In the Lisbon strategy the European Union adopted a threefold goal for its economy and the economy of its member States. The priority is to make the economy the most competitive in the world by basing it on knowledge as the crucial factor of increasing economic growth. But the strategy makes it clear that in itself economic growth, however valuable as a goal, is meaningful, if it fits into two other overarching goals. A free market economy is desirable not only to the extent that it is produces wealth, but only if it is generating more and better jobs and contributing toward greater social cohesion.

As a political instrument, the Lisbon strategy aims at reconciling economic freedom with legitimate social concerns. It promotes economic freedom, but not at the expense of employment prospects and social inclusion. This collective political exercise on the part of the Member States of the European Union is understandable and rather urgent in view of the increasing risk of unemployment and poverty in Europe today.

The Lisbon strategy evidently calls for action on several levels. One level, which is particularly significant in the context of this paper, is the ethical. Almost contemporaneously with the adoption of the Lisbon strategy, the European Commission for Employment and Social Affairs issued a Green Paper *Promoting a European Framework for Corporate Social Responsibility* (2001). This important document is a continuation and a further development of a line of thinking that has been going on both within an increasing number of European companies and within the European Union itself. Several European companies have been already trying to look at their business activities in more than just economic terms by taking into account the so-called externalities such as the impact on the environment and the impact on the community in which they have been operating. At the European level, one can mention several initiatives. The Lisbon European Council appealed to companies to develop best practice on lifelong learning, work organization, equal opportunities, social inclusion and sustainable development. Similarly, the Commission’s European Social Agenda, the European Council in Nice and at Goeteborg endorsed the principle of corporate social responsibility.

The European Union’s interest in corporate social responsibility is part of a broader picture that has been evolving at the international level in recent years. The UN launched the *Global Compact* (2000), calling on global business leaders to subscribe to nine shared
values and principles in the areas of human rights, labour standards and environmental practices. The ILO adopted the *Tripartite Declaration concerning Multinational Enterprises and Social Policy* (1977/2000) and proposed as its primary goal in the current period of global transition the securing of decent work for women and men everywhere (1999). Decent work is described as “a global demand today, confronting political and business leadership worldwide”. The OECD issued a set of fairly elaborate ethical *Guidelines for Multinational Enterprises* (2002).

In view of the growing consensus concerning the crucial importance of corporate social responsibility for the development of good and right business, one understands why the European Union has continued to follow up its initial project as detailed in the Green Paper. A significant step has been the setting up of a EU Multi-Stakeholder Forum on CSR with the aim of promoting transparency and convergence of CSR practices, through: exchange of experience and good practice between actors at EU level, bringing together existing initiatives within the EU with a view to establishing a European approach and identifying and exploring areas for further action. The latest Communication from the Commission on the subject, *Implementing the Partnership for Growth and Jobs: Making Europe a Pole of Excellence on Corporate Social Responsibility* (2006), confirms the continuing input which the EU is placing into corporate social responsibility.

The promotion of corporate social responsibility not only on a European but also on a world level rests on the *assumption* that business enterprises should be inspired and motivated by a set of values that incorporate but go beyond purely economic ones. This assumption implies an understanding of the business firm as more than a merely economic enterprise. By an “economic enterprise” what is meant is an enterprise that is established to generate wealth (through efficient use of the factors of production and channels of market distribution) for well defined constituencies, namely, shareholders (in the form of increase in share value), employees, including management, (in the form of higher wages and salaries) and consumers (in the form of good products and services at market prices).

In describing a business firm as an organization designed to generate wealth, one is evidently giving a short-hand definition, for even if it is so defined, a business firm involves a nexus of contracts, particularly those relating to work or buying/sale transactions. Some of these contracts are more defined than others but as contracts they give rise to specific rights and obligations. I am making this point, which is rather obvious but which is not always seen and made, since the implicit moral dimension is generally missed, when describing a business firm as a profit-making enterprise. So even in this, evidently narrow, sense a business firm is a moral agent in so far as it is bound by contractual obligations in its *internal* (employees) and *external* relations (suppliers, consumers and, in virtue of tax law, society).

