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Management Theory and Social Welfare: Contributions, Extensions, and Challenges

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Management Theory and Social Welfare: Contributions, Extensions, and Challenges

The purpose of this editorial introduction is to: (1) provide an overview of the motivation behind this Special Topic Forum; (2) highlight the contributions of the six articles that comprise the special issue and identify some common themes; (3) suggest some reasons that social welfare issues are difficult to address in the context of management theory; (4) provide a discussion of means of assessing social welfare (and urge scholars not to make unwarranted "wealth creation" claims); and (5) offer our own theoretical extension of one of the included articles that provides an account of the relationship between competitive advantage, a major theme in the strategic management literature, and social welfare.

Management Theory and Social Welfare: Historical and Contemporary Perspectives

Over a decade ago, Walsh, Weber and Margolis (2003) lamented the lack of attention to social welfare issues by management scholars. Using data ranging from the research topics of papers published in major journals to membership in various Academy divisions, they made a strong case that organizational scholarship had drifted from its roots – which had emphasized both the social and the economic objectives of organizations – to focus overwhelmingly on the economic objectives alone. This drift was regrettable, in their view, both because it limited the range of intellectual inquiry in organizational studies and because it meant that the findings of organizational scholarship were not being applied in ways that might result in better societies. Two years later, the *Academy of Management Journal* published a special forum on organizational research in the public interest (AMJ, 2005), again calling for more consideration of social welfare in organizational research.

Both Walsh, et al. (2003) and many of the authors in the *AMJ* special forum called for an integration of social and economic objectives. Neoclassical economists might have suggested that this call was/is unnecessary. A market-oriented economic system has been defended from a number of perspectives, including the protection of political freedom through economic freedom, the protection of property rights, and the honoring of contractual obligations. But an important foundational justification for the system is based on utilitarianism, the moral philosopher's term for social welfare – sometimes expressed as the greatest good for the greatest number. More particularly, a version of market capitalism that closely approximates neoclassical microeconomic models of perfect competition – i.e., competition based on price, a *laissez faire* approach to governmental involvement in the economy, and a profit (or shareholder wealth) maximization objective for firms – is posited to produce high levels of societal welfare because it puts society's resources to their most efficient uses. In short, social objectives could be assured if economic objectives were attained (Jensen, 2002).

Unfortunately, there are several reasons to doubt that this relationship is applicable in today's economy. First, as discussed more fully below, the characteristics of modern market capitalism bear little resemblance to the conditions under which the perfect competition model assures social welfare. This divergence of conditions strongly suggests that the model's prescriptions – in particular *laissez faire* governmental policy and a shareholder wealth maximization objective for corporations – are unlikely to lead us to ever increasing levels of social welfare.

A second and related point is that a substantial number of scholars, practicing managers, and entrepreneurs are actively engaged in making the perfect competition model even less applicable to the contemporary economy. A great deal of research in strategic management – i.e., the search for sustained competitive advantage – *depends on* market conditions that deviate significantly from those of perfect competition and, in some cases, involve an *intention* to carve out "mini-monopolies" in order to obviate competition based on price alone.[3] While it may make sense to explore means of exploiting market frictions to enhance firm profitability or start new ventures, determining whether social welfare improves is an empirical question; simply assuming that social welfare is enhanced in conjunction with improved profits is inappropriate.

Third, it takes a substantial leap of faith to conclude that some corporate actions taken to increase shareholder wealth actually improve social welfare. Consider the case of massive layoffs. These actions often do result in increases in shareholder wealth (via stock price increases), but also result in substantial hardships – economic, social, and psychological – for the displaced workers and for the surviving workers who must take on the responsibilities of their former co-workers. Thus it is not clear that all massive layoffs that enhance shareholder welfare simultaneously enhance social welfare, even in the long run. Indeed, Jones & Felps (2013b), using stakeholder happiness as their measure of social welfare, suggest that society as a whole may be made much worse off by massive layoffs, at least in the short run. A similar calculus could be applied to corporate practices at extreme ends of a "potential harm spectrum." Hiring contractors of questionable repute to dispose of hazardous wastes might anchor one end of this spectrum. Cutting

[3] While lower prices have conventionally been associated with social welfare, product variety can also be a source of social welfare benefits (Dixit & Stiglitz, 1977; Spence, 1976).

costs by increasing wait times for customer service calls might fall at the other end. In both cases, externality costs (to the environment and customers, respectively) are incurred and should be included in social welfare calculations.

Finally, the wisdom of relying on a model that focuses exclusively on alleviating economic scarcity no longer makes sense. Throughout much of history, economic scarcity was a pressing social problem and an approach focused on addressing scarcity may have been defensible, despite the social welfare problems created in its wake. However, now that material abundance better describes aggregate outcomes in most developed economies, social welfare problems, new and ongoing, are less easily dismissed. Some of these problems have emerged with a vengeance, particularly in the U.S. – e.g., scandals involving enormous sums of money, increasing inequality of wealth and income, underemployment, homelessness among former members of the middle class as well as the chronically poor, soaring health care costs, and a political system closely tied to the vested interests of corporations and wealthy individuals. Thus, although the market-oriented economic system has an enviable record of making its citizens collectively richer, it is increasingly questionable whether it is capable of addressing some other urgent social welfare problems that have emerged from the relationships between the economy and the rest of society.

Nonetheless, despite calls from scholars representing a range of disciplines (Walsh et al, 2003; Rynes & Shapiro, 2005) and the noble vision of the Academy of Management – "We inspire and enable a better world through our scholarship and teaching about management and organizations" – the management literature has been remarkably quiet on the role of managers and corporations in first creating and now solving the problems that threaten social welfare. Indeed, little appears to have changed since Walsh, et al. lamented an "eerie silence" in the management literature with respect to issues of human welfare at the societal level and urged management scholars to "bring social welfare back in" to their research agendas, most importantly by integrating social and economic objectives (2003: 860; 875). In this Special Topic Forum, our objective is to help fill this void by encouraging theoretical work that addresses important societal welfare issues related to the activities of large corporations in the economy and of those who manage them. In a later section, we will address the "eerie silence" issue.

New Approaches to Management Theory and Social Welfare: Themes and Contributions

In examining the various perspectives taken by our contributing authors, two themes emerge. First, fairness and justice are argued to be important elements of social welfare; that is, utilitarian measures of aggregate well-being – either economic (e.g., GDP) or human happiness (e.g., stakeholder happiness) -- are not adequate metrics for social welfare.

Two of the included articles – Marti and Scherer (2016) and Mitchell, Weaver, Agle, Bailey, and Carlson (2016) – argue that social welfare should not be understood in terms of economic welfare alone, at least not in terms of aggregate economic wealth (e.g., GDP). Marti and Scherer address the issue of financial regulation, beginning with an argument that social welfare is best seen in terms of three elements – efficiency (with a long scholarly history), stability (with a much shorter history), and justice (their main theme). Mitchell and colleagues make a case for a pluralistic view of social welfare. In the process, they find flaws in both economic welfare maximization (through shareholder wealth maximization) (e.g., Jensen, 2002) and stakeholder happiness enhancement (Jones & Felps, 2013b).

Justice, Fairness, and "Many Objectives"

Marti and Scherer (2016) begin by elaborating on the argument that social science theories not only describe social reality, but also shape it. With this insight in mind, they raise the vital normative question: how *should* these theories shape our world? In their illustrative example, these authors show how financial regulation has, up to the present, focused primarily on economic efficiency, with an occasional nod to economic stability. Building on the work of Habermas (1971), they argue that social welfare has three major components – efficiency, stability, and justice. While stability has clearly taken a back seat to efficiency (witness the financial meltdown of 2008) in the perspectives of both scholars and regulators, justice has been given no seat at all. Marti and Scherer submit that a very important question should be added to the list of regulatory concerns: does the proposed regulation make the economy more just? For management theorists, this question could be distilled to how the proposed regulation of financial innovations – high frequency trading in their example – affects top incomes and income inequality. In essence, the authors question whether social welfare is actually enhanced, irrespective of efficiency improvements and stability preservation, if the great bulk of the benefits flow to those already well off. Ultimately, they advocate an *inclusive* (as opposed to a technocratic) approach to financial regulation, one that focuses on both the ends and the means of promoting social welfare. Distributive justice, in the form of income inequality, also plays a prominent role in Cobb's (2016) contribution, discussed below.

Bosse and Phillips (2016) argue that if in our dominant theory of corporate governance – agency theory – we replaced the assumption of narrow self-interest with one of *self-interest bounded by norms of fairness*, then positive reciprocal behaviors on the part of managers could be increased and negative reciprocal behaviors could be reduced. This change in assumptions could not only enhance our ability to understand some anomalous agency theory-based empirical results, but also inspire corporate boards to base executive contracts on a well-documented human behavioral tendency – a quest for reciprocity and fairness – and achieve social welfare gains through *agency benefits* as well as through the avoidance of destructive agency costs based on "revenge."

Finally, Mitchell and colleagues (2016) address the metaphysical specter that haunts discussions of economic welfare, namely, the question of "one" versus "many." Having more than one objective aggravates complexity in decision-making, and it is not surprising that a major strength of traditional neoclassical economic theory resides in its use of a single valued metric; that is, "happiness" in 19th century utility theory and its twin concept, marginal utility (measured through preference rankings and indifference concepts), later on.

How about the corporation? Do we need a single yardstick or many yardsticks to evaluate its contribution to social welfare? Jones and Felps (2013a, 2013b) have argued that corporate action requires a singled-valued objective that allows managers to make principled choices among policy alternatives and that functions as an analog to the normative maxim that managers should optimize value for the firm's equity owners. In contrast, Mitchell and colleagues maintain that adopting a multi-objective approach to managerial decision making permits the engagement of a broader array of market-enhancing preferences and market signals, and allows a more inclusive process that enhances multi-dimensional social welfare. The authors envision an intra-corporate "marketplace" in which managers engage competing objectives. They argue that invoking a single-valued corporate objective would only hamstring the virtuous process of social welfare enhancement made possible by the existence of intra-corporate markets among stakeholders.

Organizational Processes

Second, several of the authors focus on the processes by which the twin objectives of economic and social welfare are enacted. Sonenshein (2016) explains how the perceived illegitimacy and equivocality of social issues act as deterrents to increased corporate attention to activities that enhance social welfare (beyond economic). Issue illegitimacy refers to perceptions that allocating resources to a particular issue falls outside of a justifiable basis for firm action, whereas issue equivocality deals with disagreement regarding the meaning of an issue, including its purpose, scope and implications for the firm. In addition, the paper offers a meaning-making perspective that unpacks how social change agents can overcome these impediments through linking specific tactics (framing, labeling, importing, and maintaining) to different types of social issues (convertible, blurry, risky, or safe). It also explores the multiple levels of meanings that shape a social issue, including very macro levels such as economic philosophies and very micro levels such as individuals' beliefs. One of the many novel ideas advanced in the paper is that although issue equivocality is often perceived as an impediment to action, it can also provide an opportunity for social change agents to favorably shape the meaning of a social issue, thus leading to corporate actions that enhance social welfare.

At the firm level, process is also a focus of Bridoux and Stoelhorst (2016), particularly with regard to a firm's relationships with stakeholders. These authors employ relational models theory to create a hierarchy of relational modes based on their joint value creation capacity. In the context of knowledge-based firm/stakeholder endeavors, Communal Sharing relationships are shown to be superior to Equality Matching, Authority Ranking, and Market Pricing relationships. The choice among these relational modes is influenced by stakeholder perceptions of the model that are made salient by the firm's behavior. The authors also argue that there is a tendency toward Market Pricing when the behavioral standards of the other modes are not met. [In our own theoretical contribution (below), we elaborate on Bridoux and Stoelhorst's work by demonstrating how their social welfare conclusions can be linked to sustained competitive advantage, a major theme in the strategic management literature, and by extension, to the conventional objective of the firm, shareholder wealth maximization.]

