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TOWARD A GENERAL THEORY OF
SOCIAL RESPONSIBILITY FOR BUSINESS

by

J. Furman Lewis*

EVERY generation tends to think of its problems as unique. The present generation of businessmen and businesswomen is no different in this respect from any that have gone before it or that will come after it. It has been confronted with a rising cacophony of voices demanding on the one hand that it rise to the challenge of a myriad of societal problems of incredible complexity and range, and on the other that it tend to its affairs and let others tend to theirs. Business leaders are simultaneously admonished on the one side to respond to the urgent demands of a society in crisis lest the very fabric of our fragile democracy be rent asunder, and on the other to hew with renewed devotion to its traditional role of profit maximization—again, lest the direst of consequences befall our democratic way of life. To chart a course between the Scylla and Charybdis of those conflicting demands is no small problem for today's businessman or woman.

But the problem is not really unique to our generation. During the years of the Great Depression one of the burning issues of the times was whether and to what extent business should shoulder the burden for the pressing needs of society. Then, as now, businessmen were importuned to act responsibly toward society as a whole by undertaking to solve the societal problems of the day, and simultaneously admonished that their sole responsibility was for the efficient use of society's resources.

The social responsibility issue, in short, is old hat. Why then are we still wrestling with it? Why should the time and energies of a surprisingly large proportion of our populace still be concerned with what should be a rather basic philosophical question, one which should have been settled long ago?

There are several possible reasons for this continued conflict. One is that we, as a people, tend to seek pragmatic solutions to immediate problems and shy away from philosophic discussion. The specific problems that gave rise to the issue during the Depression (and before and since) have been dealt with pragmatically and specifically—usually by legislation. If we have decided that business could reasonably be expected to handle a specific problem, we have imposed responsibility for that problem. The unemployment and workmen's compensation laws, the various antitrust laws, and the food and drug laws are cases in point. Such pragmatic solutions may not be intellectually satisfying since they leave the underlying philosophic issue unsettled, but they are expedient and do let the nation get on with its affairs—at least until the next problem is broached.

Another possible reason for the continued viability of the conflict rests in the nature of the conflict itself. In spite of the fact that the social responsibility issue has been debated off and on for at least four decades, there is surprisingly little consensus on what the argument is really all about. We have bogged our-

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selves down in interesting but distracting problems of semantics that have only confused the basic issues involved and prevented the formulation of a set of common assumptions upon which rational debate can be maintained. The prime example of this involves the very term "social responsibility." No really definite, agreed-upon meaning for the term exists; it is much like a sponge, expanding or contracting depending upon the context and the speaker. The result is a glaring communications gap even among those who attempt to debate the issue rationally and in good faith, not to mention those who have seized upon the issue for base motives.

An additional reason the debate has lasted so long is the fact that, by and large, it has been carried on in the context of the large, publicly held corporation. Of course, it must be acknowledged that large, publicly held corporations are important institutions today; they may even be, as so often asserted, the preeminent social and economic institutions of our time. But there are perils in this convention. To begin with, it wrongly suggests that business firms other than such corporations have no public responsibility. These other firms are also social systems, however, and their decisions also have significant social consequences. These consequences need to be taken into account, and we surely should be able to formulate a philosophic framework that will do so.

Looking at business as if it were epitomized by such giants as General Motors and AT&T does more, however, than merely divert attention from the remainder of the business sector; it is actually counterproductive. It is recognized, of course, that on occasion it may be pedagogically useful to focus on the special problems resulting from the pronounced dispersion of the share ownership of these large corporations or the overwhelming amount of assets which they control. However, focusing on the large corporation simply provides another point of debate on the scope of the duty to act in a socially responsible manner, and the heat from the debate on that issue distracts us from the ultimate objective of formulating a general theory of social responsibility.

Whatever the reasons for its continued viability, however, the fact is that the debate over the social responsibility of business goes on unabated. The purpose of this Article is to examine some of the questions presented by the debate and the competing approaches to the social responsibility issue. In doing so, notwithstanding the hazards already noted, the usual convention of focusing upon the modern corporation must, in large part, necessarily be followed. Accordingly, the competing approaches will be examined against the backdrop of the large, publicly held corporation, and in relation to the legal theory of the corporation.

The thesis of the Article is that neither of the contending approaches adequately reflects the essential purpose of the business enterprise or offers a theoretical framework within which business generally can work out reasonable responses to the demands made upon it. Criticism, however, carries with it the obligation to offer an alternative. Accordingly, an alternative approach is outlined that does offer such a framework and which is consistent with normal human expectations and prevailing legal norms.
The following descriptions of the competing approaches underlying the conflicting demands upon business in general and the modern, large corporation in particular have been distilled from a generous sampling of a rather vast and rapidly expanding sea of literature. It is not feasible in this short space to review all the individual contributions to this body of learning, and no attempt to do so will be made. On the contrary, all that can and will be done here is to describe the salient characteristics of the competing approaches. Current notions of full disclosure require the caveat that the descriptions that follow may entail some degree of oversimplification.

A. The Economic Approach

One approach to the social responsibility issue contends that business serves society best by confining itself to its traditional objective, the maximization of profit. This approach is predicated upon classic economic theory with all of its simplifying assumptions, including principally: (1) the assumption that people are motivated by self-interest; (2) the assumption that human wants are limitless while society's resources are finite; and (3) the assumption that it is socially desirable to maximize the economic freedom of the individual and to preserve a condition of competition so that freedom of choice can be exercised.

Based upon these assumptions, the economic theory posits the normative
argument that the maximization of profit by business firms will, under competitive conditions, result in the optimal allocation of resources and produce the greatest degree of satisfaction for the greatest number. Business is viewed as the medium by which this allocation is accomplished; it is the institution charged by society with the role of putting its resources to use in the most efficient manner to produce the maximum material gain for all of society. Profit is the incentive which society offers to business for the effective performance of this function, serving also as a measure of the efficiency with which business performs (i.e., whether the allocation of resources has been optimized) and as the price of capital (i.e., the incentive needed to attract a voluntary supply of capital).

If the argument of those adhering to the economic approach is accepted, one must conclude that any activity by business which is not directed toward maximization of profit is counterproductive. Altruistic behavior, even though undertaken with the intent to benefit society, fails to optimize the allocation of society’s resources and results in less, not more, benefit to society. The logical conclusion of the argument is that business’ public responsibility is to marshal society’s resources to the greatest advantage and any diversion from that role is irresponsible.

The approach is not altogether blind to the fact that society has needs that cannot be met by the silent, unseen movement of the invisible hand of the market. It contends, however, that society has created other institutions, such as government and charitable institutions, and assigned to them responsibility for meeting these needs. The concept is one of specialization of function. Business is the wealth producer, charged with the duty to produce the greatest amount of goods and services; government and other institutions (education, charitable institutions, and the like) are seen as the wealth distributors, charged with the duty of solving society's problems and equitably distributing the wealth business produces.

Those who have adopted the economic approach have tended to deemphasize the legal form which the enterprise takes. The theory is a theory of the firm—not a theory of the corporation. An individual who forms a business firm and carries it on for himself strives to maximize his return, and in a private property system has no duty to conduct his business for the benefit of anyone but himself. If he employs an agent to assist him or to conduct the business for him, there is no real distinction; the business is still operated for the benefit of the owner, and the interest of the agent is simply a claim for wages or other recompense as established by his contract with the principal. Add several other owners so that the firm takes the form of a partnership, and still no essential differ-

\[\textit{See, e.g., A. Braff, Microeconomic Analysis (1969); Asch, Economic Theory and Antitrust Policy, 12 Antitrust Bull. 865 (1967); Buchanan & Tullock, The Dead Hand of Monopoly, Antitrust L. & Econ. Rev., Summer 1968, at 85; Ranlett & Curry, supra note 3; Smith, Antitrust and the Monopoly Problem: Toward a More Relevant Legal Analysis, Antitrust L. & Econ. Rev., Summer 1969, at 19.}\]


\[\textit{See, e.g., Mayer, supra note 2; Rostow, supra note 2.}\]

\[\textit{See, e.g., Friedman, supra note 2; Mayer, supra note 2; Rostow, supra note 2.}\]

\[\textit{See Capon, supra note 5.}\]
ence exists from the standpoint of economic theory. Incorporate the enterprise, and again no substantial change is effected from the economic viewpoint. The corporate form is seen simply as a convenient mechanism for ordering the contractual and proprietary interests of the owners. Consequently, the economic school considers the owners, the shareholders in a corporation, to be the real parties in interest and deems them entitled to any profits earned by the firm. Their agents, the directors in the corporation, have no real personal interest in the firm (assuming they are not also owners), and their responsibility is to conduct the affairs of the firm for the sole benefit of the owners, to whom they are accountable. Management must operate within the legal and ethical framework of the marketplace, of course, but the accountability for its stewardship flows only to the shareholders.

