

Are Corporations Political Institutions?

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Negative Public Effects of Corporate Action

- Tax evasion (3 billion per year in the NL) – and tax competition between countries
- Executive pay discussions
- Wage/capital ratio

-> Corporations as a public problem

Public Expectations for Corporations

- Public Problems, Corporate Solutions:
 - Sustainable ecological development
 - Healthy ageing
 - Workplace diversity
 - Etc. etc.

-> Corporations as part of public solutions

Corporate Power

- Big 5 tech companies, market power and data power
- Shareholders and hostile take-overs

-> Corporate power/politics as an unavoidable dimension

Overview

1. Are Corporations Public or Private Institutions?
Refining the Question
2. The Transformation of the Market into a Public Domain
3. Corporations as Quasi-Public Institutions
4. Towards a Constitutional Democratic Framework for Corporations

What is a corporation?

	Market actors	Non-market actors
Non-incorporated groups	Partnerships	Family
Incorporated groups	Business corporations	Foundations, associations, state

Part 1

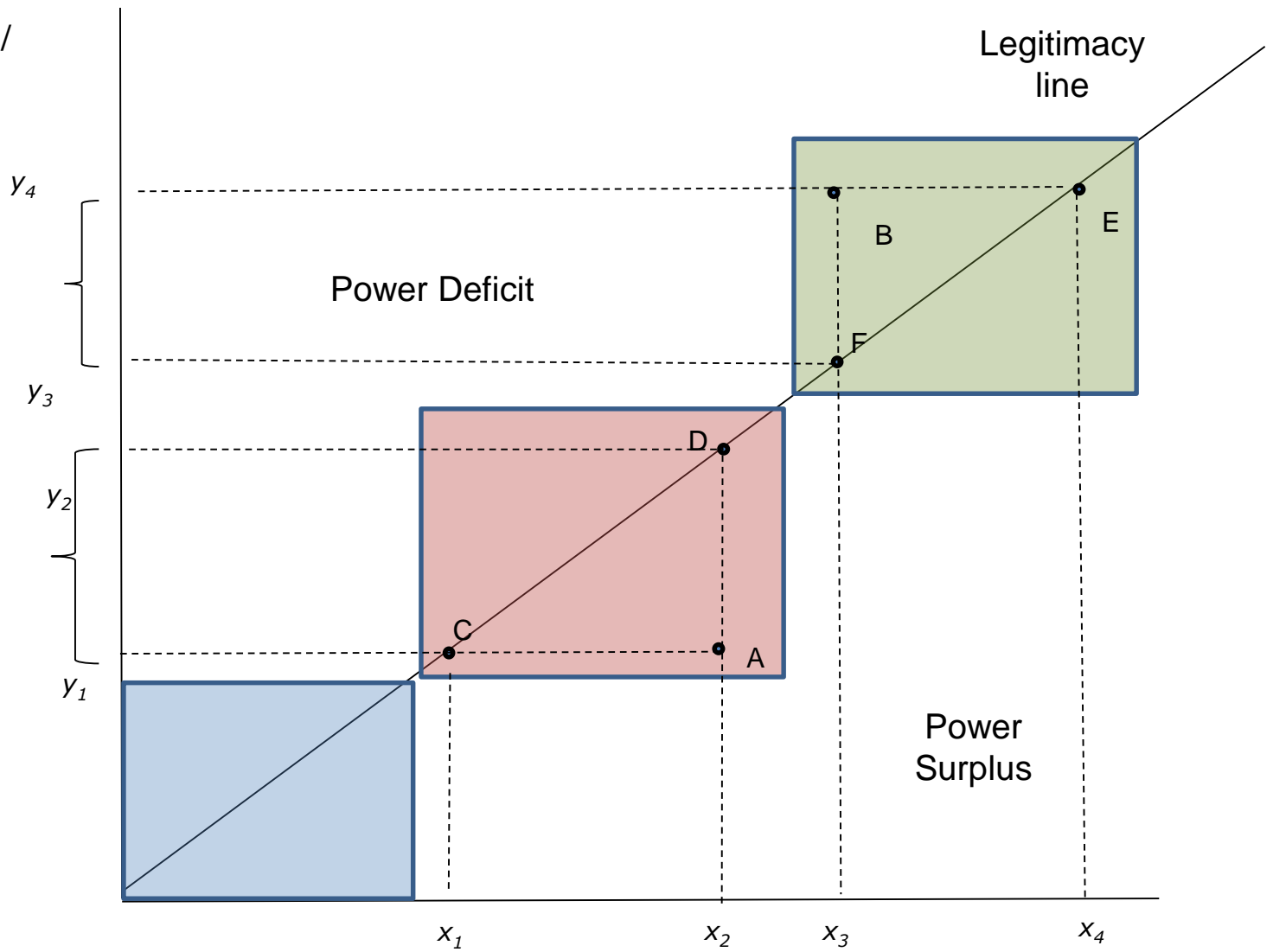
Are Corporations Public or Private Institutions?