The promotion of corporate social responsibility raises the problem concerning the real moral status of the business firm. Why should the range of responsibility of business firms be extended to a wider circle of constituencies by making firms morally responsible for other than specifically economic issues, namely, issues relating to the more efficient use of productive resources? Even more important, however, is the moral status of the business

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firm: in what sense can the firm be a moral agent? These are very important questions to consider, if corporate social responsibility is not to end up being just an “option” which business firms simply may or may not take up. The fact that many business enterprises do include social responsibility as part of their mission statements does not necessarily show that they understand its fuller moral implications. They may well be driven by motivations such as the market value of a good reputation or the fear of tighter control through further legislation. Motivations of this kind can help to a certain extent in changing corporate ways of thinking and behaving but they cannot sustain any long-term commitment to the broad set of values implied in corporate social responsibility.

The Diocesan Commission for Justice and Peace has recently issued a reflection paper on housing and related matters. I would like to begin with some reflections on this paper, as it provides a typical scenario for a discussion on corporate social responsibility in practical and concrete terms. As the concept of corporate social responsibility covers a wider set of issues than those covered in this case, I will then consider some of the basic features of corporate social responsibility as it is generally understood. Against this background, I will discuss two paradigms regarding the business firm as a moral agent, namely, the ‘contractual’ and ‘partnership’ paradigms. As I shall explain, the contractual paradigm has two versions: one based on the concept of the business firm as a profit-generating organization, while the other is based on the business firm as a nexus of a wider set of contracts than that implied in the concept of the firm as a purely economic enterprise. I shall be arguing that a business firm can develop and maintain a true sense of responsibility, if it understands itself in the light of both the contractual paradigm, in its two versions, and the partnership paradigm.

The Case of Housing

The Paper by the Diocesan Commission for Justice and Peace is written in response to the state of the housing market in Malta which does indeed give rise to serious social concern. Housing is a basic human need. As is the case with all basic human needs, the housing problem can be properly met, if it is met in a decent manner. Not any kind of accommodation would do. It should be decent accommodation. In this particular case, the problem lies in the escalating cost which young couples generally have to pay in order to find decent accommodation in which to live after marrying. Referring to the findings of The Building Industry Consultative Council, the Paper observes that the average contract price for flats increased by 16.6% in 2004 and by 20.34% in 2005. The average contract price of maisonettes increased by 17.49% in 2004 and by 15.32% in 2005. Allowing for differences in the interpretation of the statistical data published by the National Statistics Office, the Paper concludes that the price of flats and maisonettes has increased by a rate varying between 5% and 30%, depending on the size and quality of the property.

What relevance does corporate social responsibility have in relation to this problem? More specifically, one may ask: In what sense and in what way are business firms, particularly financial institutions and estate firms, expected to respond to a problem which is certainly

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2 The 5 page document “Reflection Paper on Social Issues: Housing and Related Matters”, by the Diocesan Commission for Justice and Peace was published by the Media Office, Archbishop’s Curia, Floriana, Malta on 05/01/07, hereinafter referred to as “Reflection Paper".
weighing heavily on a sector of the population but which belongs, strictly speaking, to the social and political rather than the economic domain? One position, which is not to be branded a priori as anti-social, is that originally propounded by Milton Friedman.\(^3\) It may perhaps be more properly described as social in a limited sense. In fact, Friedman himself argued that business has a social responsibility which he narrowly described as the responsibility of business to increase its profits. He accepts that there are limits to profit-making but these are established by law and the workings of a free market economy. The freedom of individuals, groups and organizations to engage in economic activity, he claims, is a basic value which should not be undermined by expecting business to promote “desirable” social ends such as providing employment, eliminating discrimination and avoiding pollution. In line with this position, business firms operating in the housing market have no particular moral obligations except the moral obligation to operate within the relevant legal provisions. The underlying presupposition of this position is that the less the law intervenes the better it would be for economic freedom and efficiency. So how should one expect business firms to respond in the context of the local scenario where the housing market is evidently creating a serious social problem?