B. The Social Responsibility Approach

There are differences among those who have adopted the economic approach, but none are really structural; such differences are collateral and do not go to the essence of the economic theory. The critics of the economic approach lack this unity. Their affinity is in their consensus that the economic approach does not adequately recognize business' responsibility. While many of their number have argued forcefully and passionately against the economic approach, and some of their suggestions would be useful as the basis for an integrated theoretical foundation of an alternative approach, there appears to be no general theory of social responsibility having application outside the context of the large modern corporation. It is something of a misnomer, therefore, to speak of the social responsibility approach, but it is, nevertheless, instructive to examine some of the criticisms made of the economic approach and the suggestions made to correct its weaknesses.

Berle and Means. The most serious of all the criticisms made of the economic approach is that it is simply irrelevant today. The critics taking this tack have argued that while the classic economic theory may have been valid through the nineteenth century and into the early years of the twentieth century, the emergence of the modern corporation has worked a revolution that has undermined (one might say, destroyed) the private property system upon which that theory was based. This argument was first articulated in a study published in 1932 by Professor Adolf Berle and the late Professor Gardiner Means.

Berle and Means posited the thesis that the traditional logic of property inhered in the nexus between ownership, or the entrepreneurial function of property, and control, or the use value of property. They observed that with the emergence of the large modern corporation had come a concomitant prolifera-

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8 See Dodd, For Whom Are Managers Trustees?, 45 HARV. L. REV. 1145 (1932).
9 See, e.g., Friedman, supra note 2; Rosnow, supra note 2. Apparently, many managers view their status in just this way. See Lorig, Where Do Corporate Responsibilities Really Lie—Not to Society, Managers Feel, BUS. HORIZONS, Spring 1967, at 51.
tion and dispersion of stock ownership. This centrifugal dispersion of the ownership function had been accompanied by the centripetal concentration of the control function, irreversibly separating the two aspects of property. This separation, they concluded, destroyed the traditional logic of property and replaced the private property system with a corporate enterprise system.

Berle and Means reviewed the history of the business enterprise, tracing its evolution from the sole proprietor who was owner, manager, and manipulator of property for his own benefit, through the first corporations in which owner and manager were one, and, finally, to the modern corporation in which ownership and control were totally divorced. As they saw it, by 1932 stock ownership had become so widespread in the largest corporations that no single shareholder or group of shareholders was able to maintain effective control. Thus, they saw throughout the continuum of history a gradual erosion of the control of the owner that culminated in the ultimate destruction of the private enterprise system in the modern corporation.

The proliferation of stock ownership was only one of the contributing causes of the breakdown in control by the shareholder, however. In the development of proxy voting and other changes in the law of corporations Berle and Means saw a causal connection with the ultimate divorcement of ownership and control. For example, the erosion of the doctrine of pre-emptive rights, the limitations upon notions of ultra vires, and the elimination of the right to remove directors without cause were all viewed as steps in a parade of changes alienating the shareholder from a position of real power. Indeed, the entire course of legal change throughout the nineteenth and early twentieth centuries, in their view, paralleled the economic development of the corporation, and tended in the direction of fewer limitations on corporate and management powers and greater separation between ownership and control. The liberalization of the state corporation statutes so as to permit proxy voting, however, came in for special notice. This liberalization, according to Berle and Means, placed in the hands of incumbent management, who controlled the proxy machinery and enjoyed the ready availability of the corporate coffers out of which to finance the solicitation process, the means to perpetuate themselves in office. They believed that by countenancing the advent of the proxy system the shareholder had forfeited the right to participate in any meaningful sense in the selection of management, and they thought that they perceived in the professional manager a new class of self-perpetuating oligarch.

The divorce of ownership and control, though the focal point of the Berle and Means study, was not the major concern of the authors. Berle elsewhere argued that the corporation law at the time treated directors as trustees for the shareholders, and that such a scheme had to be preserved in order to maintain control over management, at least until some other reasonably enforceable system of control could be devised. Nevertheless, Berle and Means accepted the fact of divorce as a datum and advocated no changes designed to restore the

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shareholder to a position of power or to revitalize the shareholder's franchise. They saw in the separation of ownership and control only one phase of what they conceived to be a metamorphosis of the modern corporation from an economic institution into a new form of political and social institution. They believed that the shareholder had forfeited his right to have the corporation operated in his sole interest and suggested that the community had been placed in a position to demand that the corporation serve all society, with management acting as a neutral technocracy balancing the claims of the various groups in society and assigning to each a share of the income stream on the basis of public policy. Further, they believed that dormant within the large corporation was a concentration of power rivaling that of the state itself and, fearful of the ultimate effects of the exercise of that power upon individual freedom, they advocated that the large corporation be treated as an institution analogous to the state and subject to the same sort of constitutional limitations.

Corporate Democracy. While Berle and Means were more concerned with the role of the corporation in society and were content to leave the powerless shareholder where events had put him, their revelation of the steady erosion of the power of the shareholder over his property prompted widespread interest in the twin questions of the legitimacy and control of corporate management. One response to these questions was the development of a new school of corporate philosophy under the banner of corporate democracy. The adherents of this approach represent a peculiar hodgepodge ranging from such perennial corporate gadflies as the Gilbert brothers to the New York Stock Exchange and the Securities and Exchange Commission. They share a dedication to the traditional view that the corporation exists for the benefit of its shareholders and the objective to return control of the corporation to its owners. Entranced by the apparent analogies with democratic government, they offer from time to time various suggestions designed to strengthen the corporate franchise. The only development of practical significance resulting from this movement, however, has been the enactment, as part of the federal securities acts, of provisions regulating the solicitation of proxies and affording dissident shareholders an opportunity to be heard.

The New York Stock Exchange and the Securities and Exchange Commission notwithstanding, most serious students of the corporation acknowledge that the corporate democracy approach is foreordained to failure. They have perceived

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14 See, e.g., L. Gilbert, Dividends and Democracy (1956); Caplin, Shareholder Nominations of Directors: A Program for Fair Corporate Suffrage, 39 Va. L. Rev. 141 (1953); Eisenberg, Access to the Corporate Proxy Machinery, 83 Harv. L. Rev. 1489 (1970). The New York Stock Exchange has imposed upon listed companies several rules against restricting the voting rights of shareholders. For example, it will not authorize the listing of nonvoting common stock or the voting common stock of a company which has outstanding nonvoting common stock. N.Y. Stock Exchange, Company Manual A-15 (1968).


17 See, e.g., Brewster, The Corporation and Economic Federalism, in Mason 72; Chayes, The Modern Corporation and the Rule of Law, in Mason 27; Hetherington, Fact and Legal
that most shareholders of large corporations simply do not sufficiently identify themselves as owners to have the concerns of owners. They view the shareholder as thinking of himself more as a creditor of the corporation holding a claim against the income of the enterprise, than as an owner of the business taking an entrepreneurial-type risk. Shareholders, they believe, do not care to take the time and expend the effort required to supervise management in the conduct of the affairs of the business. Furthermore, they argue that the individual interests of most shareholders are normally too small to make it worthwhile to take a more active role. Shareholders, they argue, could not likely afford to wage a proxy contest even if they were displeased. They conclude, therefore, that when the shareholder does become displeased with incumbent management, the shareholder's only real avenue of relief is in the stock market, and his real risk is that the market price of his stock will decline, not that the business will fail.

