The Stakeholder Concept of Corporate Control Is Illogical and Impractical

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Existing criticisms of the stakeholder concept of corporate governance, centering on the threat to private-property rights that it poses and the distortion of traditional notions of accountability in the firm that it entails, are highly persuasive (Barry 1998; Sternberg 1999). Still insufficiently recognized, however, are the *logical* flaws in the stakeholder argument. It is a serious defect of stakeholder methods of decision making that were a firm to adopt them, bad decisions would result. However, an equally serious defect is that no decisions at all might result or that the decisions reached might not reflect the values regarded as integral to the stakeholder idea. The whole stakeholder theory is vulnerable to a logical problem that has long been a feature of democratic theory and practice. This paradox was formally demonstrated by Kenneth Arrow (1963) in 1951, although it had originally been identified much earlier by the Marquis de Condorcet, the French Enlightenment thinker who died at the hands of the French revolutionaries.[1] It has perplexed democratic theorists ever since.

Business practice and business ethics are subject to intellectual strictures that belong to political philosophy because the predominant motive of much business ethics is to *politicize* or *democratize* the corporation—to take power away from the stockholders and to vest it in more inclusive groups. It is no coincidence that supporters of the stakeholder idea frequently use the term *constituencies* to refer to the groups that they think ought to have an influence on corporate governance (Kuhn

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1. Condorcet's idea has been revived from time to time. Before Arrow, Lewis Carroll, the nineteenth-century English writer and logician, had rediscovered it.

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and Shriver 1991, chap. 3), as if the members of such groups were equivalent to the voters in a representative democracy. If this claim is the primary motif of stakeholder theorists, then it is perfectly permissible, indeed obligatory, to attack the doctrine with all the artillery of orthodox social science and democratic theory.

Stakeholder theory is normally confined to academic theories of business ethics, although most publicly held corporations regularly pay some obeisance to it in their annual reports and public pronouncements. Still, as we know from environmentalism and other public-policy matters, abstract academic doctrines have a habit of reaching government and even, perhaps especially, company boardrooms. Ultimately they have an effect on business, usually adverse. The stakeholder theory is especially important because if it were applied in practical business, it would involve a radical departure from traditional methods of corporate governance. Not only would it amount to an additional cost imposed on the stockholders, as other socially oriented business policies do, but it would also completely overturn customary methods of decision making in a company and might well make capitalist enterprise impossible. The stakeholder movement wishes to reorganize companies so that the decision-making procedure would not be geared toward the maximization of share value, but instead resources would be shifted to satisfy any group or coalition of groups that could claim influence in and reward from the company irrespective of ownership claims or the lack thereof.

I am dealing here with Anglo-American business,[2] in which the stakeholder doctrine has not had much practical success, though it poses a long-term danger. To some extent, stakeholderism has historically been a feature of business in Germany, where trade union representatives sit on the supervisory boards of companies (although owners have the ultimate decision-making power), and also perhaps in Japan. Both economies have at least one thing in common that makes them appropriate models for stakeholder theory: their indifference to share value, especially in Japan, where the nominal owners of companies are virtually excluded from the decision-making process. Both countries traditionally have been hostile to the takeover mechanism, which in the Anglo-American economies is the primary method for the discipline of managers and the enforcement of the ultimate rights of ownership. Recently, share ownership has widened in Germany, and a spectacular takeover (to be discussed later), with its strong Anglo-American overtones, has occurred, but the German corporate economy still differs from the economies in English-speaking countries.

Governance of the Anglo-American Corporation

Before we can analyze the logic of stakeholderism and its deleterious effect on the traditional corporation, we must briefly consider the main features of the Anglo-American

2. Anglo-American capitalism is individualistic, concerned with profit seeking, and conducted largely by anonymous agents. It is feature of common-law countries and those that use the English language.

firm, especially its authority structure. This type of corporation is a collective body, or artificial person, recognized by law. At one time, its personhood was limited to civil law, basically in relation to torts and contracts, but in recent years, especially in the United States, corporations have been held *criminally* liable in certain cases. Now boards of directors may be personally responsible for criminal actions, and stockholders may be liable for the extraordinarily heavy fines that sometimes result. Ironically, it is difficult to imagine stakeholder theorists favoring this legal situation, even though their doctrine implies that responsibility must be shared by groups who may not be owners. Surely they would not want their favored "constituencies" to be held liable for criminal actions.