On the basis of a free-market economy, it may be argued that the market should be allowed to operate freely in the housing sector. The State would, of course, remain equally free to adapt its housing policy and update the law in the public interest, especially in the interest of those in vulnerable situations. Civil society, acting through a variety of non-government institutions, including the Church, would also be free to intervene either by giving direct help (especially to those who are unable to cope on their own) or by creating greater social awareness. Intervention on the part of the State or civil society is not in dispute, as this is an integral part of their respective responsibilities. To Friedman, however, the key point is that a corporate executive is an employee of the owners of the business, having direct responsibility to the owners. In that capacity, one’s responsibility is “to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of society both those embodied in law and those embodied in ethical custom”.\(^4\)

The business firms operating in the local housing market, I would assume, do not feel any particular responsibility for the escalating cost of houses and the problem that such a situation is creating for individual men and women, including children, and for society as a whole. One could even say for instance, that financial institutions, in providing home loans, are giving people an opportunity that they would not otherwise have, namely to buy their own home. Indeed, this is an important public service. There is, however, another side to consider. The availability of money to a relatively broad section of the population is in itself a significant factor in the escalation of prices. Whether banks have any moral responsibility for their share, albeit an indirect one, in the housing problem is very difficult to say. But the fact that the market is creating hardship for people to meet a basic need should provoke all those taking part, including firms, to review certain aspects of their practice. For instance, a bank’s board of directors may decide to give not only its employees, as some banks are


\(^4\) Ibid., p. 20.
already doing, but also couples with a low income the opportunity to borrow at a more favourable interest rate.

Initiatives of this kind would not by themselves solve the problem. The problem can only be solved through action on several levels. A case in point is the periodic intervention of the Central Bank to increase the interest rate. If no provision is made to ease the impact of such a measure on people who are already financially burdened with home loans, the problem would worsen. Moreover, positive action taken by a bank may be offset by negative action taken by an estate firm. The Diocesan Commission expresses its serious concern about “the current practice whereby, apart from the principal contracted estate agent, a number of other individuals/consortia also involve themselves, through the right of substitution, as middlemen in the chain of property deals”. What is this worrying practice? The practice may not be a general one. But irrespective of how widespread it may be, it is clearly a speculative practice. It is a form of misuse of the right of substitution. This right allows for the property being sold to change hands a number of times at the purchase/demolition/development stages before it is finally sold to the occupier. In the process, the price is increasing and the amount which one pays at the end of the deal-chain is higher, and sometimes substantially higher, than the original price. In other words, money is made simply on trading a right which the law gives to facilitate the transfer of property and presumably to prevent and not to promote inflation in a particularly vital sector of social life. In this particular case, one may not claim that inflation is not an issue for business.

This case is particularly relevant to show that regulating business by means of the law, however important and necessary, is not enough for business to maintain a human face. I shall be developing this point further when discussing the concept of corporate social responsibility as a ‘voluntary’ project which may not therefore be imposed on, but only proposed for, business firms. Are business firms simply invited to exercise social responsibility - an invitation which they may accept or refuse without incurring any legal sanction - or are they expected to exercise social responsibility out of a sense of justice which is at the basis of both morality and law? This is a basic question for understanding the nature of corporate social responsibility and in what sense a firm can be described as a moral agent. Let me first discuss the main features of corporate social responsibility.

**Corporate Social Responsibility**

As the concept of corporate social responsibility had already acquired a core meaning by the time that the European Commission through the Directorate-General for Employment and Social Affairs was preparing the Green Paper, *Promoting a European Framework for Corporate Social Responsibility* (2001), the concept was defined as it was generally understood, namely, as “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis”.

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5 “Reflection Paper”, p.3.

6 Section 2.
There are three points that I wish to consider in this definition: (i) the notion of companies as interactive entities, (ii) the responsibility of companies to integrate economic with social and environmental concerns and (iii) corporate social responsibility as a voluntary matter.