Refining the Question

Duties/
Responsibilities/
Accountability

*State
legitimacy
deficit*

*Corporate
legitimacy
deficit*



Power
Surplus

Rights/
Capacities/
Span of social influence

Three features of a public institution

1. It has *collective effects*: effects on one/some persons versus effects on all persons (scale).
 2. It protects/promotes *collective interests*. These are not amongst its restrictions but amongst its aims.
 3. It acts according to a *collective mandate*: is embedded in a hierarchy of constitutional-democratic norms and mechanisms of accountability.
- -> Concept of a **quasi-public institution**: 1+2, but not 3. Such an institution is illegitimate (off the legitimacy line).
 - -> Our question becomes: are corporations (quasi-)public institutions -> do they have collective effects/promote collective interests?

Three positions on the publicness of corporations:

- 1) NO: Corporations are private because the market is private.
- 2) YES: Corporations are public, because market action has a public aim.
- 3) YES: Corporations are public, because of their special features.

1 = dominant answer in our society, but false.

2 = second part correct, first part not -> PART 2

3 = correct answer -> PART 3

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Responsibilities/
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*State
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y_4

y_3

y_2

y_1

Power Deficit

Legitimacy
line

Power
surplus

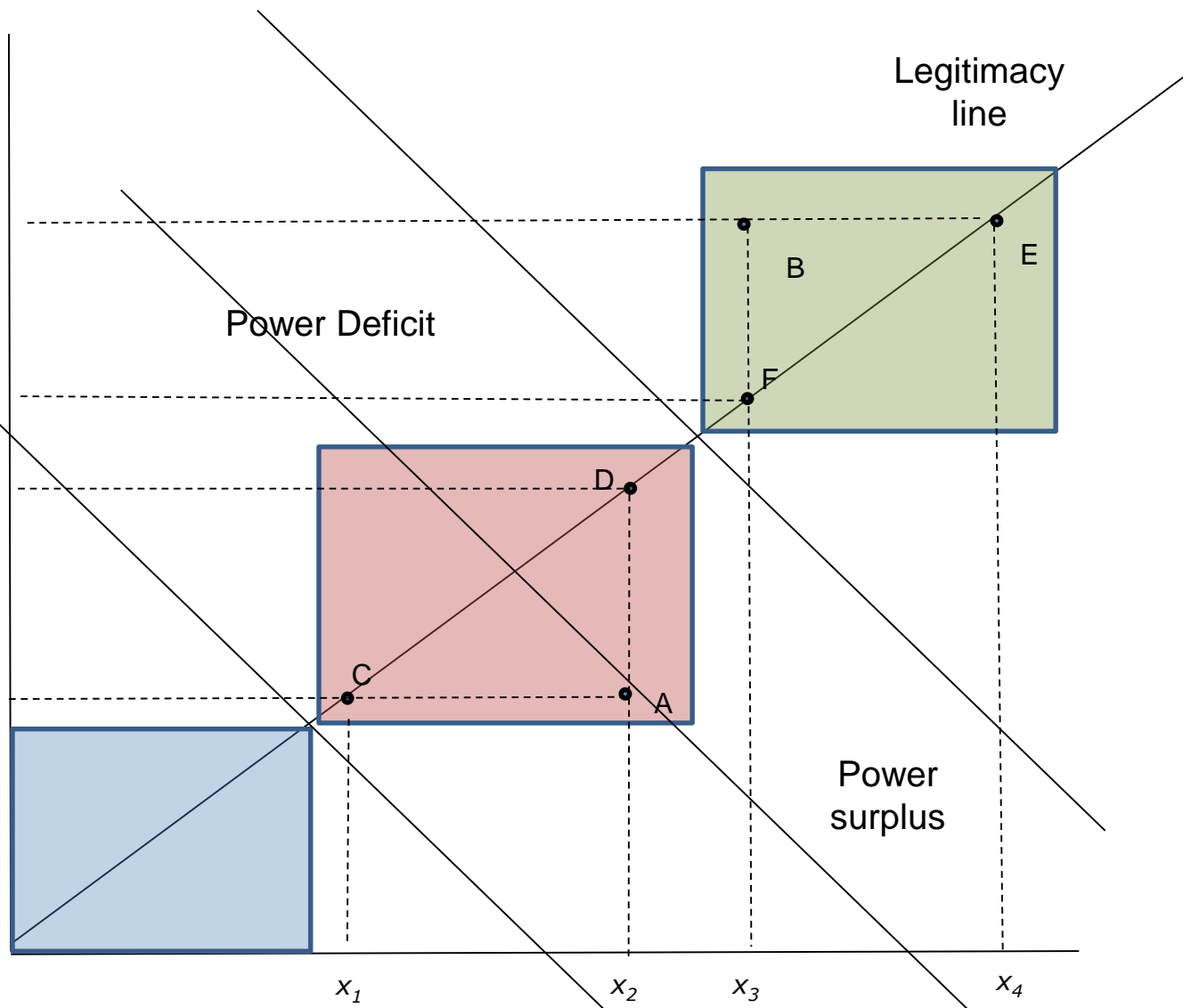
x_1

x_2

x_3

x_4

Rights/
Capacities/
Span of social influence



Part 2:

The Transformation of the Market into a Public Domain

Two Dominant Theories in Business Ethics

- Shareholder Theory: aim of corporations is to maximize shareholder value.
 - Fiduciary duty of managers
 - Only obligations are those of law and custom.
- Stakeholder Theory: aim of corporations is to balance interests of all stakeholders
 - Different views of who these are: how to decide?
 - Unclear how to balance their interests?
 - But key point remains: concept of *social wealth*

New developments in Business ethics

Shareholder Theory 2.0:

- “Enlightened Wealth Maximization”: accepting social wealth as aim
