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The Common Good of the Firm as the "Office" of the Manager

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Abstract

The paper examines how the public interest and private interests interact in the firm. The common good is not only a political but also a managerial concept. The management is not only obliged to fulfill its fiduciary duty towards the shareholders or owners and to act in their interest but must also realize the common good of the firm as the good of all members of the firm. There is an analogy between the politician and the manager: both cannot only work in the interest of their party or employers. To work for the common good is part of their office, part of the nature of their task of good governance in the interest of all.

Realizing public interest is usually seen as the task of the state and as an obligation for politicians, not for the managers of large corporations. Public interest is a concept that is used constantly, that is made concrete rarely and that is viewed as an empty concept more and more often. It seems to be a difficult obligation to work for the common good and to consider the effects of one's own action for the public good in a market society in which every one has a right to follow his or her self-interest.

Nevertheless the concept of public interest is indispensable, particularly indispensable for politics. The right of a politician to follow his or her private interest and that of her immediate clients in her office is defended by no one. The role description of the politician incorporates that he or she works for the public good in her action and not for her party's good. The demand for public interest is here no empty concept but something like a general clause that applies to all actions of politicians.

Politicians can consider their self-interest and strive for fame, prestige and career as a side effect of their intention to realize the public good, but they cannot view the common good as the side effect of the realization of their self-interest.

In a market society, the reverse causation is effective it is often said. The shareholder and the manager of a corporation realize the common good of public efficiency as a side effect of the pursuit of their self-interest and profit so that in a market society the demand to realize the common good does not hold.

According to the teaching of neoclassical economics, the common good is not realized in the market by intending it but by the working of the invisible hand of the market that turns selfish interests into efficiency and wealth creation. The kernel theorem of the invisible hand theory is that the common good of efficiency and wealth creation is realized in a market society as a side effect of the pursuit of self-interest. It is, however, not clear how far this theorem is taken by Adam Smith as a description of fact or as a normative statement.

I. The Common Good of States and the Common Good of Other Social Groups and Business Corporations

It is characteristic for the theory of the common good that it does not confine the demand for realizing the common good to the state. Every community or organization has its common good and its task to realize it.[1] The idea of the common good of groups shows that the common good is not only a concept for the totality of the common good of the whole of state and society but at the same time it is a totality of totalities that is structured internally. Every community or organization, be it a business corporations, a university, a school, is not only characterized by the private interest of each of those working in them but also by the interest of all working in these institutions. All are interested in the prospering of their institution and the continuation of this situation since the continuation of the whole institution and thereby of all the groups in it is endangered if certain individuals or groups in this institution are damaged in their good. The solidarity of the interests and of the common good of the groups or stakeholders in an or-

1 Cf. GUNDLACH (1959), col. 738.

ganization makes it impossible to define the good of an organization only by the good of a single group or only some individuals.

The connectedness or solidarity of the groups and individuals in an institution holds, however, not only for their connectedness within an institution. It also concerns, although to a lesser degree, the different individuals or institutions working in the same field – be this field a shared profession or a shared industry.

Recent research in business ethics shows that there is a common good of an industry and of a profession beside the corporate good of the corporation. The corporations of an industry or the individuals of a profession are connected in their good prosperity and share a common interest in the well-being of the industry or profession. If, e.g., certain firms damage the consumers they damage by doing so the reputation of the whole industry. The member of a profession like a medical doctor damages the reputation of the whole profession by damaging a client or patient. By her "unprofessional" behaviour, she not only damages the consumer or client but also the other members of an industry or a profession.

On the higher level of the economy of a region or continent, even of the whole world economy, a similar connectedness of the common goods holds true. Economies are connected in their common good even if this is so to a decreasing degree of intensity depending on the measure of remoteness of groups from each other. No part of humanity can prosper in the long run if another part of humanity is in desperate need.

The structure and sequence of communities results in a structure and sequence of the common goods of groups that correspond to the specific connectedness of the members of these groups. Their common good and joint interest are caused by the closeness of the humans in their respective groups and by the subsidiarity of the tasks of groups and organizations. The public interest of smaller groups and institutions is the subsidiary condition of the common good of the whole of society and vice versa. The political union or state can only prosper if the intermediary social institutions like families, corporations etc. prosper.

