

Chapter One



The Study of Business, Government, and Society

Exxon Mobil Corporation

ExxonMobil is the largest publicly traded international oil company. Although it is headquartered in Irving, Texas, and most people regard it as an American company, 69 percent of its sales, which were \$366 billion in 2006, are in more than 200 other countries.¹ Its main business is discovering, producing, and selling oil and natural gas, and it has a long record of profiting more at this business than its rivals.

ExxonMobil cannot be well understood apart from its history. It descends from the Standard Oil Trust, incorporated in 1882 by John D. Rockefeller as Standard Oil of New Jersey. Rockefeller was a brilliant strategist and organizer who crushed competitors. He believed that the end of imposing order on a youthful, rowdy oil industry justified the use of ruthless means. As Standard Oil grew, Rockefeller's values defined the company's culture; that is, the shared assumptions, both spoken and unspoken, that animate its employees. If the values of a founder such as Rockefeller are effective, they become embedded over time in the organization. Once widely shared, they tend to be exceptionally long-lived and stable.² Rockefeller emphasized cost control, efficiency, centralized organization, and suppression of competitors. And no set of principles was ever more triumphant. Standard Oil once had more than 90 percent of the American oil market.

Standard Oil's power so offended public values that in 1890 Congress passed the Sherman Antitrust Act to outlaw its monopoly. In 1911, after years of legal battles, the trust was finally broken into 39 separate companies. After the breakup, Standard Oil of New Jersey continued to exist. Although it had shed 57 percent of its assets to create the new firms, it was still the world's largest oil company. Some companies formed in the

¹ Figures in this paragraph are from Exxon Mobil Corporation, Form 10-K 2006, filed with the Securities and Exchange Commission, February 28, 2007.

² See, for example, Edgar H. Schein, *The Corporate Culture Survival Guide* (San Francisco: Jossey-Bass, 1999), part one.

breakup were Standard Oil of Indiana (which was later renamed Amoco), Atlantic Refining (ARCO), Standard Oil of California (Chevron), Continental Oil (Conoco), Standard Oil of Ohio (Sohio), Chesebrough-Ponds (a company that made petroleum jelly), and Standard Oil of New York (Mobil). In 1972 Standard Oil of New Jersey changed its name to Exxon, and in 1999 it merged with Mobil, to form ExxonMobil.

Rockefeller's influence is buried in the passage of time, but ExxonMobil's actions remain consistent with his nature. It has a centralized and authoritarian culture. Cost control, capital productivity, and strict financial controls are emphasized in operations. Profit is an overriding goal, and projects must meet strict criteria for return on investment. Unlike Southwest Airlines or Google, where having fun is part of the job, performance pressure at ExxonMobil is so intense that it "is not a fun place to work."³ Over many years it has consistently bettered industry rivals in its favorite measure, return on average capital employed, just like the old Standard Oil Trust. And competitors still find it a ferocious adversary. The company says simply that it "employs all methods of competition which are lawful and appropriate."⁴

ExxonMobil is a massive organizational force, shaping international markets, pushing against competitors, and influencing governments. However, today it exists in a more difficult environment than did Rockefeller's dominating trust. As in the old days, its power is contested and limited by the interplay of economic, political, and social forces. Only now those forces are more leveling.

Markets are more contested. ExxonMobil pumps only 8 percent of the world's daily output of oil and controls less than 1 percent of petroleum reserves. These figures are far lower than in the 1950s when Exxon was the largest of the Seven Sisters, a group of Western oil firms that dominated worldwide production and reserves, including the huge Middle East oil fields.⁵ Now its largest competitors are seven state-owned oil companies, often called the "new Seven Sisters," whose output dwarfs that of yesteryear's titans.⁶ The biggest, Saudi Aramco, is 3.5 times the size of ExxonMobil in daily output and has 32 percent of world reserves.⁷

The rise of these state-owned oil companies reflects a new resource nationalism in developing nations that want to recapture oil profits from foreign firms. Climbing crude oil prices since the late 1990s have made oil reserves more valuable, leading many countries to take over oil fields. This happened to ExxonMobil in Venezuela. It lost 2 percent of daily production in 2007 when the government seized projects valued at \$4.5 billion.⁸

ExxonMobil is on a treadmill, constantly searching for new oil and natural gas supplies to compensate for declining production in existing fields. Output from a mature

³ Fadel Gheit, a former employee and leading oil industry analyst, quoted in Geoff Colvin, "The Defiant One," *Fortune*, April 30, 2007, p. 88.

⁴ See, for example, Exxon Mobil Corporation, Form 10-K 2006, p. 2.

⁵ The Seven Sisters were Exxon, Mobil, Shell, British Petroleum, Gulf, Texaco, and Chevron.

⁶ These new "seven sisters" are Saudi Aramco (Saudi Arabia), Gazprom (Russia), China National Petroleum Company (China), National Iranian Oil Company (Iran), Petróleos de Venezuela S.A. (Venezuela), Petrobras (Brazil), and Petronas (Malaysia).

⁷ Government Accountability Office, *Crude Oil*, GAO-07-283, February 2007, fig. 9.

⁸ Chris Kraul, "Exxon, Conoco Drop Venezuela Oil Projects," *Los Angeles Times*, June 27, 2007, p. C3.

field drops 5 to 8 percent a year. To maintain profitability the company pursues new reserves wherever they are located, taking political risks and abiding unrest and corruption. In Iran and Venezuela ExxonMobil's assets were appropriated. In Chad, Angola, Nigeria, and Equatorial Guinea, it paid dictators for access to oil. Indonesian troops guard its facilities against attacks by rebel forces.⁹

Governments are more powerful and relations with them more complex than in the past. ExxonMobil's operations are restricted by the laws and regulations of each country in which it does business. In the United States alone approximately 200 federal agencies and bureaus impose rules and standards on the company. Only a handful of these existed in Rockefeller's day. In foreign countries ExxonMobil faces import and export restrictions, production taxes, price controls, and regulations to protect nature. In 2006 it supported governments by paying \$101 billion in taxes worldwide, a sum exceeding the combined revenues of Dell and Microsoft.