- Claim: Focus on shareholder value maximizes social wealth.

Market Failure Theory:

- There are always market failures (so link doesn't work) – e.g. externalities like pollution
- Solving market failure as aim of public regulation
- Governments fail to regulate (e.g. globalization)
- Fair play norm: **not exploit this market+regulatory failure** when maximizing shareholder value

Intermediate conclusion about Business Ethics

- Consensus about the ends of market actors:
social wealth maximization
- Dissensus about the means:
 - Shareholder value maximization, or
 - Remedying market failures
- For both theories: all this remains a matter of *private* actions

The Variable Publicness of the Market

- Acceptance of ‘social wealth maximization’ as aim of market domain -> market has ***public function***.
- Objection: this does not make individual market players public institutions.
- Reply: that ***depends***, i.e. on whether there are market failures – then market players must balance public interests to determine maximum social wealth.
- Conclusion: a purely private market is conceivable, at least theoretically, in the absence of market failures.
- But.... this is not what we see. Why not?

The production of market failure

- 1) Players *want* to produce market failure: this is in their competitive interest.
- 2) Players *can* produce market failure: this is made possible by the legal tool of creating corporations -> *to be shown in PART 3!*
- NB For same reasons/with same means, players want to and can also produce regulatory failure: corporate influence on capacities for state regulation (rules of the game).
- Conclusion: corporations as public institutions when they produce market failures, so that they must start making public decisions.

Part 3:
Corporations as Quasi-Public Institutions

The Middle Ages: A World of Corporations

Guilds

Towns

Monastic orders

Universities

The first business corporations:

The Dutch and British East India
Companies (17th century)

Characteristics of a corporation

1. legal personhood: ability to contract and own property as a (natural) person – the birth of a legal fiction
2. granted by the state: a charter of incorporation
3. for a specific public purpose! (-> collective interest)