Finally, Cobb (2016) examines employment processes and how they contribute to, or undermine, social welfare. A central social welfare concern has been the growth in income inequality throughout the world. Heretofore, most commentators seeking to understand income inequality have focused on government policy, technology or economic explanations to try to understand the growth in income inequality. Cobb demonstrates how scholars of organization and management can contribute to our understanding of this challenge. He argues that the way managers structure the employment relationships in their organizations is a key factor in producing relative societal income inequality. His theory contains several insights suggesting fruitful further research in management as well as public policy recommendations. For example, he demonstrates how the spread of nominally market-focused compensation practices such as pay-for-performance, external hiring and pay benchmarking lead to greater inequality within occupations, and most starkly within organizations. While management researchers have long documented the damage such systems can do to the collaboration on which organizational performance depends (e.g., Lawler, 1971; Pearce, 1987), Cobb draws our attention to the larger social welfare costs of such systems. Similarly, he documents how different ownership forms (e.g., private equity ownership) drive the management external orientation that exacerbates income inequality. His work opens a promising new avenue of management research, as well as bringing our understanding of organizations to bear on a central public policy concern in many countries.

We were somewhat surprised that none of the submissions addressed: (1) the role that religion could play in the relationship between management and social welfare, particularly in view of the recently created Management, Spirituality, and Religion Division of the Academy of

Management; or (2) possible single-valued corporate objectives that include a stronger social welfare orientation [under the assumption that shareholder wealth maximization (e.g., Jensen, 2002) and stakeholder happiness enhancement (Jones & Felps, 2013b) do not exhaust the possibilities]. In the former case, social welfare is inherently values based, and religions are inseparably connected to values. In addition, some religious organizations pursue social welfare through many types of programs in local communities and often worldwide, providing potential models for other organizations, including businesses. In the latter case, Walsh once called the corporate objective issue "arguably the most important theoretical and practical issue confronting us today" (2004: 349). In addition, whatever their shortcomings, single-valued objectives do have the benefit of radically simplifying both management practice and management scholarship. Furthermore, multiple corporate objectives could be interpreted to mean that the pursuit of any one of them is acceptable, or more cynically, that there is no objective at all. Given the impetus of this Special Topic Forum, perhaps future management scholarship will address these neglected themes.

Why the Eerie Silence?

As noted above, Walsh et al (2003) claimed that there was an "eerie silence" among management scholars with respect to issues involving social welfare. If this is still true (and we believe it is), an important question emerges: *Why* have management scholars made so little progress in addressing social welfare problems and, more specifically, integrating social and economic objectives? Here we suggest some reasons why this silence exists and, by extension, why it may emerge again, even in the wake of this special issue. First, it is entirely possible that many individual scholars who populate our discipline believe that shareholder wealth maximization on the part of corporations does indeed lead to optimal social welfare. Although not all of these scholars are likely to be familiar with the details of the logic(s) behind this theorized relationship (e.g., Jensen & Meckling, 1976; Jones & Felps, 2013a), the shareholder wealth maximization objective remains appealing for a number of other reasons. First, as a single-valued objective, it is simple to articulate and, in theory, possible to implement (because multiple objectives cannot be maximized simultaneously). Second, it has a long history of acceptance by managers and management scholars. Third, it conforms to the mandates of financial markets – i.e., "Wall Street." Fourth, social welfare issues are often thought to be the concern of government, not business. Fifth, in theory, it renders profit-motivated activity morally legitimate in utilitarian/social welfare terms.

In addition, the single-valued shareholder wealth maximization objective renders management theory-based research much more tractable and, therefore, more attractive to management scholars. Theories based on economics are certainly not "value free" as was once claimed, but the values that underpin them are widely accepted, meaning that scholars employing them rarely have to address thorny questions involving values in their theoretical and empirical work. Indeed, studies based on economics are highly amenable to the "scientific method" that conveys a great deal of legitimacy and prestige to many disciplines, including management. The assumptions of economics may not be as realistic as we might want them to be, but they render the research process much more manageable, a matter of no small concern to those of us whose careers depend on doing management research. Finally, figuring out how to assure that social welfare is improved in the context of management theory is very difficult, a topic to which we now turn.

Enhancing Social Welfare in the Economy

Social welfare is broadly defined in terms of the well-being of a society as a whole, encompassing economic, social, physical, and spiritual health. Although the term "social welfare" is often defined more narrowly to refer to government programs that provide assistance to needy individuals and families, here our reach is longer and comports with recent efforts to gauge social welfare more broadly. For example, UN-sponsored rankings of well-being rate countries on a range of factors including economic (e.g., GDP per capita), health (e.g., healthy life expectancy), social (e.g., social support), and moral (e.g., generosity and corruption) dimensions (Helliwell, Layard & Sachs, 2013). Gallup (2014) similarly ranks regions by well-being based on perceived social, financial, community, and physical health. Filling out our understanding of social welfare *writ large* by focusing on the role of the corporate sector is our task in this Special Topic Forum.

In theory, there is an array of net benefits – benefits less costs for each individual – that is socially optimal. Indeed, there is no reason that such an optimum could not include concerns about stability and justice as well as efficiency (Marti & Scherer, 2016) or even several other dimensions of welfare (Mitchell et al, 2016). Practically however, such an optimum would be enormously difficult to achieve even in a static world. In a dynamic world, the slightest disturbance would require a new optimal array of net benefits, rendering its achievement impossible in all but a theoretical sense.

If we narrow our focus to economic variables alone, microeconomic theory (specifically, the first fundamental theorem of welfare economics) maintains that such an optimum can be achieved when a competitive equilibrium is reached. Such an equilibrium is possible only under conditions of perfect competition – e.g., markets consisting of many buyers and many sellers; competition based on price alone, markets undistorted by government policies, perfect information, undifferentiated products, zero externalities. In equilibrium, a state of Pareto Optimality obtains; that is, no one can be made better off without making someone else worse off. The role of the firm in this scenario, from both practical and moral perspectives, is simple: firms should attempt to maximize profits. From a practical perspective, profits are the measure of firm efficiency and assure firm survival. From a moral perspective, profit maximizing firms play their designated role in a "rule utilitarian" moral system that assures maximal social welfare (Jones & Felps, 2013a). Thus, the primary objective of managers is to maximize firm profits.

Unfortunately, many of the assumptions of perfect competition – many buyers, many sellers, etc. – are violated in contemporary market capitalism and, according to the Theory of the Second Best (Lipsey & Lancaster, 1956-7), *all* of the assumptions must be met for optimality to be achieved. Importantly, moving closer to any one assumption (making it "more true") – e.g., breaking a large firm into several smaller firms through anti-trust action – does not necessarily increase, and may actually decrease, aggregate social welfare. This means that management cannot simply maximize shareholder returns and expect social welfare gains to emerge; improving social welfare has become a much more complex and less well understood undertaking.

From the perspective of the principal-agent model taught to most business school students, complete contracting is assumed and shareholders are (by construction) the only residual claimants. However, in our world of incomplete and implicit contracts, there can be multiple residual claimants, i.e., stakeholders (Klein, Mahoney, McGahan, & Pitelis, 2012). From this perspective as well, because managerial decisions can have an impact on multiple stakeholders, improving social welfare becomes far more complex than simply maximizing shareholder wealth.

As compelling as the arguments of Marti and Scherer (2016) and Mitchell and colleagues (2016) with respect to multiple dimensions of social welfare may be, they further complicate the task of identifying improvements (let alone optima) in social welfare. Since the components of social welfare *writ large* – e.g., efficiency, stability, and justice (Marti & Scherer, 2106) – are incommensurable – i.e., lacking a means of making principled tradeoffs – we cannot deal with multiple dimensions of social welfare *simultaneously*, making a *social* optimum a destination beyond our reach. Combined with the futility of pursuing an *economic* optimum – equilibrium under perfect competition – as discussed here, focusing on *Pareto Improvements* in aggregate economic welfare becomes a reasonable approach, albeit an incomplete one since it ignores questions of justice (Marti & Scherer, 2016) and intrinsic values (Donaldson & Walsh, in press), among others (Mitchell et al, 2016). We can make *someone* economically better off without making anyone else worse off. Therefore, in the analysis that follows, incomplete though it may be, we focus on *improvements* in aggregate *economic* outcomes – Pareto Improvements – as our standard for the improvement of social welfare as well as on improvements in firm profitability, the driving force behind many corporate actions. We will return to the issue of multiple measures of social welfare at a later point in the discussion.

Pareto Improvements and Firm Profitability

As noted above, the term Pareto Improvements applies to exchanges/relationships wherein one (or more) parties is (are) made better off without making any other party (parties) worse off. Because one party's gain does not involve another party's loss; there is always a net gain, resulting in unambiguous improvements in economic welfare. There are three generic ways to increase firm profits (along with various combinations of the three types), each with implications for social welfare.[4] As derived from Figure 1a, firms can: 1) increase economic value and price while holding input costs constant; 2) reduce input costs while holding economic value and price constant; and 3) increase/reduce price while holding economic value and input costs constant. Under certain

[4] Note that under equilibrium conditions, firms are *price takers*; they have no power to raise or lower their prices. Since we are dealing exclusively with conditions of economic *dis*equilibrium, firms can raise or lower their prices and will presumably do so in accordance with the price/quantity relationship of the product/service in question.

conditions, each of these profit enhancing actions also enhances (or at least does not harm) non-shareholder stakeholders.

[Insert Figures 1a and 1b Here]

[Figure 1b presents the components of economic cost in somewhat greater detail and makes explicit the participation of corporate stakeholders – e.g., employees, suppliers, creditors, neighboring communities – in addition to customers (as recipients of consumer surpluses) and shareholders (as recipients of producer surplus). A reservation price is either: a) the most that a buyer is willing to pay for a good or service, or b) the least that a seller is willing to accept for a good or service. When these prices overlap, voluntary exchange can occur and, since few exchanges are made *at* the reservation price of either the buyer or the seller, both parties usually receive surpluses.]

Under category 1, firms meet the Pareto Improvement standard if they: a) develop new products/services or improve or differentiate existing products/services (thereby assuring market *dis*equilibrium) without increasing costs; b) raise prices no more than the incremental economic value added; and c) appropriate/capture no more than the incremental surplus created by price increases and/or increased volume. New wealth is created and no one is made worse off. However, if the firm, assumed to have some market power under conditions of disequilibrium, raises prices *more* than the incremental economic value created, then surpluses for continuing customers will decline, violating the Pareto Improvement standard.

In addition, Priem (2007) outlines a number of ways that go beyond new or improved products/services and that allow firms to grow the “top line.” Noting that value creation involves the willingness of consumers to pay more for a product/service, he describes means of increasing the *use value* of a product/service so that the *exchange value* (price) can be increased, calling this the "consumer benefit experienced (CBE)" approach.

Under category 2, with economic value and price held constant, reductions in input costs that result from production costs and/or transaction costs efficiencies will result in Pareto Improvements as long as the firm does not appropriate more than the savings created. However, assuming that it has power resulting from *dis*equilibrium conditions, a firm can also increase its profits by reducing the prices paid to its input suppliers, resulting in wealth *transfers* from the firm's input suppliers. No new wealth is created, suppliers suffer losses, and the Pareto Improvement standard is not met. Thus, the nature of input cost reductions is critical to the link between profit seeking and wealth creation.

Under category 3, Pareto Improvements can also be achieved by firms that can increase profits by reducing prices – an outcome dependent on the price/quantity relationship – while holding economic value and input costs constant, thus increasing the consumer surplus of existing customers and adding new customers. However, firms with power resulting from disequilibrium conditions may also attempt to increase profits by increasing prices. Even if profits do increase, the losses incurred by customers result in a failure to meet the Pareto Improvement standard.

We emphasize the point that we elaborate on the role of Pareto Improvements because, at the level of discrete economic transactions/relationships, they represent the only actions that can be definitively tied to improved social welfare. Pareto Improvements *do not* represent a robust and exhaustive representation of social welfare. They do, however, reveal problems with the shareholder wealth maximization model and with the use of the term *wealth creation* in the strategic management literature, as discussed below. Since we are not able to identify an ideal criterion for improving social welfare, we rely on one that yields *better* outcomes.

