



Munich Personal RePEc Archive

Binding stakeholders into moral communities: A review of studies on social responsibility of business

Nair, Tara S. and Pradhan, Rachayeeta

Gujarat Institute of Development Research

2 January 2010

Online at <https://mpra.ub.uni-muenchen.de/20767/>

MPRA Paper No. 20767, posted 23 Aug 2010 02:13 UTC

**Binding stakeholders into moral communities:
A review of studies on social responsibility of business**

Tara S. Nair, Associate Professor, Gujarat Institute of Development Research,
Ahmedabad, India

Rachayeeta Pradhan, Graduate student, Maxwell School, Syracuse University, USA

**Paper published in *Asia Pacific Business Review*, Vol. V, No. 4 October - December
2009. Pp. 86-97.**

Abstract

This paper revisits the issue of business social responsibility with a view to reiterate its relevance in the contemporary scenario characterised by an overarching presence of private businesses and blurring of the barriers between not-for-profit and for-profit enterprises. The paper reviews the evolution of major theoretical positions of business social responsibility to demonstrate how the basic understanding of the term traversed through time and alongside changes in forms of business organisation and interpretations of the morality of private property. It draws on stakeholding and social contract theories to underscore the moral and social responsibility of businesses to broaden their vision beyond profit and stakeholder value.

Binding stakeholders into moral communities: A review of studies on social responsibility of business

What are businesses for? How do businesses relate to society? Do businesses have to consider and oblige stakeholders other than their owners or shareholders? In the contested terrain of business ethics and business social responsibility these questions have been asked and answered umpteen number of times. The answers have varied depending upon one's political and moral preferences regarding what businesses represent and reproduce. Thus, those who view businesses as upholding the institution of private property, the backbone of the capitalist economic order, which, by its very dynamics reproduces economic growth and wellbeing, responsibility is coterminous with shareholder wealth maximisation. Here, the implicit policy direction is to promote the wealth-seeking ambition of owners and investors in an unconstrained fashion so that general economic and social well being can be automatically taken care of. Within this position a concern like social responsibility is a redundant issue. There is a counterview that the legitimacy of business rests on its service to the society and not on its ability to generate profit for its owners. Thus, society as represented by a host of distinct constituencies, is the predominant stakeholder of any business which makes societal obligation the *raison d'être* of its functioning. A more rational position, however, seems to lie somewhere in between – business neither exists for serving the unbridled self aggrandisement of ambitious and greedy investors nor for furthering some altruistic motives to the complete neglect of the economic calculus of the owners and investors.

In this paper we attempt to revisit the issue of business social responsibility with a view to reiterate its significant relevance in the contemporary scenario, mainly for two reasons. First, increasingly, private business has come to occupy the centre stage in the growth strategies across countries, including the ones that used to follow statist development policies in the earlier decades. Unique ways are evolved by many economies to engage private business even in spheres that have hitherto been dominated by the bureaucracy (for instance, basic services). Second, the concept of business responsibility has become more complex as the not-for-profit organisations, driven by the compulsion to achieve

economic sustainability, have started organising some of their activities on for-profit mode. Addressing such initiatives from the point of view of business responsibility may, *prima facie*, look inconsequential as the very rationale for their incorporation is located in their social change mission. However, it is important to recognise that profit-maximisation objective demands amends in the overall culture and behavioural patterns of even not-for-profit entities, which, in turn, may produce outcomes that do not necessarily increase overall societal wellbeing or serve the entity's original, altruistic goal of social transformation.

The paper is divided the following way. Section 1 reviews the evolution of the major theoretical approaches and concepts relating to business social responsibility. We will discuss here the theoretical debates around social responsibility and attempt to trace the evolution of the central concepts. In Sections 2 and 3, we will elaborate the theories of stakeholding and the social contract theory respectively with a view to expound the core question of who should businesses be responsible to and how they can potentially bind the salient stakeholders into moral communities. While stressing the need for businesses to enlarge their vision beyond profit maximisation to address the interests and claims of non-shareholding stakeholders, we will also review the relevant analytical schemes that can provide useful insights to the management in deciding on stakeholder salience.

Section 1

Socially Responsible Business: Meanings and Interpretations

There is a considerable body of work that seeks to develop and apply theoretical frameworks to the question of the role of business in society. They help disentangle issues that are central to business ethics and social responsibility. This field of study is also a contested one as there exist competing and mutually exclusive visions about the nature and purpose of corporations (Dunfee, 1999). Two distinct ethical approaches are found to have influenced these visions – the positive or the descriptive approach and the normative approach. Under positive ethical approaches are included empirical enquiries

into the ethical attitudes and behaviours of various actors in the business space. The normative approaches set out to prescribe, by delving deep into the basic questions of right and wrong, what 'ought to be' done by businesses for them to be called socially responsible. There are multiple perspectives even among theories that are prescriptive in nature. At one end of the spectrum are theories that position business social responsibility within the larger principles of egalitarian social development, while at the other end are those that uphold the utilitarian view that the business of business is to make profits.