A key element in the definition of corporate responsibility is the idea of companies as interactive entities. Business activity is interactive. People interact with each other in all spheres of life, either on a personal or on an organizational level. The social space created through so many forms of human interaction at various levels depends on the nature and quality of the way in which people are interacting with each other. In other words, the yardstick that we need in order to determine the value of any human activity can ultimately have only one frame of reference, namely, the kind and quality of inter-relations which human interactions are establishing and maintaining. Since all human activity has a moral dimension, this yardstick holds for every type of human activity.

A characteristic feature of business activity is that the medium through which people interact with each other is money. In business, money is the universal medium of exchange. Work is exchanged for money, products and services are exchanged for money, the value of one’s property, in whatever form, is calculated in monetary terms. The performance of business firms is established on the basis of the balance sheet of income and expenditure. The country itself assesses its economic strength in terms of the Gross National/Domestic Product. Money, as we know, is a source of temptation, as the desire to possess can tempt one to all sorts of wrong-doing. This is the primary reason why the law would have to intervene to protect the interests of the vulnerable side. But the law can only provide protection up to a certain extent, since it generally lays down the minimum required in the socio-historical circumstances of the time.

The law establishes the minimum wage. Indeed, one expects to be remunerated for one’s work, but the meaning and value of work cannot be determined in monetary terms and certainly not by the minimum wage. Work means much more than the wage or salary one receives. Similarly, implementing adequate safety requirements involves additional production costs but doing this is a measure of the kind of respect shown for the safety of people at work. The price paid for a product or a service means more than a gain to the seller and a cost to the buyer or receiver; it reflects the respect of the seller for the dignity and respective rights of the buyer. Cost-cutting is a continuing imperative in business. When costs are cut to render the business more ‘efficient’, it is only reasonable to ask at whose expense the exercise is being carried out.

In saying all this, one is not trying to minimize or to under-rate in any way the value of the financial aspect of business. But the original frame of reference for a truly meaningful activity of any kind, including business, is the nature and quality of interactions and inter-relationships that are being established. Of course, business is business in that its efficiency is determined by the logic of income and expenditure. It can serve, however, a truly ‘human’ purpose to the extent that it is enabling human beings to live a decent life.

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The definition of corporate social responsibility presumes that firms can be in a position to integrate a variety of concerns into their business operations and into their interaction with stakeholders. As a moral concept, responsibility involves precisely the virtue or the capability (so it needs to manifest itself as part of an ongoing practice) of integrating a variety of concerns which in their ensemble reflect a basic respect for the good of the person as a whole and of each and every person.

The way in which corporate social responsibility is defined presupposes the way in which business is generally organized. On one side, there are the companies themselves operating in accordance with the policies set by the Board of Directors, representing the owners; on the other, there are the people working for the companies, the local communities in which the companies are operating, business partners, suppliers and consumers, and, one may say, society (even mankind) at large in so far as business operations can have an impact on the dignity and rights of human beings and the environment. The idea that there are several constituencies (people) who have a stake in the operations of business companies ties up with the idea of businesses as interactive entities. Interaction creates inter-dependence. Inter-dependence requires an effective regulatory framework to prevent the stronger from taking advantage of the weaker and more vulnerable side. The contractual paradigm of the firm, as I shall be explaining, presumes precisely that the firm has contractual obligations, some of a legal and others of a moral nature, toward several constituencies or stakeholders.

The nature of corporate social responsibility can be easily misunderstood if its fuller implications as a voluntary matter are not adequately brought out. By ‘voluntary’, what is generally meant is ‘not obligatory’. Corporate social responsibility may be promoted by political authorities on the local, regional and global levels and it may be endorsed by a variety of non-government institutions, including religious ones - as is actually the case - but the decision as to whether to adopt and implement it, or not, lies with the individual company. There can be ‘sanctions’ on those companies that decide to ignore it in their operations. These are, however, not legal sanctions but various forms of pressure from trade-unions, consumers, investors, non-governmental organizations and even to an extent from governments themselves.

Can the drive for corporate social responsibility be effective in practice, if CSR remains essentially an ‘option’ which business firms may or may not take up? Would not a better strategy be to elaborate a more comprehensive legislative framework for the various areas of business in order to make them comply with legitimate social expectations and environmental needs? A major risk with the concept of corporate responsibility is precisely that it may generate the belief that, being a purely voluntary matter, it is not so important for business companies to change their internal and external operations to satisfy social and environmental concerns. There is certainly this risk, but this is the kind of risk that accompanies every human behaviour as moral behaviour.