Externalities

Profitable actions taken by the firms that either: 1) create *positive* externalities; or 2) create *no* negative externalities, also result in Pareto Improvements. In economic analysis of social welfare in the context of shareholder wealth maximization, the caveat "no negative externalities" is usually invoked. Negative externalities result when losses are incurred by parties not involved in a given (mutually beneficial) transaction/relationship. The production of untreated toxic waste as a by-product of manufacturing processes is an obvious example of a negative externality. However, if a reasonably broad definition of stakeholder is used – one that includes *those affected by* corporate actions (Freeman, 1984) – the caveat involving negative externalities becomes redundant. Actions involving Pareto Improvements will, by definition, not harm (and may benefit) those affected by the firm's actions – i.e., stakeholders.

Pareto Inferior Actions

In our analysis thus far, we have focused on Pareto Improvements – corporate actions that result in Pareto *superior* outcomes. The other side of the coin is Pareto *inferior* actions – those that result in losses for one or more corporate stakeholders. A short list of Pareto inferior actions should facilitate understanding of what we regard as actions that, at a minimum, are not unambiguously socially beneficial and, in some cases, may be socially harmful.

- Employee layoffs or salary/wage cuts
- Reductions in employee benefits – e.g., health care coverage, pensions, sick leave
- Allowing "normal attrition" to overburden remaining employees
- Price concessions imposed on suppliers
- Non-price concessions imposed on suppliers – e.g., delivery schedules, payment terms

- Reduced customer service – e.g., lengthy waits for poorly-trained customer service representatives; reduced warranty coverage; product/service price increases unsupported by cost increases
- Tax exemptions, zoning relaxation, or infrastructure improvements extracted from local communities
- Environmentally risky resource extraction practices – e.g., BP's operations in the Gulf of Mexico
- Careless disposal of toxic wastes – e.g., tannery wastes in Woburn, Massachusetts; disposal in countries without protective regulations

In short, a number of common corporate actions intended to increase profits certainly do not meet the Pareto Improvement standard and may not improve *net* social welfare. Simply equating improvements in shareholder wealth to social welfare improvements (wealth creation), as is often done in the strategic management literature [see Klein et al. (2012) and Peteraf & Barney (2003) for explicit exceptions], is not justifiable. Unless the profit improving action can be shown to actually improve social welfare – i.e., create new *net* wealth – no conclusion to that effect should be drawn or implied.

Pareto Improvement and Other Elements of Social Welfare

While Pareto criteria are assumed to be applied in a world in which economic exchanges are voluntary – i.e., if one party does not benefit, s/he does not make the exchange – power differentials between exchange partners make it likely that, even if no one loses, the gains of the powerful will be greater, perhaps far greater, than the gains of the less powerful. Thus, repeated applications of the Pareto criterion could result in increased concentrations of wealth, which re-raises the issue of multiple measures of social welfare.

Marti and Scherer (2016) deal specifically with the (distributive) justice aspect of social welfare. In terms of financial regulation, they argue, scholars and regulators put far too much emphasis on efficiency, too little on stability, and almost none at all on justice. In fact, a criterion based on Pareto Improvement could be applied to economic policy writ large – that is, efficiency (or stability or justice) should not be improved at the expense of the other two. For example, regulatory changes intended to improve efficiency in financial markets could not be implemented if they resulted in less stability in financial markets or an increase in the Gini Coefficient,[5] a measure of equality – e.g., income, wealth – in the population. However, given the economic collapse of 2008 and ongoing increases in concentrations of wealth, we suspect that many citizens of western democracies would sacrifice a fair amount of efficiency for improved stability. Those in the U.S. would probably prefer more egalitarian distributions of wealth and income as well.

Kaldor Improvements

Situations under which profit-generating corporate actions do not harm any non-shareholder stakeholders – Pareto Improvements – are far from exhaustive of the social welfare possibilities, however. Indeed, opportunities for Pareto Improvements are likely to constitute a relatively small proportion of potential corporate actions. Kaldor (1939) offered one means of extending Pareto Improvements to include actions for which tradeoffs between shareholders and other stakeholders are required.[6] If the benefits anticipated by one party are great enough to allow compensation adequate to "make whole" those who would be harmed, the policy in question would

[5] Higher Gini Coefficients connote less equal distributions of wealth or income; lower coefficients connote greater equality. Among national economies, most Gini Coefficients fall in a range of 0.20 to 0.50. For example, for OECD countries, over the 2008–2009 time-period, after-tax Gini Coefficients ranged between 0.25 and 0.48, with Denmark the lowest and Mexico the highest. For the United States, the country with the largest population in OECD countries, the after-tax Gini Coefficient was 0.38 in 2008–2009.
[6] Some economists believe that Kaldor's extension of the Pareto criterion should be applied only at the macro level – e.g., governmental regulations. We see no reason that it cannot be applied at the corporate policy level as well.

be regarded as an improvement in welfare and desirable under Kaldor's criterion.[7] Although Kaldor's formulation involves only *hypothetical* compensation, it is sufficient to meet the standards of many forms of utilitarianism – i.e., those that focus solely on aggregate economic welfare, without regard for the distribution of harms and benefits. As long as the "winners" gains exceed the "losers" losses, utilitarian standards are met. Those whose wealth/income is dependent on shareholder returns would become richer due to "efficient" (but uncompensated) wealth transfers from non-shareholder stakeholders, who would become progressively poorer.[8]

Indeed, repeated applications of the Kaldor criterion could result in even more rapid increases in concentrations of wealth/income than repeated applications of the Pareto criterion. Under Pareto, there are no losers; under Kaldor, not only are there losers, but they are uncompensated. In addition, the Pareto approach has the advantage of being based on voluntary exchanges, while the Kaldor approach could be highly coercive. Although the Kaldor criterion would seem to be an improvement on the apparent current "social welfare" criterion (i.e., shareholder wealth creation *is* wealth creation) because corporate actions resulting in reductions in net social welfare are not allowed, the distributive justice implications remain very significant. For these reasons, we do not endorse Kaldor Improvements as an alternative to Pareto Improvements.

Perhaps because Kaldor was concerned only with hypothetical compensation, *actual compensation* of those harmed by corporate policies – i.e., wealth transfers, externalities – has never been seriously considered. Nor is it surprising that such harms do not play a role in attributions of economic efficiency that accrue to profit maximizing corporate behavior. However,

[7] What we have called the Kaldor criterion is often referred to in the economics literature as *Kaldor-Hicks efficiency* after Kaldor and John Hicks (1939), who added the provision that those potentially harmed by an action could (in theory) pay the potential actor not to proceed with the action.
[8] Some commentators (e.g., Hartman, 2006; Smith, 2012) believe that this process is already well underway.

the fact that we rarely calculate the extent of harms caused by specific corporate policies, let alone compensate those harmed, does not diminish the harms themselves. And, because the Kaldor criterion is itself fraught with thorny problems both theoretical and practical (e.g., Layard & Walters, 1978; Sidak & Spulber, 1996; Williamson, 1996), we cannot endorse a criterion such as *Kaldor Improvements with Compensation*.[9] We do, however, suggest that, given the problems with other options – i.e., equating shareholder wealth creation to wealth creation/social welfare improvement, Pareto Improvements, and Kaldor Improvements – such a criterion might represent an intriguing line of inquiry for future exploration,[10] but one that is far too complex to examine with any thoroughness here.

We now turn to an extension of one contribution to this Special Topic Forum by offering a theoretical link between social welfare improvement (in the form of economic wealth creation) through Communal Sharing firm/stakeholder relationships (Bridoux & Stoelhorst, 2016) and sustained competitive advantage, a major theme in the strategic management literature. Our larger goal is to offer an example of compatibility between the firm's practical mandate (and conventional normative mandate) – i.e., enhancing profitability – and social welfare improvement, compatibility that we have argued cannot simply be assumed.

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[9] On its face, compensating non-shareholder stakeholders for wealth transferred to producer surplus (Figure 1b) makes no sense. If producer surplus is used to compensate non-shareholders for their losses, there is no net gain in producer surplus. Indeed, this sort of wealth transfer is a zero-sum game; that is, *producer surplus* increases (approximately) equal (non-shareholder) stakeholder surplus decreases. It appears that no new wealth is created. However, when producer surplus (profit) is translated into shareholder wealth, this is no longer true. Because price/earnings (P/E) ratios for corporate shares are almost universally greater than 1 to 1 [Among S&P 500 firms, P/E ratios averaged from 13.01 to 16.66 in the period from September 2011 through December 2012 (ycharts.com, 2013)], shareholder *wealth* gains – share price increases – are likely to be greater than stakeholder losses, leaving resources available to compensate harmed stakeholders. *Importantly, compensation must be paid in company stock*. An unpublished working paper authored by two of the co-editors of this Special Topic Forum entitled "Sustainable Wealth Creation" (Jones & Freeman, 2013) begins an exploration of this possibility.

[10] To paraphrase Williamson, "… to argue that (an approach) is flawed does not establish that there is a superior feasible alternative." (1996: 1014). All feasible options may be flawed and choices must be made from the feasible alternatives (Williamson, 1996).

The Relational View of Competitive Advantage

In this theoretical effort, we envision the firm as a *nexus of relationships*. Viewing the firm as a "nexus of contracts" (Jensen & Meckling, 1976) is satisfactory as long as the contracts can be relational as well as transactional (Macneil, 1980) and are allowed to be incomplete and implicit in many cases. The well-known "hub and spoke" stakeholder model of the firm (e.g., Freeman, 1984; Jones, 1995), with managers at the hub and stakeholders – e.g., shareholders, creditors, employees, customers, suppliers, neighboring communities, governmental agencies – at the ends of the spokes, is a useful visual depiction of these relationships. Relationships can be multilateral, but are often bilateral. Because corporate managers manage these relationships on behalf of the firm, management theory is an essential link between competitive advantage and economic wealth creation. We are concerned with ways that firms can achieve competitive advantage and improve social welfare simultaneously by focusing on relationships between/among the firm and its stakeholders.

A number of authors have advanced theoretical/conceptual arguments to the effect that the manner in which a firm conducts relationships with its stakeholders can make a difference in its financial performance. For example, Freeman (1984) introduced the idea that effective management of stakeholder relationships could enhance firm performance. Dyer (1997), using interviews and survey data, advanced five propositions linking characteristics of firm/supplier relationships to lower transaction costs and higher transaction value. Dyer and Singh (1998), departing from the resource-based view (RBV) of the firm, identified relational elements of interfirm alliances that can lead to competitive advantage. Pfeffer (1998) made similar points with respect to firm-employee relationships. Leana and Rousseau (2000; see also Coff & Rousseau, 2000) developed the notion of "relational wealth." Preston and Donaldson summarize this view by noting that "...specific economic benefits – and, hence, increases in organizational wealth – can be generated by certain types of relationships between corporations and their various stakeholders" (1999: 619). Although Bridoux and Stoelhorst (2016) do not explicitly present a theory of sustained competitive advantage based on their social welfare insights, they have established a strong foundation for doing so. To use a golf metaphor, they have positioned the ball on the green; we must provide only a key putt or two.

The notion of trust was added to the "relational view" in the theories of Barney and Hansen (1994), who argued that "strong form" trust in exchanges with partners can be a form of competitive advantage, and Jones (1995), who developed the more general argument that firms that are able to deal with their stakeholders on the basis of mutual trust and cooperation can achieve competitive advantage through reduced transaction, agency, and team production costs. Empirical studies have also identified trust as a key element in successful firm/stakeholder relationships (e.g., Browning, Beyer, & Shetler, 1995; Doz, 1996; Uzzi, 1997; Zaheer, McEvily, & Perrone, 1998). One remarkable result was found by Dyer and Chu (2003) in a study of supplier/automaker relationships. The least trusted automaker experienced supplier transaction (procurement) costs that were "almost six times higher than" those of the most trusted automaker (Dyer & Chu, 2003: 64). These and other research efforts make it clear that trustworthiness can be a valuable resource in firm/stakeholder relationships.