Characteristics of the business corporation

1) Entity shielding

2) Limited liability

Investors/
shareholders

4) Control right:
election of the board

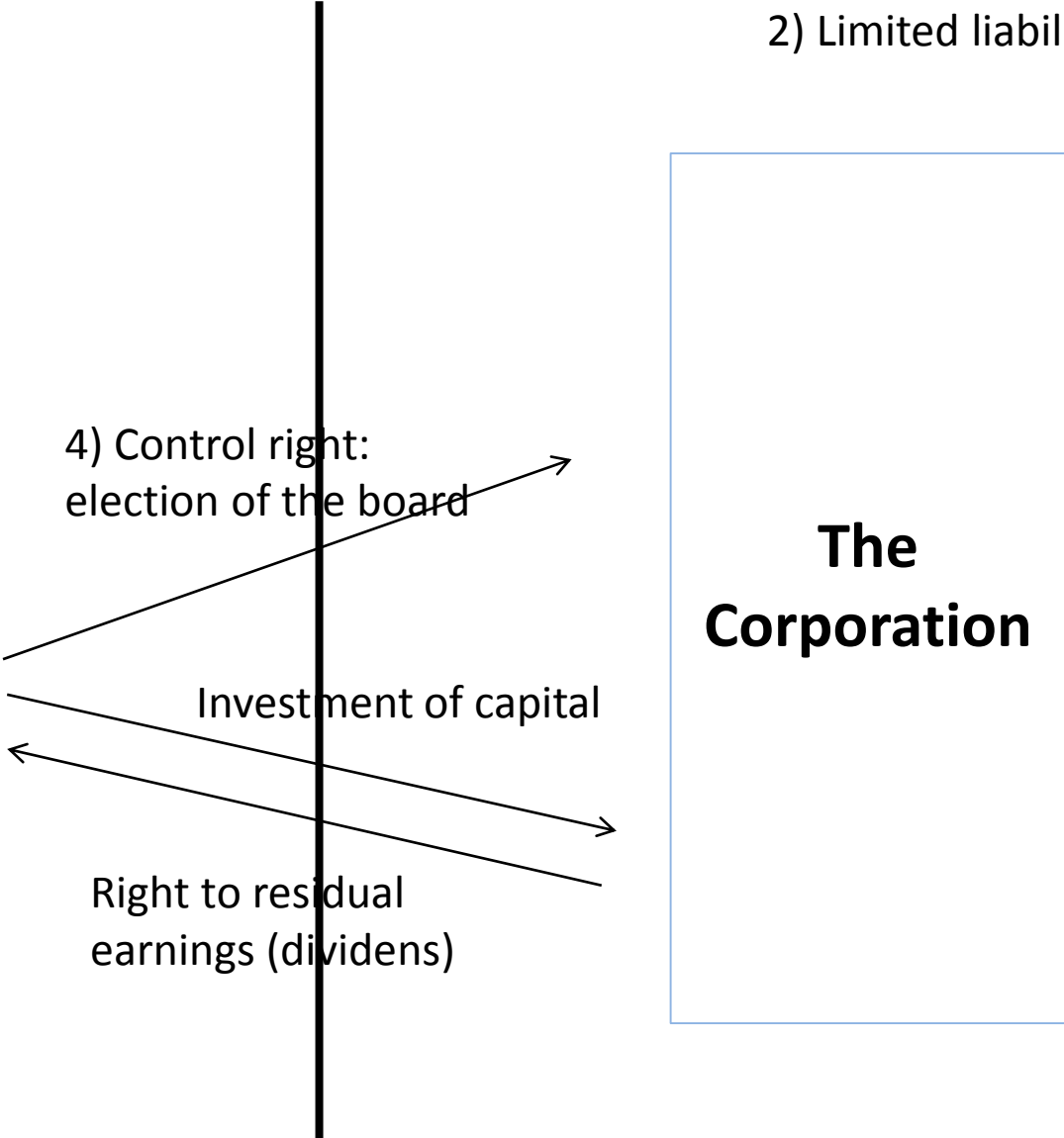
**The
Corporation**

Investment of capital

3) Asset lock-in

Right to residual
earnings (dividends)

5) Transferable
shares



Effects of the corporate form

- History: in 1840s new laws in UK/US giving freedom of incorporation
- Hence: no public purpose required any longer
- + a massive pooling of capital for a single purpose
-> efficiency gains from scale effects
- - loss of responsibility -> opportunities for irresponsible behavior

Limited liability – a moral matter?

Until its passing, argued Edward Cox, the editor of *The Law Times*, the law of partnership had been:

. . . that he who acts through an agent should be responsible for his agent's acts, and that he who shares the profits of an enterprise ought also to be subject to its losses; that there is a moral obligation, which it is the duty of the laws of a civilised nation to enforce, to pay debts, perform contracts and make reparation for wrongs. Limited liability is founded on the opposite principle and **permits a man to avail himself of acts if advantageous to him, and not to be responsible for them if they should be disadvantageous; to speculate for profits without being liable for losses; to make contracts, incur debts, and commit wrongs, the law depriving the creditor, the contractor, and the injured of a remedy against the property or person of the wrongdoer, beyond the limit, however small, at which it may please him to determine his own liability** (Cox, 1856, pp. i–ii)

(quoted in P Ireland, 2010, p. 844)

Part 4:

Towards a Constitutional Democratic Framework for Corporations

Four core principles of legitimacy in a constitutional democracy

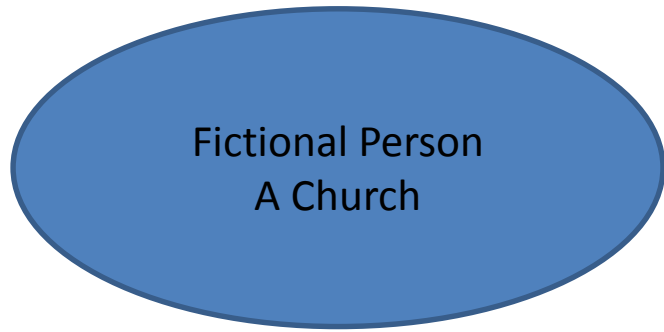
Q: how to render the exercise of corporate power legitimate? (bringing corporations back on the legitimacy line)

The exercise of public power is legitimate when it is...

1. ...**bound by law**: separation of person and office -> valid authorization
2.restricted by **fundamental rights** of citizens (constitutional or human rights) -> mandate
3.dispersed over various institutions: **separation and balance of powers**
4. ...checked by **democratic** mechanisms of accountability

Thomas Hobbes (*Leviathan*, 1651)

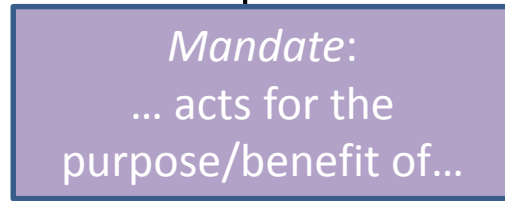
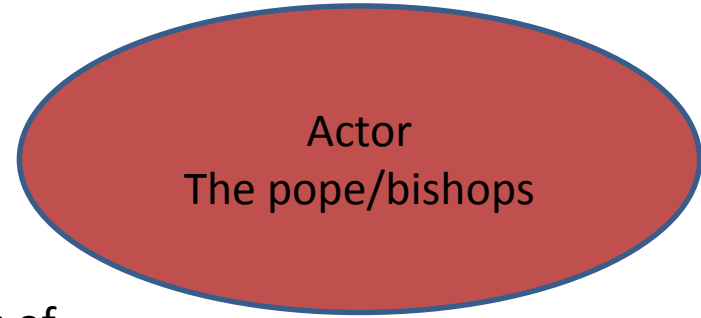
- Legitimacy of exercise of power x over y: matter of correct authorization of y by x.
- Authorization relation:
 - Author (fictional person) authorizes actor (natural person) to represent him.
 - Actor represents author. Actor has ‘authority’ to act on behalf of author; however, responsibility for these acts remain with the author (attribution).
- Problem: authorization for groups.



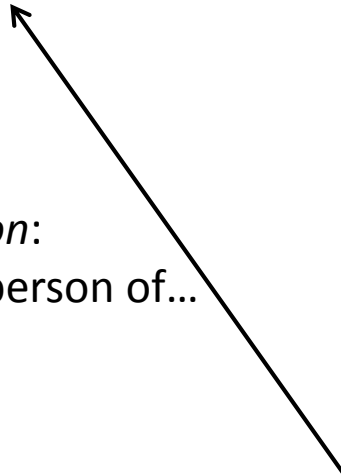
Representation:
... acts on behalf of ...



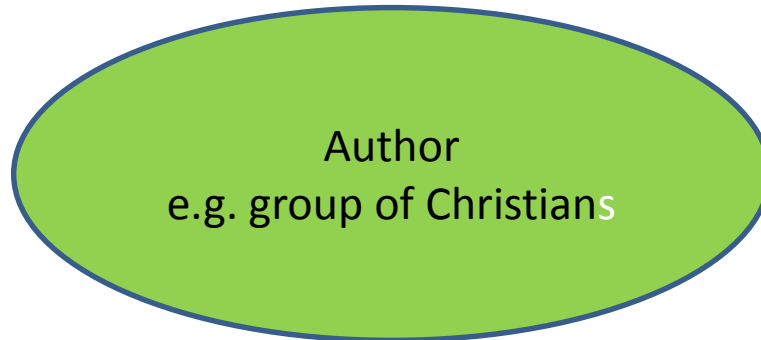
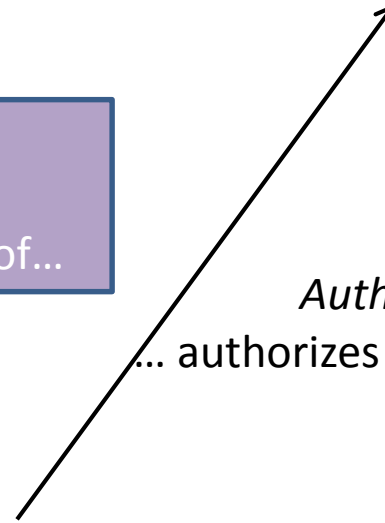
Attribution:
... is responsible for the acts of...