ExxonMobil also faces a demanding social environment. As a leader in the world's largest industry, it is closely watched by environmental, civil rights, labor, and consumer groups—some of which are actively hostile. For years the company has agitated environmentalists by rejecting the scientific case for global warming. Alone among major oil companies, it refuses to make significant investments in renewable energy sources such as ethanol, solar, wind, or tidal. A former CEO called such investments “a complete waste of money.”¹⁰ Energy from renewables is more expensive to produce than energy from oil, gas, and coal, which will be the dominant sources of energy far into the future. Therefore, ExxonMobil shuns renewables, which lack promise of satisfying its lofty return on capital standards.

ExxonMobil got a good public caning because for years it funded the research of groups that denied global warming. In 2006 Britain's scientific academy, the Royal Society, took the unprecedented step of writing to the company's management, asking that it stop “misinforming the public.”¹¹ Then two senators, Olympia Snowe (R-ME) and John Rockefeller IV (D-WV), the great grandson of the company's founder, sent a letter to the CEO and members of its board of directors. They asked that ExxonMobil end its “climate change denial strategy” because it was adversely affecting the credibility of the United States in the international community.¹²

Such pressure led CEO Rex Tillerson to grant publicly that the world is warming. But he did not make any notable strategic changes.¹³ His reversal of belief failed to satisfy critics, especially ExxposeExxon, a coalition of environmental groups that opposes the company's policies. The coalition includes Defenders of Wildlife,

⁹ The company faces murder charges brought by villagers who claim it was complicit when government troops attacked area natives sympathetic to the rebels. See *Doe v. Exxon Mobil Corp.*, 473 F.3d 345 (2007).

¹⁰ Lee Raymond, quoted in “The Unrepentant Oilman,” *The Economist*, March 15, 2003, p. 64.

¹¹ David Adam, “Scientists Attack Climate Change Denial,” *The Guardian Weekly*, September 29, 2006, p. 14.

¹² Quoted in Steven Mufson, “At Exxon Meeting, a Storm Outside but Calm Within,” *Washington Post*, May 31, 2007, p. D2.

¹³ Jeffrey Ball, “Exxon Softens Climate-Change Stance,” *The Wall Street Journal*, January 11, 2007, p. A2.

Greenpeace, the Natural Resources Defense Council, the Sierra Club, and the Union of Concerned Scientists. This league of greens continues to hound the oil giant. Its banner outside the firm's 2007 shareholder's meeting read "No Planet, No Dividends."

As a corporate citizen ExxonMobil funds worldwide programs to benefit education, communities, health, nature, and the arts. Its largest contributions, about 25 percent of the total, go to higher education. Other projects range from a \$13 million campaign to save the world's tigers from extinction, an appropriate project since the tiger is the company's brand symbol, to sponsorship of free poetry readings in Singapore, where the company owns a chemical plant. In 2006 ExxonMobil gave \$139 million to such efforts. This is a large sum from the perspective of an individual. However, for ExxonMobil it was one-twenty-sixth of 1 percent of its \$366 billion revenues, the equivalent of a person making \$1,000,000 a year giving \$385 to charity. Does this giving live up to the elegant example of founder John D. Rockefeller, the great philanthropist of his era?

The story of ExxonMobil raises central questions about the role of business in society. When is a corporation socially responsible? How can managers know their responsibilities? What actions are ethical or unethical? How responsive must a corporation be to its critics? This book is a journey into the criteria for answering such questions. As a beginning for this first chapter, however, the story illustrates a range of interactions between one large corporation and many nations and social forces. Such business–government–society interactions are innumerable and complicated. In the chapter that follows we try to order the universe of these interactions by introducing four basic models of the business–government–society relationship. In addition, we define basic terms and explain our approach to the subject matter.

WHAT IS THE BUSINESS–GOVERNMENT–SOCIETY FIELD?

In the universe of human endeavor, we can distinguish subdivisions of economic, political, and social activity—that is, business, government, and society—in every civilization throughout time. Interplay among these activities creates an environment in which businesses operate. The business–government–society (BGS) field is the study of this environment and its importance for managers.

To begin, we define the basic terms.

Business is a broad term encompassing a range of actions and institutions. It covers management, manufacturing, finance, trade, service, investment, and other activities. Entities as different as a hamburger stand and a giant corporation are businesses. The fundamental purpose of every business is to make a profit by providing products and services that satisfy human needs.

Government refers to structures and processes in society that authoritatively make and apply policies and rules. Like business, it encompasses a wide range of activities and institutions at many levels, from international to local. The focus of this book is on the economic and regulatory powers of government as they affect business.

business

Profit-making activity that provides products and services to satisfy human needs.

government

Structures and processes in society that authoritatively make and apply policies and rules.

society

A network of human relations composed of ideas, institutions, and material things.

idea

An intangible object of thought.

value

An enduring belief about which fundamental life choices are correct.

ideology

A bundle of values that creates a particular view of the world.

institution

A formal pattern of relations that links people together to accomplish a goal.

A *society* is a network of human relations that includes three interacting elements: (1) ideas, (2) institutions, and (3) material things.

Ideas, or intangible objects of thought, include values and ideologies. *Values* are enduring beliefs about which fundamental choices in personal and social life are correct. Cultural habits and norms are based on values. *Ideologies*—for example democracy and capitalism—are bundles of values that create a certain world view. They establish the broad goals of life by defining what is considered good, true, right, beautiful, and acceptable. Ideas shape every institution in a society.

Institutions are formal patterns of relations that link people together to accomplish a goal. They are essential to coordinate the work of individuals who have no personal relationship with each other.¹⁴ In modern societies, economic, political, cultural, legal, religious, military, educational, media, and familial institutions are salient. There are multiple economic institutions including financial institutions, the corporate form, and markets. Collectively, we call these business.

Figure 1.1 shows how a range of institutions supports markets. Capitalism as an economic system shows wide variation in the nations where it exists because supporting institutions grow from unique historical and cultural roots. In developed nations these institutions are highly evolved and mutually supportive. Where they are weak, markets work in dysfunctional ways. An example is Russia, which introduced a market economy after the fall of communism.