The Missing Link – Relational Ethics Strategies

In accordance with our focus on the relational view, we introduce the notion of *relational ethics* as a means to link sustained competitive advantage -- a concept closely tied to the resource-based view of the firm (RBV) – to social welfare, the theme of this Special Topic Forum. Sustained competitive advantage – e.g., "sustained superior financial performance" (Barney, 1986: 656); "sustained above-normal returns" (Peteraf, 1993: 185); "superior financial returns within its industry (or strategic group) over the long run" (Ghemawat & Rivkin, 1999) – involves a firm being more profitable than other firms in its industry over a significant period of time.

Since competitive advantage is closely tied to firm profitability, its pursuit can be consistently linked to social welfare/economic wealth creation only under conditions of perfect competition, conditions far removed from those of contemporary competition as described above.[11] Given these more realistic competitive conditions, a new approach to creating a link between firm behavior and social welfare is needed. To the best of our knowledge, only one other normative theory has been advanced that answers the question "what should the objective of the firm be in order to promote social welfare?" as applied to all firms in the economy. Unfortunately, the corporate objective put forward by Jones and Felps (2013b) – stakeholder happiness enhancement – has yet to gain much traction among scholars or managers. Indeed, with respect to the promotion of social welfare, there may be no universally applicable corporate objective. Even if social welfare is represented narrowly in terms of economic wealth creation, theory intended to promote it may have to be highly contingent. With this perspective in mind, the theory we describe in this editorial introduction applies only within certain boundary conditions. It does, however, demonstrate how firms can promote aggregate economic welfare and, simultaneously, achieve competitive advantage.

Since social welfare is an aggregate concept, relationships are bilateral (or multilateral), and competitive advantage is a firm-level resource/capability, the relevant question becomes "what resource(s)/capability(ies) will allow firms to join with key stakeholders in the most efficient relational wealth creation efforts?" To answer this question, we propose a continuum of relational ethics "strategies" and argue that one of these strategies – consummately-cooperative relational

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[11] Jones and Felps (2013a) provide a detailed critique of the apparent theory behind the claim that "profit maximization leads to maximal social welfare," casting serious doubt on its veracity.

ethics (CCRE) – can be a firm-level resource/capability that, within certain boundary conditions, can lead to sustained competitive advantage while also improving social welfare.

Since some scholars regard "strategic ethics" as a contradiction in terms, we begin by explaining what we mean by "ethical strategies." We define ethical strategy as intended ethical (or unethical) behavior *regardless of underlying motives*. In other words, when a firm adopts an ethical strategy – for example, one of *conventional* relational ethics (defined below) – it means that the firm *intends to behave* in a manner compatible with conventional business ethics in its relationships with certain stakeholder groups. The firm's intentions may be grounded in either: a) *authentic* conventional ethics, defined as the belief that conventional ethics are morally appropriate in relationships with these stakeholders; or b) *instrumental* conventional ethics, defined as ethical standards that, if adhered to, will result in benefits to the firm – i.e., they have instrumental value. For readers who believe that motives are essential to determinations of ethical propriety (e.g., Kantians), we plead *nolo contendere* and accept that they may view the term *ethical strategy* as *ethical "strategy"* where it appears in the text. Later in the paper, we address the important difference between authentic and instrumental ethics.

We frame the discussion in terms of *ethical* strategy because the way that we treat others is a central concept in ethics, and how a firm treats key stakeholder groups in economic relationships certainly fits into this category. Furthermore, trust is a term from the vocabulary of ethics that can be linked to how firms and their stakeholders treat each other (Barney & Hansen, 1994; Jones, 1995; Dyer & Chu, 2003). Our theory hinges on the assumption that corporate relational ethics strategies, as defined above, fall along a continuum from pathologically self-interested to self-destructively altruistic. At the former end would reside criminal enterprises, which fall outside the scope of our analysis, and at the latter end, businesses that are essentially charities in corporate form, the sustainability of which in a market economy is dubious indeed. Therefore, we describe in greater detail three more realistic points along this continuum – *opportunistic* relational ethics, *conventional* relational ethics, and *consummately-cooperative* relational ethics. At this point in our analysis, we are concerned with relational ethics strategies applied to business units[12] within firms. Later, we will examine the value of relational ethics strategies within entire firms.

Opportunistic Relational Ethics (ORE)

Business units with *opportunistic* relational ethics (ORE) strategies believe that acting exclusively in their self interest in dealings with stakeholders is the best means of achieving financial prosperity and, more specifically, that the reputational costs of so doing are less than the costs of opportunities foregone. Furthermore, they will regard opportunism – self-interest seeking *with guile* (Williamson, 1975; 1985) – as an appropriate extension of self-interest. One form of opportunism involves undertaking actions designed to build trust with an exchange partner and, once trust is established and the stakes are high enough, taking advantage of the partner. Opportunistic business units will use power differentials and information asymmetries whenever their use is advantageous. The use, even flagrant use, of monopoly power is well within the charter of an ORE business unit. They will regard promises as provisional, honoring them only as long as it is advantageous to do so. Even formal contracts may be regarded as provisional; opportunistic business units will take the legal costs potentially imposed by an aggrieved partner into account in deciding whether or not to honor a contract with that partner. Claims of trustworthiness made by ORE business units are mere pretense; stakeholders who trust them do so at their own peril. ORE business units might also change the terms of employment of their workforce – e.g., health care

[12] We use focus on *business units* because instances in which entire firms (of any size) are engaged in a single relationship are likely to be rare.

benefits, vacations, sick leave – or non-price elements of firm/supplier contracts – e.g., delivery schedules, payment terms – without qualm or attempt to "hold up" partners who have made investments in project-specific assets. Disputes between such units and their stakeholders, involving relationships which lack safeguards, will usually be settled by: (1) stakeholder capitulation; (2) settlements unbalanced in favor of the opportunistic business unit; or (3) litigation.[13] These units will also regard the law and regulations as provisional, routinely testing the limits of standards set by government authorities. In short, something analogous to *caveat emptor*, such as "let the stakeholder beware," applies to relationships with ORE firms.

Conventional Relational Ethics (CRE)

Conventional relational ethics constitutes a broad category of behavioral norms. Business units adopting *conventional* relational ethics (CRE) strategies adhere to the standards of fair competition in which firms access the resources of stakeholder groups mostly through arms-length exchanges and negotiated contracts. However, CRE can be applied in relational situations as well.

Indeed, the term "ethics of compliance" could be applied to CRE units; they comply with legal and regulatory standards as well as commonly-held ethical norms. Their ethical stance is similar to that advocated by Milton Friedman (1970) in his classic article "The social responsibility of business is to increase its profits." Friedman argued that firms should "make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom" and "without deception or fraud." (1970). These standards, while eclectic, do constitute a clear division between *conventional* relational ethics (CRE) and

[13] Ketokivi and Mahoney (forthcoming) maintain that many scholars who draw parallels between Machiavelli's logic of "get them before they get you," and the logic of transaction cost economics (TCE) have missed the punchline: pre-emptive opportunism is "a very primitive response" (Williamson, 1985: 48). The wise prince seeks both to give and receive credible commitments to safeguard the relationship. The main message of TCE is not only constructive and positive, but is also consistent with a stakeholder theory of management.

opportunistic relational ethics (ORE). They outlaw practices such as: (1) making promises that the firm does not intend to honor; (2) reneging on commitments; (3) violating the terms of contracts; and (4) breaking the law. In addition, although Friedman does not explicitly address these issues, we would add that CRE firms will not: (5) test the limits of the law or contract terms (adhering to the spirit as well as the letter these legal devices) and will negotiate in good faith with legal or regulatory authorities when disagreements arise; (6) take excessive advantage of power differentials or information asymmetries to gain leverage over such stakeholders as customers, suppliers, employees, local governments, or local communities. Nor will they abuse monopoly power.

Although they prefer to operate under the terms of formal contracts, CRE units may make non-contractual promises that they intend to honor. However, such promises are explicitly articulated, relatively specific, and temporally bounded, as opposed to implicit, general, and open-ended. Units adopting CRE strategies regard competition with other firms as their primary concern and are fully aware of the zero-sum nature of many transactions and negotiations. [Although *voluntary* firm/stakeholder exchanges by definition involve benefits for both parties, the specific terms that establish the distribution of benefits are regarded as zero-sum – i.e., A's gain is B's loss and vice versa.] CRE units endorse fair exchanges, but may regard *voluntary* as a sufficient condition for *fairness*.

Importantly, units employing CRE strategies *do not* regard stakeholders as partners in joint efforts to create wealth in which the distribution of gains is postponed until after the gains are made. Bargaining is done in order to maximize gain for the firm, rather than gain for the partnership. Such firms may also believe that benefits of a reputation for fair dealings with stakeholders outweigh the benefits of exclusively self-interested or opportunistic behavior, but it is not necessary that they hold this belief. In short, CRE units are reasonably trustworthy, but dependence on their trustworthiness should be grounded in prudence and an understanding that they are primarily engaged in competitive endeavors. They will be guided by widely-held, if not always clear, standards of business practice, many of which are captured by Hendry (2004) under the banner of traditional morality, which bounds self-interested behavior with norms of honesty, fairness, and respect for obligations and duties.

Consummately-Cooperative Relational Ethics (CCRE)

Business units with *consummately-cooperative* relational ethics (CCRE) strategies believe in the propriety of actively cooperative, generous, and joint benefit-oriented relationships with stakeholder groups. CCRE units can be motivated in either of two ways: (1) they believe in the moral propriety of CCRE norms – that is, they believe that relational partners should be treated in certain ways for moral reasons (a heuristic approach); or (2) they believe that adherence to CCRE norms will result in benefits to the firm that outweigh the costs of employing them (a calculative development of decision heuristics). (We discuss the relative value of these two motivations below.) Consummately-cooperative business units are able to identify with the joint interests that result from their relationships with partners. Further strengthening of Communal Sharing relationships may develop through what Sluss and Ashforth (2007) call relational identification, wherein individuals come to think of themselves as part of a relational dyad.

CCRE strategies use many of the characteristics of CRE strategies – e.g., keeping promises, honoring the spirit as well as the letter of laws and contracts, refraining from taking advantage of power imbalances or information asymmetries (including those arising from changed circumstances) – as starting points their behavior in Communal Sharing relationships. Rather than making (and keeping) explicit, specific, and temporarily bounded promises, as CRE units may do, they favor the implicit, general, and open-ended promises to cooperate voluntarily, spontaneously, and generously with their partners in joint-wealth creation efforts. Fair distributions of obligations and rewards are valued goals for CCRE units. Although power imbalances and information asymmetries often exist, shared and cooperative decision making and voluntary transfers of important information, respectively, neutralize them. CCRE business units also engage in what we call "relational citizenship behaviors" (RCBs).[14] They: (1) willingly share information of value to the joint venture without regard for either its proprietary value to the CCRE unit's firm or its potential appropriation by relationship partners; (2) make voluntary contributions to joint efforts; and (3) address emerging problems and settle disputes in a cooperative manner (e.g., by pursuing equitable and productive solutions rather than establishing blame and penalizing the offender), and resort to litigation only under the most dire circumstances. They also prefer to operate without elaborately written formal contracts. In particular, unforeseen events – e.g., unanticipated problems or changes in economic conditions or regulatory environments – are dealt with through cooperative means rather than through litigation. In general, these norms reflect high levels of mutual trust and willing cooperation. Importantly, while we submit that relationships between firms adopting CCRE strategies are rare (below), they do exist, as is made clear in the discussions of work by Uzzi (1997), Browning, Beyer, & Shetler (1995), and Doz (1996) below.

