Leadership and Ethics: Corporate Accountability to Whom, for What and by What Means?  

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ABSTRACT. This paper argues that ethical evaluation of leadership requires standards of assessment that are independent of the definition of “leader.” It suggests that Stakeholder Theory is incapable of providing a substantive standard of assessment. It suggests an alternative model for adjudicating between stakeholders’ conflicting claims of right and it applies that method to determine what responsibilities corporate management might have to employees and how management might be held accountable for discharging those responsibilities.

Despite the variety of views on leadership types (e.g., transactional, transformational, empowering, and change leadership), all leadership ultimately reduces to a dyadic relation between leader and follower. The first thing to note about that relationship is that “leader” is an achievement term that denotes some degree of success in eliciting collective behavior from others in pursuit of a goal to be achieved. However, there are ways other than leading to get others to act—compulsion at gun point for one example. So, in order to distinguish “leading” from simple coercion through force or threat, “leading” is taken to require some level of buy-in by followers to the leader’s goals and methods, strategies and tactics.

Some might use this need for followers’ buy-in as a reason for defining good (that is, non-morally good, successful or effective) leadership as inherently ethical, since, after all, the existence of such buy-in can be taken to denote respect for the autonomy of followers. However, the degree to which followers buy-in, and the mechanisms used to encourage such buy-in, can fall far short of those necessary for true consent. Historically, leaders have used psychologically manipulative tactics and deception to entice followers, tactics that are far from consistent with respect for the autonomy of followers as rational beings and tactics that are not compatible with morally significant levels of consent.

And, even if followers’ buy-in were achieved by methods compatible with true consent, that is at best a necessary and not sufficient condition for morally good leadership. It is certainly possible, for example, that followers freely adopt their leader’s morally corrupt value scheme. Thus, the moral status of a given exercise of leadership requires attention to the tactics used and the impacts on those who follow. It also requires attention to the impact on those who are merely in the way. After all, Alexander the Great was, by definition, a great, that is, effective, leader. Yet he was known for the intense brutality that he inflicted on some conquered populations.

So, clearly definitions of leadership which attempt to identify effective leadership with moral leadership are both stipulative and counterfactual. Joseph Stalin, Adolph Hitler, Rev. Jim Jones and Pol Pot show that powerful and effective leadership is compatible with extraordinary moral evil. The moral assessment of leadership requires the application of ethical criteria that are independent of the definition of “leadership.” Such criteria must be applied to the leader’s impact on all those affected. This means, in the
usual contemporary parlance, that an assessment of corporate leadership must address the leader’s impact on all corporate stakeholders.

We might, then, look to Stakeholder Theory for criteria by which to assess the moral status of leadership. Stakeholder Theory, after all, is the primary contemporary perspective that urges corporate leaders to consider the interests of all affected by the corporation. However, while Stakeholder Theory provides an attractive idiom emphasizing the need to extend the consideration of corporate leaders beyond the interests of shareholders, the theory, as is well known, has had substantial difficulty articulating just what specific interests of what specific constituencies must constrain the leader’s pursuit of corporate profit. Who counts as a stakeholder and which interests must be respected for those who so count are notoriously under-argued questions. For instance, employees are intuitively stakeholders but do all of their interests, e.g., their interest in a winning regional sports team, have a moral claim on management attention? Competitors, too, are obviously affected by corporate actions but should they count as a constituency which holds a legitimate claim against a firm’s management? Must management consider the damage done to a competitor’s market position when deciding on a marketing strategy? These questions show how little in the way of determinate advice is provided by a simple “consider stakeholders” prescription.

In fact, more recent work in Stakeholder Theory often sees it as a skeletal model of corporate responsibility, admitting a variety of conflicting specific answers to these questions. Ed Freeman, for instance, has suggested that Stakeholder Theory is best seen as a meta-theory that allows multiple instantiations which differ according to what he calls their respective “normative cores.” He explicitly states that attempts to fully define the content of “stakeholder theory” as such are misguided (Freeman, 1997). Recent work has also recognized that corporate obligations to those who have a stake in the corporation comprise only a subset of corporate obligations. Rob Phillips notes that Stakeholder Theory is best used for identifying persons who bear a special relationship to the firm because of their contributions. These special relations generate particular obligations of fairness on the part of the firm and its management. But these special obligations in no way exhaust the obligations of the firm (Phillips, 1997). There are other duties firms owe to individuals merely on the basis of those individuals’ moral personhood, duties all owe to all. Duties to stakeholders are merely added duties owed to those who are contributing participants in corporate activity.