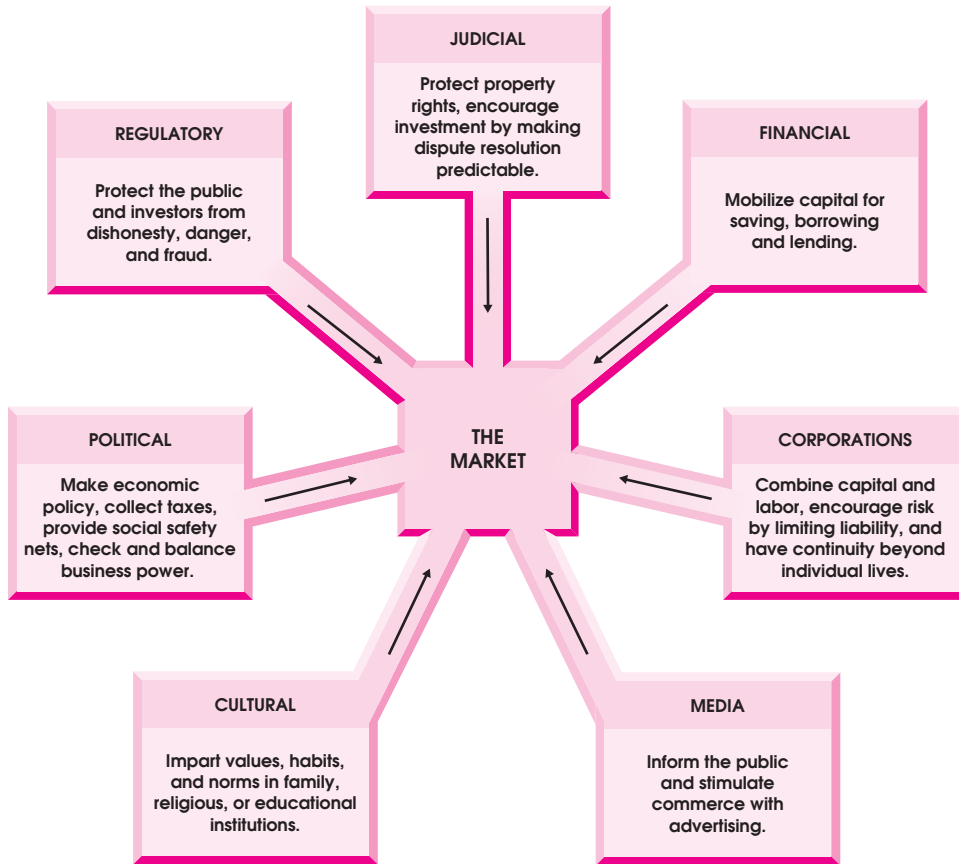
Institutions that had evolved under Soviet political repression and state planning were ill-suited to support a free market. The story of labor is an example. In the old system workers spent lifetimes in secure jobs at state-owned firms. There was no unemployment insurance and, since few workers ever moved, housing markets were undeveloped. A free market economy requires a strong labor market, so workers can switch from jobs in declining firms to jobs in expanding ones. But in Russia the development of a labor market was arrested. The government did not yet provide unemployment benefits to idled workers, so there was no safety net. And housing markets were anemic. Company managers, out of basic humanity, were unwilling to lay off workers who got no benefits and who would find it difficult to move elsewhere.¹⁵ As a result, restructuring in the new Russian economy was torpid. The lesson is that institutions are vital to markets.

Each institution has a specific purpose in society. The function of business is to make a profit by producing goods and services at prices attractive to consumers. A business uses the resources of society to create new wealth. This justifies its existence and is its priority task. All other social tasks—raising an army, advancing knowledge, healing the sick, or raising children—depend on it. Businesses must, therefore, be managed to make a profit. A categorical statement of this point comes from Peter Drucker: “Business management must always, in every decision and

¹⁴ Arnold J. Toynbee, *A Study of History*, vol. XII, *Reconsiderations* (London: Oxford University Press, 1961), p. 270.

¹⁵ Joseph E. Stiglitz, *Globalization and Its Discontents* (New York: W. W. Norton, 2002), p. 140.

FIGURE 1.1 How Institutions Support Markets



action, put economic performance first.”¹⁶ Without profit, business fails in its duty to society and lacks legitimacy.

material things

Tangible artifacts of a society that shape and are shaped by ideas and institutions.

The third element in society is *material things*, including land, natural resources, infrastructure, and manufactured goods. These shape and, in the case of fabricated objects, are partly products of ideas and institutions. Economic institutions, together with the extent of resources, largely determine the type and quantity of society’s material goods.

The BGS field is the study of interactions among the three broad areas defined above. The primary focus is on the interaction of business with the other two elements. The basic subject matter, therefore, is how business shapes and changes government and society, and how it, in turn, is molded by political and social pressures. Of special interest is how forces in the BGS nexus affect the manager’s task.

¹⁶ *Management: Tasks–Responsibilities–Practices* (New York: Harper & Row, 1973), p. 40.

WHY IS THE BGS FIELD IMPORTANT TO MANAGERS?

To succeed in meeting its objectives a business must be responsive to both its economic and its noneconomic environment.¹⁷ ExxonMobil, for example, must efficiently discover, refine, transport, and market energy. Yet swift response to market forces is not always enough. There are powerful nonmarket forces to which many businesses, especially large ones, are exposed. Their importance is clear in the two dramatic episodes that punctuate ExxonMobil's history—the 1911 court-ordered breakup and the 1989 *Exxon Valdez* oil spill.

In 1911 the Supreme Court, in a decision that reflected public opinion as well as interpretation of the law, forced Standard Oil to conform with social values favoring open, competitive markets. With unparalleled managerial genius, courage, and perspicacity, John D. Rockefeller and his lieutenants had built a wonder of efficiency that spread fuel and light throughout America at lower cost than otherwise would have prevailed. They never understood why this remarkable commercial performance was not the full measure of Standard Oil. But beyond efficiency, the public demanded fair play. Thus, the great company was dismembered.

In Alaska a sudden crisis changed ExxonMobil's political and social environments, leading to billions of dollars of sanctions. Today ExxonMobil operates its tanker fleet with extreme care. It has new environmental safeguards and randomly tests crew members for drugs and alcohol. Remarkably, it is now so disciplined that it measures oil spills from its fleet of tankers in teaspoons per million gallons shipped. In 2003 it reported losing less than one teaspoon per million gallons.¹⁸

Recognizing that a company operates not only within markets but within a society is critical. If the society, or one or more powerful interests within it, does not accept a company's actions, that firm will be punished and constrained. A basic agreement or *social contract* exists between the business institution and society. This contract defines the broad duties that business must perform to retain society's support. It is partly expressed in law, but it also resides in social values.