Social responsibility broadly can be defined as the ethical orientation of an entity – be it a person, a body corporate or a government – to contribute to the egalitarian development of the society of which it is part. As Bobo (1991) argues social responsibility is an aspect of egalitarianism. He further defines social responsibility as a cluster of beliefs that acknowledges the existence and consequences of social and economic inequality and an obligation to contributing towards its mitigation. The egalitarian view, according to Bobo, is not the opposite of individualism; they are “concurrent ideological commitments that may assume different levels of importance across individuals” (pp.74-75). This definition of social responsibility, when applied to the realm of business would mean responsiveness of business entities to societal issues which motivate them to go beyond their economic, technical and legal obligations.¹

The concerns about the ethical orientation of businesses and their sense of social responsibility have evolved through the past seven to eight decades interacting with varying forms of business organisations and different ethical and legal interpretations as to their rights and duties. Merrick Dodd of the Harvard Law School was one of the earliest scholars to have discussed the issues of trust and fiduciary responsibility that bind managers and owners and its consequences for social well being. Writing in the early 1930s, in a world reeling under the effect of the Great Depression, Dodd (1932) stated: Business -which is economic organization of society – is private property only in a qualified sense, and society may properly demand that it be carried on in such a way as to

safeguard the interests of those who deal with it either as employees or consumers *even if the proprietary rights of its owners are thereby curtailed* (p.1162, emphasis added).²

In Dodd one sees the germination of the debate that later attracted significant degree of intensity and rigour – do businesses have a ‘fiduciary type obligation’ to their ‘stakeholders’? This question has been addressed in the later years by several scholars and their interpretations largely reflected the dominant mode of business of their times. Even Dodd’s concerns were shaped by the business environment prevalent in his times wherein many of the enterprises were owned by absentee investors who took little or no interest in their running and management, while the sole function of the corporate managers was thought to be of helping the stockholders obtain maximum amount of profits. He envisioned a future where the law will “regard all business as affected with a public interest” (p.1149). He also imagined the dawn of a new spirit that would drive businesses “to become a profession of public service not primarily because law had made it such but because a public opinion shared in by businessmen themselves has brought about a professional attitude” (p.1153). In the early 1950s, the writings of Frank Abrams (1951) and Howard R. Bowen (1953) were critical in legitimising ‘corporate social responsibility’ (CSR) as a distinct field of study. According to Abrams, businessmen, like all other professionals have “a duty to conduct the affairs of the enterprise to maintain an equitable and workable balance among the claims of the various directly interested groups, a harmonious balance among stockholders, employees, customers and the public at large”.³ In his book titled *Social Responsibilities of the Businessman* (1953), Bowen referred to the responsibility of businessmen to pursue those policies, decisions and actions that are desirable in terms of the social objectives and values.⁴ CSR became a hot topic of discussion during the decade that ensued – “a deadly serious occupation”, to quote Levitt (1958) - among intellectuals, business leaders and political elite alike.

The harshest critique of the reformers’ preoccupation with social responsibility in the 1950s can be seen in the essay published in 1958 by Theodore Levitt, *The Dangers of Social Responsibility*, where he argued that “the function of business is to produce sustained high level profits” (Levitt, 1958: 44). He apprehended that if corporations

buckled under the pressure of reformers to commit themselves to the 'new orthodoxy' of doing social good they will eventually assume a monolithic influence which is completely against the spirit of capitalism that can thrive only in pluralistic societies with political democracy and personal freedom. In such societies there is a separation of everyday functions in the realms of economical, political, social and spiritual. "In the end", he wrote, "business has only two responsibilities – to obey the elementary canons of everyday face to face civility (honesty, good health, and so on) and to seek material gain" (p. 49).

The primacy of the shareholder was the basic building block of the utilitarian ethics and is most vociferously represented by Milton Friedman. In his essay, *The Social Responsibility of Business is to Increase its Profits* published in 1970 Friedman opposed any form of moral responsibility of business entities towards society. Regarding the role of corporate executives he stated that in a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business, an agent serving the interests of his principal. His direct responsibility is to his employers and 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". Private competitive enterprise has great virtue in that '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. This position indeed reflects some of the classical political economy notions about business social responsibility. In an engaging essay titled, *Smith vs Marx on Business Morality and the Social Interest* William J. Baumol (1986) says that Adam Smith had a strong distrust for businessmen and their commitment to social responsibility. Social good cannot be achieved by depending on anybody's good intentions. The market mechanism governed by the doctrine of self interest is the best way to make human beings work in the service of general welfare.