II. Modernity as the Emancipation of Self-Interest?

The era of modernity is often seen as the epoch of the emancipation of self-interest in which the demand for a consideration of the common good in the individual pursuit of interest has become obsolete. Modernity seems to have no need for the motive of intending to realize the common good. Some thinkers of Public Choice theory and its model of democracy go so far to say that even the political order of the democratic state cannot be understood in categories of the common good but must be seen as the mere result of the composition of individual self-interested votes and of self-interested politicians. Public Choice theory is an important innovation if it is understood as a critical theory of the actual motivation of politicians and as a critique of the naive idea that politicians have different and *per se* better motives than the decision-makers of the private sector. Public Choice theory becomes, however, problematic if it excludes *a priori* the possibility that politicians try to find out and to realize the common good.

Adam Smith who is considered by some social scientists the founder of modernity has stated only as a fact, not as a norm, that it is not from the benevolence, but from the self-interest of the butcher, brewer or baker that we expect to get what we need for food. This statement by Adam Smith[2] seems to be interpreted by some of today's economists to be a normative statement describing how it *ought* to be. They contend that it is not only a fact that we depend on the producer's self-interest but it is normatively demanded that we ought to depend only on the producers' self-interest for being provided with goods.

From the textual base and from the synopsis of his two works, *The Theory of Moral Sentiments* and *The Wealth of Nations*, it must be concluded that Adam Smith took his statement only as a statement of fact and not of normative content. The butcher is free, of course, to provide his services also for the common good, even for philanthropic or altruistic reasons. The market cannot rely on these higher motives but it does not exclude it as a norm that ought or must be followed. The exasperation of the self-interest theorem to a normative principle would make the "Adam Smith Problem" of how Smith's ethical and economic theory is compatible, unsolvable. Since Smith has written both treatises they must be reconcilable in his mind. The market coordinates self-interested action. The content of the motives of self-interest is left open by the price system. Common good orientation is as possible as narrow self-interest, and possible are also mixed mo-

[2] ADAM SMITH: *The Wealth of Nations*, in: *The Works of Adam Smith,* Vol. 2, 1811-12, Reprint Aalen (Otto Zeller) 1963, Book 7, chap. 2, 21.

tives and an over-determination of human action by various self-interested and common good motives.

III. The Public Interest of Institutions and the Increase of the Responsibility for the Public Interest to the Degree of the Power of Those Managing the Institutions

Every organization and institution possesses its specific idea of the public interest and has the task to realize the interest of the organization as a whole. The obligation towards the orientation on the public interest increases with the increasing impact of decisions and with the decision-maker's increasing power since the side-effects, the positive and negative side-effects of an action, increase with the action's impact. The acting persons are obliged to consider the public interest in those ranges of action that are relevant for the public interest. The fact that the decision problem becomes more difficult and complex by the duty to consider the public interest must not imply that the increasing complexity of the decision frees the decision-maker from the consideration of its side-effects on the public interest. The increasing complexity of decision-making only implies that in judging the success of a decision in itself and in considering the public good the difficulty of the task has to be taken into consideration.

The obligation to include the side-effects of one's decision-making on the public good increases with increasing power. This increasing obligation to consider the public good indicates that power itself is a moral phenomenon. The more power a person possesses the more the person must consider the side-effects of his or her decision-making. The idea of the public interest points to this relationship between power and the duty to consider the public good.

As Roman Herzog has demonstrated[3] it has been Thomas Aquinas who has introduced two insights to political philosophy by his idea of the common good: first the insight that sovereignty and the exercise of political power do not have their criterion of action in themselves but refer to a higher authority and are therefore constraint in their freedom, and secondly the insight that the state *and* the individual are bound by the common good. Thomas Aquinas starts from monarchy in his theory of the common good and binds the ruler to an authority outside of the ruler's own will and self-

[3] HERZOG (1974), col. 256.

interest. The ruler cannot only follow his free and sovereign will. He is not only directed by his own interest but by the higher authority of the common good and is constraint by it in his will and sovereignty.