Unfortunately for managers, the social contract is not as clear-cut as are the economic forces a business faces, as complex and ambiguous as the latter often are. For example, the public believes that business has social responsibilities beyond making profits and obeying regulations. If business does not meet them, it may suffer. But precisely what are they? How is corporate performance measured? To what extent must a business comply with ethical values not written into law? When meeting social expectations conflicts with maximizing profits, what is the priority? Despite these questions, the social contract contains the expectations of society, and managers who ignore or violate it are courting disaster.

social contract

An underlying agreement between business and society on basic duties and responsibilities business must carry out to retain public support. It may be reflected in laws and regulations.

¹⁷ For discussion of this distinction see Jean J. Boddewyn, "Understanding and Advancing the Concept of 'Nonmarket,'" *Business & Society*, September 2003.

¹⁸ Exxon Mobil Corporation, "All Ahead Safe," *National Journal*, March 20, 2004, p. 888 (advertisement).

FOUR MODELS OF THE BGS RELATIONSHIP

Interactions among business, government, and society are infinite and their meaning is open to interpretation. Faced with this complexity, many people use simple mental models to impose order and meaning on what they observe. These models are like prisms, each having a different refractive quality, each giving the holder a different view of the world. Depending on the model (or prism) used, a person will think differently about the scope of business power in society, criteria for managerial decisions, the extent of corporate responsibility, the ethical duties of managers, and the need for regulation.

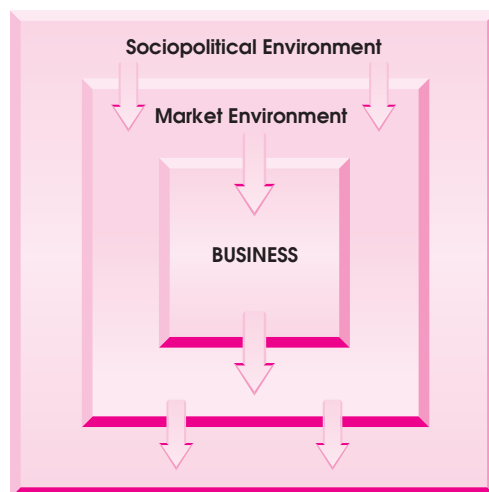
The following four models are basic alternatives for seeing the BGS relationship. As abstractions they oversimplify reality and magnify central issues. Each model can be both descriptive and prescriptive; that is, it can be both an explanation of how the BGS relationship does work and, in addition, an ideal about how it should work.

The Market Capitalism Model

The market capitalism model, shown in Figure 1.2, depicts business as operating within a market environment, responding primarily to powerful economic forces. There, it is substantially sheltered from direct impact by social and political forces. The market acts as a buffer between business and nonmarket forces. To appreciate this model, it is important to understand the history and nature of markets and the classic explanation of how they work.

Markets are as old as humanity, but for most of recorded history they were a minor institution. People produced mainly for subsistence, not to trade. Then, in the 1700s, some economies began to expand and industrialize, division of labor developed within them, and people started to produce more for trade. As trade grew, the market, through its price signals, took on a more central role in directing

FIGURE 1.2
The Market
Capitalism
Model



Full Production and Full Employment under Our Democratic System of Private Enterprise, ca. 1944, a crayon and ink drawing by Michael Lenson, an artist working for the Works Progress Administration Federal Art Project. Lenson focuses on the virtues of market capitalism.
Source: Courtesy of The Library of Congress.



market economy

The economy that emerges when people move beyond subsistence production to production for trade, and markets take on a more central role.

capitalism

An economy in which private individuals and corporations own the means of production and, motivated by the desire for profit, compete in free markets under conditions of limited restraint by government.

the creation and distribution of goods. The advent of this kind of *market economy*, or an economy in which markets play a major role, reshaped human life.

The classic explanation of how a market economy works comes from the Scottish professor of moral philosophy Adam Smith (1723–1790). In his extraordinary treatise, *The Wealth of Nations*, Smith wrote about what he called “commercial society” or what today we call *capitalism*. He never used that word. It was adopted later by the socialist philosopher Karl Marx (1818–1883), who contrived it as a term of pointed insult. But it caught on and soon lost its negative connotation.¹⁹ Smith said that the desire to trade for mutual advantage lay deep in human instinct. He noted that the growing division of labor in society led more people to try to satisfy their self-interests by specializing their work, then exchanging goods with each other. As they did so, the market's pricing mechanism reconciled supply and demand, and its ceaseless tendency was to make commodities cheaper, better, and more available.

The beauty of this process, according to Smith, was that it coordinated the activities of strangers who, to pursue their selfish advantage, were forced to fulfill the needs of others. In Smith's words, each trader was “led by an invisible hand to promote an end which was no part of his intention,” the collective good of society.²⁰ Through markets that harnessed the constant energy of greed for the public welfare, Smith believed that nations would achieve “universal opulence.” His genius was to demystify the way markets work, to frame market capitalism in moral terms, to extol its virtues, and to give it lasting justification as a source of human progress. The greater good for society came when businesses competed freely.

¹⁹ Jerry Z. Muller, *The Mind and the Market: Capitalism in Modern European Thought* (New York: Knopf, 2002), p. xvi.

²⁰ Adam Smith, *The Wealth of Nations*, ed. E. Cannan (New York: Modern Library, 1937), Book IV, chap. II, p. 423. First published in 1776.

managerial capitalism

A market economy in which the dominant businesses are large firms run by salaried managers, not smaller firms run by owner-entrepreneurs.

laissez-faire

An economic philosophy that rejects government intervention in markets.

In Smith's day producers and sellers were individuals and small businesses managed by their owners. Later, by the late 1800s and early 1900s, throughout the industrialized world, the type of economy described by Smith had evolved into a system of *managerial capitalism*. In it the innumerable, small, owner-run firms that animated Smith's marketplace were overshadowed by a much smaller number of dominant corporations run by hierarchies of salaried managers.²¹ These managers had limited ownership in their companies and worked for shareholders. This form of capitalism has now spread throughout the world. Nowhere does it work exactly like Smith's theory. Nevertheless, the market capitalism model continues to exist as an ideal against which to measure practice.