This view of the shareholder as an investor, rather than an owner, is probably an accurate one. If so, however, the conversion of the shareholder from owner to investor may be viewed not as a great tragedy, but as a source of tremendous benefit to society. Our largest corporations would have been unable to function without such a wide dispersion of share ownership. While the town meeting type of democracy envisioned by the corporate democrats might be a desirable ideal for government (a dubious assumption at best), it clearly is not for the modern corporation. One can conceive of no better way to bring the operation of a publicly held corporation to a standstill than to place the administration of its affairs in the hands of the shareholders and then require that the owners perform their function through their franchise exercised personally in a meeting of the whole. Ownership and control would be united all right, but the logistical problems being what they are, nothing would be accomplished. To permit management a wide ranging discretion in the carrying on of the affairs of the corporation, and to allow the voting process to be carried on by proxy, may tend to weaken the position of the shareholder, but at least it permits the corporation to operate.¹⁸

Corporate Constitutionalism. Another response to the questions of control and legitimacy is that of another new school of corporate philosophy which has taken up the suggestion in the Berle and Means study that the modern corporation has taken on the attributes of sovereignty and ought to be subjected to the same sort of constitutional limitations of due process and equal protection. Several adherents of this school have argued with some force that the modern corporation has become a political institution—a system of private government whose "constituencies" consist of those groups which come into contact with it.¹⁸ They further assert, without any empirical support, however, that the

¹⁸See Garrett, Practicing Lawyer's Viewpoints, 26 BUS. LAW. 545 (1970); Garrett, Atti-

¹⁸See, e.g., Brewster, supra note 17; Chayes, supra note 17; Latham, The Body Politic of the Corporation, in MASON 218; Miller, Private Governments and the Constitution, in THE CORPORATE TAKEOVER 122 (A. Hacker ed. 1964); Miller, Toward the "Techno-Corporate"

corporation has amassed tremendous power over these "constituencies." Further, since these "constituencies" have no real voice in the way the power will be exercised, corporate management is seen as the possessor of wholly irresponsible power—a state of affairs which, in the view of these scholars, poses an inherently pernicious contradiction with fundamental democratic principles. This is the crux of the problem of legitimacy: the possession of power by management with no responsibility to or control by those subject to that power.

To most of the followers of this school the corporate democracy approach is not the solution to the problem of legitimacy both because the futility of that approach is perceived, and because the shareholders are seen as the constituency least in need of protection due to their ability to sell their stock and remove themselves from the power of the corporation. Accordingly, while sharing the corporate democrats' fascination with the governmental analogue, the followers of this school would eschew any scheme designed to strengthen the shareholder's position, and would instead resolve the legitimacy issue by the application of constitutional principles of equality of treatment and due process to the many relationships of the corporation, both internal and external. Some, such as Professor Berle, would opt for the literal application of formal constitutional limitations, specifically including the fourteenth amendment. Indeed, Berle has professed to see the first tentative embraces of the corporate constitutional approach by the courts in a line of cases most prominently including the United States Supreme Court's decision in *Marsh v. Alabama*.

Others, though less sanguine than Berle about the "jurisprudential transfer of constitutional doctrine" to the corporation, to use Professor Manne's phrase, nevertheless believe that constitutional principles have been applied in the corporate context through specific legislation, such as the Automobile Dealer's Franchise Act and the Robinson-Patman Act.

Insofar as the corporate constitutionalists are arguing that the Constitution has literal application to the corporation, it seems reasonably self-evident that their position is unsound. As even some of the adherents to this approach have themselves recognized, the obstacles to such an application created by the linguistic problems involved are virtually insurmountable, and the courts, rather than embracing the proposals of corporate constitutionalism, have generally

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23See, e.g., Brewster, supra note 17; Chayes, supra note 17.

24See, e.g., Brewster, supra note 17.
rejected them. The Marsh case remains as something of a sport, as, indeed, it should. For there is a fundamental difference between governmental power and private action that cannot and should not be obscured by facile and emotionally appealing recourse to constitutional analogies. On the other hand, to the extent that the corporate constitutionalists are suggesting that there is an underlying principle requiring the corporation to act fairly with respect to those with whom it comes in contact and maintains relationships, the soundness of their proposition can hardly be questioned. Indeed, as will be more fully developed later, it is a thesis of this Article that prevailing legal norms require such fundamental fairness. The raison d'être of statutes such as those mentioned is to make explicit the imposition of a duty to act fairly which would probably exist in any event. Such statutes do require due process and equality of treatment in certain identified circumstances. They do not necessarily imply the application of constitutional principles, however, but rather the manifestation of the underlying principle of fairness in relations. Furthermore, to the extent that the corporate constitutionalists are suggesting that the modern corporation, simply because it is the modern corporation, has some special obligations not incident to anyone maintaining similar relationships, their position has no foundation in law or reason and is contrary to the very underlying equitable principle which they are striving to establish. There simply is no basis in fact for this sort of discriminatory treatment of the large, publicly held corporation—certainly not because the corporation has some vast, undefined "economic and social power of the highest consequence for the condition of our polity." This notion that the modern corporation stands poised, ready to unleash a vast reservoir of power may, as Professor Manning has put it, make "our minnow's blood race a bit," but it is less than realistic and does little to aid rational analysis.

Super Board. Several commentators also concerned with the question of the legitimacy of management's power and who recognize the futility of trying to restore the individual shareholder to a position of real control have attempted to resolve the issue by suggesting that various agencies outside the corporation select management and review its conduct of the corporation's affairs. At least one author has even gone so far as to suggest the complete disfranchisement of the shareholder and the vesting of authority for reviewing management's behavior in a new, but unspecified type of machinery.

Of all of the proposals to vest control in some sort of "super board of directors," the one most likely to have any lasting and practical consequence is the suggestion that the institutional investors take an active role in selecting man-

26 See text accompanying note 85 infra.
27 Chayes, supra note 17, at 28.
29 See, e.g., W. DOUGLAS, DEMOCRACY AND FINANCE (1940).
30 Manning, supra note 17.
31 For this purpose, the term "institutional investor" includes all corporations and other institutions which acquire and hold shares, such as pension and profit-sharing plans, invest-
agement and supervising its performance. The suggestion proceeds from the observation that these institutional investors are rapidly reconcentrating share ownership and could exercise control to a degree that individual shareholders could never approach. The philosophical basis for the suggestion is that persons having the ability to control occupy a fiduciary relationship to those who do not, and have a duty to actively supervise management to insure that the corporate affairs are conducted for the benefit of the shareholders as a whole.

A variation on this theme of employing the share ownership of the institutional investors to exert control over their portfolio companies is the movement to politicalize those institutions. This variation is reflected in the movement to have the institutional investors require the managements of large portfolio corporations to undertake a variety of social and political reforms not necessarily in furtherance of the objectives or purposes of either the institutional investors or the portfolio companies or in the interest of the shareholders or beneficiaries of either. In this willingness to have the corporation operated other than in the interests of the shareholders, the movement departs radically from the older proposals to have the institutional investors act as some sort of super board. These earlier proposals were designed simply to vest effective control in some entity outside management—the institutional investors simply being, by happy accident, a convenient mechanism. There was never any intent, however, that the institutional investors, as a super board, should cause the corporation to be operated for the benefit of anyone other than the shareholders. In this, the proposals were entirely consistent with traditional views of the corporation. The more modern movement to politicalize the institutional investors, on the other hand, is representative of an even broader movement to politicalize and socialize the corporation, and some of its proponents have been candid enough to

32See, e.g., J. LIVINGSTON, THE AMERICAN STOCKHOLDER (1958). There are several legal limitations upon the ability of certain of the institutional investors to amass sufficient ownership to control their portfolio companies. For example, banks, trust companies, and insurance companies are subject in most states to limits upon their investments in the securities of any one corporation. See statutes collected in the Blue Sky Law Reporter. In addition, the House Banking Committee is considering imposing a 10% limitation upon the stock of any corporation held by a bank in trust. BNA SEC. REG. & L. REP. NO. 105, June 9, 1971, at A-7. Furthermore, given a control position, there are numerous present and proposed statutory and decisional limitations upon their ability to exercise control. For example, the Banking Reform Act of 1971, H.R. 5700, 92d Cong., 1st Sess. (Mar. 8, 1971), if enacted will prohibit banks from voting stock held in trust unless required by the terms of the trust agreement or the beneficiary. BNA SEC. REG. & L. REP. NO. 105, June 9, 1971, at A-7. See also Enstam & Kamen, Control and the Institutional Investor, 23 BUS. LAW. 289 (1968). Even with these limitations, however, the observation made in the text appears to be valid. See, e.g., SEC Institutional Investor Study Report 41-79, summarized in BNA SEC. REG. & L. REP. NO. 92, Mar. 10, 1971, extra ed., at 77.