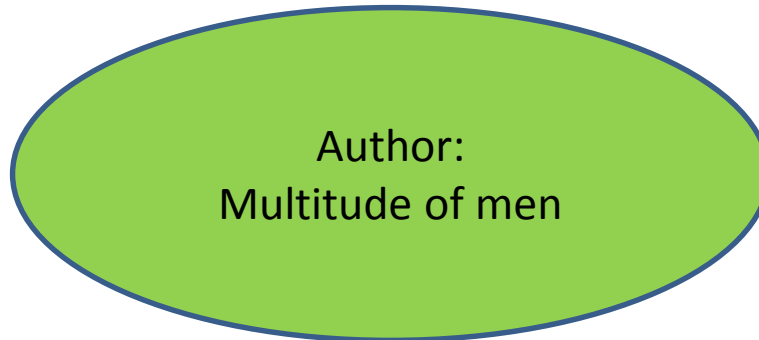
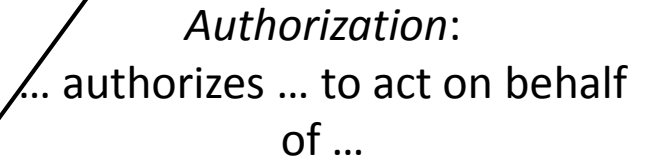
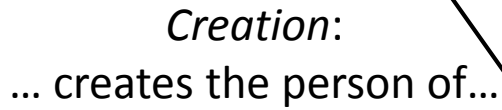
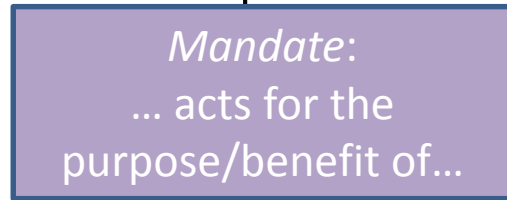
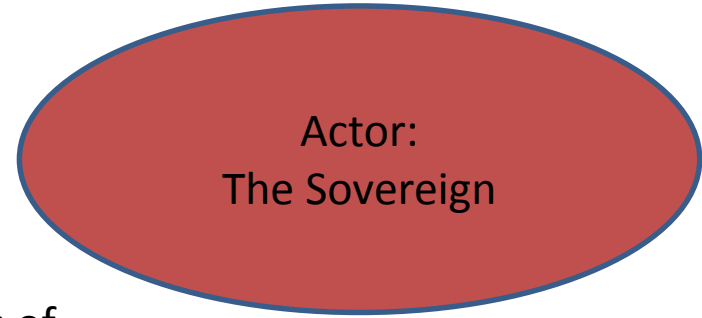
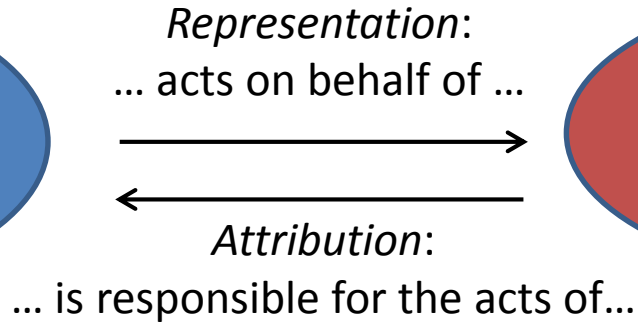
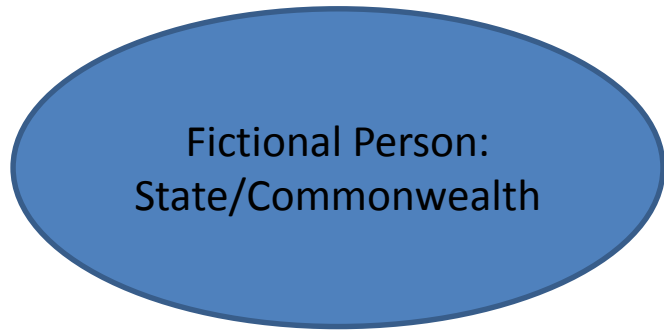


Creation:
... creates the person of...