As a result, what first looked as if it might provide a promising way of assessing the moral status of leadership, turns out to be of little help when we need specifics. And, even if, contrary to the preceding, Stakeholder Theory could identify just which interests of which persons need to be considered, it seems to lack any clear normative method for adjudicating between the inevitably competing interests (both of contributors and of those merely affected) that arise in corporate activities. A purely Utilitarian method, of course, could be employed to weigh competing interests. But then all the deficiencies of Utilitarian decision procedures arise. For instance, there is trouble finding a common measure by which to assess the various competing interests. On what common metric might we assess interests in money, power, security, and fulfillment? Most importantly, there is little attention paid to the claims of right that are the hallmark of most stakeholders’ demands.

Another apparently promising idea is found in those who argue that corporate leaders, just as leaders in the political realm, must be accountable to those whose interests the leaders effect (Brenkert, 1992). But, here too, an analysis of accountability requires us to specify precisely to whom, for what effects and by what means the corporate leader should be held morally accountable.

We need, then, a mechanism for adjudicating between the competing claims of conflicting parties. Since it is unlikely that a corporation could ever satisfy all the claims made of it, the best we could hope for is that the firm respect the legitimate rights of those who it impacts. This includes both the negative rights (rights to non-interference) and the positive rights (rights to receive goods or assistance) of those affected by corporate actions. However, rights claims, too,
frequently conflict with each other. In business, conflicts typically arise between owners’ claims and the claims of other constituencies. Owners claim both rights to control and rights to residual income. Other constituencies, such as employees, claim rights to things like severance payments that might limit both owners’ control and return on investment. What we need, then, is a method for identifying and adjudicating between the rights claimed by both owner and non-owner stakeholders. Such a method would move us toward answering questions about both the range of, and the process for, morally adequate corporate accountability.

A reasonable method for resolving such conflicts between right claims must directly assess the merits of the competing claims. Moreover, a reasonable method will do more than consider the relative importance of the conflicting rights in some general and abstract way. Rather, resolving conflicts between right claims requires us to focus on the particular cases where the conflict arises since the conflict between rights typically occurs in defined marginal areas. That is, rights conflicts are rarely such that giving precedence to one right in a given case of conflict will mean the full destruction of the other.

In order to grasp this point, consider a case to which we will shortly return in more detail: Some employee advocates claim that workers are entitled, as a matter of right, to due process before dismissal (Werhane, 1985). Such a right would clearly limit an owner’s ability to control who has access to corporate facilities. However, recognizing such a job security/due process right for employees will not eliminate all rights associated with property. It does not change anything about non-corporate property rights, nor will it even impact all aspects of corporate rights. It does not, for instance, interfere with the corporate property owner’s right freely to sell her shares in the market. Hence the debate is not over property rights in some general sense. It is over the correct understanding of the scope of property rights at their margin.

We can satisfy the requirements for a reasonable assessment of rights conflicts if we ask two questions of each of the competing claims made by stakeholders: (1) What are the justifying or foundational reasons for this right (why is it a right)? (2) What harm would be done to those underlying values if we recognized a conflicting right claim and thus marginally constrained the scope of a particular right? To continue with the above example of a specific conflict between owners and employees, we might ask “What are the foundations of property and job security rights?” and “What harm would be done to those respective values if we denied a right to job security and gave owners the right to terminate at will or, alternatively, if we denied owners that right and mandated a Just Cause or Due Process policy?”

In what follows, I will briefly sketch how this proposed method might help determine the obligations of firms to one set of stakeholders – their employees. Hopefully, the contours, if not the details, of an argument will appear, an argument capable of identifying how and for what firms should be held accountable to their employees. I think that the basic form of this argument can be transferred to the claims of other, non-employee constituencies as well.

Consider three rights often claimed by employees or their advocates: substantive due process before termination, severance pay in the event of a layoff, and participation in corporate governance. It is easy to see how each of these might conflict with more traditional pictures of the property rights of corporate owners. Each places limits, to greater and lesser degrees, on the ability of owners, through their agents, to control property and to profit from it. (As an aside, “greater” and “lesser” are important adjectives to note here. Too often, American commentators treat all extensions of employment rights as if they have the same consequences. This is decidedly not the case as I will explain below.) If we follow the proposed method of analysis, then, we can assess these competing rights claims by inquiring into their respective justifying values.

Private corporate property rights have traditionally been justified by appeals to utility, autonomy and fairness. In utility arguments, private ownership is touted as more efficient because, as Adam Smith said, individuals privately pursuing their own gain will be led, as if by an invisible hand, to produce a greater common
good. The private marketplace, it is held, imposes a discipline that forces the most efficient use of resources. Moreover, the possibility of privately acquiring property is lauded as providing valuable incentive for work effort, with the consequence that overall productivity increases.