People form the collective entities called corporations to acquire wealth, although corporations might have other purposes (as they did historically in both Britain and the United States): the articles of incorporation specify the entity's precise purposes. The modern corporation has an economic rationale first identified by Ronald Coase (1937), although he was actually dealing with "the firm" in general, not necessarily with the corporate firm. He showed that because of transactions costs, it would be inefficient to conduct business entirely through pure market relationships, in which every individual deals with every other individual on a contractual basis; therefore, the firm operates by means of an authoritarian management structure designed to reduce transactions costs. In the modern corporation, persons are not linked to each other by a series of individual contracts (multilateral contracting); instead, they are tied to the firm by a single, bilateral contract—the "master-servant" relationship par excellence. Of course, in widely held corporations, the separation of ownership and managerial control, with the shareholders being largely passive, produces an "agency problem." How do the principals, the owners, ensure that their agents (employees from top managers down to shopfloor workers) work for the company and not for themselves by shirking on the job, cheating, stealing, and so forth? For lower-level personnel, the ultimate threat is dismissal, which is especially effective in a regime of "employment at will" contracts.[3] For top managers suspected of indolence or "rent seeking,"[4] the takeover threat may be necessary (takeovers often result in job losses at the higher levels). Short of these sanctions, the firm has the authority and a power structure to enforce day-to-day discipline. Of course, transaction costs may change over time. In recent years, for example, working from home has become more common, and use of the Internet in the "information economy" has fostered greater resort to individually negotiated and often short-term contracts. Hence, the large-scale public corporation and its bilateral contracting

3. "Employment at will" contracts allow either side to terminate the agreement with little or no warning or justification. They have withered somewhat in United States in recent years and do not exist at all in Europe, which is replete with laws relating to unfair dismissal.

4. Rent seeking is the attempt of some agent(s) to capture the wealth created by others. Stakeholder firms would encourage rent seeking on a grand scale.

may be in decline. In such a new commercial world, what meaning would attach to "the social responsibility of the corporation"?

In the conventional structure of the firm, the nexus of rights comprises *residual rights, control rights,* and *decision rights* (Ricketts 1994, chap.4). The residual rights, held by the stockholders, entitle them to the surplus (profit) that remains after all the operating costs have been paid. Control rights pertain especially to the appointment of managers; the shareholders normally delegate these rights to the board of directors. The managers in turn exercise decision rights in their day-to-day oversight of the production process. Thus, because of the separation between ownership and control, shareholders are usually remote from the exercise of decision rights, although ultimately they may withdraw the control rights (by appointing new directors) from which the operational decisions derive. Clearly, in this hierarchical structure of the company, the various personnel have different rights according to the positions they occupy. Not surprisingly, such differences often entail substantial inequality of decision-making power (and of income earned) in the firm. The determining factor in all this is property, for its possession determines the final distribution of power and authority.

Stakeholderism

In the stakeholder theory, things are quite different, for here differential property ownership has been removed from its decisive role in ultimate decision making (Donaldson 1982; Evan and Freeman 1993; Freeman 1984; Goodpaster 1993). Indeed, once property rights cease to be decisive, the whole telos of the organization is radically transformed. The pursuit of shareholder wealth no longer determines what is to be done. Instead, various groups with some connection to the business are regarded as deserving some influence over such matters as plant relocation, remuneration policy, and anything else that might affect the well-being of the enterprise and all those somehow connected with it. In this pluralist model, no one group should be decisive, but a balance should be struck among all those affected by the business. Such parties include trade unions, residents of the locality in which the firm is situated, suppliers, and any others touched in some way by the activities of the enterprise. Even shareholders are thought to be significant and their views worthy of consideration. Of course, a cynic might justifiably observe that because the importance of a group to the firm does not depend on the group's property rights in the firm, strictly there is no limit to the number of affected groups. Inasmuch as the firm has some impact on, say, the community at large, then "society" itself ought to be considered a stakeholder. Indeed, this conclusion was an implication of Ralph Nader's early plan for the federal chartering of corporations (Nader, Green, and Seligman 1976).

