinct meanings and implications. For Plato, *sophrosynē* is a key virtue that reflects wisdom and self-knowledge. *Enkratia*, while valuable, is seen as a more preliminary or basis stage of self-mastery. Aristotle distinguishes between the 'continent' person (*enkrates*) who practices *enkratia* to resist desires, and the 'temperate' person (*sophron*) who embodies *sophrosynē* and feels no such conflict. Source: ChatGPT, 5 December 2024.

¹⁵⁴ MacIntyre (1981), p. 216.

¹⁵⁵ D'Andrea, T. (2006) *Tradition, Rationality, and Virtue*, Milton Park: Routledge, p. 272–73.

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- ¹⁷¹ I thank Steve Wood for pointing this out!
- ¹⁷² Clark, R. (1985) 'Agency Costs versus Fiduciary Duties', in: Pratt J.; and Zeckhauser, R. (eds) *Principals and Agents: The Structure of Business*, Cambridge, MA: Harvard Business School Press; and Dodd, E. (1932) 'For whom are corporate managers trustees?', *Harvard Law Review*, vol. 35,

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¹⁷³ Quoted in Dodd, M. (1932) ‘For whom are corporate managers trustees?’ *Harvard Law Review*, vol. 45, no. 7, pp. 1145–63. <https://doi.org/10.2307/1331697>.

¹⁷⁴ The afterword is also in a sense an afterthought, inspired by listening to an episode of *In Our Time* on BBC Radio 4 titled ‘Socrates in Prison’ which was broadcast on 23 January 2025.

¹⁷⁵ Socrates is attributed the statement ‘the unexamined life is not worth living’ in Plato’s *Apology* (38a5–6) when, during his trial, he emphasises the importance of philosophical enquiry and self-reflection.

¹⁷⁶ Article copyright Milton Friedman, reproduced with permission from the Milton Friedman estate. First published in *The New York Times*, 13 September 1970. <https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html>.

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