35See Blumberg, The Politicalization of the Corporation, 26 BUS. LAW. 1551 (1971); Manne, Good for General Motors?, Barron's, May 18, 1970, at 1, col. 1. The politicalization of the corporation is in itself a form of super board approach with the so-called public interest group or individual performing the function of the super board. The control relationship between the super board and the corporation is just not formalized and the super board
Surprisingly, the movement to politicalize the institutional investors has met with significant success. The institutional investors with increasing frequency are lending their support to socially-oriented proposals by the so-called public interest groups and, in some cases, even advancing their own such proposals. Several church groups, for example, have argued strenuously that their portfolio companies should withdraw from foreign countries practicing apartheid and have been successful in getting corporate management to include proposals to this effect in their proxy statements pursuant to the SEC's shareholder proposal rule, rule 14a-8.40

Many of the institutions, however, have resisted efforts to inject them forcibly into the social responsibility issue. For example, in one recent development Professor Roy Schotland, assistant dean at Georgetown University Law Center, requested Fidelity Trend Fund, Inc., an investment fund, to include in its proxy statement various proposals which, among other things, would require the Fund to analyze the performance of its present and prospective portfolio companies with regard to pollution control, minority hiring practices, and the like and to invest only in those found to have acted responsibly. The Fund refused to include the proposals, and Professor Schotland elicited the aid of the staff of the SEC, which supported his endeavor and threatened action against the Fund if it persisted in its refusal to include the proposals.45

The movement to politicalize the institutional investors has significantly affected their attitudes and altered their traditional behavior patterns vis-à-vis their portfolio companies. Whether these changes have had any practical im-

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39 The Domestic and Foreign Missionary Society of the Protestant Episcopal Church, for example, submitted a proposal to General Motors for inclusion in the company's 1971 proxy statement which would have amended the certificate of incorporation so as to preclude the corporation from conducting manufacturing operations in South Africa. 1971 GM Proxy Statement at 39.
40 The SEC's rule 14a-8 (17 C.F.R. § 240.14a-8 (1971)) provides that subject to various conditions and limitations, a shareholder having the right to vote at a meeting of a company subject to the rule may submit a proposal to management which management is required to set forth in its proxy statement. If management opposes the proposal, the shareholder is also entitled to have printed in the proxy statement a statement of not more than 100 words in support of the proposal. For purposes of the social responsibility issue, the circumstances most pertinent are: (1) that the proposal is, under the laws of the state of the issuer's (corporation's) domicile, not a proper subject for action by security holders; (2) that the proposal is submitted for the purpose of promoting general economic, social or similar causes; and (3) that the proposal consists of a request or recommendation that management take action with respect to a matter relating to the conduct of the ordinary business of the issuer.
none
nominal owners. For if a direct shareholder is not likely to be interested enough
in the corporation to take an active part in the management of corporate affairs,
how much less likely is the indirect shareholder—the shareholder or beneficiary
of the institutional investor? Other potential solutions to the problem of pyra-
miding control similarly raise problems of their own.

Other difficulties with the super board approaches have to do with the ab-
sence of established criteria (apart from the traditional indicator—profit) for
judging the effectiveness of either the corporate management or the super
board. Opinions can and usually do vary about whether a given activity or
course of action is or is not in the best interest of those for whose benefit the
action is taken. In the context of the corporation, whether one concludes the
enterprise ought to be operated for the benefit of the nominal owners exclusive-
ly or for society as a whole, standards are wanting to judge whether a given de-
cision will inure to the benefit of the corporation or society. In the area of social
responsibility, criteria are particularly lacking.

It was for just such a reason that the courts felt constrained to devise their
business judgment rule when faced with the supplications of shareholders to
review the conduct of corporate management. Lacking objective criteria, de-
tailed knowledge of the business, and expertise to evaluate what facts they had,
they were forced pragmatically to eschew direct interference with the prudential
judgments of management. As many institutional investors have been wise
enough to perceive, it is less than realistic to assume that a super board could
do otherwise than the courts have done, at least if they themselves are not to
take over the function of management; they simply cannot become well enough
informed, either in terms of what the corporation is doing or what it should do
to review specific decisions of management.

The problem of an absence of criteria is compounded for the institutional
investors. Besides not having any standards to judge how the portfolio corpora-
tions should be operated, they are faced with a divergence of opinion on the
standards by which they themselves should be judged. As indicated, some have
taken the position that the institutional investors, as controlling shareholders,
must act so as to benefit the corporate shareholders as a whole. Contrasted with
that position is the traditional view that such institutional investors as corporate
trustees, pension plans, and the like should act solely for the benefit of their
own shareholders or beneficiaries. Most investment managers have traditionally
translated this duty of loyalty to the institution's beneficiaries into financial
terms, assuming that they must make their investment decisions solely on the
basis of the effect upon the return on investment, and striving always to maxi-
mize that return. While the traditional approach of the institutional investors
is deemed to be overly restrictive, the fact that their traditional roles are being
questioned makes a complex issue even more troubling for the investment man-

48 See the sources cited at note 43 supra.
49 See text accompanying note 34 supra.
50 See, e.g., Manne, The "Higher Criticism" of the Modern Corporation, 62 COLUM. L.
REV. 399 (1962); Rosenfeld v. Black, 445 F.2d 1337 (2d Cir. 1971), noted in BNA SEC.
51 See the sources cited at note 43 supra.
52 See note 87 infra.
agers of these institutions, and casts doubt upon those suggestions looking to the establishment of the institutional investors as super boards.

**Economic Statesmanship.** One of the more provocative suggestions of the Berle and Means study was that through the forfeiture of the shareholders' ability to have the corporation operated for their sole benefit, society had been placed in a position to demand that corporate profits be distributed in a way which would benefit all of society. The study went on to suggest that corporate management should act as a neutral technocracy responding to the claims of the various groups of society according to public policy. One manifestation of the philosophy underlying this suggestion is the so-called "economic statesmanship" or "corporate conscience" approach to the social responsibility issue.

Actually, the genesis of the economic statesmanship approach predated the Berle and Means study. Even before the popularization of the notion by the Berle and Means study, there were those business leaders who had opted for a broader view of management's responsibilities. The following quotation, taken originally from an address by Mr. Owen D. Young, then an executive officer of General Electric, is illustrative of the sort of remarks businessmen were beginning to make as early as 1929:

If there is one thing a lawyer is taught it is knowledge of trusteeship and the sacredness of that position. Very soon he saw rising a notion that managers were no longer attorneys for stockholders; they were becoming trustees of an institution.

If you will pardon me for being personal, 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?

My conception of it is this: That there are three groups of people who have an interest in that institution. One is the group of fifty-odd thousand people who have put their capital in the company, namely, its stockholders. Another is a group of well toward one hundred thousand people who are putting their labor and their lives into the business of the company. The third group is of customers and the general public.

Customers have a right to demand that a concern so large shall not only do its business honestly and properly, but, further, that it shall meet its public obligations and perform its public duties—in a word, vast as it is, that it should be a good citizen.

Now, I conceive my trust first to be to see to it that the capital which is put into this 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 I have described. One no longer feels the obliga-
Academically, too, the underlying philosophy of the economic statesmanship approach was being vented. Berle himself contributed to this airing, and in many respects his work represents something of an intellectual curiosity when viewed in the light of the Berle and Means study. For example, prior to his work with Professor Means, Berle published two articles which argued that the powers of corporate managers were powers in trust for the benefit of the shareholders. This position was challenged by Professor E. Merrick Dodd, Jr., who argued that while Berle's position may have been supported by then existing legal orthodoxy, public opinion even at that time was demanding that businessmen recognize the claims of other groups in society upon the corporate income stream, and that the law had already been modified somewhat in reflection of such public opinion. Dodd further argued that the state of corporation law was such that the corporate manager could view himself as trustee for the enterprise rather than the shareholders, and as such could legally recognize his broader responsibilities to society. While apparently concurring conceptually with the philosophical foundation for Dodd's argument, as evidenced by the position taken in the joint work with Professor Means, Berle replied by pointing out that if the traditional legal norm were abandoned, enabling management to operate the corporation for the benefit of others besides the shareholders, there would be no enforceable system of control to insure that managers would not divert the income stream to their own self-aggrandizement. Dodd acceded to this position, and their debate terminated.