To make some sense of the doctrine, however, we must limit the important groups to those with a direct, tangible interest in the firm. What is crucial to the argument is that the owners do not have a decisive influence in decision making. Whether the various groups have an equal say is less important than the fact that the shareholders clearly have no overriding voice. Indeed, in this radical reinterpretation of the telos of the business corporation, the firm's very last function is to enhance shareholder wealth. As prominent stakeholder theorists William Evan and Edward Freeman assert, "The very purpose of the firm is to serve as a vehicle for stakeholder interests" (1993, 82). According to these explicitly Kantian writers, a utilitarian consideration, such as wealth maximization, ought to have no normative bearing on what the firm should do; at most, it should be considered along with other stakeholder concerns.

How should a firm make appropriate decisions when the owners' views are not decisive and a variety of interests should be taken into account? Clearly, the removal of the predominant authority of shareholders and of their clear (normally single) purpose of maximizing shareholder wealth leads inevitably to the politicization of the firm in that many groups and a number of almost certainly competing purposes must now be considered. As traditionally understood, however, the business corporation is not a political institution. Its ends and means are set by its owners, who need not take into account the preferences of subordinate groups, although firms are often advised to do so for prudential reasons. If they do decide to take others' preferences into account, that decision cannot have a strict Kantian rationale (*contra* Evan and Freeman); in Kantian ethics, an action is morally right or wrong regardless of its consequences for any one person or group. However, consistent interpretation of Kantianism might well be used to legitimize the claims of the shareholders, for the doctrine specifically condemns as immoral the use of one person or persons merely as a means to the ends of others, and stakeholderism could be said to permit the use of the property and persons of the shareholders for the interests of others (nonowning stakeholders) in precisely this way.

The "Arrow Problem" and Decision Making in the Firm

Clearly, stakeholderism aims to take rights away from the owners, who can be assumed to constitute a single body with a common purpose, and to give those rights to a plurality of groups, which would include shareholders but in a much diminished role. Stakeholder groups are unlikely to have a common purpose; more likely, they will display all the rivalry that interest groups exhibit in legislative assemblies. Economist Kenneth Arrow (1963) has famously analyzed the logic of decision making under majority rule, asking whether and under what conditions such collective decisions might ever evince the same rationality as individual decisions. Because under stakeholderism the corporation is to be politicized and the influence of shareholders removed or attenuated, Arrow's conclusions (proofs) about collective choice pertain directly to the possible business organization of the future.

Arrow argues that a rational collective-choice procedure has to have certain properties. The most important of these properties is *transitivity,* which means that if an individual prefers *x* to *y* and *y* to *z*, then he must prefer *x* to *z*. Thus, an individual's preferences are consistently ordered. Can collective choice (by majority rule) exhibit the same transitivity? Arrow's answer: no, it cannot.

If we impose some fairly mild conditions on a collective-choice procedure (such as majority rule), then, following Arrow, we can show that where more than two choices exist, a social ordering of preferences can rarely be derived from all the possible individual orderings. Thus, problems arise whenever there are at least three possible choices and at least three potential choosers. The conditions imposed are: ***collective rationality*** (social choice must exhibit the same logic as an individual's choice); the ***"Pareto" principle*** (if every individual prefers *x* to *y,* then the social ordering ranks *x* over *y*); ***independence of irrelevant alternatives*** (the social choice must not be affected by alternatives not within the feasible set); and ***nondictatorship*** (no one individual's preferences always take precedence over all other individuals' preferences). This final condition is crucially important in a stakeholder firm because decisions there may be possible only if they are made by a dictator.

The "impossibility" of rational majority rule can be shown with the aid of the following table, which exhibits a pattern of preferences that produces intransitive voting:

Individual	***A***	***B***	***C***
	x	*y*	*z*
	y	*z*	*x*
	z	*x*	*y*

Three individuals—denoted **A**, **B**, and **C**—have transitive preferences for three options *x, y,* and *z,* as follows. Person **A** prefers *x* to *y* and *y* to *z;* **B** prefers *y* to *z* and *z* to *x;* **C** prefers *z* to *x* and *x* to *y.* In a series of pair-wise comparisons (each decision being voted on separately), a majority prefers *x* to *y,* a majority prefers *y* to *z,* and a majority prefers *z* to *x*. Thus, although individual preferences are transitive, the collective-choice procedure of majority rule yields an intransitive result.