The idea of the common good leads to the development of the modern idea of office. The political office is obliged to realize the common good, it is not there to increase the power or advantage of the office holder and his self-interest. It is not only the self-interest of the state, the *raison d'état*, or the sovereignty of the prince or king and his self-interest that matter. The office, particularly the political office, bears in itself the obligation to good governance and is bound by the effect of the decisions on the common good.

The idea of office that is concluded from the idea that power is bound by the public good does not only constrain political, but also economic, cultural, and religious power. The idea of office shows that power is a moral phenomenon and therefore always related to the common good. Not only political power is an office that is not only defined by the sovereign will of the one in power and that is subject to what is demanded by the realization of the common good. The same holds true for the holder of economic, religious, and cultural power.

The obligation to include the idea of the common good in the individual decision-making of economic, religious, and cultural power as well as in those of political power follows from the fact that the individualist decision-making processes of the market and of democracy cannot function without such a consideration of the public good since frictions in the economic and political realm are the consequence if they are based on self-interest only.

The need for the consideration of the common good in the market and in democracy arises first from the problem of the aggregation or composition of individual decisions determined by self-interest to a market price and to a political decision. The phenomena of market failure and of democracy failure describe such frictions of coordination in the market and in democracy. The need to consider the common good also arises on the other hand from the fact that the holder of economic and political responsibility are not only the agents or fiduciaries of the principals that give them the fiduciary power but also of those, even if so to a lesser degree, that they do not represent but whose life they influence by their decisions. They must consider the common good of the institutions which they direct beyond their mere fiduciary duties to those who gave them fiduciary power, their principals.

IV. The Obligation of Managers to Realize the Common Good of Their Corporations

The obligation to consider the common good is not only valid for the politician. The politician is not only the agent of her constituency and party but is always at the same time the representative of those that did not vote for her. Likewise, the manager of a large firm is not only the fiduciary of those who employed him but also of those who work under his leadership. The obligation to realize the common good of the institution is therefore also valid for the manager of the large firm.[4] The manager is not only the agent of his principals, be they shareholders or single owners, and he has more duties than those of realizing the interest of the shareholder group in profit maximization only. He must consider the interest of the other stakeholders as well when he realizes the legitimate shareholder interest in return on investment. By maximizing shareholder value the manager must at the same time realize the common good of the entire firm.[5] The manager's task to realize the maximum productivity of the firm cannot be secured by the market, competition and the price system alone. The manager must realize productivity even where the power of competition does not force him to do so as e.g. in imperfect markets or in developing nations. This indi-

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[4] Cf. H. ALFORD and N. NAUGHTON: „Working the Common Good: The Purpose of the Firm", in: S. A. CORTRIGHT and MICHAEL J. NAUGHTON (Eds.): *Rethinking the Purpose of Business. Interdisciplinary Essays from the Catholic Social Tradition*, Notre Dame, Indiana (University of Notre Dame Press) 2002.

[5] This need for a constraint on self-interest applies also to the stakeholder theory of the firm. One might be tempted to think that the stakeholder approach is closer to the common good idea than the shareholder approach since it includes, ideally, all stakeholders in the firm whereas the shareholder group is only one group of the firm. The stakeholders may, however, form coalitions against the shareholders or form other coalitions against other stakeholders, coalitions that do not represent the common good of the firm. The shareholders as the outside controlling institution of the firm may have to enforce the common good of the firm against stakeholder coalitions that are not in the interest of the long run survival of the firm.

cates that the productivity of the firm is a kind of public good for the firm beyond mere profit maximization.[6]

The decision-maker of an institution cannot dispense him- or herself from the responsibility for the common good of the institution by pointing to the fiduciary duty towards the shareholders. The reference to a narrow fiduciary relationship can include an element of exculpation from responsibility. Every kind of fiduciary relationship or of acting for the sake of someone else and of someone else's goals leads to a reduction in the moral obligation since, by the fiduciary relationship, the responsibility for actions is divided between the principal and the agent and can be shifted forward and backward between them.