The model incorporates important assumptions. One is that government interference in economic life is slight. This is called *laissez-faire*, a term first used by the French to mean that government should "let us alone." It stands for the belief that government intervention in the market is undesirable. It is costly because it lessens the efficiency with which free enterprise operates to benefit consumers. It is unnecessary because market forces are benevolent and, if liberated, will channel economic resources to meet society's needs. It is for governments, not businesses, to correct social problems. Therefore, managers should define company interests narrowly, as profitability and efficiency.

Another assumption is that individuals can own private property and freely risk investments. Under these circumstances, business owners are powerfully motivated to make a profit. If free competition exists, the market will hold profits to a minimum and the quality of products and services will rise as firms try to attract more buyers. If one enterprise tries to increase profits by charging higher prices, consumers will go to a competitor. If one producer makes higher-quality products, others must follow. In this way, markets convert selfish competition into broad social benefits.

Other assumptions include these: Consumers are informed about products and prices and make rational decisions. Moral restraint accompanies the self-interested behavior of business. Basic institutions such as banking and laws exist to ease commerce. There are many producers and consumers in competitive markets.

The perspective of the market capitalism model leads to these conclusions about the BGS relationship: (1) government regulation should be limited, (2) markets discipline private economic activity to promote social welfare, (3) the proper measure of corporate performance is profit, and (4) the ethical duty of management is to promote the interests of shareholders. These tenets of market capitalism have shaped economic values in the industrialized West and, as markets spread, they do so increasingly elsewhere.

There are many critics of capitalism and the market capitalism model. As promised by its defenders, capitalism has created material progress. Yet there are trade-offs: It is argued that capitalism creates prosperity only at the cost of rising inequality. Karl Marx believed that owners of capital exploited workers and used imperialist foreign policies to spread markets. Others believe that markets erode virtue. The avarice, self-love, and ruthlessness that energize them are base values that drive out virtues such as love and friendship. Another

²¹ Alfred D. Chandler, Jr., "The Emergence of Managerial Capitalism," *Business History Review*, Winter 1984, p. 473.

enduring fear is that markets place too much emphasis on money and material objects. Pope John Paul II, for example, cautioned against a “domination of things over people.”²² Critics see these problems as inherent to markets. Still other criticisms focus on the flaws that sometimes, perhaps inevitably, appear in them. Without correction they may reward conspiracies and monopoly. Also, the profit motive has led companies to pollute and plunder the earth.

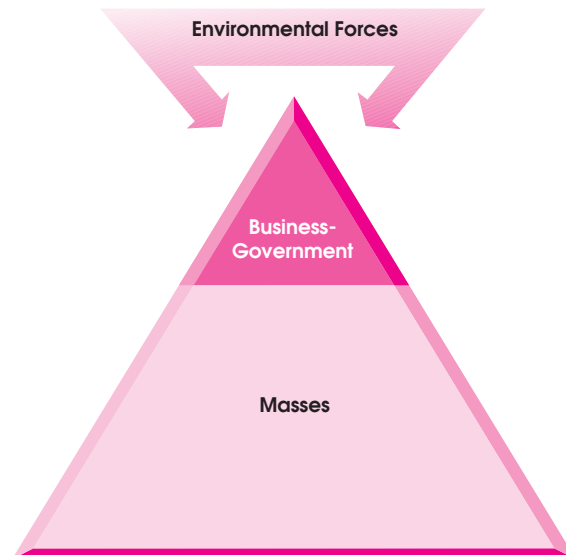
All these criticisms of capitalism are pronounced today, but none are new. They represent a series of recurrent attacks that wind through the Western philosophical tradition. Adam Smith himself had some reservations and second thoughts. He feared both physical and moral decline in factory workers and the unwarranted idolization of the rich, who might have earned their wealth by unvirtuous methods. In his later years, he grew to see more need for government intervention. But Smith never envisioned a system based solely on greed and self-interest. He expected that in society these traits must coexist with restraint and benevolence.²³

The ageless debate over whether capitalism is the best means to human fulfillment will continue.²⁴ Meanwhile, we turn our discussion to an alternative model of the BGS relationship that attracts many of capitalism's detractors.

The Dominance Model

The dominance model is a second basic way of seeing the BGS relationship. It represents primarily the perspective of business critics. In it, business and government dominate the great mass of people. This idea is represented in the pyramidal, hierarchical image of society shown in Figure 1.3. Those who subscribe

FIGURE 1.3
The
Dominance
Model



²² Encyclical Letter, *Centesimus annus*, May 1, 1991, p. 16.

²³ *The Theory of Moral Sentiments*, ed. E. G. West (Indianapolis: Liberty Classics, 1976), pp. 70–72. Originally published in 1853.

²⁴ Muller, *The Mind and the Market: Capitalism in Modern European Thought*, pp. x–xiv.

to the model believe that corporations and a powerful elite control a system that enriches a few at the expense of the many. Such a system is undemocratic. In democratic theory, governments and leaders represent interests expressed by the people, who are sovereign.

Proponents of the dominance model focus on the defects and inefficiencies of capitalism. They believe that corporations are insulated from pressures holding them responsible, that regulation by a government in thrall to big business is feeble, and that market forces are inadequate to ensure ethical management. Unlike other models, the dominance model does not represent an ideal in addition to a description of how things are. For its advocates, the ideal is to turn it upside down so that the BGS relationship conforms to democratic principles.

In the United States, the dominance model gained a following during the late nineteenth century when large trusts such as Standard Oil emerged, buying politicians, exploiting workers, monopolizing markets, and sharpening income inequality. Beginning in the 1870s, farmers and other critics of big business rejected the ideal of the market capitalism model and based a populist reform movement called populism on the critical view of the BGS relationship implied in the dominance model.

Populism is a recurrent spectacle in which common people who feel oppressed or disadvantaged in some way seek to take power from a ruling elite that thwarts fulfillment of the collective welfare. In America, the populist impulse bred a sociopolitical movement of economically hard-pressed farmers, miners, and workers lasting from the 1870s to the 1890s that blamed the Eastern business establishment for a range of social ills and sought to limit its power.

This was an era when, for the first time, on a national scale the actions of powerful business magnates shaped the destinies of common people. Some displayed contempt for commoners. “The public be damned,” railroad magnate William H. Vanderbilt told a reporter during an interview in his luxurious private railway car.²⁵ The next day, newspapers around the country printed his remark, enraging the public. Later, Edward Harriman, the aloof, arrogant president of the Union Pacific Railroad, allegedly reassured industry leaders worried about reform legislation, saying “that he ‘could buy Congress’ and that if necessary he ‘could buy the judiciary.’”²⁶ It was with respect to Harriman that President Theodore Roosevelt once noted that “men of very great wealth in too many instances totally failed to understand the temper of the country and its needs.”²⁷

populism

A political pattern, recurrent in world history, in which common people who feel oppressed or disadvantaged seek to take power from a ruling elite seen as thwarting fulfillment of the collective welfare.