In such circumstances, no single determinate decision will be reached; rather, "cyclical" (perhaps better called "rotating") majorities will produce an ever-changing outcome. We can illustrate this outcome more clearly with a political example. Imagine that the preferences of voters are ordered in the following way, letting **C** stand for conservatives, **S** for socialists, and **L** for liberals. In these examples, the votes of individuals are amalgamated into party votes, and each party is treated as a single person:

Group	*C*	*S*	*L*
	(42%)	(36%)	(22%)
1st preference	**C**	**S**	**L**
2d preference	**L**	**C**	**S**
3rd preference	**S**	**L**	**C**

Given these conditions, in a series of three votes,[5] we get the following results:

(1) **S** beats **C** (36% + 22% beats 42%)

(2) **L** beats **S** (42% + 22% beats 36%)

Now, if **L** beats **S**, and **S** beats **C**, then, for the social ordering of outcomes to be transitive, **L** must beat **C**. However, the figures show that **C** beats **L** (42% + 36% beats 22%). Thus, where choosers can rank alternatives, there is always the possibility that the democratic process might produce intransitive results.

If the system does generate cyclical majorities of the sort just illustrated, with no clear winner, then a definitive result can be obtained only by relaxing one of Arrow's conditions. It is most likely that a dictator will be allowed to impose a decision. That method, of course, is exactly the one employed in the conventional firm.

Theoretically, in the stakeholder model, we have to assume that members of the various groups can be treated as if they belonged to one block with uniform opinions. Thus, shareholders can be treated as a united front of individuals demanding the maximization of shareholder wealth, and other, rival groups, such as trade unions or local residents, can be similarly understood as united with respect to each group's distinctive objective. Of course, dissident shareholders may exist—usually small numbers of individuals who buy a few shares and attend annual general meetings in order to disrupt the proceedings and to recommend policies that would destroy or badly damage the company—but for my argument they can be treated as members of groups with different interests from regular shareholders.

It is a disheartening thing for a democrat, in the political or business context, to recognize that for a result to occur it must to be imposed by a dictator. In regular two-party democracies, this problem does not arise because voters get only a single choice between two options. Even in a three-party race, they get only one choice, not a series of votes by which they can express their ordered preferences between parties. It is quite likely that the biggest minority (a plurality) will win on the first and only round. If a series of votes were to be held, different minorities would win, and therefore no definitive result would ever be reached. In some European presidential elections, a second round is held between the leading two candidates on the first ballot, and all lower-ranked candidates have to drop out, but, of course, this procedure does not

5. In the usual democratic system of voting, of course, such voting does not happen; rather, we have only one vote or choice, and we have no means of expressing fully how we rank our preferences.

produce a genuine democratic winner: we would need successive voting rounds, with no one dropping out, to achieve that result. Even then, as I have shown, a definitive outcome might still be impossible to reach.

This problem often arises in committee decision making, where the final result depends on the order in which the votes are taken. For example, suppose that the three people designated **A**, **B**, and **C** in the earlier layout decide to vote first on *x* versus *y* and then on the winner of this contest versus *z*. Because a majority prefers *x* to *y*, the second contest will be between *x* and *z*, and *z* will win that matchup. If, instead, they decide to choose first between *z* and *x*, and then match the winner of this vote against *y*, then *z* wins on the first vote, but *y* defeats *z* in the second round. Thus, the identity of the ultimate winner depends on the order in which the various alternatives are offered to the voters (Varian 1999, 558). In regular elections, the full range is often never offered to the voters.