Consummately-Cooperative Relational Ethics (CCRE) and Sustained Competitive Advantage

Although we have articulated the characteristics of three points along the continuum of relational ethics "strategies" in order to enrich the background for our theory, we highlight only

[14] The semantic similarity of RCBs to organizational citizenship behaviors (OCB) is deliberate. RCB is defined as "individual behavior that is discretionary, not directly or explicitly recognized by the formal reward system, and that in the aggregate promotes the effective functioning of the organization" (Organ, 1988: 4) with the word *relationship* substituted for *organization.*

one of them – consummately-cooperative relational ethics (CCRE) – for elaboration as a source of competitive advantage. In the following sections, we will show that, unlike ORE and CRE, CCRE meet all of the criteria for sustainable competitive advantage. They: (1) are valuable; (2) are rare; (3) are not easily imitated; and (4) cannot easily be substituted for (Barney, 1991). We begin by highlighting and elaborating on a number of important conclusions drawn from Bridoux and Stoelhorst's (2016) work on social welfare.

(1) The theory applies only to high task and outcome interdependent environments (p. 5) within which the authors focus on knowledge-intensive tasks (p. 16). We also focus on "high velocity" environments because they share many of the relational demands of knowledge-intensive environments. Firms operate in industries of widely varying rates of change – e.g., products, processes, customer preferences, new entrants, and regulatory regimes. Dynamic industries, featuring high or unpredictable rates of change (Dess & Beard, 1984), exist alongside stable industries where there is little need for innovation (Jansen, Van den Bosch, & Volberda, 2006).[15] These dynamic "high velocity" industries require constant adaptation to new competitive, technological, and regulatory conditions, requiring rapid and thorough learning and knowledge transfer as well as complex/reciprocal coordination of activities. These limitations constitute boundary conditions on the theory presented below.

(2) In economic relationships, there are four principal modes of relating – Market Pricing, Authority Ranking, Equality Matching, and Communal Sharing. Within the boundary conditions noted above, these relational modes can be arranged in the order listed here based on increasing joint value creation efficiency (pp. 10-13).

[15] Stable "low velocity" industries are often characterized by well-established rules for success (Prahalad & Bettis, 1986), and success is likely to depend more on market position and substantial capital investments than on innovation (Eisenhardt & Brown, 1997).

(3) Irrespective of which relational mode is in force, the relational norms of that mode must be consistently adhered to (p. 36). Inconsistently applied norms produce outcomes worse than any of the principal relational modes consistently applied.

(4) There is a tendency toward Market Pricing relationships when more efficient relational modes cannot be maintained because stakeholders perceive self-interested behavior on the part of the firm (p. 6).

(5) Moving stakeholders away from Market Pricing toward more efficient relational modes is more difficult than moving toward Market Pricing (p. 25).

(6) Although the authors focus on how the contributions of individual stakeholders (p. 3) depend on how they frame their relationships with other participants (p. 4), they allow for shared views within stakeholder groups on how they should relate to other parties (p. 32). They represent "the firm" as a central actor capable of conveying situational cues regarding appropriate relational modes (p. 9). The firm makes the desired relational mode salient to stakeholders thorough its perceived behavior (p. 19). We will limit our analysis to stakeholder *groups* and address the issue of moral homogeneity within these groups as well as within the firm.

(7) Stakeholder representations of appropriate relational modes may also depend on how the firm behaves with respect to other stakeholders (p. 28).

Our addendum to this list is that each party in a relational dyad must have confidence in the ability and willingness of its partner to adhere to the norms of the relational mode under examination. In the particular case of Communal Sharing, this addendum distills to trust in the intention of the partner to adhere to the norms of Communal Sharing.[16]

[16] Communal Sharing norms include the following. Individuals "see themselves and their relational partners as community members who are equivalent, undifferentiated, and who share motivations and goals." They "are motivated to contribute altruistically (i.e., regardless of personal rewards) to the achievement of these common goals, and the appropriate behavior regarding cooperation is to pitch in and help." "(C)ommunity members receive

The gap between Bridoux and Stoelhorst's (2016) work on social welfare and a theory of sustained competitive advantage can be summarized as follows. Because Communal Sharing relationships are the most efficient mode of economic relationship in high-velocity, knowledge intensive environments, they have value. Because CCRE business units are capable of successfully adopting norms appropriate to participation in Communal Sharing relationships and providing the situational cues required for the development of such relationships, they will, all else being equal, be uniquely attractive partners in these valuable relationships. Therefore, if a business unit can: (1) acquire a reputation for adhering to CCRE standards (in order to attract appropriate partners); (2) actually adhere to CCRE standards (in order to maintain Communal Sharing relationships with partners); (3) select partners that will adhere to CCRE standards; and (4) appropriate/capture some of the incremental value created through Communal Sharing relational efficiencies, it will have a competitive advantage over firms that cannot.

In addition, because Communal Sharing relationships are valuable, CCRE business units will be able to attract better stakeholders for the purposes of the Communal Sharing relationship, further expanding the wealth created and, by appropriating/capturing a share of that additional wealth, acquire additional competitive advantage. Elaborations of these two theoretical extensions are presented following our arguments that successfully implemented CCRE strategies are valuable, rare, difficult to imitate, and not easily substituted for.

CCRE Strategies Can Be Valuable

CCRE strategies can be valuable for two reasons. First, they allow the business unit to participate in Communal Sharing relationships which are more efficient than other forms of economic relationships in knowledge-intensive, high-velocity environments, thus creating more

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what they need without expectations about a specific contribution to the community in return." "Decisions are made by consensus." (Bridoux & Stoelhorst, 2016: 10-11) wealth to be shared between/among the relationship partners (Bridoux & Stoelhorst, 2016). Second, because Communal Sharing relationships create more sharable wealth, potential stakeholders will be attracted to these relationships, allowing the CCRE business unit to select partners that are well suited to the tasks to be undertaken – i.e., better stakeholders.

The boundary conditions described above – knowledge-intensive, high velocity competitive environments – are important because these environments present two particularly pressing problems – the coordination of activities and the transfer of relevant knowledge – that can be solved in Communal Sharing relationships by business units with well implemented CCRE strategies.

Complex/Reciprocal Coordination and Knowledge Transfer

<u>Complex/Reciprocal Coordination</u> Management scholars dating back to Barnard (1938), Mayo (1945), Fayol (1949), and Thompson (1967) have regarded coordination as essential to organizational (and inter-organizational) success. Thompson (1967) describes three modes of coordination, one of which – reciprocal coordination (where needed contributions depend on the nature and extent of previous contributions and mutual adjustment is required) – is relevant to the environments of concern here.[17] Reciprocal coordination is needed when tasks are complex, novel, multifaceted or "high velocity" (Thompson, 1967; Gomory, 1992; Nelson; 1992). Plans, rules, and contracts are poor substitutes for mutual adjustment when tasks involve reciprocal interdependence (Barki & Pinsonneault, 2005). CCRE units provide value by allowing communal sharing relationships to function (as they must) without elaborate plans, rules, or contracts (Bridoux & Stoelhorst, 2016). The substantial costs of explicit contracting are avoided as well, creating more

[17] The other two are: 1) pooled (where individual contributions are simply added together); and 2) sequential (where each contribution must occur in a certain order).

incremental value. Critical to the wealth creation potential of complex/reciprocal coordination are high levels of mutual trust. A number of essential elements of Communal Sharing relationships – e.g., operating without formal contracts; making voluntary contributions to joint efforts; settling emerging problems in a cooperative manner – would be impossible to achieve without high levels of mutual trust.

<u>Knowledge Transfer</u> A number of scholars, including Hosmer (1994), Grant (1996), and Leonard-Barton (1992; 1995), have emphasized the importance of "relationship quality" on the effective utilization and dissemination of knowledge between parties. The role of knowledge as a vitally important source of competitive advantage for firms has been understood for several years (e.g., Grant, 1996; Bennis, 2002; Murtha, Lenway, & Hart, 2001). Firms engaged in joint efforts often must share knowledge and, although much knowledge is generated and stored by employees (Argote, 1999), learning from other stakeholders is also important to competitive success (e.g., von Hippel, 1988; Jeffries & Reed, 2000; Rosenkopf & Schilling, 2007).

Knowledge has at least three attributes that distinguish it from other forms of property – e.g., consumer durables, manufacturing equipment, and real estate – and each is relevant to the relational ethics strategy employed to make use of it. These attributes include its easy appropriability, its combinatory value, and its tacit nature. First, knowledge is appropriable; once disclosed, it can be used by others free of charge.[18] Second, knowledge may be useful only when combined with other capabilities, such as knowledge from other sources or the manufacturing facilities or distribution chains of other firms, and the value of the combination and the contributions of individual partners are unknown *a priori* (Jeffries & Reed, 2000). Third, much

[18] Of course, patent law provides some protection against this sort of appropriation. However, many ideas are not patentable and many others are not worth the time and trouble. In any case, litigation is expensive.

knowledge is tacit and cannot easily be formally transferred from one partner to another (Nelson & Winter, 1982). In some situations, the value of formally transferred knowledge is reduced substantially without the concomitant transfer of tacit knowledge. Full value knowledge transfers often involve ongoing and close interactions between the transferor and the transferee.

With these characteristics of knowledge in mind, it becomes clear that trust is enormously important to its effective knowledge sharing between firms and their stakeholders. Given the substantial value and easy appropriability of some proprietary knowledge, its transfer would involve either very elaborate (and expensive) formal contracts, including monitoring and enforcement, as well as frequent re-negotiation, or very high levels of inter-firm trust. Indeed, appropriation is unlikely under norms of CCRE, since each partner seeks to treat the other fairly (von Hippel, 1988).

In addition, in cases in which the value of knowledge cannot be known with any precision until it is combined with other resources, formal contracting becomes virtually impossible, necessitating a substantial reliance on trust as a governing mechanism. The norms of CCRE dictate fair compensation, allowing partners to contribute knowledge to the joint effort without fear of being exploited.

Finally, the sharing of tacit knowledge, knowledge that often substantially enhances the value of formally transferred knowledge is, by definition, not subject to formal contracting. Since even the existence of tacit knowledge may be unknown by the potential recipient, it must be shared through voluntary transfers based on trust. Firm-stakeholder relationships based on norms of CCRE make the transfer and absorption of tacit knowledge more complete than those based on the norms of other relational ethics strategies. CCRE norms include respecting and valuing the other party, a foundation that inspires each side in a partnership to appreciate the insights of the other and to want to share its own. Moreover, these norms involve the development of the shared perspectives and shared vocabularies that are necessary for the transmission of subtle forms of tacit knowledge (Baumard, 1999; von Hippel, 1988). In an empirical study, Uzzi (1997) found that "embedded" relationships were characterized by high quality – i.e., detailed, tacit, and holistic – information exchanges. In sharp contrast, the firm may overlook, or be unaware of, useful tacit knowledge because other relational ethics norms involve more psychological distance and less trust between the firm and its stakeholders. Thus, for several different reasons, organizational scholars have argued that embedded, trusting relationships – e.g., Communal Sharing – with stakeholders are superior to other relational modes for learning and knowledge sharing.

Empirical Evidence

Three articles involving case studies offer insights into the role of trust in relationships of interest to our theory. First, Uzzi (1997) found that trust was an essential ingredient in firm success in a "high velocity" segment of the fashion industry. He found evidence that embedded ties, characterized by "trust, fine-grained information transfer, and joint problem-solving arrangements," were often critical to a firm's success in this market segment. Trust accelerated decision-making, economized on cognitive resources, and improved access to "privileged and difficult-to-price resources that enhance competitiveness" (1997: 43).

Second, Doz (1996) found that trust was a primary differentiating factor in longitudinal studies of two unsuccessful and one successful "partnership cycles." AT&T and Olivetti's failed minicomputer venture in the mid-1980s was marked by a lack of cooperation and little trust, as was Ciba-Geigy and Alza's unsuccessful drug development effort in the late 1970s and early 1980s. In sharp contrast, GE and SNECMA's joint jet engine program featured trust and cooperation and, over time, expanded to include their entire line of engines for the civilian market.

Doz describes this phenomenon as a “self-reinforcing cycle of heightened efficiency expectations, strengthened institutional commitments, deeper interpersonal trust, joint sense-making, and greater flexibility and adaptability” (1996: 73).