For Friedman, corporate establishments as opposed to the public and political state are private apolitical actors. The doctrine of social responsibility, according to him, 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. In his book *Capitalism and Freedom* published in 1962 Friedman had called corporate social responsibility a ‘fundamentally subversive doctrine’ in a free society. He argued: 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 (Friedman, 1970). He contests the view that corporations have to submit their decisions to public scrutiny. They do not need to so long as they are governed by the legal and moral framework of the state. Private actions are legitimised by the results they create and the self interested market transactions of the corporate establishments do contribute to social wellbeing.⁵ According to Friedman social responsibility is one way for a corporation to generate goodwill ‘as a by-product of expenditures that are entirely justified on its own self-interest’. He urged corporate executives to refrain from this ‘hypocritical window-dressing’ because it harms the foundation of a free society.

Expectedly, discussion on business ethics and social responsibility is irrelevant in the Marxist scheme of thought, the ideological opposite of the liberal free market thinking. Baumol (1986) argues that Marx being a historical materialist was not concerned with the personal morality of the capitalist. For him, capitalist is the product of historical process. “...the capitalist did evil deeds not because he was born or raised to be a moral cripple but because the natural circumstances left him no choice” (p.4). Also, as Shaw (2009) points out, excessive focus on the morality of individual units thwarts attention from the systemic vices of capitalism. What is relevant is critique and eventual overthrow of capitalism and its replacement with a totally different and better socio-economic order.

Even within positions that strongly endorse the need for corporates to be responsible, there exist distinctly different logical streams. One line of thinking is informed by the economic theory of the firm and values social responsibility for the economic returns that

it may yield. Thus, the virtue of social responsibility is that it increases the long term value of the firm or improves its economic performance. It has an instrumental value in that it enhances the legitimacy of the firm among the stakeholders to develop a positive image (Morimoto, Ash and Hope, 2004) and serves as a success factor. Hence, the social responsibility objectives of business firms are invariably shaped by the expected economic results of business firms (Laczniak and Murphy, 1993).

The prescriptive conceptions of social responsibility, as we discussed earlier, are concerned with what corporates ought to do and what they ought not. They emphasise on the ethical sensitivity of management and seek to examine, justify and improve the moral quality of business behaviour even when there are no pressures from external power groups. Businesses must follow ethical behaviour and governance of organisations (respecting basic human rights, reducing environmental pollution/ degradation, reducing gender gap, promoting decent work standards). Exclusive focus on shareholder value is looked is both ‘morally wrong and socially damaging’.

As noted earlier, the question seeking normative justification for the existence of business evolved through the years in consonance with the changes that came about in the very form and nature of business. At the time when Dodd wrote, many of the enterprises were owned by absentee investors who were indifferent to the way business was conducted; their singular interest was dividend. For Dodd it was hardly thinkable to imbue these stockholders with a spirit of public service. Three decades and two World Wars later, the business scenario was markedly different in the developed part of the world. In the face of declining demand, shrinking margins, rising competition and increasing concentration of ownership in the hands of financial institutions (through the mediation of capital markets), managerial performance came under close scrutiny in the 1980s and 1990s. There was widespread restructuring of business enterprises in the US and Europe with a view to enhance returns to investment. As Owen observed, by that time, managerial capitalism had given way to investment capitalism.⁶ Shareholder interests came to assume primacy in corporate economics, which has not only changed the rules of the game in the conduct of business, but has also brought newer ethical concerns to the fore.

The Discursive Approach to Social Responsibility

It is evident that the dominant interpretations of business social responsibility are all positioned within the realm of the economic. While the virtues of a liberal democracy are celebrated as most necessary for the successful functioning of business, the major functions of society are assumed to be mutually exclusive. The operational sphere of business is understood as completely apolitical and asocial. Or, as Sherer and Palazzo (2008) argue, the political framework of rules and regulations is taken as efficient and well functioning. The contemporary phase of capitalist development, however, has negated many of these conventional notions as the boundaries of the exclusive fields of human activity have been blurred or their sphere of influence changed or eroded. For instance, globalisation has meant expansion of businesses trans borders and beyond the regulatory scope of individual nations (*Ibid*). The current phase of capitalist expansion also has given rise to new actors, institutions and forms of governance that defy a monotonic interpretation of the role of business in society.

A broader idea of business social responsibility that addresses some of the complex interrelationships between business, society and polity is presented in Sherer and Palazzo (2007 and 2008). They base their idea on Jurgen Habermas' conception of 'deliberative democracy', rooted strongly in the belief in the primacy of democracy to philosophy. Its advantage over the utopian approaches to business social responsibility is that it accommodates both ethical discourse and economic bargaining as it views economic rationality as being circumscribed by democratic institutions and procedures. With businesses and markets going global, there is a definite need to 'domesticate economic pressures by democratic control' and to find new actors who can assume the responsibility of governance along with the traditional nation state. Firms can assume this political role as and when necessary by 'authoring rules with public impact'. The discursive approach that Sherer and Palazzo propose suggests the criticality of discourse - the process of deliberation and argumentation - among the stakeholders in order to critique and justify social claims and interests, and forming ethical strategies. The

legitimacy and credibility of business action is enhanced in a discursive model as it is open to public scrutiny and debate.