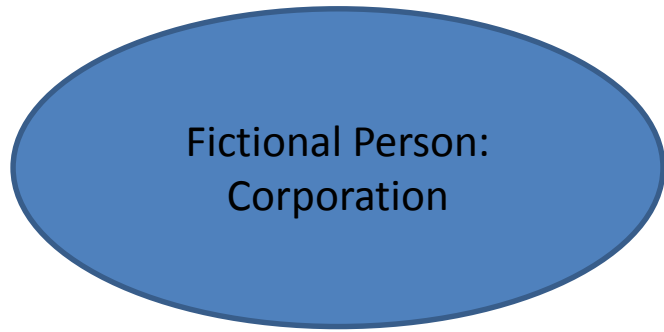
Authorization:
... authorizes ... to act on behalf
of ...





Two Criteria of Legitimacy

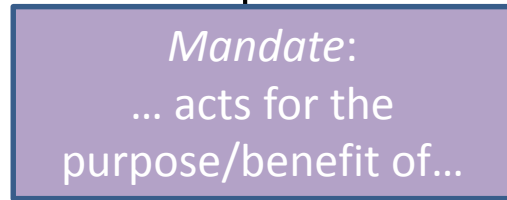
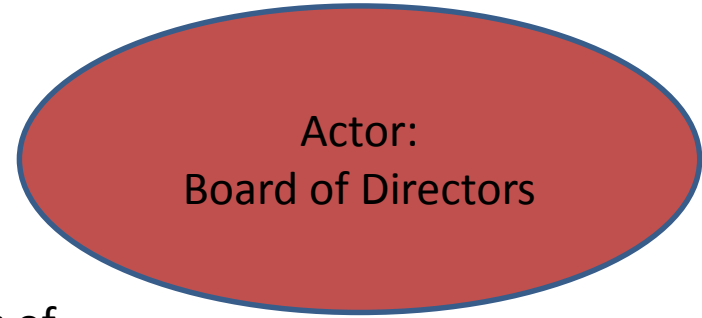
- 1) Formal criterion: A valid act of authorization
 - In Hobbes: people consent to submission to the sovereign's will. Duty not to interfere with his acts.
- 2) Substantive criterion: given by the mandate.
 - In Hobbes: 'whatever is expedient for their Peace and Common Defence' - almost unlimited mandate.
- Later developments: fundamental rights and democratic accountability.



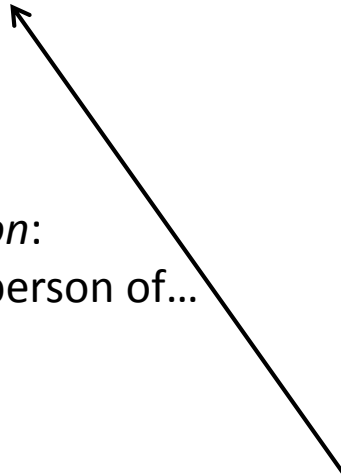
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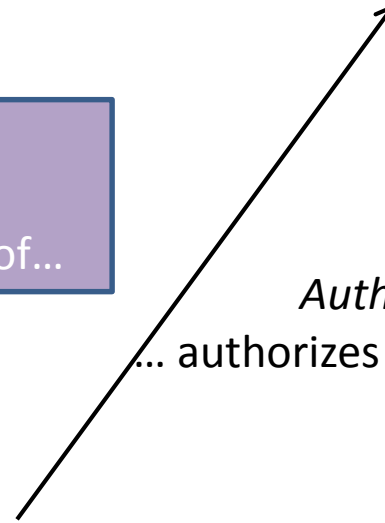
Attribution:
... is responsible for the acts of...



Creation:
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Authorization:
... authorizes ... to act on behalf
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What about the corporation?

- Hobbes distinguishes two types of collectives:
 - Absolute/independent collectives: the sovereign
 - Dependent/subordinated collectives: ‘Subordinate to some Sovereign Power’, in turn subdivided in:
 - ‘Bodies Politique’: e.g. colonies, towns, universities, companies of merchants – authorized by ‘Letters from the Sovereign’
 - ‘Persons in Law’: e.g. family, represented by the Father
- Hobbes’s scheme creates the familiar liberal dualism: Intermediate collectives are *either assimilated to private or to public authority!*
- Corporations as challenge to the sovereign: they are ‘many lesser Commonwealths in the bowels of a greater, like wormes in the entrayles of a natural man.’