Third, Browning, Beyer, and Shetler’s (1995) study of the semiconductor industry’s manufacturing technology consortium (SEMATECH) revealed that trust was a key element in the venture’s success. These research findings differ from those of Uzzi (1997) and Doz (1996) because explicitly moral language was used to describe the relationship. The project, initially marked by “private agendas, new faces, and an equivocal structure” evolved into a “moral community in which individuals and firms made contributions to the industry without regard for immediate and specific payback” (125; 113). This tangible victory for SEMATECH’s “moral community” seems to have been replicated in the successful relationships described by Uzzi (1997) and Doz (1996) as well, although the explicit moral language was not so clearly in evidence.

In addition, Zaheer, McEvily, and Perrone’s (1998) examination of the electrical equipment manufacturing industry found that lower negotiation costs and less conflict accompanied better overall performance (a summation of price, timeliness, and quality) when high levels of inter-organizational trust between firms were present. Similarly, Dyer and Chu (2003) found that total (buyer and seller) transaction costs, mainly *ex post* (monitoring and enforcement) rather than *ex ante* (contracting) costs, were negatively and significantly related to mutual trust in buyer/supplier relationships in the automobile industry.

In addition to unpacking relational sources of wealth creation and identifying trust as a key element of successful relationships, these studies validate two relational activities in which high levels of trust can be an important element of venture success. All of these joint efforts involved either substantial technical complexity (mini-computers, drug development, semiconductor manufacturing, or jet engines) or "high velocity" environments (the fashion segment examined by Uzzi). These are the very the attributes identified above as boundary conditions for our theory. Ventures of this type rely heavily on two specific relational activities – complex/reciprocal and rapid coordination and extensive, thorough, and rapid knowledge sharing – to be successful. In the words of Dyer and Chu, trustworthiness may be valuable in "[c]omplex product industries" in which it is "often necessary to coordinate on nonroutine, complex tasks that are reciprocally interdependent" and where information sharing is a "particularly valuable resource due to product complexity and industry uncertainty" (2003: 67). In our terminology, mutual trust can be particularly valuable where complex/reciprocal coordination and knowledge transfer are requisite features of venture success.

Attracting Better Stakeholders[19]

While the value of being able to participate in Communal Sharing relationships is obvious from the analysis above, the attraction of better stakeholders is not, thus leading to our second theoretical advance. Substantial variation exists in the quality of stakeholders of many types – customers, suppliers, employees, neighboring communities, and (even) shareholders. Although an economic world in which low prices are paid to suppliers, high prices are extracted from customers, low wages are paid to employees, low wage standards and low taxes exist in communities, and shareholders are "patient" investors constituted an ideal complement of

[19] Although firms have always been in competition for stakeholders (customers and employees come immediately to mind), the notion of competing for stakeholders was recently introduced as a "follow-on efficiency" by Tantalo and Priem in an article entitled "Value Creation Through Stakeholder Synergy" (2014: XXX). These authors write that "(t)he additional value offered to each essential stakeholder group will, in turn, allow the firm to compete more effectively for the fully engaged participation of high-quality stakeholders" (Tantalo & Priem, 2014: XXX). In a paper submitted to, but rejected by, AMR for this Special Topic Forum, these authors (and two co-authors) include the term "competing for stakeholders" in the paper's title and describe various means by which firms could compete successfully. Since none of the competitive strategies outlined in their paper have anything to do with the way that firms and stakeholders conduct their relationships, and since we eschew use of the term "competing for stakeholders," we are leaving these authors ample scholarly space for the development of their ideas.

stakeholders may never have existed, it certainly does not exist in the contemporary economy. The quality of a stakeholder group is defined in terms of the group's ability to contribute to the joint wealth creation effort of the focal firm in conjunction with its other relevant stakeholders. It is a function not only of many attributes, but also the fit of those attributes into the entire wealth creation effort centered on the focal firm. Examples of forms of variation among stakeholder groups include the following.

Customers will vary with respect to prices paid, product quality expected, flexibility regarding delivery schedules, ability to contribute to innovative product development, and ability and willingness to adhere to the relational norms that lead to greater wealth creation, among others.

Suppliers will vary with respect to prices charged, product or service quality, timeliness and flexibility regarding delivery, ability to contribute to innovative product development, adaptiveness with respect to changed conditions, and ability to adhere to the relational norms that lead to greater wealth creation, among others.

Employees will vary in terms of salaries/wages expected, talent (creativity, analytical skills, "people skills," adaptability, trainability), effort (perseverance, willingness to work additional hours when needed), loyalty to the company, and ability to adhere to the relational norms that lead to greater wealth creation, among others.

Communities vary in terms of local salary/wage standards, the presence of a skilled workforce, quality schools, tax rates, zoning restrictions, infrastructure quality, cultural and recreational attractions, and an ability to adhere to the relational norms that lead to greater wealth creation, among others.

Shareholders, sometimes thought to be concerned only with short-term share price increases, can also vary in ways that are quite important to firms. The existence and benefits of so-called “patient” capital are documented by Harford, Kecskes, and Mansi (2015). Shareholder propensities to file shareholder derivative and class action lawsuits also affect shareholder quality, as does the ability to adhere to the relational norms that lead to greater wealth creation.

What makes a stakeholder group “better”? Since there are a variety of attributes that make a stakeholder group a desirable partner, there is no obvious formula for superiority. However, one criterion must be met in all cases; the stakeholder group must be capable of consistently adhering to the norms of Communal Sharing relationships. This attribute is a necessary (but not sufficient) condition for stakeholder superiority, because without it the incremental wealth creation potential of Communal Sharing relationships drops to zero and the stakeholder becomes an inappropriate partner in the joint wealth creation effort. Furthermore, because firms with successful CCRE strategies are capable of engaging in valuable Communal Sharing relationships, they will be able to attract stakeholders with better portfolios of attributes (including adherence to appropriate norms), resulting in another source of value for CCRE business units.[20]

CCRE Strategies Are Rare

CCRE strategies are likely to be *rare* because many business units, for reasons related to organizational cultures, strategic choice, and economic incentives, will either not attempt to adopt the requisite norms or will fail to implement them successfully.

[20] Stakeholders may also be attracted to CCRE business units because the Communal Sharing relationships that they are capable of participating in allow them to be an integral part of something “larger than themselves,” an opportunity not readily available in non-CCRE firms.

First, not all managers recognize the potential gains – for their firms (competitive advantage) or for society as a whole (social welfare) – that may be available if they are able to successfully adopt CCRE strategies. For the most part, business education has stressed the pursuit of organizational self-interest as a means of achieving corporate goals (Ghoshal, 2005). Second, managers may believe that maximizing shareholder wealth is *morally* appropriate, particularly since scholars from Adam Smith (1776) to Michael Jensen (2002) have argued that social welfare is best achieved when corporations maximize profits. Therefore, they may believe that pursuing common interests leads to inferior outcomes, not only for themselves, but for society as well.

Second, not all managers are willing to adopt CCRE strategies. Many managers are subject to incentives – e.g., stock options, performance bonuses – that direct their attention to short-term (vs. long-term) financial goals. Since developing Communal Sharing relationships is likely to be a long-term endeavor, such managers may be reluctant to make the attempt. The longer-term benefits of CCRE strategies may be irrelevant if short term goals are not met.

Furthermore, CCRE strategies are risky. They involve a leap of faith that many managers may be unwilling to make. For example, revealing valuable proprietary information to a stakeholder partner without substantial safeguards can be quite costly if the partner proves untrustworthy. The same is true in cases in which the relationship operates without a formal contract and disputes arise over the appropriate distribution of responsibilities and/or benefits.

In addition, even managers willing to look beyond their short-term self-interest may believe that the behavioral changes required for the firm to adopt and sustain the lofty standards of good relational ethics would be too difficult to achieve. In other words, the dominant cultures of some firms may be too self-regarding to permit the building of trust between the firm and its stakeholders over any reasonable time span, thereby lessening the motivation of their managers to make the attempt. In some cases, managers may doubt the moral integrity of stakeholders in general (actual and potential) and may not be sufficiently motivated to ferret out suitable partners. Instead, they may prefer to rely on the reassuring safety of written contracts, monitoring, and potential sanctions.

Third, for a number of reasons, not all business units will be able to implement CCRE strategies successfully. The ambitious behavioral standards of CCRE are difficult to achieve and sustain, particularly since approximately half of all individuals begin with social dispositions that are either self-regarding and individualist (38%) or competitive (12%) (Au & Kwong, 2004; Bridoux & Stoelhorst, 2016). Furthermore, although slipping from Communal Sharing (or Equality Matching or Authority Ranking) relational modes to Market Pricing is quite easy, the reverse is difficult (Bridoux & Stoelhorst, 2016). Existing relational ethics norms within the business unit may be far removed from those of CCRE, or may be unclear or inconsistent. For example, the dominant objective of the firm may be too self-regarding – i.e., maximizing firm profits – to allow an individual unit to hew to the highly other-regarding norms of CCRE. In addition, managers of a relevant business unit may be concerned that evidence of self-regarding behavior on the part of their firms with respect to other stakeholders could make stakeholder partners reluctant to engage in Communal Sharing wealth creation efforts.

Furthermore, even if corporate objectives allow for other-regarding behavior, the unit's ability to consistently adhere to the norms of CCRE may not be adequate to sustain the relationships in which they are most valuable; that is, their partners, actual or potential, may not trust them enough to establish (or continue) relationships without formal governance structures such as written contracts, monitoring, and sanctions. This result could obtain if the culture of the focal unit is not strong enough or its strategy is not sufficiently coherent (or clearly articulated or adequately enforced). In addition, Communal Sharing relationships are likely to be quite vulnerable to perceived self-interested behavior (Bridoux & Stoelhorst, 2016) or breaches of trust (Jones, 1995). Even if the firm is able to adhere to the standards of Communal Sharing relationships, its reputation may not accurately reflect that ability, making potential partners reluctant to engage with them on the basis of CCRE behavioral norms.

Fourth, for many of the reasons outlined above, relatively few potential stakeholder partners will be willing or able to adhere to the norms of CCRE strategies. And because finding stakeholder partners with the requisite CCRE strategies can be difficult, managers may be reluctant to make the effort to identify them. Managers may doubt that the reputations of potential partners, on which judgments regarding potential adherence to CCRE norms are based, are reliable enough to assure Communal Sharing behavior on part of relational partners.

Authentic CCRE Strategies are Difficult to Imitate

A number of authors have emphasized the value of authentic ethics in situations that require trust (Frank, 1988; Jones, 1995). Schultz, Hatch, and Larsen (2000) argue that only authentic representations of a firm's character are likely to result in strong reputations. Because the stakes are often high in Communal Sharing relationships, strong reputations for CCRE are often necessary for the establishment of such relationships. Bridoux and Stoelhorst (2016) do not deal with authentic ethics *per se*, but they do stress the importance of high levels of behavioral consistency if any of the four of the relational modes that they describe are to succeed. More specifically, when a partner's actions are inconsistent, people tend to weigh *violations* of normative standards very heavily in assessing the partner's character (Fombrun, Gardenberg, & Barnett, 2000; Lewicki & Bunker, 1995).

Some firms may recognize the economic value of having good reputations for CCRE and will then try to acquire such reputations without being morally committed to the norms that underlie them – an example of *instrumental* behavior in the taxonomy of Jones, Felps, and Bigley

(2007). According to Barney and Hansen, "…exchange partners that are not *strong form* trustworthy have a strong incentive to assert that they are" (1994: 186). These "strong incentives" may lead firms to go beyond mere assertions. They may seek reputations for CCRE through instrumental actions – actions intended to build trust in order to take advantage of trusting partners if/when the resulting relationships cease to be advantageous, a textbook example of opportunism – i.e., self-interest *with guile* (Williamson, 1975; 1985). For our theory to be compelling, stakeholders (or firms) must be able to discriminate, with reasonable accuracy, between firms (or stakeholders) that are morally committed to the norms of CCRE and those that merely employ them instrumentally.