Social Responsibility and Social Performance

Does commitment to be responsible to society result in desirable outcomes to the business entity? How do businesses translate their noble intentions to functional processes? What guidelines do they use to address and manage social issues? The concept of corporate social performance (CSP) is seen as the integrative approach to look at these questions by exploring the underlying interaction among three dimensions - principles (CSR responsibilities - philosophical orientation), processes (Corporate social responsiveness - institutional orientation) and policies (Social Issues Management – organizational orientation) (Wartick and Cochran 1985).

Wood (1991) tried to advance Wartick and Cochran's definition thus: "a business organization's configuration of principles of social responsibility, processes of social responsiveness, and policies, programs, and observable outcomes as they relate to the firm's societal relationships" (p.693). Wood argues that in CSP one needs to examine:

1. the degree to which principles of social responsibility motivate actions taken on behalf of the company (assumes that principles motivate actions);
2. the degree to which the firm makes use of socially responsive processes (specific responsive processes are environmental assessment, stakeholder management and issue management); and
3. the existence and nature of policies and programs designed to manage the firm's societal relationships, and the social impacts (i.e., observable outcomes) of the firm's actions, programs, and policies.

Also, principles, processes, and outcomes are to be examined "in conjunction with each other to permit identification of analytically crucial but politically difficult results such as good outcomes from bad motives, bad outcomes from good motives, good motives but poor translation via processes, good process use but bad motives..."(p.693).

Though CSP has been put forward as solution to the problem of an analytical disconnection between social responsibility and social responsiveness, its ability to do so has been questioned by scholars. The critics point out that CSP models are the best illustrations of the utilitarian view of management. As Sherer and Palazzo (2007) maintain, “Their implicit goal is to produce technical knowledge about how organisations work and how their survival in a competitive environment can be achieved” (p.8). By their very logic, SP models accept the status quo without striving to criticize or justify the norms that govern corporate strategies and thus may promote ‘morality of the mighty’.

Section 2

Social Responsibility and Stakeholder Discourse

The central question is who should businesses be responsible to? As Jones (1980) asks, if corporations have an obligation to groups in society other than stockholders or owners and beyond that prescribed by law or union contract, “What are these groups? How many of these groups must be served? Which of their interests are most important? How can their interests be balanced? How much corporate money should be allotted to serve these interests?” (pp. 59-60). As we have seen earlier, the justifications for endorsing social responsibility orientation of business straddle extremes. Positions as boundless as addressing social justice and equity render the desired field of action for businesses so wide that the fundamental purpose of business existence stands diluted. Too focused and narrow interpretations like that of shareholder primacy create an illusion of a very limited sphere of influence of businesses.

Western stakeholder theorists have made significant contribution towards unpacking – if not completely resolving - the above dilemma by helping in the identification of certain classes of entities as stakeholders.⁷ However, they differ considerably on the issue of taking a broad or narrow view of a firm’s stakeholder universe. A rather broad definition of stakeholder was provided by Edward Freeman, according to whom stakeholder is “any group or individual who can affect or is affected by the achievement of the organisation’s

objectives”.⁸ While tracing the history of the term, Freeman argues that the concept was originally defined as ‘those groups without whose support the organisation would cease to exist’. Such groups could include shareholders, consumers, users, neighbours, governments, suppliers, creditors, and distributors.⁹ Donaldson and Dunfee (1999) proffered a more pragmatic explanation of who a stakeholder is: one who has an ‘obligation-generating stake’ in an organization’s decision that results from the possibility of getting affected by that decision or from a potential risk. The concepts of stake (including non-financial stake) and risk help one focus sharply on those entities with legitimate claims, irrespective of their power to influence the firm. The theories of stakeholding emphasise the complexity of transactions that involve multitude of factors.

The theoretical positions that assume a pluralistic view – the view that emphasizes broader constituencies of corporations - are in conflict with the monotonic view that ‘shareholders claim the corporation’s heart’.¹⁰ For those who believe in the primacy of shareholders, focus on extra-shareholder interests reflects “inappropriate social and political considerations” (Dunfee, 1999: 130). These considerations are incompatible with the substantive business objective as they undermine private property and the possibility of maximizing values to particular groups as also reject the objective of long term owner value (Sternberg, 1999). Also, by implying accountability to multiple masters the pluralistic theories complicate the functioning of corporate governance system.

An issue of central concern to the social responsibility debate is whether organizations pursue the satisfaction of stakeholder interests for economic reasons or simply because doing so has intrinsic merit. As Donaldson and Preston (1995) would put it, the former reflects an ‘instrumental approach’ (‘certain outcomes are more likely if firms/managers behave in certain ways’) to stakeholder management and the latter, a normative approach (‘firms/managers ought to behave in certain ways’). Obviously, business entities that behave as opportunists do not acknowledge the intrinsic reason for being socially responsible. An unfortunate fall out of this may be that powerless stakeholders are shunted aside to make way for the ‘morality of the mighty’ (Freeman and Gilbert, 1988).