Almost a century before Smith, John Locke defended private property for the contribution it makes to a person’s independence. In Locke’s account, secure possession of land can help you to sustain your own life and to escape, to some degree, the control of others. Hence, property can be a device for increasing autonomy.

Locke also argued for property as the fair return for effort expended (and perhaps for risks taken). Again, using an agrarian example, he suggested that a person who cleared, tilled and planted unimproved land had a moral claim to the fruits of those labors.

Interestingly, the claimed employee rights of due process, severance and participation can be defended on these very same grounds. It doesn’t require much imagination to see how workers with rights to severance, or with guarantees that they will be fired only for cause, gain in autonomy because they have greater economic security and, hence, increased ability to control their lives. Participation rights also can give workers greater control over important decisions which inevitably impact their lives. All three rights have been argued as providing a fair distribution for the workers’ contribution and risk exposure at work. And, finally, some suggest that utility would be increased by these employment rights both because the workers will be better off and because happier workers will be more productive.

While this is not the place for a careful and detailed assessment of these competing rights claims, we can see that such an assessment will turn on the respective impact on autonomy, on fair treatment and on utility if one of the competing rights were recognized as taking primacy. To what degree, for example, would owners’ autonomy be damaged if workers had rights that assured them a voice in the running of the corporation? To what degree would employees’ autonomy be lessened if they had no such right? Clearly, answers to these questions will involve issues of fact and judgments of relative significance.

Clearly, also, each particular conflict (property vs. severance, property vs. due process, property vs. participation) will need to be assessed separately. For it is likely that providing due process assurances would have a different impact on relative autonomy or utility than would guaranteeing substantial severance in cases of redundancies. For instance, severance guarantees predictably raises the cost of labor in a way that due process guarantees do not. Severance might thus have greater impact on demand for labor (and thus on employment levels and on overall social utility) than does due process protection. I say “might” here because labor costs, as Jeffrey Pfeffer argues, need to be considered in light of any potential systemic benefits that may accrue due to admittedly more costly policies (Pfeffer, 1998). This shows that we need to address separately each proposed expansion of U.S. employee rights and not tar all proposals, as did Reagan, with the prospect of Eurosclerosis.

Even granting that this is not the forum for careful assessment, we might be able to suggest that in the case of each pair of competing rights, the approach which best promotes the respective underlying values is the approach which extends new (at least for the U.S.) rights to employees. The impact on the autonomy of owners may be small, given that the recognition of such rights only limits the scope of property rights and does not destroy them. The autonomy benefit of corporate ownership comes primarily through the wealth brought by holding shares. There is substantial evidence that neither due process protections, guarantees of severance, nor carefully crafted employee participation need cause decreases in firm performance. In fact, there is emerging evidence that the best performing labor systems possess all three characteristics. For instance, significant research (of both empirical and theoretical sorts) finds that uses of contingent “pay for performance” compensation schemes and flexible staffing policies works best when embedded in a labor system which includes both conditional job security and substantial employee participation. (See, Abraham
and Houseman, 1994; Buechtemann, 1993; Ichniowski, 1992; Levine and Tyson, 1990; Pfeffer, 1998; Freeman and Lazear, 1995; Freeman and Rogers, 1993; Regalia, 1995; Rogers, 1995) Properly structured employee rights, then, need not cause inefficient labor market rigidities nor need they cause declines in productivity per worker. (Empirical research also tells us we should be careful before accepting the hypothesis – and it is a hypothesis only – that Europe’s relative economic and employment woes are due primarily to its more protective labor market institutions.)

Workers with these three rights, however, gain substantially increased economic security and the independence that accompanies such security. When workers need not fear that they might lose a job without cause, when they have the guaranteed cushion of severance should the economic need for their services disappear, when they have serious voice in the creation and implementation of corporate policy, then they have much greater ability to control their lives.

Of course, some might argue that employees already have this control because they can freely contract for whatever rights they desire. This response, however, suffers from a number of defects. First, it is not clear that employees have the bargaining position to achieve these rights in the marketplace. Most of us economically depend more on our jobs than our employer depends on us. Second, and more importantly, this response presupposes that employees must buy these rights from ownership. That presupposition merely begs the question. For here the very issue in dispute is over the acceptable scope of ownership rights. It will not do to assume that rights to fire at will, to dismiss without severance, to full control over decision making are included in property rights when what we are trying to decide is if such an understanding of property advances autonomy better than vesting workers with those rights to due process, severance and participation. After all, with such vesting, we might say in a similar vein that owners are free to pay employees to relinquish those three rights. The response that employees are free to bargain for these rights simply cannot answer the question about which initial distribution of rights best advances the value of autonomy.