At this point, the important distinction between *authentic* CCRE – those implemented because the unit believes that CCRE are morally appropriate in relationships with relevant stakeholders – and *instrumental* CCRE strategies – those implemented because the unit believes that it will benefit from adherence to CCRE norms in relationships with relevant stakeholders – becomes important. As the research summarized above makes clear, authentic CCRE is the best way to reap the benefits of Communal Sharing relationships; instrumental CCRE may not achieve the desired results. Nonetheless, since Communal Sharing relationships are the most efficient mode of relating, and business units with CCRE are capable of engaging in them, many firms may try to imitate CCRE; that is, they may try to employ CCRE norms instrumentally. The relevant question with respect to imitability becomes: can instrumental CCRE strategies successfully imitate authentic CCRE?

The difficulty with which a resource/capability can be imitated is closely linked to the sustainability of competitive advantage. Imitability, in turn, is related to path dependence (the manner in which firm resources develop over time), causal ambiguity (difficulties in determining the sources of a firm's competitive strengths), and social complexity (difficulties in replicating complex social phenomena) (Barney, 1991). The internal workings of particular firm/stakeholder relationships are likely to be opaque to outsiders, especially since CCRE norms have numerous facets, most of which are not visible to competing firms. Therefore, Communal Sharing relationships may be causally ambiguous as well as socially complex (not to mention counterintuitive in a competitive economic environment). Although we believe that these features are sufficient to make CCRE relatively inimitable, we focus on elements of CCRE that make them even more difficult to imitate. In the discussion that follows, we address both the difficulty of imitating CCRE successfully and the difficulty of acquiring and maintaining a reputation for CCRE.

Imitating authentic CCRE is likely to be difficult. Several potential pitfalls may foil attempts to apply instrumental CCRE strategies successfully. First, the standards of CCRE – i.e., those compatible with the norms of Communal Sharing relationships – are high indeed. It would likely be quite a stretch for a firm accustomed to ORE, based on opportunistic behavior, or CRE, based on competitive behavior within "rules of the game," to suddenly adopt such "aspirational" behaviors as making voluntary contributions to joint endeavors or willingly sharing relevant knowledge, especially proprietary knowledge.

Second, participation in successful communal sharing relationships requires that relevant business units adhere to the norms of CCRE strategies virtually all, if not all, of the time. This consistency must be maintained across all members of the unit as well as over time. Indeed, the relevant business unit must achieve a very high level of moral homogeneity, meaning that all members of the unit must exhibit nearly uniform moral behavior around the norms of Communal Sharing – CCRE in this case. [The uniformity standard applies to Equality Matching, Authority Ranking, and Market Pricing relational modes as well (Bridoux & Stoelhorst, 2016).] While theoretical and empirical support for substantial levels of moral homogeneity among organizational employees is generally strong,[21] some empirical evidence has suggested that very high levels may be difficult to achieve (O'Fallon, 2007; O'Fallon & Butterfield, 2011). Furthermore, if the level of adherence to theses norms is not very high, the behavioral standards required for successful Communal Sharing may not be met. Even if a mere hint of intellectual property appropriation from a contributing partner damages no one, it could do irreparable harm to mutual trust in the relationship. Furthermore, in cases of actual IP theft, if the thief does not intend to stay with his/her organization, assurances of corrective sanctions by his/her organization may be moot. For another example, if a dispute emerges and one party threatens, or even suggests the possibility of, legal action, proceeding further without a formal (expensive and cumbersome) contract may be difficult. In short, the norms of CCRE have to be adhered to with a very high degree of consistency. Furthermore, as Frank (1988) and others have argued, reputations for moral behavior are difficult to build and easy to lose; one breach of commitment could reveal a calculus of self-interest and destroy a reputation for CCRE. Work on reputations in social networks suggests that negative information about character flaws spreads more rapidly and more completely than positive information (Burt & Knez, 1996; Fombrun, Gardenberg, & Barnett, 2000). Second, even if intentions are uniformly good, cultures are notably difficult to change and may be especially so if the direction of change runs counter to the forces that make the norms of CCRE strategies *rare*, as argued above.

In addition, when the risks of opportunism are high – e.g., when project-specific investments or proprietary knowledge are involved – stakeholders (or firms) trying to identify partners suitable for

[21] Theoretical and empirical support for moral homogeneity can be found in a large number of literatures, including the attraction paradigm (Byrne, 1971), value homophily (Lazarfeld & Merton, 1954), conformity research (Asch, 1951), conformity by omission (Sorrels & Kelley, 1984), cognitive moral development (Kohlberg, 1969), organizational identification (Bruner, 1957; Dutton, Dukerich, & Harquail, 1994), moral approbation (Jones & Ryan, 1997), social learning (Bandura, 1977), hierarchical authority (Milgram, 1963), social identification (Ashforth & Mael, 1989), person-organization fit (Chatman, 1989), attraction-selection-attrition (Schneider, 1987), groupthink (Janis, 1972), automatic ethics (Bargh, 2006), "Monkey See, Monkey Do" (Robinson & O'Leary-Kelly, 1998), organizational scripts (Gioia & Poole, 1984), assortative matching (Becker, 1973), and corrupt organizational forces (Pierce & Snyder, 2008), among others.

Communal Sharing relationships will have substantial incentives to invest considerable effort in making appropriate choices. Careful identification of potential partners will result in fewer errors, further strengthening the link between corporate reputations for relational ethics and actual corporate behavior.

Reputations and Authentic CCRE

In order for the central claim of this essay – i.e., under certain circumstances, successfully adopting CCRE can lead to sustained competitive advantage – to be compelling, firms *and stakeholders* must be able to identify, with reasonable accuracy, those potential partners with whom they can engage in Communal Sharing relationships – i.e., those they can trust to uphold the standards of CCRE.

Since the propensities of firms and stakeholders to adopt CCRE may be hidden from view, they cannot affect a firm's access to such relationships directly. Instead, they must be perceived by others, directly or indirectly, based on observable behavior and, to some extent, on articulated intentions (Barney & Hansen, 1994). The mechanisms through which such perceptions are formed, maintained, and modified have been subsumed under the heading of corporate reputation. Fombrun, in consolidating perspectives from several academic disciplines, defines corporate reputation as "...a collective representation of a company's past actions and future prospects that describes how key resource providers interpret a company's initiatives and assess its ability to deliver valued outcomes" (2002: 10).

Several features of this definition are worth emphasizing. First, as noted above, reputations are perceptual; they must be derived from interpreted information, either first hand or through others.[22] Second, they are externally perceived and cannot be directly controlled by managers (Barney, 1986). Third, they represent the collective judgments of many individuals. Fourth, they are simultaneously past- and future-oriented, representing assessments of future behavior based on past behavior. Finally, Fombrun (1996; 2002) regards reputations as reconciliations of multiple images of the firm held by others that represent its *overall* attractiveness to stakeholders. However, we agree with Carter and Deephouse (1999), who argued that corporate reputations can be productively broken into components, allowing for a more nuanced assessment of their effects. Our position is that reputations for relational ethics need not be fully compatible with overall reputations. For example, a firm could have an excellent reputation for ethical dealings with its stakeholders without having a reputation for highly innovative products. In addition, reputations for relational ethics may vary across stakeholder groups.

With respect to the establishment of relationships based on the norms of CCRE, reputations are particularly important because they convey valuable information about firm trustworthiness and cooperativeness (in the absence of formal contracting, incentive alignment, monitoring, and sanctions) and, therefore, about their attractiveness as partners in such relationships (Jones, 1995). Indeed, empirical studies have found that firms with reputations for low status, incompetence, or *unethical behavior* are comparatively undesirable exchange partners (Podolny, 1993; Stuart, Hoang, & Hybels, 1999; Sullivan, Haunschild, & Page, 2007).

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[22] Since reputations are social constructions (Fombrun, 2002), an individual firm's reputation is a function not only of its "true" nature, but also of interpretations made by third parties – e.g., financial analysts, the media, rating agencies – and by stakeholders themselves. Since attractive stakeholder perceptions of the company can be an important element of competitive advantage (Rindova & Fombrun, 1999), firms will often attempt to alter, strengthen, or maintain their reputations through corporate-level impression management. Rindova and Fombrun (1999) use the term "strategic projections" to describe corporate attempts to convey favorable signals to others in the marketplace through such devices as advertising campaigns, communications with analysts, contributions to charities, and campus receptions. Godfrey (2005) provides an excellent analysis of the role of philanthropy as a form of strategic projection.

What factors affect the reputations that firms have with respect to relational ethics? First, the intentions of a firm's top management team can make an important difference. Firms with managers who believe in and intend to employ either ORE or CRE in their dealings with stakeholders will be unlikely to be mistaken for firms that wish to employ the norms of CCRE for two reasons. First, their behavior, compatible with the norms of these "arm's length" relationships, will be so far removed from the behavior required to acquire and maintain a reputation for CCRE that potential partners will rarely, if ever, try to engage them on the basis of CCRE. Second, these firms will spend few resources on "strategic projections" (Rindova & Fombrun, 1999) intended to enhance their reputations since they see little value in so doing. Thus, firms that employ arm's length norms will almost always have reputations that reflect that orientation. Similarly, firms fully committed to dealing with stakeholders based on the norms of Communal Sharing will rarely violate those norms and, therefore, will usually be able to establish and maintain reputations for CCRE with relative ease. Although behavior and reputations will not always be perfectly correlated for such firms, the identification process should be reasonably accurate, bestowing good reputations on most firms whose relational ethics are compatible with Communal Sharing relationships.

Of course, reputations for relational ethics can never perfectly reflect the commitments that underlie them. Barney and Hansen call the signaling process "noisy" (1994: 187). Thus, the reputations of some firms that instrumentally project an artificial commitment to the norms of CCRE may be sufficiently good that stakeholders will be convinced that their commitment is genuine, and establish Communal Sharing relationships with them.

The accuracy of reputational information with respect to relational ethics is, of course, an empirical issue that we cannot resolve here. However, in the following section we present theoretical reasons for optimism regarding a reasonably strong link between *reputations* for commitment to CCRE norms and *actual commitment* to those norms. In other words, we maintain that reputations for relational ethics will reflect, in general, the true intent of the firms (or stakeholders) in question and will constitute a good basis for discriminating between authentic and instrumental projections of CCRE.

One important difference between authentic relational ethics and instrumental relational ethics involves the decision criteria employed. Authentic relational ethics, in which behavior is based on the belief that "this is the right thing to do," involves a set of heuristics – i.e., decision rules to apply in certain situations. Instrumental relational ethics, in which behavior is based on a belief that "this will benefit us," is likely to involve a cost/benefit calculus regarding "what behavior will benefit us." As Frank (1988) and Jones (1995) argue, the difference is critical. The use of a "right thing to do" heuristic will consistently result in behavior compatible with the norms of the relational mode in question. The use of a "this will benefit us" calculus leaves open the question of appropriate behavior when the benefit is in doubt. Business units morally committed to complying with the norms of CCRE will not apply the calculus of self-interest to their relational commitments and will be unlikely to behave in ways that will damage their reputations.

Firms applying CCRE instrumentally may view behavior consistent with Communal Sharing relationships as an investment in a reputation for CCRE. That is, the opportunity foregone when the firm acts altruistically toward its relational partner(s) constitutes a cost that it hopes to more than compensate for in benefits from the Communal Sharing relationship. This approach to the establishment of the desired reputation has its perils, however.

Since reputation maintenance mainly involves the cost of opportunities foregone, and since managers (like people in general) are strongly biased in favor of immediate and definite (rather than temporally distant and potential) benefits (Frank, 1988; Jones, 1995), firms attempting to use relational ethics instrumentally are unlikely to forego short term payoffs often enough to build or maintain reputations for CCRE. Furthermore, in situations with both cooperative and competitive norms at work, self-interested norms tend to dominate (Chatman & Barsade, 1995; Malhotra & Murnighan, 2002; Ratner & Miller, 2001). In addition, the incentives faced by managers – e.g., rewards based on short term results – are unlikely to change easily to allow Communal Sharing relationships to develop.