Deciding Stakeholder Salience: A Managerial Challenge

Given the diversity in the stakeholder universe, how do managers achieve a fair balance between the needs and concerns of these diverse stakeholders? Is there a way to identify salient and legitimate stakeholders? An interesting attempt to answer these questions came from Mitchell, Agle and Wood in the form of a conceptual scheme to classify stakeholder on the basis certain crucial attributes. They presented an exhaustive list of stakeholder classes while trying to model stakeholder identification and salience, like owners and non owners of the firm; owners of capital or owners of less tangible assets; actors or those acted upon; those existing in a voluntary or an involuntary relationship with the firm; rights-holders, contractors, or moral claimants; resource providers to or dependents of the firm; risk-takers or influencers; and legal principals to whom agent-managers bear a fiduciary duty. According to the scheme, there are three attributes by which classes of stakeholders can be identified. The attributes are: i) power (to influence the firm decisions); ii) legitimacy (of relationship with the firm); and (iii) urgency (of claims on the firm). The authors argued that based on the possession, or the attributed possession, of one, two, or all three of the attributes the various classes of stakeholders might be identified.

Seven stakeholder types emerged from the various combinations of the attributes - three possessing only one attribute, three possessing two attributes, and one possessing all three attributes. These are classified under three broad categories – dormant, expectant and definitive (Exhibit 1). In Exhibit 1 we have tried to depict the typology.

Exhibit 1: Stakeholder types by attributes

Class	Type	Attribute	Ability to demand attention
Latent Stakeholders	Dormant	Power	No or little interaction
	Discretionary	Legitimacy	Managers are not encouraged to interact
	Demanding	Urgency	Irksome, but do not warrant attention of management
Expectant Stakeholders	Dominant	Power and Legitimacy	Expect and receive attention, but not the full attention of managements
	Dependent	Urgency and Legitimacy	Support of other stakeholders or guidance by internal management's value needed
	Dangerous	Urgency and Power	Potential risks to stakeholder-manager relationship; to individuals and entities involved
Definitive Stakeholders	Definitive	Power, Legitimacy and Urgency	Managers have clear and immediate mandate to attend to their claims; expectant stakeholder can move to become definitive stakeholder; common occurrence is movement from dominant stakeholder to definitive stakeholder category

Source: Mitchell, Agle and Wood (1997).

The classification can help firms identify the entities that should be considered stakeholders from which managers can select the ones that they perceive as salient. Entities with none of the three attributes in relation to the firm cannot be seen as stakeholders and, hence, the management cannot ascribe any salience to them. The major

limitation of the model is that the identification of stakeholders depends decisively on managerial perception.

Identifying salient stakeholders is the first step towards the complex process of building ethical business strategies by incorporating their concerns and priorities. Social contract theory offers a valuable framework to conceptualise and operationalise a deliberative process for strategisation. We will elaborate this in the following section.

Section 3

Social Contract: A Framework to Create Moral Communities of Stakeholders

The theory of social contract originated in Europe and evolved through the 17th and 18th centuries as part of the intellectual pursuit of political theorists like Thomas Hobbes, John Locke and Jean Jacques Rousseau to find a philosophy that legitimizes the role of government and the authority of the state. For Hobbes the social contract helps men avoid the undesirable consequences of the State of Nature like distrust and destruction. According to him, social contract is a set of laws by which all agree to abide and an enforcement mechanism for these laws. For John Locke, who imagined the State of Nature as having certain inconveniences, but not as harsh or cruel, social contract is a set of mutually satisfactory rules that serves as a mechanism for assuring the welfare of individuals (Snyder et.al., 2006). He maintained that citizens' cooperation and consent to legal authority is the basis for their adherence to law. The social contract that he propounded is an expression of the reciprocal obligations of citizens and state (Dunfee, Smith and Ross, 1999). Enforcement did not figure in his theory as he believed that reason and not coercion is at the base of social cooperation.

A strong advocate of the values of liberty, equality and fraternity, Rousseau's idea of social contract involves people recognizing a collective 'general will' that represents the common good or public interest to which all citizens should be committed irrespective of what their personal interests are. Rousseau has elaborated the term social contract thus:

“Each one of us places in common his person and all his powers under the supreme direction of the general will; and we receive back as a corporate body, each member, as an indivisible part of the whole” (Singh, 2006: p.13). According to this conceptualization, ‘a people is a group who have made a contract of a special kind that has both changed their natures and individual personalities and created out of their isolated natural selves, a collective agency capable of both embodying and legislating over their individual wills’. Rousseau insisted that the social contract is not a permanent phenomenon. It needs continuous reaffirmation by the citizens.