What does all this have to do with business? With respect to the traditional corporation, it is irrelevant; this corporation is a dictatorship by virtue of the property rights of its shareholders. Bilateral contracting gives nonowner individuals or groups no power in the organization unless the owners delegate decision rights to them. Dictatorship in this context does not have the pejorative overtones it has in politics. Those who put up the capital *should* decide the outcome of any dispute among the parties contracting with their enterprise. Potential employees, of course, have a choice among competing dictators in the market. They have no rights within the firm (or much freedom there, either) analogous to those they have in the polity, but they have the right to exit, which they normally do not have in political dictatorships. Of course, "Arrow problems" might occur at a board of directors meeting, but they are likely to be trivial—*instrumental* disputes about how to maximize shareholder wealth, not fundamental quarrels about the nature of the enterprise. As a rule, crises occur in business only when groups *outside* the structure of ownership—for example, trade unions, government officials, or "community representatives"—get involved in its affairs. In these situations, "voice" predominates, giving rise to fractiousness and ultimate irrationality.

In the pluralistic stakeholder model of the corporation, the disputes are logically irresolvable in the circumstances described previously. Suppose a question about plant relocation were to arise involving three possible sites: the existing one and two alternatives. Obviously, at least three rival groups would emerge, each with a moral claim based on community values or some other contemporary ethic. If the property owners—the risk takers and profit seekers—do not have a preeminent place in the decision-making system, no determinate solution is possible. When separate votes are taken between rival sites, cyclical majorities will emerge.

The Arrow problem can be avoided in a democracy if the preference orderings of individuals are "single-peaked" (McLean 1987, 203–4). (Arrow's work showed that for a social-decision procedure to be valid, it must be able to handle *all* possible preference orderings.) Single-peaked preference orderings are those that exhibit a strict consistency or pattern (which can be represented on a graph) so that, in political terms, a left-wing person will consistently rank policies or parties from left to right (or a right-wing person from right to left). The "moderate" person will consistently rank policies and parties to both the right and left of his preferred position, those farthest to the right and to the left being his least preferred. Thus, if a three-party contest were to go to a second or third round (which, as we have noted, does not ordinarily happen in conventional democratic systems), a so-called *Condorcet winner* would be produced. In the earlier example, the orderings would be single-peaked if liberal supporters switched their second and third preferences so that they preferred conservatism to socialism. In that case, **C** (42% + 22%) beats **S** (36%), and **C** also beats **L** (22%). The conservative is therefore the winner.

Although in party systems the voters' preferences might be single-peaked (in three-party Great Britain, for example, it is likely that Conservatives would prefer Liberal Democrat to Labour and Labour would prefer Liberal Democrat to Conservative), it is scarcely conceivable that this condition would exist if business decision making were to be conducted through the methods suggested by stakeholderism. The stakeholders would be disparate groups not at all consistent in their preferences. In our highly politicized world, stakeholder groups are likely to be self-interested factions (in the correct Madisonian sense) solely concerned with the interests of their own members (trade unions are a good example), and there is no telling how their representatives might rank their preferences on issues that did not affect their main concern. Other groups are single-issue organizations, such as environmental zealots, who care little about anything else.

If stakeholderism were to replace the original conception of the corporation as a voluntary creation by individuals concerned to maximize long-term shareholder wealth, only chaos could result. Moreover, if the response to the democratization of the board of directors were to follow orthodox voting lines, with the winner securing total power although it is perhaps only the biggest minority (a regular happening in parliamentary democracies such as Great Britain's), genuine pluralistic stakeholder theorists should be outraged, for important minorities might be permanently excluded. Yet if such minorities were to be included by means of repeated elections, then Arrow problems (cyclical majorities) would emerge, and definitive decision making would prove to be impossible. Only the price system and the pursuit of shareholder wealth can order all the competing demands consistently in a business organization, but this approach is explicitly excluded from a stakeholder company's telos.

The scheme of corporate organization suggested by Evan and Freeman would certainly produce the illogical outcomes and corporate immobilization suggested here precisely because shareholders are eliminated from the decisive role. These writers say, "The reason for paying returns to owners is not that they 'own' the firm, but that their support is necessary for the survival of the firm, and they have a legitimate claim on the firm" (1993, 82). One wonders, however, whether any returns would exist under their system. They are honest enough to recognize that conflicts would exist among various groups of stakeholders, and they concede that the rival demands would somehow have to be reconciled, but their solution to this problem is bizarre. They recommend not a complex voting system that might circumvent Arrow problems, but a "metaphysical director" (Evan and Freeman 1993, 82). That person would be above the fray, not beholden to any particular group, and therefore able to make objective decisions. Get serious: nobody is above the fray; everybody (including the philosopher) is a utility maximizer and a potential rent seeker. The metaphysical director would divert rents to himself up to the point (and no further) at which his rent-seeking destroys the viability of the corporation; otherwise, all parties lose their jobs.