In 1954, however, Berle detected a system of restraints upon corporate managers which, though informal, was deemed to be an effective control mechanism. Thinking the manager sufficiently restrained from acting in his own self-interest by what he termed the "public consensus," Berle concluded that the alternative system of control previously thought missing had been supplied and that corporate management, having rightfully assumed its proper role of public trustee within the constraints of that system, had been legitimated.

The economic statesmanship approach has gained a substantial following among businessmen today. Comments similar to those of Mr. Young quoted above, which were so noteworthy a generation or two ago, are now commonplace. Virtually every issue of the various business periodicals adduces new

55 Address of Owen D. Young, Jan. 1929, quoted in Dodd, supra note 9, at 1154-55.
57 Dodd, supra note 9.
58 Berle, For Whom Corporate Managers Are Trustees: A Note, 45 HARV. L. REV. 1365 (1932).
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evidence of business' awareness of its social responsibility. Business leaders increasingly acknowledge the social responsibility of business and exhort their brethren to widen their outlook and to take up the challenge of society's problems.

The touchstone of the corporate conscience or economic statesmanship approach has a universal appeal which may serve to explain the readiness of so many pragmatic, yet fair-minded, businessmen to espouse it. It is founded upon the fundamental truth that society requires all of its members, including business, to recognize and satisfy the responsibility inherent in their many relationships. Being predicated upon this immutable truth, the validity of the basic thrust of the approach can hardly be doubted.

The only serious criticism that can be made of the approach (or more properly of its proponents) lies in the failure to articulate clearly its theoretical foundation and just what it really signifies so far as the public is concerned. It is one thing to acknowledge acceptance of some public responsibility; it is something else to define the limits of that responsibility. This shortcoming of the approach and its adherents is not without significance. Repeated protestation by business of a nascent recognition of its social responsibility has to raise public expectations of the public role business is going to play. However, if the businessman's conception of social responsibility differs in type or degree from that of his public, the latter's expectations may likely go unfulfilled; the result being that both will be frustrated, the public because it gets less responsible conduct than it expected, and the businessman because he did all that he intended, but finds it less than graciously received. Thus, the failure to communicate clearly just what is implied by the economic statesmanship approach can be tangibly counterproductive.

It must be noted that the approach has not been so generously viewed by all concerned with the social responsibility issue. Some have denigrated the approach vehemently, and criticisms have been numerous. One criticism that is especially noteworthy both because of the frequency with which it has been raised and because of its particular speciousness relates to the notion which Professor Berle has chosen to call the "public consensus." The notion that businessmen are restrained in any real sense by public opinion is disparaged by scholars on both sides of the social responsibility issue. Pedantic protests notwithstanding, however, public opinion is a real, if nonquantifiable, force, and businessmen do react to it. To be sure, one must be clear about what is encompassed in the term public opinion, but in the sense in which it is used here, and in which Berle apparently intended his "public consensus" synonym to be understood, public opinion is an effective control mechanism.


Public opinion is used here to denote the totality of the several opinions and attitudes toward business of the various groups within society with which business maintains relations. It is expressed in the myriad of ways in which people communicate to business. See text following note 89 infra.
II. SOME ADDITIONAL CRITICISMS OF THE CONTENDING APPROACHES

In addition to the criticism of irrelevance leveled by Berle and Means at the economic approach, there are several other criticisms that can be made. Perhaps the most basic, however, is that it assumes away reality by virtually ignoring all of the noneconomic factors to which human persons react. It disregards the social nature of man, assuming him to be motivated solely by economic considerations. Even a casual observation of the real world reveals, however, that man is both a social and an economic person. He is motivated by an intricate complexus of economic and noneconomic desires and aspirations. Thus, the economist's assumption that man is going to act in his own self-interest and will try to maximize the benefits accruing to him is valid only if it takes cognizance of the whole complexus of social and economic benefits to which man aspires; otherwise, it is only a convention, useful for pedagogic purposes perhaps, but totally unrealistic. Similarly, the description of the role assigned to business, i.e., the efficient use of resources to produce the maximum benefit for society, is adequate only if it comprehends both the social and the economic goods and consequences which business produces. To ignore business' social consequences and to acknowledge only its economic products simply disregards reality. While it may be useful for pedagogical or analytic purposes to construct economic abstractions—to make simplifying assumptions that disregard the social nature of the world—one must not lose sight of the fact (as many of the proponents of the economic approach apparently have) that the resultant model is only an abstraction. Such a model cannot be fully adequate for the purpose of prescribing how business should act in the real world, especially when such a value-related subject as social responsibility is concerned.

This criticism of the economic approach does not mean, of course, that the fundamental assumptions of economic theory or many of its normative arguments need be abandoned. The marketplace, with its price mechanism, is still the best device yet conceived for the allocation of resources, and economic theory remains a useful analytical tool. All the criticism implies is that if economic theory is to be used for prescriptive purposes in the social responsibility arena, it must be modified so that social, as well as economic, costs and benefits are taken into account.

One further thing to be said in criticism both of the economic approach and of the social responsibility approach is that both seem to have their genesis in a deep-rooted fear of bigness, whether it be in business or government. The economic approach, which one would not think to be generally fearful of business, hedges its theory with various constraints on the accumulation of market power. Its adherents welcome and, indeed, insist upon strict antitrust and other similar laws to insure competitive conditions in the product and capital markets, while it is normally bigness in relation to the market, not bigness per se, which

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\footnote{See Elbring, supra note 63.}

\footnote{See Manne, The Myth of Corporate Responsibility—or—Will the Real Ralph Nader Please Stand Up?, 26 BUS. L.W. 533 (1970).}
is objectionable to the theory, its adherents manifest a clear preference for a market structure closely approximating the economist's pure competition model—that is, an atomized industry.

The economic approach also reflects a fear of businessmen themselves. Businessmen are not trusted to make the "right" social decisions. They lack the training to make equitable choices, according to the theory's adherents, and could work all sorts of mischief if turned free with a broad mandate to go and "do equity." This is one of the reasons for a decision model, ostensibly objective, which is supposed to eliminate any value judgments on the part of the businessman. Furthermore, according to some of the theory's adherents, if businessmen were to accept such a mandate, it would be tantamount to issuing an open invitation to big government to intervene, with all the resulting inefficiencies inherent in a large bureaucracy.

On the other side of the coin, the social responsibility adherents are fascinated with bigness; hence, their proclivity to view the entire business sector as if epitomized by General Motors. Suffering from the so-called "GM Syndrome," they have become so mesmerized by the size of General Motors and a few other large corporations that they have lost sight of the fact that size is not necessarily synonymous with power, economic or otherwise. They have focused so myopically on the large corporation that they ignore the remainder of the business sector and shun a theoretical framework within which the social responsibility of business generally can be rationalized. Transfixed upon the myth of the modern corporation and its power, they clamor for ill-conceived schemes to control and "legitimate" the corporation.

The general fear and mistrust of bigness, of business, and of businessmen which seems to pervade academia is founded upon the myth that business is powerful and without effective control. This fear is wholly irrational. Our corporations, however large, are not above the law, as some have suggested, nor are they repositories of some unconstrained, god-like power over the course of history. On the contrary, they are in large degree prisoners of the written and unwritten laws of a very complex legal-social-economic system. They are perhaps more stringently controlled than any other form of business. Moreover, businessmen, whether their firms be large or small, are generally responsive to the social needs of the community and endeavor to act in an honest, responsible, equitable way which is fair to all of those with whom they come into contact. They are, as Berle has argued, very sensitive to the "public consensus."