(Here, opponents of this type of argument often resort to the Coase Theorem which claims that in exchanges with low transaction costs, the initial assignment of rights has little impact on final distributions or efficiency. The claim is that, in a case like this, workers and employers will simply automatically find themselves bargaining to the most efficient distribution. The appeal to Coase, however, is problematic for a number of reasons. First, the assumption of low transaction costs may not be accurate. Levine and Tyson (1990), for instance, show how there can be impediments that prevent bargaining to the optimal results. Second, recent work in behavioral economics (e.g., Millon, 1998) calls attention to an “endowment effect” under which those given an initial endowment of a right tend to value the right more than do those who do not initially possess the right. The consequence is that initial rights endowments will matter in determining the actual outcome of a bargaining, contrary to the Coase Theorem’s assertion.)

The question of respective impacts on fairness can also arguably be settled in favor of the three employee rights. Whether one looks to contribution to the firm or to risk, fairness is enhanced by recognizing the three rights for employees. Recent work in management and industrial relations, for example, has emphasized that the crucial resource for gaining sustainable competitive advantage is the possession of a skilled and committed workforce (Pfeffer, for instance) Employees’ contribution to the success of the firm is substantial, then. Employees’ risk exposure is also substantial. Not only do they experience risk to physical and mental health on the job, they, without due process, severance, or participation, carry the risk of economically devastating job loss. Even in the tight U.S. labor markets, employees who lose jobs suffer long, perhaps permanent, periods of relative income loss (Blair, 1995). Owners, on the other hand, typically have diversified portfolios that reduce the risk of losses from any one investment.

I don’t think it will do, either, to suggest that labor markets guarantee that remuneration is fair and adequate for employees’ relative level of con-
tribution and risk. First, there are reasons for believing that employees have relied on representations of employers that dismissal will only be for cause. Courts, in fact, have in the past found an implied contract exception to the ruling U.S. doctrine of employment at will. (Unfortunately, that judicially created exception has little import anymore. Courts have accepted that a signed waiver indicating an understanding that employment is at will is sufficient to rebut the implied contract.) Some have argued that reliance can lead to legitimate expectations of continued employment (Singer, 1988). Second, recent work on internal labor markets suggests that some wages are deferred in return for a promise of continued employment, a promise that is subject to predatory employer abuse. For instance, there is some evidence that employees are paid less than their marginal contribution early in their careers. That pay structure can be a device which benefits firms by reducing monitoring costs and making quitting more expensive. The deferred compensation bargain, however, is not a legal contract and is subject to employers reaping benefits without having to pay for them – as when workers are dismissed without cause or laid off without severance (Blair, 1995; Weiler, 1990). For these reasons, it is not easy to assert that employees have been fully compensated for their contributions and risk.

Participation rights in corporate governance, too, provide workers a potentially significant guarantee that their interests are heard and are treated fairly. Without such rights, corporate decisions are subject only to the dictates of one constituency – shareholders. And we have enough experience to know that there are possible forms of substantial employee participation which will not damage return to shareholders but rather will lead to increased productivity (Freeman and Lazear, 1995; Regalia, 1995; Rogers, 1995). Freeman and Lazear, for example, catalog a number of potential productivity benefits of employee participation, including moderated wage demands, greater worker provided information, greater employer-employee cooperation, and greater willingness of workers to invest in the firm and to take a long term perspective.

Third, and finally, the empirical research referenced above suggests that considerations of utility, just as those of autonomy and fairness, might point in the direction of granting employees rights to due process, severance and participation. Since carefully structured and inter-related employment policies can reinforce each other and can lead to increased productivity, there seems little in the way of collective welfare considerations that might provide a basis for rejecting these three rights out of hand.

One ending caution about these defenses of employee rights: The analysis has throughout presumed a context of moderately large, publicly traded corporations. If, however, we change the context and consider smaller, privately held business, the autonomy, fairness and utility impacts of these rights might change. There may be reasons for thinking, for example, that due process guarantees have a different impact on autonomy for the corner, mom-and-pop grocery. If that is the case, perhaps some size limitation in the application of employment guarantees would be in order.

Whatever decision we reach about that application question, it should not obscure the basic point. The point here was to sketch a process of analysis for deciding to whom, for what and by what means corporate leadership should be accountable. Using the above line of argument as a model, I think we can develop a method which will allow reasoned and specific decisions about those questions of accountability. That method directs us to identify the competing rights claimed by those involved in or affected by corporate activity. It then requires us to discover the justifying values for the respective rights and to determine which right, if acknowledged in the marginal sphere of conflict, would do least damage to those foundational values. I’ve suggested that when applied to employees, the method may generate reasons for holding both that corporate leadership be especially accountable in the area of job security and that the method of accountability be one which gives employees a direct say in leadership decisions.
References


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