For these reasons, there is likely to be: 1) considerable "under-investing" in CCRE by those hoping to do so instrumentally; and 2) significant penalties for those who violate the standards of CCRE. Because the norms of CCRE represent a heuristic, rather than a calculative, approach to firm-stakeholder relationships, firms adopting CCRE norms face a far less difficult decision making process than those applying relational norms instrumentally. In the latter case, "irrational" decisions may be hard to avoid. Maintaining a reputation for CCRE will be quite problematic for many firms that attempt to do so instrumentally. It will be difficult for them to consistently "get it right" – i.e., to act morally when, and only when, it is in their best long-term interest. Thus, stakeholders and firms will often be able to discriminate between authentic and instrumental applications of CCRE, making the latter difficult to parlay into good reputations.

Imitating authentic CCRE may be difficult for another reason. The relational ethics of the entire firm of which the focal business unit is a part may be relevant to a stakeholder selecting partners for a Communal Sharing relationship as well. If a firm treats another stakeholder group substantially worse than it treats potential partners in Communal Sharing relationships, the instrumental nature of this selective application of morality may not be lost on potential partners, making engaging *any* stakeholder group on the basis of CCRE norms difficult. The best way to *appear* authentic may be to *be* authentic by maintaining consistently good relational ethics (if not CCRE) in dealings with all stakeholders. Bridoux and Stoelhorst (2016) provide three reasons and reference a number of studies in support of this conclusion.

To consolidate, we have argued that there are good reasons to expect that: 1) it is difficult to imitate the behavioral standards of CCRE; and 2) reputations for CCRE will be a reasonably good means of discriminating between authentic and instrumental versions of CCRE strategies. In short, it is difficult to imitate the relational ethics compatible with valuable Communal Sharing relationships.

CCRE Strategies Are Not Easily Substituted For

Because the attributes of CCRE strategies are qualitatively different than those of ORE and CRE strategies, they are uniquely compatible with Communal Sharing relationships. The behavioral standards of ORE strategies, with their opportunistic orientation toward economic partners, are thoroughly unsuited to Communal Sharing relationships and certainly cannot be substituted for CCRE strategies. Firms that act exclusively in their self-interest, even if they do so *with guile*, will not be able to maintain the reputations necessary to find willing partners for long (Jones, 1995; See also Frank, 1988). If they repeatedly use power differentials and information asymmetries to their advantage and are frequently involved in litigation with stakeholders, prospective partners will require, at minimum, the protection of detailed, highly specified and costly contracts.

CRE strategies are also incompatible with Communal Sharing relationships because they lack the capacity to make voluntary contributions of effort and knowledge that such relationships require. In addition, firms with CRE strategies prefer not to operate without reasonably specific written contracts, which are expensive and time-consuming to write, making the speed and flexibility requirements for successful operations in the relevant environments impossible to achieve. More generally, CRE strategy firms retain a self-interested posture that makes a joint wealth creation partnership orientation impossible. Some level of mutual trust is possible under CRE strategies. They will not make promises that they do not intend to honor, renege on their commitments, or violate the terms of contracts. However, where contracts cannot be precisely written or become imprecise as conditions change over time, CRE firms will press any advantage that emerges with company interests firmly in mind. Nor can CRE firms be trusted to eschew the use of information advantages in "zero-sum" negotiations and they may view litigation as a preferred means of settling disputes. In short, CRE firms will play by generally understood rules of business practice; that is, they regard firm/stakeholder relationships as having a substantial competitive element as well as elements of cooperation. With CRE firms, the idea of "stakeholders as partners" has very limited applicability. As such, they are incapable of facilitating complex, high velocity, reciprocal coordination and sharing of valuable knowledge. Clearly, the three points that we highlighted on the continuum of relational ethics strategies – ORE, CRE, and CCRE – have very different implications for the establishment of mutual trust in firm/stakeholder relationships; high levels of mutual trust are critical elements of Communal Sharing relationships.

Firms with CCRE strategies, however, can be viewed as highly trustworthy with respect to the critical facets of firm/stakeholder cooperation – complex/reciprocal coordination and knowledge sharing. The *consummately-cooperative* trustworthiness associated with CCRE goes well beyond the trustworthiness inherent in CRE. CCRE firms regard their relationships with relevant stakeholders as partnerships wherein joint goals are sought by both partners. With respect to coordination, they engage in cooperative decision making that seeks better solutions for the partnership as a whole, rather than only for the focal firm. They make voluntary contributions to the joint effort and address disagreements or changed conditions in a cooperative manner. Since they prefer to operate without formal contracts, they rarely, if ever, resort to costly litigation. With respect to information sharing, firms with CCRE strategies willingly share information relevant to the joint effort and, because they can be trusted not to exploit proprietary knowledge revealed by their partners, encourage these partners to do the same. Opportunities for which the value of knowledge cannot be known in advance can be exploited because the partners will work cooperatively to distribute rewards once the venture has succeeded. Finally, since tacit knowledge is valuable, and often essential, to the joint effort, it will be readily shared as well. In short, CCRE strategies facilitate the very high levels of cooperation implied by the term *consummately-cooperative*. As such, CCRE firms are positioned to fully exploit coordination and knowledge sharing efficiencies: ORE and CRE strategies are not.

Conclusions and Implications

The most striking conclusion that can be drawn from the six excellent articles that make up this Special Topic Forum and our own examination of the role of social welfare in management theory is that assessing and measuring social welfare is a very complex and difficult undertaking. One theme that emerges from the included articles is that social welfare cannot be understood in terms of economic efficiency alone. Two articles (Marti & Scherer, 2016; Mitchell et al 2016) directly address this issue, and a third (Cobb, 2016) addresses it implicitly. Marti and Scherer (2016) and Cobb (2016) focus on issues of distributive justice, while Mitchell et al (2106) make it clear that there are multiple values worth preserving. Unfortunately, assessing social welfare in terms of multiple incommensurable measures is well beyond our current capabilities. As a result, we focus on economic welfare first and take distributive justice into account after the fact.

In terms of economic welfare – i.e., wealth creation – alone, we examined three possible approaches to improving social welfare and speculated on a fourth. First, we concluded that the current practice of equating shareholder wealth improvement to social welfare improvement – explicitly or implicitly – should be abandoned in both management theory and management practice. The assumptions on which the model that supports this conclusion is based bear no resemblance to the realities of 21st Century market capitalism. Furthermore, many actions taken by corporate managers in order to improve company profits harm non-shareholder stakeholders of the firm. The losses must simply be absorbed by these stakeholders. Indeed, they are rarely, if ever, measured or counted in calculations of economic efficiency. For this reason, it is likely that some of these actions do not result in net improvements in social welfare, and some may actually result in social welfare losses. Furthermore, in many cases, because shareholders gain at the expense of other stakeholders, distributions of incomes and wealth become increasingly unequal, a distributive justice concern. Finally, actions taken under the banner of shareholder wealth improvement are fundamentally coercive; that is, the losses of non-shareholders are not voluntarily accepted.

The one approach that yields unambiguous improvements in social welfare, at least with respect to the discrete action under consideration, is the Pareto Improvements criterion. Making someone better off without making anyone else worse off does improve social welfare. However, corporate actions for which there are winners but no losers make up a relatively small proportion of all such actions, meaning that the Pareto criterion cannot be widely applied. Furthermore, although voluntary economic exchanges, by definition, improve the welfare of both parties, differences in bargaining power may mean that repeated Pareto improving exchanges lead to increasingly unequal distributions of income and wealth. Nonetheless, no coercion is involved in the voluntary exchanges that underpin Pareto Improvements.

Employment of the Kaldor Improvements criterion holds out the possibility of obtaining actual social welfare improvements for a full range of corporate decisions. If winners could (hypothetically) compensate losers for their losses and still register gains, social welfare would be improved. The hypothetical nature of this criterion is key here. As long as no actual compensation is involved and the gains of the winners exceed the losses of the losers, the Kaldor criterion is satisfied. And, although greater economic efficiency is achieved, distributions of income and wealth are likely to become substantially more unequal. In addition to this distributive justice concern, Kaldor Improvements clearly involve coercion; losers do not accept their losses voluntarily.

An approach that we represented as an "intriguing line of inquiry for future exploration" might be called Kaldor Improvements with Compensation. Because this approach is laden with thorny theoretical and practical problems, a full exploration of the prospects for this criterion would involve an analysis well beyond the scope of this paper. However, other scholars might give this possibility further consideration, particularly in view of the fact that shareholder wealth gains are measured in share price increases which grow in proportion to the price/earnings ratio of the firm's stock (usually 10-1 or more) rather than in direct proportion to stakeholder losses. If this relationship holds, ample resources could be made available to compensate (in company stock) those harmed by actions taken to increase shareholder wealth.

We note that two of the articles included in this Special Topic Forum appear to be based on Pareto Improvements, the one social welfare criterion that can be unambiguously linked to social welfare improvement. Bridoux and Stoelhorst (2016) show that Communal Sharing firm/stakeholder relationships are more efficient than other relational modes. Since no other stakeholders appear to be harmed, the Pareto criterion is met. The same conclusion can be reached with respect to the Bosse and Phillips (2016) article. Introducing notions of fairness and reciprocity into the contracting process involving the firm's board and its top executives could result in reduced agency losses and possible agency benefits in corporate governance. No stakeholder group appears to be harmed in this revised process, again meeting the Pareto Improvement criterion.

Our own contribution also relies on the Pareto Improvement criterion, albeit indirectly through the work of Bridoux and Stoelhorst (2016). The Pareto Improvement noted above survives our attempt to link sustained competitive advantage, a major theme in strategic management research, to the social welfare gains well documented by these authors. This theoretical extension of the work of these authors through the introduction of Consummately-Cooperative Relational Ethics (CCRE) represents an example of the compatibility of some profit improving measures with the social welfare enhancement – i.e., real wealth creation.

In terms of the implications of this Special Topic Forum in general, and of our editorial introduction in particular, we offer the following. With respect to management scholarship, Marti and Scherer (2016) remind us that our theories not only describe social reality, they also shape it. With this caveat in mind, we strongly urge management scholars to take social welfare considerations into account in their theorizing and empirical research. This consideration could take the form of a thoughtful assessment of the social welfare implications of their work; relying on the assumption that increasing shareholder wealth invariably leads to social welfare advances can no longer be justified. The same recommendation applies to practicing managers as well; Friedman's (1970) claim that "the social responsibility of business is to increase its profits" cannot be taken as gospel any longer. In addition, we hope that management scholars will be inspired to directly address social welfare concerns in their theory building and empirical studies. If they do, we need not experience another "eerie silence" with regard to social welfare issues in management research once the dust settles on this Special topic Forum. And, if theories do shape social reality, as we believe they do, the "better world" envisioned by the Academy of Management may begin to take shape.

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Figure 1a – The Economics of Profit Making (from Peteraf & Barney, 2003)

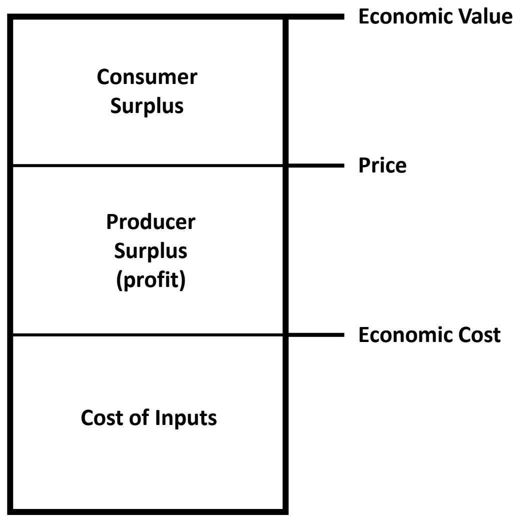

Figure 1b – The Components of Economic Value