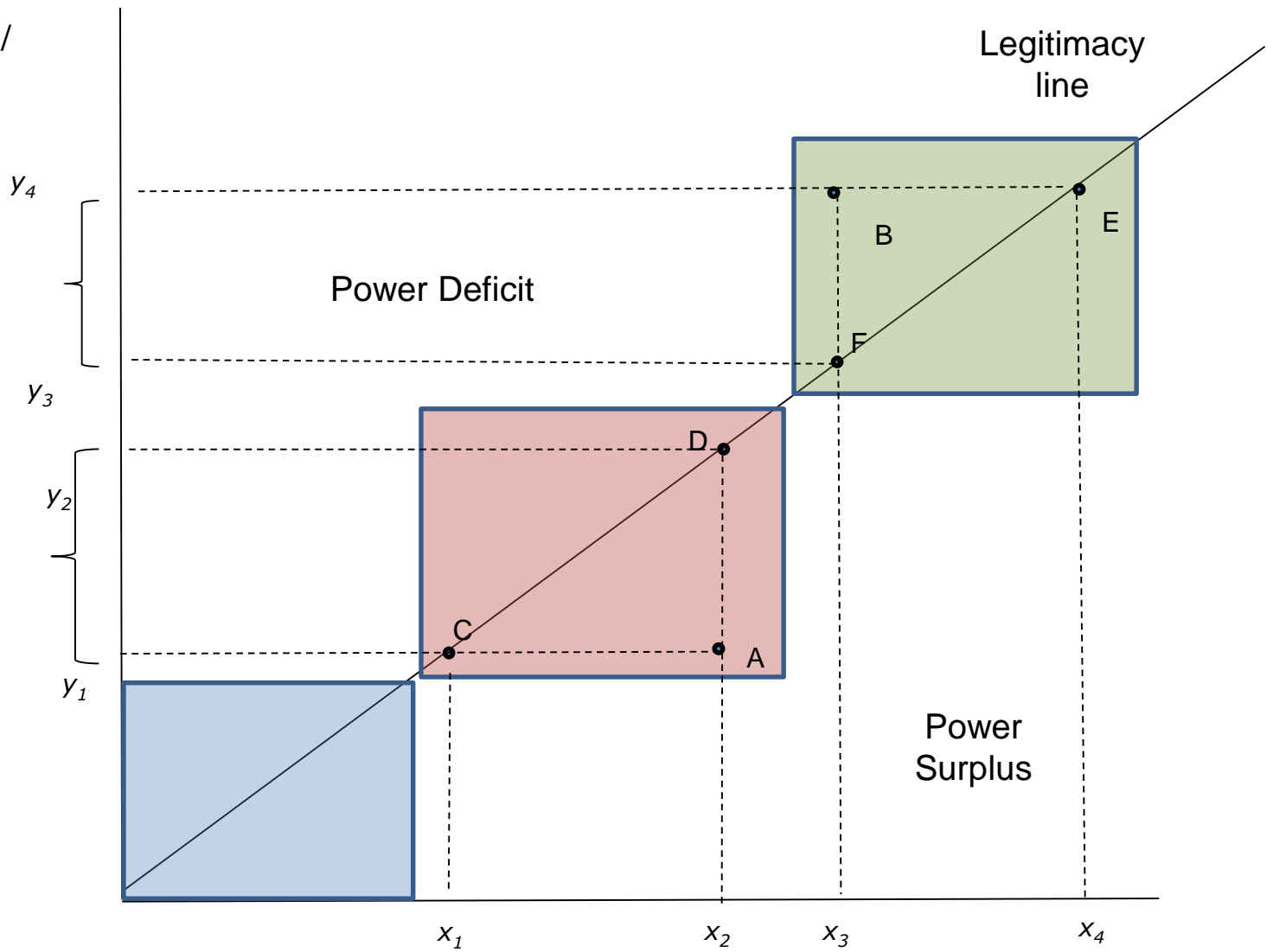
Fitting the Corporation into Constitutional Democracy

- Bound by law: back to public act of incorporation?
- Restricted by fundamental rights: but checked by whom?
- separation & balance of powers?
-> role for non-market associations?
- Subjected to democratic mechanisms of accountability: but by whom?
- Or.... abolishing the (privileges of) the corporation altogether?

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Conclusions

1. Are Corporations Public Institutions? Matter of (i) collective effects, (ii) promote collective interests (iii) a collective mandate?
2. Corporations share in the market's public interest of social wealth maximization when there is market failure – which they can produce themselves.
3. Corporations as Quasi-Public Institutions: corporations have special legal privileges which increase their ability to have large-scale, collective effects (power).
4. Towards a Constitutional Democratic Framework for Corporations: Application to corporations of the four key features of Public Legitimacy.

Thanks for your attention