Even if a solution might be found for Arrow problems (if a determinate decision might be reached by means of a series of votes), this result does not necessarily make the decision economically, politically, or morally satisfactory. In democracies employing repeated votes in order to secure a Condorcet winner, profoundly repellent policy outcomes might emerge. Imagine a community characterized by racial tension, where single-peakedness would merely represent differing degrees of hostility to rival ethnic minorities. In this setting, there would be a Condorcet winner, but also many losers. In business, almost certainly, successive voting among stakeholder groups, even if it were consistent, would generate inefficiency because without significant property interests dominating the firm, rival groups would not act in the firm's long-term interests: they would simply exploit it.

In a large organization, members of stakeholder factions would face a public-good trap: they might know that persistent exploitation of the company for short-term advantage would ultimately ruin it and cost them their jobs, but they would have no incentive to eschew this course of action. The avoidance of the destructive outcome requires self-restraint, but no group can be sure that others will act so virtuously, and therefore each would press for its own advantage. The upshot would be a desperate, self-destructive scramble for the assets of the company. We see this sort of behavior in the "mixed economies" in which stakeholder groups seem to be especially powerful. Expressive commitments to act for the public good may sometimes be achieved, but in practice a Hobbesian "war of all against all" breaks out among groups, rather than among individuals, as Hobbes imagined. Similarly, policies regarding prices and incomes always end up this way in social democracies. Even apart from the logical problems of generating determinate decisions from a variety of decision makers, however, more informal arguments suggest that the stakeholder model is deeply flawed.

Fundamental Problems of Stakeholderism

The illogicalities and insoluble conundrums of stakeholderism have arisen over the past twenty years because the doctrine itself has changed significantly. Indeed, the very meaning of the word has changed. Although it now denotes a process that is simply inimical to the traditional business system, it once described a benign form of corporate strategy consistent with the pursuit of shareholder wealth. The original meaning of *stakeholder* was sensible and consistent with rationality in the conduct of business. The Stanford Research Institute first used the word in the literature in 1963 (Sternberg 1999, 12–16) to refer to a small set of people who are intimately involved in the running of the business—typically shareholders, employees, suppliers, and those with technical skills essential to the company's operations. These stakeholders might not hold property in the company, but they are essential to corporate planning and the success of the firm; their views should be taken into account in deciding policy. There is no "ideology" of stakeholderism in this conception, only a sensible business practice to involve in the decision-making process those people who are genuinely affected by the activities of the business. Even in Anglo-American economies, "trust" may be more efficient than contract, and the support of stakeholders may be secured by the encouragement of certain noncontractual business arrangements.

Still, no Arrow problems can arise here because ultimate authority continues to rest with the owners—the "dictators." No serious conflict of purposes arises because in a normal business only one aim is pursued: the interest of the owners. The disagreements that will undoubtedly occur are secondary and resolvable by reference to shareholder wealth. The relative homogeneity of interests among the stockholders means that the collective-choice problems of stakeholder-driven corporations are unlikely to occur.[6]

The shift in the meaning of *stakeholder,* however, has brought with it irresolvable problems. As we have noted, the range of stakeholders has been extended beyond the persons with a direct interest in the operation of the firm to include those who claim merely to be "affected" by its activities. This extension goes beyond members of the local community to, potentially, citizens of the country or even to those of foreign countries with which the business has some involvement. Even anonymous consumers are sometimes considered to be stakeholders, which is an absurd identification because consumers have an obvious weapon against a company they dislike—namely, boycotting the product.

The new stakeholders make wildly divergent claims on the corporation. Some want shorter hours, others more pay; many wish to forgo profit for some environmental consideration; and even more want guaranteed job security. Once comprising those whose skills and cooperation are necessary for the functioning of the firm, stakeholders have become merely all those who claim something *from* it, as if they had entitlements to the wealth generated by its operation. In a stakeholder firm, their divergent demands are irreconcilable.