Moral behaviour is authentic to the extent that it is voluntary. This means that commitment rather than ‘compliance’ is the hallmark of a truly moral behaviour. Commitment involves people, whether acting on the personal or organizational level, at the deepest possible level. People can commit themselves to something, if they believe that it is conducive to their individual and collective wellbeing and if they engage in it freely. A business firm can act as
a moral agent to the extent that on the internal front it engages its employees into a project that is more than just an economic enterprise and on the external front it cooperates with different stakeholders in the interest of the common good. This is the reason why the notion of contract, however necessary, can only explain the nature of the firm as a moral agent up to a certain extent. Contracts establish rights and obligations. They specify what is “yours” and what is “mine”. But for people to promote something which they share in common, they need to look beyond their individual and group interests, even if they are legitimate, and see what it is that they share in common. The partnership model presupposes that human living is ultimately not merely a matter of “my rights” and “your obligations” and vice versa, but a matter of cooperating for the common good.

The Contractual and Partnership Model

The contract theory of the firm presupposes a foundational contract in virtue of which a firm is established as a legal entity. The parties are the shareholders who would be considered “to own” the firm. Ownership entitles the shareholders to extensive power which they exercise essentially through the board of directors. The board of directors is responsible to the shareholders, whose interest essentially lies in securing a profitable return on their capital. This evidently gives overall power to capital holders and, in a sense, priority to profit-making. It is an arrangement that places shareholders, along with their interest in profits, in a dominant position within the firm. This position has been traditionally justified on the basis of ownership rights. More recently, it has been argued that in contrast with other stakeholders, such as workers, consumers and suppliers, whose rights are more or less fixed by work, purchase or sale contracts, shareholders face residual risks, associated with liability claims and possible loss of profits. “The argument for shareholder primacy”, John R. Boatright states, “is completed by contending that only residual risk bearers have the appropriate incentives for making discretionary decisions that maximize the creation of wealth by a firm”.  

How is management expected to operate within the firm? What are its responsibilities? Managers are employees of the firm. Their contract entails that the firm be managed along business lines to render it as profitable as possible. The contractual paradigm of the firm implies precisely the development of firms into profit-making enterprises. The creation of wealth is a foundational good both for the shareholders and workers, including management: the share value as well as salaries and wages are secured. This is surely not the only level on which a firm operates but it is, nonetheless, a basic and a crucial level. It would distort the moral status of the firm if its responsibility, as a corporation, to function profitably, were not taken seriously.

However, does the concept of the firm as a hub of contractual relations among the shareholders and between the firm as an employer and its employees bring out sufficiently well the nature of the firm? Does it involve more than economic rights and obligations, that

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9 Ibid, p. 4.
is rights and obligations that can be understood in purely monetary terms? Shares, salaries and wages constitute financial goods which are certainly valuable for their respective constituencies within the firm. But is not the firm really meaningful, if it is seen within a wider framework of contractual relations and a wider range of non-marketable rights and obligations? Besides, is not a firm morally responsible to the extent that it is operating within a set of values that incorporates but goes beyond the economic ones?

A ‘full’ contractual theory of the firm would reflect the nature of the firm as a truly human entity (and not simply a legal device for profit-making) if it recognized the importance of what I am calling “non-marketable” rights and obligations on which one cannot, strictly speaking, put a price, even if their exercise or fulfillment can be costly. Take the question of the responsibility of the firm towards its workers. By and large, it is management that exercises this responsibility in practice. One may say that the specific rights and obligations of workers are laid down in the employment contract and that management is bound to abide by the respective contractual requirements. Employment contracts are, however, part of a regulatory framework, established by law and stipulating the minimum requirements for decent conditions of work. Moreover, such contracts would need to be understood and interpreted within a still broader context or plan of action adopted by international organizations such as the ILO or promoted by significant actors within civil society, including churches, in support of the rights of people at work. The firm, as a moral agent, needs to acknowledge and respect its contractual obligations in this broad sense, as it would otherwise be seeking to make profit-making the exclusive driving force of its operations.