Social contract theory has been applied to business by scholars like Thomas Donaldson and Thomas Dunfee. The social contracts, according to Donaldson and Dunfee, are informal, implicit, but critical agreements that exist within industries, national economies, trade groups and corporations and that bind these into moral communities (Donaldson and Dunfee, 1999). Donaldson, considered a pioneer in this respect, argues that the modern social contract grants protection to corporations in return for being efficient producers of goods and services and not for abusing those who provide them with these rights including customers and employees. He questions the conventional wisdom that ‘shareholder wealth maximization is the great good for business’ (Fort and Noone, 1999). Corporate legitimacy, according to Donaldson, is established only through the cooperation and commitment of society articulated through an agreement between the two. “If General Motors holds society responsible for providing the condition of its existence, then for what does society hold General Motors Responsible? What are the terms of the social contract?”.¹¹ Social contract theory is thus used by Donaldson to ascertain that the business corporations have a moral foundation. While resolving business dilemmas, productive organisations are bound to follow minimum standards of justice like avoidance of fraud and deception, respect for workers as human beings, avoidance of any practice that systematically worsens the situation of a given group in society.

Dunfee, on his part, emphasizes upon the extant social contracts while arguing that the actual legal contracts enacted by specific communities serve as the basis for moral rules.

He argues that “The shareholder primacy norm, if fully incorporated into the legal regime, would still require that stakeholder interests be considered when doing so has a foreseeable impact upon shareholder wealth” (Dunfee, 2000: p.135). The corporate constituency statutes enacted by many of the American states since the early 1980s are seen as having limited impact on the stakeholder constituency as they do not have a mandate to consider stakeholder interests. Dunfee contests this view and maintains that “corporate law allows management to act in furtherance to many types of interests other than pure short-term shareholder wealth maximization” (*ibid*: p. 136-7).

Combining the empirical studies of business behaviour and the normative evaluation of it Donaldson and Dunfee proposed a new social contract theory - the Integrated Social Contract Theory (ISCT) - in the early 1990s. This theory is based on the idea that the rules of behaviour within communities are founded on social norms. In this model community is defined as a “self-defined, self circumscribed group of people who interact in the context of shared tasks, values, or goals and who are capable of establishing norms of ethical behaviour for themselves” (p.262). The ISCT encompasses two types of social contracts: (i) a normative, hypothetical macrosocial contract used as a heuristic device; and (ii) multitude of actual microsocial contracts found in various living communities (Dunfee, Smith and Ross, 1999). The ISCT strives to define social contract as an agreement that ‘overcomes bounded moral rationality’ and provides a moral framework for economic activity while reflecting the diverse personal precepts of the contractors (Donaldson and Dunfee, 1994 and 2000). Bounded moral rationality, an extension of concept to bounded economic rationality, posits that moral agents are constrained in terms of “information, time, and emotional strength to make perfect judgements consistent with their moral preferences” (Dunfee, Smith and Ross, 1999: p.18). The limitations of bounded morality and the particularities of personal circumstances can be circumvent through a macrosocial contract.

The terms of the macrosocial contract put forward by Donaldson and Dunfee can be elaborated thus:

- Local economic communities have ‘moral free space’ in which they may generate ethical norms for their members through microsocial contracts.

The term ‘moral free space’ is used to denote the right of the local communities to define the critical aspects of their morality. It reflects the enormous variety in cultural, religious and moral preferences among individuals and communities and provides an ethical justification for diversity.

- Norm generating microsocial contracts must be grounded in consent, buttressed by the rights of individual members to exercise voice and exit.¹²

This clause suggests that there are limits to moral relativism as implied by the term ‘moral free space’. While communities have differing norms within the moral free space they may generate ‘authentic norms’ or the norms to which members have consented in a real and informed way (Fort and Noone, 1999). The consent, however, also means that the community respects the right of its members to exit and raise voice. In sum, a norm supported by the attitudes and behaviours of a substantial majority of community members who recognise the right to voice and exit becomes an authentic norm.

- In order to become obligatory or legitimate, a macrosocial contract norm must be compatible with hyper norms.

Hypernorms are the universal principles that limit the moral free space and bound the authentic norms. They are fundamental principles that are used to judge the community generated norms. Three types of hypernorms are identified by Donaldson and Dunfee: structural, procedural and substantive. Structural hypernorms are principles that establish and support essential background institutions in society (e.g., to honour institutions that promote justice and economic welfare). Conditions that support consent in macrosocial contracts are called procedural hypernorms (e.g., rights to voice and exit). Substantive social norms consist of fundamental concepts of the right and the good (promise keeping, respect for humanity).

A social contract among all the salient stakeholders of the organisation plays a very strategic role in the day to day running of the firm as also in achieving its long term goals. It is relevant here to reiterate Sacconi's (2004) elaboration on the need for social contract. Firstly, it serves as a touch stone to review and assess the outcomes of the day to day functioning of the organisation. Secondly, a typical social contract ensures avoidance of force, fraud and manipulation. Thirdly, it allows each party to negotiate on the basis of its capacity to contribute and its assessment of the utility of each agreement/non agreement. Fourthly, it makes sure that each stakeholder derives from the social contract at least the reimbursement of the cost of specific investment that it makes towards surplus generation. The overarching significance of trust must be emphasised in evolving and operationalising social contract, which can serve as an instrument to regulate surplus distribution and, given the rigidities in information flow, act as a tool to match organisational commitments and stakeholder expectations.