At the heart of the "social responsibility of the corporation" thesis is the claim that the corporation owes some duty to society, the fulfillment of which constitutes its

6. Members of "noncapitalist" business organizations, such as mutuals or cooperatives (Ricketts 1998), also have a similarity of interests.

license to act. Of course, that nebulous entity "society" is easily translated into pressure-group demands that the company channel largesse to the demanding groups. Certain alleged stakeholders have interests, normally political in inspiration, that are inimical to the ends of the company. For some time, Royal Dutch Shell has been plagued by activist shareholder groups that have no interest in the well-being of the company and have blamed it for everything from damaging the environment to being a party to military dictatorships in Nigeria. Whereas at one time shareholder activism was a valuable method of holding managements to account and compelling them to fulfil their fiduciary duties, it is now a device to wreck the company.

In the real world during the past few years, the stakeholder idea seems to have lost something of its allure, despite the praise for it from philosophers and even from business itself. Perhaps more immediate economic concerns are exerting their inexorable and irresistible pressure. Americans are not great savers, and they are coming to rely on their stocks for retirement security in the face of a risky Social Security system. In these circumstances, no firm can survive for long if it does not make shareholder wealth its primary goal. It might well face shareholder lawsuits because U.S. corporate law still places a fiduciary duty on agents (directors, managers) to maximize the long-term interests of principals (shareholders). Also, a stakeholder firm would certainly attract the interest of predators who would promise to look out for shareholders—one reason why stakeholder theorists oppose the takeover mechanism.

Politics

The overriding problem with the stakeholder model of the corporation is that it tries to make the business system operate like the political system. As citizens, we expect access to the political system to be more or less equal. Voting rights no longer depend on property ownership, and "voice" is the predominant mode of influence. To the extent that government actions affect people equally, the democratic imperative requires that no one group should always dominate public affairs. That government actions involve much more than the supply of public goods, that these actions do not affect all people equally, and that a formal representative government may be captured by elites not fully accountable to the people—these are problems germane to democratic theory but irrelevant to the issues being discussed here. Business is different. In business, "exit"—whether by shareholders selling out to a raider or by workers changing jobs—is the prime method of influencing policy. The penetration of the business world by politics promises to bring all the disadvantages of voting, as well as the enervating effect of pressure groups, to an activity that depends on personal freedom and individual initiative to fulfil its promise.

Perhaps the most deleterious effect of the politicization of business is the grave damage it does to the potency of the takeover process, for in a free economy that process is the most effective protection against managers who depart from the goal of maximizing shareholder wealth. The corporate restructuring that took place in the United States in the 1980s was the most important single microeconomic cause of the subsequent prosperity. Now, however, stakeholder groups can combine to form alliances that inhibit the industrial restructuring that benefits *anonymous* members of economic society. Stakeholderism, by contrast, helps or privileges *known* individuals and groups. The movement against takeovers, concentrated in the state legislatures of the United States in the late 1980s, brought short-term benefits only to incumbent managers and to trade unions; it did not benefit economic society at large. In non-Anglo-American economies, the situation has been much worse, even without the assistance of the law. In Germany in 1997, Thyssen made a hostile bid for Krupp, but a coalition of stakeholders consisting of banks, unions, and management transformed that would-be takeover into a tame merger. An important condition of the ultimate deal was that nobody should lose his job. No doubt sufficient unanimity existed in this case to surmount the Arrow problem, which only goes to show that the solution to a collective-action problem need not be the best economic remedy. In general, stakeholderism of the sort exemplified by the Thyssen/Krupp merger poses a threat to the rationality, freedom, and potential prosperity of a market economy. But even in Germany rationality is being restored. Vodafone's recent spectacular and successful hostile bid for Mannesman (see Barry 2000) was achieved against the usual array of stakeholders. It received important assistance from a characteristically Anglo-American and individualistic maneuver: a court threat to enforce the fiduciary duty of management to act in the best interests of shareholders. Ultimately, the unanimous body of shareholders, once its ownership rights had been asserted, regained its position as the firm's "dictator."

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