²⁵ “Reporter C. P. Dresser Dead,” *New York Times*, April 25, 1891, p. 7. In fairness to Vanderbilt, the context of the remark is elusive. It came in response to questioning by a reporter who may have awakened Vanderbilt at 2:00 A.M. to ask, perhaps insolently, if he would keep an unprofitable route in service to the public. Vanderbilt’s response was magnified far beyond a cross retort to become the age’s enduring emblem of arrogant wealth. See “Human Factor Great Lever in Railroading,” *Los Angeles Times*, October 20, 1912, p. V15; and Ashley W. Cole, “A Famous Remark,” *New York Times*, August 25, 1918, p. 22 (letter to the editor).

²⁶ Quoted from correspondence of Theodore Roosevelt in Maury Klein, *The Life & Legend of E. H. Harriman* (Chapel Hill: University of North Carolina Press, 2000), p. 369.

²⁷ *Ibid.*, p. 363.

This 1900 political cartoon illustrates a central theme of the dominance model, that powerful business interests act in concert with government to further selfish money interests. Although the cartoon is old, the idea remains compelling for many.

Source: © Bettmann/CORBIS



IN THE HANDS OF HIS PHILANTHROPIC FRIENDS.

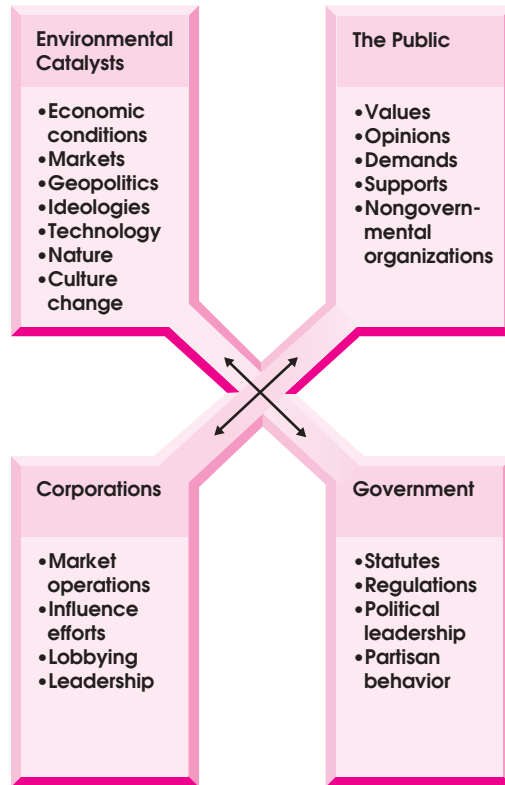
The populist movement in America ultimately fell short of reforming the BGS relationship to a democratic ideal. Other industrializing nations, notably Japan, had similar populist movements. Marxism, an ideology opposed to industrial capitalism, emerged in Europe at about the same time as these movements, and it also contained ideas resonant with the dominance model. In capitalist societies, according to Karl Marx, an owner class dominates the economy and ruling institutions. Many business critics worldwide advocated socialist reforms that, based on Marx's theory, could achieve more equitable distribution of power and wealth.

In the United States the dominance model may have been most accurate in the late 1800s when it first arose to conceptualize a world of brazen corporate power and politicians who openly represented industries. However, it remains popular. Ralph Nader, for example, speaks its language.

Over the past 20 years, big business has increasingly dominated our political economy. This control by corporate government over our political government is creating a widening “democracy gap.” The unconstrained behavior of big business is subordinating our democracy to the control of a corporate plutocracy that knows few self-imposed limits to the spread of its power to all sectors of our society.²⁸

²⁸ “Statement of Ralph Nader,” in *The Ralph Nader Reader* (New York: Seven Stories Press, 2000), pp. 3 and 4.

FIGURE 1.4
The Counter-
vailing Forces
Model



In recent years fear of transnational corporations has given the dominance model new life in a global context. Running for president in 2004, Nader tried “to rescue our public authorities from the corporate government of big business,” particularly “large multinational corporations” that are “increasingly and pervasively replacing the sovereignty of the people.”²⁹

The Countervailing Forces Model

The countervailing forces model, shown in Figure 1.4, depicts the BGS relationship as a flow of interactions among the major elements of society. It suggests complex exchanges of influence among them, attributing dominance to none.

This is a model of multiple or pluralistic forces. Their strength waxes and wanes depending on factors such as the subject at issue, the power of competing interests, the intensity of feeling, and the influence of leaders. The counter-

²⁹ See “Ralph Nader Announcement of Candidacy: Toward a ‘New Birth of Freedom’ and Justice,” February 23, 2004, and “In the Spirit of the Common Good—A Request for Views” (undated), both at www.votenader.org.

vailing forces model reflects the BGS relationship in industrialized nations with democratic traditions. It differs from the market capitalism model, because it opens business directly to influence by nonmarket forces. Many important interactions implied in it would be evaluated as negligible in the dominance model.

What overarching conclusions can be drawn from this model?

1. Business is deeply integrated into an open society and must respond to many forces, both economic and noneconomic. It is not isolated from its social environment, nor is it always dominant.
2. Business is a major initiator of change in society through its interaction with government, its production and marketing activities, and its use of new technologies.
3. Broad public support of business depends on its adjustment to multiple social, political, and economic forces. Incorrect adjustment leads to failure. This is the social contract at work.
4. BGS relationships continuously evolve as changes take place in the main ideas, institutions, and processes of society.

stakeholder

An entity that is benefitted or burdened by the actions of a corporation or whose actions may benefit or burden the corporation. The corporation has an ethical duty toward these entities.

primary stakeholders

Entities in a relationship with the corporation in which they, the corporation, or both are affected immediately, continuously, and powerfully.

secondary stakeholders

Entities in a relationship with the corporation in which the effects on them, the corporation, or both are less significant and pressing.