In the process that leads to the structuring and formulation of social contract, it is not enough that the stakeholders are consulted. A multistage deliberative process is required to generate impartially acceptable agreements. It must be ensured that stakeholders with different power and resources participate in a discourse that is inclusive, democratic and free of power asymmetries.¹⁴ What is to be emphasised is that the ethical validity of the final agreement depends as much on the process as on the outcome.

Conclusion

In this paper we have revisited the issue of business social responsibility with a view to reiterate its significant relevance in the contemporary scenario characterised by an overarching presence of private businesses and blurring of the conventional barriers between not-for-profit and for-profit enterprises. We have reviewed the evolution of major theoretical positions and ideological interpretations of business social responsibility to demonstrate how the basic understanding of the term traversed through time and alongside changes in forms of business organisation and interpretations of the underlying morality of private property. Thus one encounters extreme ideological

positions – ‘subverting freedom’ to ‘subserving greed’- with respect to social responsibility of businesses. We have specifically drawn on the theoretical streams relating to stakeholding and social contract to underscore the moral and social responsibility of businesses to broaden their vision beyond maximising profit and stakeholder value to address the interests and claims of non-shareholding stakeholders.

We argued that focussing exclusively on shareholder value may bring about morally wrong and socially damaging consequences. Most importantly, the dynamic and discursive nature of business-society interrelationship warrants an ongoing discourse – a process of deliberation and argumentation - among the multiple stakeholders who hold salience to the business entity to critique and justify the claims and interests of different moral communities. Social contract provides a meaningful mechanism to facilitate such a discourse by binding the salient stakeholders into moral communities. Moreover, a discursive model of business social responsibility enhances the legitimacy and credibility of business action as it is open to public scrutiny and debate.

REFERENCES

- Baumol, William J., 1976. Smith vs. Marx on Business Morality and the Social Interest. *American Economist*, 20 (2), Fall, 1-6.
- Bobo, Lawrence, 1991. Social Responsibility, Individualism and Redistributive Policies. *Sociological Forum*, 6 (1), 71-92.
- Dantwala, M.L., 1985. Trusteeship: Its Value Implications. *Gandhi Marg*, November-December, 504-08.
- Dodd, Merrick E., Jr., 1932. For Whom are Corporate Managers Trustees?. *Harvard Law Review*, XLV (7), 1145-1163.
- Donaldson, Thomas, & Lee E. Preston, 1995. The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications. *Academy of Management Review*, 20 (1), 65-91.
- Donaldson, Thomas, & Thomas W. Dunfee, 1994. Toward a Unified Conception of Business Ethics: Integrative Social Contracts Theory. *The Academy of Management Review*, 19 (2), 252-84.
- Donaldson, Thomas, & Thomas W. Dunfee, 2000. Ties that Bind: a Social Contracts Approach to Business Ethics, Boston, MA: Harvard Business School Press.
- Dunfee, Thomas W., 1999. Corporate Governance in a Market with Morality. *Law and Contemporary Problems*, 62 (3), Summer, 129-157.
- Dunfee, Thomas W., N. Craig Smith, & William T. Ross, Jr., 1999. Social Contracts and Marketing Ethics. *The Journal of Marketing*, 63 (3) July, 14-32.

- Fort, Timothy L., & James J. Noone, 1999. Banded Contracts, Mediating Institutions, and Corporate Governance: A Naturalist Analysis of Contractual Theories of The Firm. *Law and Contemporary Problems* 62 (3), Summer: 163-213.
- Frederick, William Crittender, 2006. *Corporation, Be Good! The Story of Corporate Social Responsibility*, Indianapolis: Dog Ear Publishing.
- Freeman, R. Edward, & D.R. Gilbert, 1988. *Corporate Strategy and the Search for Ethics*, New Jersey: Prentice- Hall.
- Freeman, R. Edward, & John McVea, 2001. A Stakeholder Approach to Strategic Management. *Working Paper No. 01-02*. University of Virginia. Retrieved from http://papers.ssrn.com/paper.taf?abstract_id=263511.
- Friedman, Milton, 1970. The Social Responsibility of Business is to Increase its Profits. *The New York Times Magazine*. September 13. Retrieved from <http://www.ethicsinbusiness.net/>
- Henderson, David, 2001. *Misguided Virtue: False Notions of Corporate Social Responsibility*, The Institute of Economic Affairs, London.
- Jones, Thomas M., 1980. Corporate Social Responsibility Revisited, Redefined. *California Management Review*, 22 (3), 59–67.
- Laczniak, Gene R., & Patrick E. Murphy, 1993. *Ethical Marketing Decisions: The Higher Road*. Needham Heights, MA: Allyn and Bacon.
- Levitt, Theodore, 1958. The Dangers of Social Responsibility. *Harvard Business Review*, September-October.