The danger of an economic system in which the rights of capital have absolute priority and capital accumulation is the primary driver of economic development is that those “goods” which are essential for the economy to retain a human face would be at best minimally respected and at worst completely ignored. Religious institutions have been particularly sensitive to this danger. In line with the warnings voiced by his predecessors about the threats of a capital-driven economy, Pope John Paul II spoke as follows about business firms:

“When a firm makes a profit, this means that productive factors have been properly employed and corresponding human needs have been duly satisfied. But profitability is not the only indicator of a firm’s condition. It is possible for the financial accounts to be in order, and yet for the people - who make up the firm’s most valuable asset - to be humiliated and their dignity offended. Besides being morally inadmissible, this will eventually have negative repercussions on the firm’s economic efficiency. In fact, the purpose of a business firm is not simply to make profits, but is to be found in its very existence as “a community of persons” who in various ways are endeavouring to satisfy their basic needs, and who form a particular group at the service of the whole of society.”

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11 John Paul II, Centesimus Annus, par. 35. For the Catholic teaching on economic life, the following Papal encyclicals are important: Leo XIII, Rerum Novarum (1891); Pius XI, Quadragesimo Anno, (1931); John XXIII, Mater et Magistra (1961); Vatican Council II, section of the Pastoral Constitution Gaudium et Spes on socio-economic life; John Paul II, Laborem Exercens (1981) and Centesimus Annus (1991). The Compendium of the Teaching of the Church, published by
The description of the firm as a community of persons takes the contractual view of the firm a step further. A contract articulates the rights and obligations of the contracting parties. It is indeed an indispensable institution for society to ensure that people can have a secure base for protecting their individual or collective interests. That the diverse interests of parties within the firm should be determined on the basis of contractual provisions is quite obvious. Collective agreements are the normal tool through which unionized workers generally try to ensure and promote their own legitimate interests. But can the firm be more than just an arena of actual or potential conflicts between the interests of one side and those of the other? How can an organization, that is exposed continually to the risk that the more powerful side can assert itself and promote its own interests, be a moral agent at all? It can be a moral agent only if it can transform itself into a community where all sides are contributing to make the enterprise profitable and at the same time sharing in its profits according to fair criteria of distribution and enabling each other to develop their personality through their participation in the whole enterprise. Relations within the firm would still be regulated by means of appropriate contracts that may vary in their type and degree of formality, as no organization, much less a business organization, can become a community of persons without the assurance that each other’s legitimate interests are being adequately safeguarded. The concept that the parties forming the business firm are stakeholders implies that each party is dependent on the other: for being able to secure one’s capital and hopefully increase it; for earning a living, working in a healthy and safe environment and finding satisfaction in one’s work; for the sense of making a contribution to the well-being of others.

This partnership paradigm may seem too far removed from the way in which business is actually organized in the context of the prevalent neo-liberal and neo-capitalist economies today. Indeed, this has the character of a proposal that can open the way for what the National Conference of Catholic Bishops called, in perhaps the most original and challenging chapter of their Pastoral Letter on the U.S. Economy, “partnership for the common good”. Corporate social responsibility can only be exercised in a true moral sense by firms that aim higher than profitability and that have succeeded in transforming themselves into organizations in which people are not just stakeholders but partners in a common human project.

One may object against this kind of proposal that “corporations are limited, and organized for only certain purposes”. This is a valid point in so far as it cautions rightly against placing too high a moral ideal on an organization which exists essentially for a business purpose. One may, however, look at the kind of responsibilities which businesses are being encouraged or pressed to assume in their operations both in relation to their employees and in relation to suppliers, customers, the local community and society at large. How can business firms assume such onerous responsibilities so long as they continue to view the Pontifical Council for Justice and Peace, London and New York, 2004, contains an extensive introduction to Catholic teaching on work and economic life.


themselves and act only as wealth-generating devices? Are they not too morally fragile for the high tasks they are being assigned?