The danger of such a reduction of the total responsibility of management for the common good of a firm can be demonstrated in the exaggeration of the shareholder value principle as the only goal of the firm. The theory that it is the task of the firm to increase the value of the firm and its shares for the owner of the firm only and that the management success is only measured by the attainment of this goal reduces the complexity of the management's obligation towards the common good of the firm.[7] All other goals of groups of firm members are rendered to be only means for the final end of the return on the owner's investment. The effect is that the management can exculpate itself from the responsibility towards the other groups of the firm.

The manager is not only the agent of the owners but at the same time the steward of all groups in the firm. This distinction between agency and stewardship holds true even more for the politician who has a democratic mandate. The politician cannot be seen as the agent of his immediate constituency only. He must accept that he has the duty of office towards the common good or of representation of all voters. Politics and management

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[6] Cf. also L. A. TAVIS: *Power and Responsibility: Multinational Managers and Developing Country Concerns*, Notre Dame, Indiana (University of Notre Dame Press) 1997.

[7] Cf. P. KOSLOWSKI: „Shareholder Value and the Purpose of the Firm",in: S. A. CORTRIGHT and MICHAEL J. NAUGHTON (Eds.): *Rethinking the Purpose of Business. Interdisciplinary Essays from the Catholic Social Tradition*, Notre Dame, Indiana (University of Notre Dame Press) 2002.

are an office that does not only include the duty towards furthering the interests of the principals, be they shareholders or voters or constituency, but that implies beside the immediate fiduciary duty towards the principal a duty of stewardship towards the common good. The interest of the principal, of the voter or the shareholder, and the interest of all people concerned, of the total voting population or of all employees of the firm, must be considered at the same time. There is no unlimited autonomy of the voter or of the shareholder as principals to define the duties of their agents, the politician or the manager.

By giving fiduciary power to a member of parliament or to a manager, the fiduciary of this power, the politician or the manager, cannot be obliged to neglect the public interest and to realize only the interest of his or her immediate principals. In the market as well as in politics, the consumer, the shareholder, and the manager representing them as well as the voter and the member of parliament representing the voter must understand their right to decide to be an office that aims at the public interest. The politician or the manager cannot understand themselves as autonomous lobbyists or fiduciaries only of that segment of the constituency or the firm that voted for them or employed them.

The idea of the public good and of the boundness of decision-makers in government and economic institution by it is not an idea imposed from the outside and in a normativist way on the principals' and the fiduciaries' individual self-interest, be they voters and politicians in the political arena or shareholders and managers in the market. The idea of the common good does not impose a situation of heteronomy on them. Rather, the idea of the common good demands the inclusion of the public interest in the enlightened self-interest of those that have power to decide. Powerful decision-makers can only realize their own and their principals' self-interest if the institutions they direct are flourishing. Decision-makers cannot reply to the objection that the public good of their institutions is not realized by replying that they acted only as agents of her principals. The politician cannot exculpate herself in cases of government failure by answering she only acted in the interest of the own voters that gave her their vote. The manager whose firm is becoming smaller and smaller while it pays high dividends to shareholders cannot justify his or her action by pointing to the fact that the interest of the shareholders have been realized.

The idea of the common good implies that the general or total interest of an institution is fulfilled. The total interest of an institution is to be derived from the nature of the task of the institution. The neglect of the common good leads to a violation of the total interest of an institution and therefore to functional friction and to the incomplete fulfillment of the task of the institution.

The idea of the common good of an institution shows that institutions cannot reach their optimal performance and due diligence without anticipating their common good in the self-interested decisions of the people acting in them. The interest on the realization of optimal performance and due diligence leads to acknowledging the inevitable task to consider as well the common good as the self-interest of its member in the governance of institutions, be they political or economic. The purely individualistic pursuit of goals in the market or in democracy without consideration to the public interest in the individual interests of those who have to make far-reaching decisions causes sub-optimality of the institution in question, the market or democracy.

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