III. THE LEGAL THEORY OF THE CORPORATION

The outlines of the legal construct of the corporation hardly need elaboration. Briefly, the corporation is an artificial person, created by and existing only

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67 E. Mason, INTRODUCTION TO THE CORPORATION IN MODERN SOCIETY (1960); Austin, Who Has the Responsibility for Social Change—Business or Government?, HARV. BUS. REV., July 1965, at 45; Rostow, supra note 61.
68 Manne, supra note 63.
in contemplation of law. It is *sui juris*, legally capable of owning, holding and disposing of property, of contracting in its own name, of suing and being sued. It has certain constitutional rights.\(^7\)

The fiction is less than reality, however; the personification is incomplete. In traditional terms the corporation is a creature of limited powers; it may do only such things as may be permitted, expressly or by necessary implication, by the law under which it is formed and by its charter. It may exercise only such powers as will further its purpose, and its purpose has traditionally been viewed ultimately as the production of profit for the private gain of the collection of individuals who own it.\(^7\) Mirroring the concepts of the classic economic theory, the corporation has been treated as a mechanism through which a group of individuals could conveniently order their relationships in carrying out a socially useful, but business-oriented, purpose. It has been assumed that the affairs of the corporation would be carried on for the benefit of the shareholders, and the law historically imposed twin duties of loyalty and care upon the agent-managers to insure that this assumption was indeed the basis upon which management acted.\(^7\) As Professor Berle put it, the powers of management were traditionally viewed as powers in trust, and the beneficiaries of the trust were the shareholders.

In keeping with this view of the corporate manager as a fiduciary for the shareholders, the law circumscribed their relationship with a complex matrix of rules designed to protect the shareholders and to insure that they controlled the destiny of their creature. Changing, however, to reflect the changing attitudes and mores of the society it serves, the law, as Berle and Means observed, gradually evolved a new conception of the manager-owner relationship. As society and business grew more complex, the demands for commercial expediency increased, and the law of the corporation changed to mirror this changing environment. Corporation laws were revised to increase the discretion of management to permit a more flexible response to changing business conditions. Proxy voting was introduced; the doctrine of pre-emptive rights eroded away. Other changes were made with the object of serving the convenience of the enterprise. Without them it is unlikely that the corporate form would have so long endured or that business would have been able to succeed in producing the vast amount of wealth which this country has realized.

Such changes were not made without due regard for the shareholders. The judges and legislators who fabricated the modern law of the corporation retained many of the safeguards of a former era or devised new ones. In spite of the impression conveyed by the Berle and Means theory of separation of ownership and control, possibly no other relationship has surrounding it the degree of regulation which the relationship of corporate owner and corporate manager has. The elements of the matrix may have changed over time, but the matrix is still there.

The regulation of this relationship begins when corporate existence begins. The state corporation laws under which corporations are created typically con-

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\(^7\) See, e.g., D. Votaw, *Modern Corporations* (1965); 1 P-H Corp. § 1101 (1970).
\(^7\) See, e.g., W. Cary, *supra* note 34.
tain numerous provisions bearing upon the relationship and establishing a
framework for its government. Theoretically, these provisions assume that the
ultimate authority over the enterprise remains in the shareholders. For example,
while it is normally provided that the affairs of the corporation shall be man-
aged by a board of directors, through their franchise the shareholders retain
a potentially large degree of visitorial power over the directors and the affairs of
the corporation. The directors must be elected by the shareholders, and the
shareholders retain the power to make organic changes in the corporation and
to dissolve it.

Furthermore, the provisions of the state corporation statutes constitute merely
a small sampling of the total body of regulatory measures applicable to the
owner-manager relationship. Beyond those statutes is a vast array of common-
law rules emanating from the decisions of the state and federal courts and em-
body in the legion of cases dealing with the many faceted relationship of
shareholder and manager. In addition, there exists a large and growing num-
ber of federal statutes and administrative regulations which also bear upon
this relationship, pre-eminent among which are the federal securities laws.

The continuing evolution in public attitudes toward the corporation and the
relationship between the manager and the shareholders reflected in the changing
legal theory of the corporation has resulted in a curious ambivalence in the law
toward the owner-manager relationship. On the one hand, the relationship is
viewed in traditional terms as approaching that between principal and agent or
trustee and cestui que trust. In this view of the relationship the manager is
deemed to serve as the elected representative of the shareholders, deriving from
them his authority to act in the conduct of the enterprise and accountable to
them for the profits of the business. On the other hand, the manager is some-
times viewed as essentially independent of the shareholders, deriving his au-
thority not from them but from the corporation itself. In this view, the manager
is a trustee not for the shareholders, but for the corporation.

The first of these two views is reflected in the organizational provisions of
the state corporation laws already outlined. As mentioned, these provisions vest
in the shareholders substantial power and reflect a classical scalar chain of com-
mand leading from the shareholders, as the holders of the ultimate authority,
down through the directors to the officers and other agents and employees of
the corporation.

The second of these views considers the corporation as an entity in itself,
separate and apart from the shareholders, with its own interests which may or
may not coincide with those of the shareholders. This view is reflected in those
provisions of the state corporation laws vesting the corporation itself with a
series of powers which the directors, in the absence of contrary provisions in
the articles of incorporation, are empowered to exercise in the conduct of the
affairs of the corporation. It is further manifested in numerous court decisions
affirming the proposition that the shareholders retain the power to alter the or-
monic structure of the corporation and elect the directors, but not the right to
interfere with the day-to-day operation of the business of the enterprise.83

Given this ambivalence in legal theory of the corporation, can it be said that
the law offers any real guidance on which of the two approaches to the social
responsibility issue is valid, or on the course the businessman should follow
when confronted with conflicting demands? The answer, unfortunately, is that
it cannot.

The traditional view that the manager is trustee for the shareholder is, by
necessity, consistent with the economic approach, having been developed largely
in reflection of the classic economic theory underlying that approach. The view
is not for that reason necessarily inconsistent with the social responsibility ap-
proach, however. It has been forcefully argued, for example, that if the actions
usually explained in terms of social responsibility were analyzed correctly, their
relation to the profit maximization standard would become obvious and could
be justified under the traditional legal theory of the corporation.84 Basically, the
argument is that most business activities which are presented as having been
undertaken in satisfaction of the social responsibility of the corporation actually
inure to the long-run benefit of the shareholders, and would be upheld under
the business judgment rule in any event. This argument has been justifiably
met with substantial skepticism.85 As Berle has suggested,86 it is perhaps as likely
that the business executive reacts to the social demands made upon the corpora-
tion humanly, with pure altruism, and only after having so reacted feels com-
pelled by outmoded legal rules to justify his actions in terms of long-run profit
maximization. The manager, Berle says, only rationalizes his altruism when he
cloaks his conduct in the mantle of long-run benefit, and Berle laments that
the state of the law is such that the executive must feel so constrained.

The truth probably lies somewhere between these positions. Business execu-
tives do undoubtedly act on occasion out of pure altruism; they would be less
than human otherwise. To conclude from that observation that businessmen do
not normally try to take explicitly into consideration the long-run effect of their
socially oriented actions, however, is naive. Clearly, the precise effects of such
actions upon the long-run profit position of the firm cannot be accurately quan-
tified, but the same thing might be said of research and development and ad-
vertising programs. Admittedly, some intuitive judgments are necessary. Never-
theless, as rational beings businessmen must make an attempt to gauge the
effects of the social actions of the firm.

Rationalization or not, social action can normally be justified as being con-
ducive to the maximization of the firm’s long-range profits. This being so, the

83 See the cases cited in 1 P-H Corp. §§ 2009-10 (1969).
84 See, e.g., Friedman, supra note 2; Ruder, Public Obligations of Private Corporations,
85 See, e.g., Safire, "Silvertoe: Financial Adventure of James Debenture—A Parody with
social responsibility approach can be viewed as promoting the interests of the shareholders and, therefore, consistent with the traditional legal view of the fiduciary duty of the manager. The traditional legal theory of the corporation is thus consistent with both the economic and the social responsibility approaches.

By similar logic it can be shown that the more modern view of the manager's responsibility is also compatible with the two approaches to the social responsibility issue. If social action taken in the name of the corporation can be explained on the basis of its contribution to the long-run benefit of the enterprise, then the action can be upheld against legal attack. However the income stream is distributed once it has entered the enterprise, if the conduct of the manager is directed at the goal of maximizing that stream, his conduct is valid under the familiar business judgment rule.

IV. AN ALTERNATIVE APPROACH

If, as here argued, neither of the contending approaches to the social responsibility issue is satisfactory, and neither of the legal views of the corporation provides any real guidance on the social duty of the manager, is there any way in which the social responsibility issue can be rationalized? Can there be developed any theoretical framework to aid the manager and the businessman in making rational decisions when confronted with demands to take action in the public interest—and to do so conformably with prevailing legal norms? It is submitted that such a framework can be developed, and the following is offered as an outline of the shape it might take.