The Stakeholder Model

The stakeholder model in Figure 1.5 shows the corporation at the center of an array of mutual relationships with persons, groups, and entities called *Stakeholders*. Stakeholders are those whom the corporation benefits or burdens by its actions and those who benefit or burden the firm with their actions. A large corporation has many stakeholders. These can be divided into two categories based on the nature of the relationship. But the assignments are relative, approximate, and inexact. Depending on the corporation or the episode, a few stakeholders may shift from one category to the other.

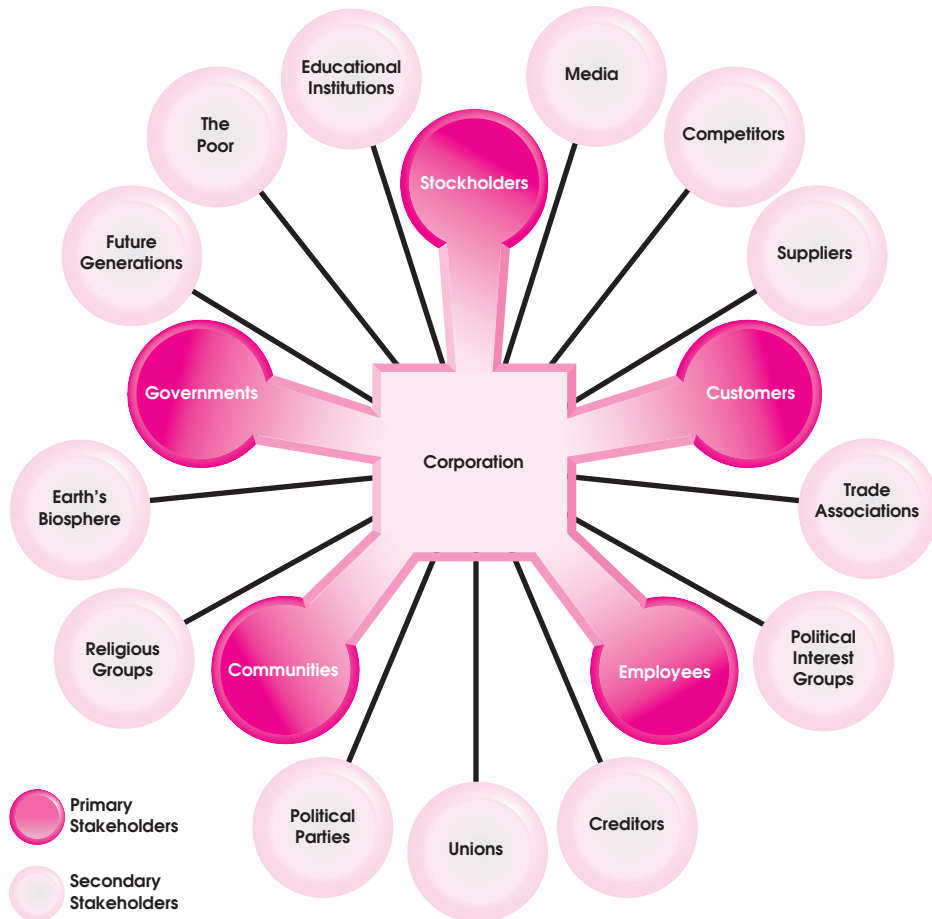
Primary stakeholders are a small number of constituents for which the impact of the relationship is immediate, continuous, and powerful on both the firm and the constituent. They are stockholders (owners), customers, employees, communities, and governments and may, depending on the firm, include others such as suppliers or creditors.

Secondary stakeholders include a possibly broad range of constituents in which the relationship involves less mutual immediacy, benefit, burden, or power to influence. Examples are activist groups, trade associations, and schools.

Exponents of the stakeholder model debate how to identify who or what is a stakeholder. Some use a broad definition and include, for example, natural entities such as the earth's atmosphere, oceans, terrain, and living creatures because corporations have an impact on them.³⁰ Others reject this broadening, since natural entities are represented by conventional stakeholders such as environmental groups. Some include competitors because, although they do not work to benefit

³⁰ See, for example, Edward Stead and Jean Garner Stead, "Earth: A Spiritual Stakeholder," *Business Ethics Quarterly*, Ruffin Series no. 2 (2000), pp. 321–44.

FIGURE 1.5
The
Stakeholder
Model



the firm, they have the power to affect it. At the furthest reaches of the stakeholder idea lie groups such as the poor and future generations. But in the words of one stakeholder advocate, “[s]takeholder theory should not be used to weave a basket big enough to hold the world’s misery.”³¹ If groups such as the poor were included in the stakeholder network, managers would be morally obliged to run headlong at endless problems, taking them beyond any conceivable economic mission.

The stakeholder model reorders the priorities of management away from those in the market capitalism model. There, the corporation is the private property of those who contribute its capital. Its immediate priority is to benefit one group—the investors. The stakeholder model, by contrast, is an ethical theory of management in which the welfare of each stakeholder must be considered as an end.

³¹ Max Clarkson, *A Risk-Based Model of Stakeholder Theory* (Toronto: The Centre for Corporate Social Performance & Ethics, 1994), cited in Robert Phillips, *Stakeholder Theory and Organizational Ethics* (San Francisco: Berrett-Koehler, 2003), p. 119.

Stakeholder interests have intrinsic worth; they are not valued only to the extent that they enrich investors. Managers have a duty to consider the interests of multiple stakeholders, and because of this, “the interests of shareowners . . . are not always primary and never exclusive.”³²

Stakeholder management, then, creates duties toward multiple constituents of the corporation—duties not emphasized in the practice of market capitalism, which tends toward domination of the environment and enrichment of shareowners. Management must raise its gaze above profits to see and respond to a spectrum of other values. One group of scholars, for example, urges that corporations “should adopt processes and modes of behavior that are sensitive to the concerns and capabilities of each stakeholder constituency.”³³ The stakeholder model is intended to redefine the corporation. It rejects the shareholder-centered view of the firm in the market capitalism model as “ethically unacceptable.”³⁴

Not everyone agrees. Critics of the stakeholder model argue that it is not a realistic assessment of power relationships between the corporation and other entities. It seeks to give power to the powerless by replacing force with ethical duty, a timeless and often futile quest of moralists. In addition, it sets up too vague a guideline to substitute for the yardstick of profits for investors. Unlike traditional criteria such as return on capital, there is no single, clear, and objective measure to evaluate the combined ethical/economic performance of a firm. According to one critic, this lack of a criterion “would render impossible rational management decision making for there is simply no way to adjudicate between alternative projects when there is more than one bottom line.”³⁵ In addition, the interests of stakeholders so vary that often they conflict with shareholders and with one another. With respect to corporate actions, laws and regulations protect stakeholder interests. Creating surplus ethical sensitivity that soars above legal duty is impractical and unnecessary.³⁶