- Mitchell, Ronald K., Bradley R. Agle, & Dona J. Wood, 1997. Toward a Theory of Stakeholder Identification and Salience: Defining the Principles of Who and What Really Counts. *The Academy of Management Review*, 22 (4), October, 853-86.
- Morimoto, R., J. Ash, & C. Hope, 2004. Corporate Social Responsibility Audit: From Theory to Practice. *WP 14, Research Papers in Management Studies*. The Judge Institute of Management, University of Cambridge.
- Reynolds, MaryAnn, & Kristi Yuthas, 2008. Moral Discourse and Corporate Social Responsibility Reporting. *Journal of Business Ethics*, 78, pp. 47-64.
- Sacconi, Lorenzo, 2004. Corporate Social Responsibility (CSR) as a Model of “Extended” Corporate Governance: An Explanation Based on The Economic Theories of Social Contract, Reputation and Reciprocal Conformism. *Liuc Papers n. 142, Serie Etica, Diritto ed Economia 10, suppl. a febbraio*. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=514522.
- Sethi, J. D., 1985. Trusteeship and the Crisis in Economic Theory. *Gandhi Marg* November-December, 540-59.
- Shaw, William H., 2009. Marxism, Business Ethics, and Corporate Social Responsibility. *Journal of Business Ethics* 84, 565–576.
- Sherer, Andreas Georg, & Guido Palazzo, 2007. Toward a Political Conception of Corporate Responsibility: Business and Society Seen from a Habermasian Perspective. *The Academy of Management Review*, 32 (4), 1096-1120.
- Sherer, Andreas Georg, & Guido Palazzo, 2008. Globalization and Corporate Social Responsibility. In A. Crane, A. McWilliams, D. Matten, J. Moon and D. Siegel

- (Eds.), *Oxford Handbook of Corporate Social Responsibility* (413-31). New York: Oxford University Press.
- Singh, N.K. (ed.), 2006. *Jean Jacques Rousseau, Of the Social Contract of Principles of Political Right*. New Delhi: Global Vision Publishing House.
- Snyder, Johnny, Don Carpenter, & Gayla Jo Slauson, 2006. MySpace.com: A Social Networking Site and Social Contract Theory. *Proc ISECON* 2006, 23. Retrieved from <http://proc.isecon.org/2006/3333/ISECON.2006.Snyder.pdf>.
- Sternberg, Elaine, 1999. The Stakeholder Concept: a Mistaken Doctrine. *Issue Paper No.4*, London, Foundation for Business Responsibilities, November.
- Wartick, Steven L., & Philip L. Cochran, 1985. The Evolution of the Corporate Social Performance Model. *The Academy of Management Review*, 10 (4), October, 758-69.

FOOTNOTES

1. McWilliams and Siegel (2001) define social responsibility of corporates as “actions that appear to further some social good, beyond the interests of the firm and that which is required by law”. In other words, social responsibility equires corporates to go beyond abiding by what the law prescribes. They elaborate this pointing out that when a company “avoids discriminating against women and minorities, it is not engaging in a socially responsible act; it is merely abiding by the law” (p.117).
2. Coincidentally, almost around the same time, at the other end of the world, deeply entrenched within the freedom movement of India, M.K. Gandhi was trying to give shape to his idea of ‘trusteeship’. But he had a rather wider view of the social role of the ‘owners of wealth’. His concept of ‘trusteeship’ “provides a means of transforming the capitalist order into an egalitarian one” by giving the owning class a chance to ‘reform’. It does not recognise any right of private ownership of property except so far as it may be permitted by society for its own welfare. Under the economic order that underlies the working of this concept, the character of production will be determined by social necessity and not by personal whim or greed (Dantwala, 1985). Trusteeship is interpreted as a theory of need-based production, equitable distribution and social justice (Sethi, 1985).
3. Quoted in Frederick (2006), p.7.
4. Howard R. Bowen, quoted in Wartick and Cochran (1985).
5. Milton Friedman and Fabienne Peter as discussed in Sherer and Palazzo (2007).

6. Sir Geoffrey Owen, in his forward to Henderson's monograph on CSR (2001).
7. Having originated in the mid 1980s with the publication of Edward Freeman's work, *The Strategic Management: A Stakeholder Approach*, stakeholder theory has evolved into an integral part of strategic management. For an interesting discussion on the evolution of stakeholder theories, see, Freeman and Mc Vea (2001).
8. Quoted in Sternberg, 1999: p.46.
9. Some of the broad definitions of stakeholders are provided by Alkhafaji ("groups to whom the corporation is responsible") and Thompson Wartick and Smith (groups "in relationship with an organisation"). See, Mitchell, Agle and Wood (1997) for details.
10. Gordon Smith, as quoted in Dunfee (1999).
11. Donaldson (1982), quoted in Dunfee, Smith and Ross (1999): p.17.
12. Dunfee, Smith and Ross (1999) use the term 'protected informed consent' to denote this.
13. To borrow the terminology of Reynolds and Yuthas (2008).