Candor requires disclosure at the outset that this suggestion offers nothing which is genuinely inventive. It innovates, if at all, only by synthesizing familiar concepts and applying them in the business context.

The alternative approach is founded upon the basic assumptions and normative arguments of economic theory. As indicated, this theory is a very useful analytical tool and when modified so as to conform to the social nature of man and society can also be a helpful prescriptive device. Accordingly, the basic assumptions of the theory already outlined—modified to recognize that men are both social and economic beings, having both social and economic needs and aspirations, and that the business enterprise is a social, as well as an economic system, producing social, as well as economic, goods and consequences—are deemed a firm foundation upon which to construct a theory of social responsibility.

The normative argument of economic theory which postulates that the maximization of profits will tend to result in the optimal allocation of resources and produce the greatest benefit for the greatest number is likewise considered an essentially sound proposition and is an important part of the alternative approach. Again, certain modifications are required, however. For one, the benefits being maximized must be recognized to comprehend both economic and noneconomic goods. More importantly, profit in the suggested model is not accorded the degree of importance that the economic theorists give to it. Profit in the alternative approach does play a significant role; however, whereas the role of profit in classic economic theory is that of the single indicator of busi-
ness' efficiency in the use of society's resources, its role in the alternative approach suggested is that of only one of many indicia—albeit an extremely important one.

As Professor Berle has argued, "public consensus" or public opinion is the force which ultimately directs and restrains the field of action of the businessman. Public opinion makes itself felt in many ways. If the public is satisfied that an enterprise is giving a fair product for a fair price, that the quality of its output is not substandard, that it will honor its warranties, that it will, in short, respond in a way in which the public expects a seller of goods and services should act with respect to those with whom it comes into contact and maintains relations as buyers, the public will reward the firm with its custom in the product market. If the public believes that the enterprise makes fair disclosure of material information, pays its debts, honors its commitments, and otherwise responds the way the public believes a firm should act with respect to those with whom it comes into contact and maintains relations as investors, the public will reward the firm with its custom in the capital market. In like manner, if the firm responds in the way the public expects it should act in its other myriad relationships, the public will support the firm, and the result will be that its profits will tend to be maximized, its securities will tend to be marketable, its labor relations will tend to be good, and so on. On the other hand, if the firm does not respond in the manner in which the public expects, public opinion will make itself felt in the marketplace, in the legislature, in personal contacts, and in the multitude of other ways that the public communicates to business. The public's custom and, hence, profits are simply one way in which the public communicates and profits are, therefore, but one indicator of how the public believes the firm is contributing to the effectuation of the purpose which society has assigned to business generally.

Just as the foundation of the alternative approach is constructed of familiar materials, so are the supporting pillars. These pillars, theorems fashioned from familiar principles of purpose and relation, are as follows:

(1) The business enterprise, being a human endeavor, is purposive.

(2) Its purpose gives the enterprise its cohesive force, provides it with direction and imbues its leaders, management, with the authority to accomplish that purpose.

(3) The relationship of the enterprise to others creates responsibility to them, the degree of responsibility being a function of the degree of dependency involved in the relationship.

The first of these theorems stems from the principle of purpose, a postulate based upon the observation that rational beings do not behave irrationally; they have a reason for doing things, a purpose. Persons (the insane and small children aside) are rational beings, and they bring to their organizations their rationality. The business enterprise, being a human endeavor, is thus imbued with rationality, and, therefore, is purposive. Society has assigned to business generally the purpose of utilizing its resources in the optimal manner to produce the

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greatest good, social and economic, for the greatest number. Each individual business organization, being a subsystem of business generally, shares that overall purpose, and the subgoal of each subsystem must conform to that purpose. In other words, while an enterprise may have as its immediate purpose some specific business objective, that goal must conform to the goal of business generally, that is, the specific objective must somehow tend to maximize the social and economic goods available to society and optimize the allocation of society's available resources.\(^7\)

The second theorem is based upon what has been referred to as the principle of finality.\(^8\) That principle is a recognition that rational beings act in such a way as to serve their final goals or ends; that is, they adopt the means necessary to accomplish their purposes. The corollary of this principle is that the nature of a being must be such as to enable it to effect its purposes, and no being can act in a way which does not reflect its nature. The business enterprise, being a human organization, must act in a manner in furtherance of its purposes, and its purposes determine its nature and the way in which it must act. Thus, the manager would rationally strive to operate the firm in order to attain the specific business objective which the enterprise has as its immediate purpose. Further, in the event there are two or more equally efficacious methods of attaining that objective, the manager rationally will opt for that method which will tend to optimize the allocation of resources and maximize the benefits to society, since the firm must also serve the purpose of the overall business system of which it is a part.

The third theorem is an adaption of the notion of relation.\(^9\) This notion is founded upon the belief that human beings are endowed with a complexus of rights which must be respected by all other persons. When people come into contact, each must respect the rights of the other. Hence, the relationship of the two people implies mutual responsibility, the degree of responsibility being dependent upon the nature of the relationship and the relative positions of the parties. Again, since the business enterprise is a human endeavor, it is imbued with similar rights and responsibilities with respect to those with whom it comes into contact—including its employees, its owners or shareholders, its customers, and so on.

The foregoing theorems are demonstrably consistent with prevailing legal norms. As already noted, in legal theory the corporation is a purposive entity, and the law postulates that the corporation will exercise such powers as may be required to carry out that purpose. Therefore, at least so far as the corporation is concerned, the law clearly reflects the first two of those theorems. It can be likewise demonstrated that the law reflects these same theorems so far as other business forms are concerned. However, in the interest of brevity the hypothesis is offered here without strict proof. It is submitted that the proposition may be accepted intuitively on the ground that if the law views the corporation as a convenient mechanism for ordering the affairs of its owners, as is frequently

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\(^7\) See, e.g., McFarlane, *The Search for Purpose*, CONFERENCE BOARD RECORD, Feb. 1965, at 29.


\(^9\) Id.
and cogently suggested, it will treat similarly other media through which people carry on their business affairs, recognizing, of course, that each business form does have its own unique rules. That is, so far as business forms can be treated generically, it is suggested the law will so treat them, and it can treat them generically so far as it is necessary to recognize that they are organizations, that they are purposive, and that their purposes do give them cohesion, direction, and authority.

With respect to the third theorem, it is suggested that the notion of relation is visible in all areas of the law. One of the most graphic illustrations of this is in the tort field where it is reasonably well settled that a stranger has no legal duty to go to the aid of another in distress; he can pass by and suffer no liability. If the stranger does go to the aid of another in distress, however, then (absent statutory exoneration) he incurs toward the other a duty to exercise such care as a reasonable man would do under the circumstances and, failing to do so, is liable for any damages proximately resulting from his negligence. The notion of relation is clearly operative in this situation. The creation of the relationship between the Good Samaritan and the injured imposed upon the former a responsibility—i.e., the duty to act prudently under the circumstances (which is another way of saying that the responsibility depended on the degree of dependency).

Another example closer to home for the businessman can be found in the concept of unconscionability embodied in section 2-302 of the Uniform Commercial Code.99 Under that section a contract may be set aside by a court if it is found to be unconscionable because of unfair surprise or inequity or because one of the parties occupied a bargaining position grossly superior to that of the other party. In such an instance the parties would normally have certain mutual responsibilities of fair dealing arising out of their contractual relationship anyway, but because of the special circumstances involving the unusual dependence of one of them, the law imposes the additional responsibility upon the dominant party not to take advantage of his dominance. Fairness requires that the positions of the parties be equalized.

The same logic underlying these examples is operative in the law dealing with the many other relationships which the business enterprise has with individuals and groups of individuals inside and outside the organization. The workmen's compensation laws, for example, are really but a codification of the notion of relation; the employment relationship creates a duty, among others, that the employer provide a safe place in which the employee can work. The various antitrust laws can be similarly explained in terms of the notion of relation, as can the federal and state securities laws, the law of partnership, the law of agency, other facets of commercial law, and the various laws dealing with the relationship between director and shareholder.