Some puzzles exist in stakeholder thinking. It is not clear who or what is a legitimate stakeholder, to what each stakeholder is entitled, or how managers should balance competing demands among a range of stakeholders. Yet its advocates are compelled by two arguments. First, a corporation that embraces stakeholders performs better. A corporation better sustains its wealth-creating function with the support of a network of parties beyond shareholders. Put bluntly by one advocate of the stakeholder perspective, “[e]xecutives ignore stakeholders at the peril of the survival of their companies.”³⁷ Second, it is the ethical way to manage because stakeholders have moral rights that grow from the way powerful corporations affect them. Irrespective of academic debates, in practice many large

³² James E. Post, Lee E. Preston, and Sybille Sachs, *Redefining the Corporation: Stakeholder Management and Organizational Wealth* (Stanford, CA: Stanford University Press, 2002), p. 17.

³³ Clarkson Centre for Business Ethics, *Principles of Stakeholder Management* (Toronto: Clarkson Centre for Business Ethics, 1999).

³⁴ Post, Preston, and Sachs, *Redefining the Corporation*, p. 16.

³⁵ John Argenti, “Stakeholders: The Case Against,” *Long Range Planning*, June 1997, p. 444.

³⁶ Anant K. Sundaram, “Tending to Shareholders,” *Financial Times*, May 26, 2006, p. 6.

³⁷ “R. Edward Freeman, “The Wal-Mart Effect and Business, Ethics, and Society,” *Academy of Management Perspectives*, August 2006, p. 40.

corporations have adopted methods and processes to analyze their stakeholders and engage them. This trend is discussed in Chapter 6.

OUR APPROACH TO THE SUBJECT MATTER

Discussion of the business–government–society field could be organized in many ways. The following is an overview of our approach.

Comprehensive Scope

This book is comprehensive. It covers many subjects. We believe that for those new to the field seeing a panorama is helpful. Because there is less depth in the treatment of subjects than can be found in specialized volumes, we suggest additional sources in footnotes.

Interdisciplinary Approach with a Management Focus

The field is exceptionally interdisciplinary. It exists at the confluence of a fairly large number of established academic disciplines, each of which contributes to its study. These disciplines include the traditional business disciplines, particularly management; other professional disciplines, including medicine, law, and theology; the social sciences, including economics, political science, philosophy, history, and sociology; and, from time to time, natural sciences such as chemistry and ecology. Thus, our approach is eclectic; we cross boundaries to find insight.

The dominant orientation, however, is the discipline of management and, within it, the study of *strategic management*, or actions that adapt the company to its changing environment. To compete and survive, firms must create missions, purposes, and objectives; the policies and programs to achieve them; and the methods to implement them. We discuss these elements as they relate to corporate social performance, illustrating successes and failures.

Use of Theory, Description, and Case Studies

Theories simplify and organize areas of knowledge by describing patterns or regularities in the subject matter. They are important in every field, but especially in this one, where innumerable details from broad categories of human experience intersect to create a new intellectual universe. Where theory is missing or weak, scholarship must rely more on description and the use of case method.

No underlying theory to integrate the entire field exists. Fortunately, the community of scholars studying BGS relationships is building theory in several areas. The first is theory describing how corporations interact with stakeholders. The second is theory regarding the ethical duties of corporations and managers. And the third is theory explaining corporate social performance and how it can be measured. Theory in this last area focuses on defining exactly what a firm does to be responsible in society and on creating scales and rulers with which to weigh and measure its actions. Scholarship in all three areas shows increasing sophistication and wider agreement on basic ideas.

Despite the lack of a grand theory to unify the field, useful theories abound in related disciplines. For example, there are economic theories about the impact of

strategic management
Actions taken by managers to adapt a company to changes in its market and sociopolitical environments.

theory
A statement or vision that creates insight by describing patterns or relationships in a diffuse subject matter. A good theory is concise and simplifies complex phenomena.

TABLE 1.1
Select
Multinational
Corporations
with High
Percentages
of Sales,
Assets, and
Employees
Outside Home
Countries,
2005

Source: United Nations Conference on Trade and Development, *World Investment Report, 2007* (New York and Geneva: United Nations, 2007), annex A, table A.I.13.

Company	Sales	Assets	Employees
Nokia (Finland)	99%	65%	57%
Nestlé (Switzerland)	98	65	97
Honda (Japan)	80	74	87
ExxonMobil (United States)	69	69	63
McDonald's (United States)	66	65	78
Procter & Gamble (United States)	57	44	51

government regulation, scientific theories regarding industrial pollution, political theories explaining corporate power, and legal theories on subjects such as negligence applied by courts to corporations when, for example, industrial accidents occur. When fitting, we discuss such theories; elsewhere we rely on descriptions of events. We also use case studies at the end of each chapter to raise issues for discussion.

Global Perspective

Today global capitalism animates the planetary stage, creating movements of people, money, goods, and information that, in turn, beget conflicts as some benefit more and others less or not at all. Viewing any nation's economy or businesses in isolation from the rest of the world is myopic. Every government finds its economic and social welfare policies judged by world markets. Every corporation has a home country, but as shown in Table 1.1, many large multinational corporations have more sales, assets, and employees outside its borders than within. For now, global capitalism is ascendant. It brings unprecedented wealth creation and new material comforts. But it also imposes burdens on human rights and the environment, challenges diversity of values, and creates conflict with those who are fed upon in the lively predation or who stand aloof from the free market consensus. A fitting perspective on the BGS relationship must, therefore, be global.

Historical Perspective

History is the study of phenomena moving through time. The BGS relationship is a stream of events, of which only one part exists today. Historical perspective is important for many reasons. It helps us see that today's BGS relationship is not like that of other eras; that current ideas and institutions are not the only alternative; that historical forces are irrepressible; that corporations both cause and adapt to change; that our era is not unique in undergoing rapid change; and that we are shaping the future now. When appropriate, we examine the antecedents of current arrangements.

history

The study of phenomena moving through time.