Approaching the many relationships of the businessman in this manner would be much more productive of sound analysis than the talismanic approach now typically used. For example, it really serves no good purpose to state doctrinairely that a director is a trustee for the shareholders, or for the enterprise,
or for some other group or public. The use of the term "trustee" in this context is really simply a shorthand way of stating that there is a relationship which entails certain duties and that the extent of the duties depends upon the degree of dependency in the relationship. The director is not a trustee in a strict sense, however, and using the term all too frequently serves only to confuse the issue and to misdirect the focus of the analysis. A much sharper appreciation of the issues would result if the use of the term in this context were abandoned altogether and the problem recognized as a question of relationship involving some degree of dependency. The degree of the resulting responsibility could then be rationally analyzed.

It may be objected that the notion of relation is simply another way of proposing that the businessman act fairly with those with whom he comes into contact. This is, certainly, the essence of the concept; it is basically a mandate to act fairly and equitably under the circumstances with respect to those with whom relationships are maintained. This, however, should create no disquietude. This is the underlying principle of most rules of law, and it clearly reflects the expectations of society at large. Law and society do expect that businessmen act fairly in their business relationships and not engage in sharp practices or overreach those with whom they do business. To say so is simply to give voice to reality.

It is true that the mandate to do equity is indefinite, but it is upon just such a mandate that lawsuits are decided and business transactions completed. Moreover, it is really no less definite a formula than most of the others used in law and economics. The profit maximization formula, for example, however objective it may sound is impossible of strict application. No one can determine whether profit has really been maximized or whether a strategy or decision actually optimizes the allocation of resources. Reasonable minds can and do differ about such things. The ideal is imprecise and it is for that reason that we have such equally imprecise rules as the business judgment rule and the prudent director test with which to judge performance.

If there were such a thing as perfect knowledge, then a deterministic decision model like the profit maximization formula would be realistic. The fact of the matter, however, is that all judgments are made under conditions of uncertainty and, hence, involve a greater or lesser degree of intuition. Decision models, such as that provided by classic economic theory, can only pretend to geometric precision; in the real world of imperfect knowledge all decision guides are indefinite and uncertain. To tell the businessman to go and do equity is, therefore, no more and no less ambiguous than to tell him to go and maximize profit. If he does either perfectly, it will only be by purest chance.

If the alternative suggested is based upon principles which are so indefinite, it is reasonable to ask whether it can possibly be very useful. This question depends on what one expects the theory to do. If the theory is expected to yield specific results with computer-like accuracy, then its utility is quite doubtful. On the other hand, if it is expected only to provide a theoretical framework within which the businessman can bring to bear his judgment and acumen, then, hopefully, it can be quite useful. The latter, of course, is all that is claimed for the
approach and, given this standard of utility, it is submitted that the approach can be an effective device for rationalizing the analysis of business problems involving the social responsibility issue. It will not tell the manager how to act in specific circumstances. How a manager acts in a given case is a matter of prudence. But prudential judgment can be aided by a meaningful framework of theoretical principles which will assist the manager in focusing upon the relevant issues, and that is what this approach is intended to do.

To see how the theory would be applied by a businessman adopting it, it might be useful to examine some of the decision points that would be relevant in a situation involving a demand that the enterprise undertake some action in the name of social responsibility. The businessman's first consideration would be whether there were any relationship with the group to be benefited. If none, then there would be no duty to act. If there were some relationship, however, then that relationship would have to be examined with a view to determining its nature and the degree of responsibility flowing from it. Assuming that the relationship were such that some action is required, the duty to act would have to be reconciled with the objectives of the enterprise and its overriding purpose to maximize the social and economic benefits to society. The businessman would need to fashion a strategy to effect this reconciliation and to satisfy the duty to act. In forming and carrying out this strategy, he would apply all of the analytical tools provided by the economist's kitbag, recognizing the modifications made necessary by the simplifying assumptions of economic abstractions. Finally, after putting his strategy into effect, he would judge the results of his efforts by the criterion of public opinion—as expressed in the firm's profits, stock market performance, threatened or pending litigation, legislation, and so on—and based upon this he would modify his strategy as necessary.

Viewing the suggested approach in perspective, it can be seen that it is predicated upon two principal concepts:

(1) That business and businessmen have responsibilities to all of those with whom they have relationships and, conversely, have no duty to those with whom they do not have relationships; and

(2) That whatever the immediate objective of an enterprise, it must serve the shared purpose of business to maximize the social and economic benefits to society and optimize the allocation of society's resources, and its structure and operations must tend to carry out that purpose.

In these two concepts lies the essence of the social responsibility of business.  

91 The social responsibility of other institutions may be similarly distilled to notions of relation and purpose. For example, as pointed out in the text, the suggestion that the institutional investors perform the function of a super board raises a number of very serious problems, many of which have only recently been discerned. So far, the same sort of doctrinaire approach to these problems has been taken as in the case of the social responsibility of business, the result being that the antagonists tend to talk in terms of slogans and fail to make a really useful analysis of the pertinent issues. The suggested approach could be helpful in identifying and resolving these issues and provide some guidance to the investment managers of the institutional investors in responding to some of the socially-oriented demands made upon them.

One of the more serious questions in the institutional investor controversy is whether the institutions have the right or duty to assume responsibility outside the sphere of their own shareholders or beneficiaries. Some of them are trustees or fiduciaries in a strict sense and, hence, in traditional terms have a duty of undivided loyalty. However, even these, not
If business recognizes and satisfies its responsibilities to those with whom it
maintains relationships, and does so in a manner consistent with its purpose to
produce the greatest good, economic and noneconomic, for the greatest number,
then it satisfies its social responsibilities. If it does this, society will surely com-
municate its approval through an improved socio-economic environment; on
the other hand, if it does not, society will just as surely communicate its dis-
approval.

V. CONCLUSION

It is no news that business is confronted today with a multitude of conflicting
demands involving the social responsibility issue. It is also probably no real
revelation that neither of the contending approaches to that issue provides an
adequate normative framework for an analysis of these demands. This Article
has tried to describe some of the shortcomings of these approaches and suggest
an alternative that is believed to be workable and consistent with prevailing
legal norms and public expectations. This alternative approach will not yield
any timeless and immutable rules for the guidance of harried businessmen or
their legal counsel. It may, however, help to direct their attention to those con-
siderations which are truly relevant.

One final word is in order concerning the approach suggested here and the
issue of business' social responsibility. There will undoubtedly be situations en-
countered in which the theoretical framework suggested will lead in what may
appear to be an inequitable or antisocial direction. For example, it will doubt-
less occur that business is asked to respond to a situation in which there is no
relationship and, therefore, no duty to act, but which cries out for a humanistic
reaction. Should business respond in spite of the absence of a clearcut duty to
do so? Should business be the Good Samaritan? The answer depends upon
whether the situation at hand fits logically into the purposes of any of the many
other useful institutional arrangements created by society. Business and society
both must remember that business is not the only institution with social respon-
sibilities. We live in a wonderfully pluralistic world with a variety of institu-
tions, each having its own purposes, relationships, and responsibilities. If a
to mention the other types of institutional investors, have relationships with others besides
their beneficiaries and they therefore have the responsibilities which inhere in these relation-
ships. These responsibilities also need to be recognized and satisfied.

If it be accepted that the institutional investors do have responsibilities beyond the nar-
row class of their own shareholders or beneficiaries, there remain such questions as whether
their investment policies can and should be used in satisfying those responsibilities and, if
so, how they should establish their criteria for making investments. These questions should
be approached in a rational way from the standpoint of the basic purposes of the institutions
themselves. One such purpose—the one of overriding significance in the present context—is
the intermediation of savings. These institutions—most of them—are rather efficient money
pumps, moving excess savings from the consumer sector to business where it can be used
for investment in additional capital. In performing this role, the institutional investors per-
form a socially useful function. However, if that function is to be productive of the greatest
social benefit, the savings flow must be channeled toward those industrial and service com-
panies which can most nearly maximize the benefits to society. One way of determining
which companies do tend to maximize these benefits is to consider the profits of these com-
panies. Although, just as the business firm should view profit as only one of several indicia
of how the public is judging its performance, the institutional investor should similarly
view the profits of its portfolio companies. The ultimate indicator, of course, is public opinion
in all its expressions.
particular situation can be more effectively handled by one of these other institutions, then there is a misallocation of resources effected in an attempt by business—though well-meaning—to undertake it. It may appear to be socially irresponsible to pass by a stranger in need, but society will benefit more greatly in the long run if the proper institution is permitted to "do its own thing" and to fulfill its own proper role of Good Samaritan.