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Suzanne Konzelmann, Victoria Chick and Marc Fovargue-Davies

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Suzanne J. Konzelmann
Birkbeck, University of London
s.konzelmann@bbk.ac.uk

Victoria Chick
University College London
v.chick@ucl.ac.uk

Marc Fovargue-Davies
Centre for Business Research, University of Cambridge
m.fd@me.com

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Abstract

The debate about corporate purpose is a recurring one that has re-emerged today. What should be the guiding principles of business: the pursuit of profit or a contribution to public well-being? We trace key elements in this debate in the UK and the US from the interwar years, when John Maynard Keynes and Adolf Berle made important contributions, to the present. Both the earlier and the current debates are centred around whether we see business institutions as strictly private entities, transacting with their suppliers, workers and customers on terms agreed with or imposed upon these groups, or as part of society at large and therefore expected to contribute to what society deems to be its interests. Whether current developments will ultimately produce a shift in corporate purpose akin to the one that followed the Second World War remains to be seen. But the parallels to the interwar debates, and the uncertain economic, political and social environment in which they took place, are striking. Our objective is to see what might be learned from the past to inform the current direction of thought concerning capitalism and corporate purpose.

Key words: Corporate Purpose, Shareholder Primacy, John Maynard Keynes, Adolf Berle

JEL Codes: B31, L21, P16

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1. Introduction

The debate about corporate purpose – and management power in this context – has a long history. The industrial revolution brought unprecedented social and economic change, much of it resulting from a 'laissez-faire' approach to the then novel idea of 'capitalism', in which the means of production were owned, initially, by sole proprietors or partners. Fierce competition eliminated inefficiency and misallocation of capital but resulted in insecure jobs, low wages, long hours and dangerous working conditions. These gave rise to an increasingly dense membership of trade unions, new political parties to represent those interests and sustained pressure for wider suffrage. All of this tempered the single-minded striving for profit (Davoudi, McKenna & Olegario, 2018).

During the early twentieth century, these developments combined with the emergence and growth of large joint-stock companies, in which capital and power were increasingly concentrated, to cause a questioning of capitalism as it then existed. In Britain, both David Lloyd George and Winston Churchill regarded the concentration of capital and power as a threat to society. This resulted in Lloyd George's 1910 Peoples' Budget, which laid the foundations for the welfare state, with many of the wealthy being taxed for the first time in order to pay for it (Konzelmann, Deakin, Fovargue-Davies & Wilkinson, 2018, pp. 83-91). A scant eight years later, the devastating economic and social effects of the First World War, and a deadly flu pandemic, were becoming clear; this was followed a decade later by the Wall Street crash and global financial crisis, itself caused by highly suspect business practices, which in turn caused a deep and lengthy worldwide depression. In this context, the ineffectiveness of long held economic ideas sparked wide-ranging debates about both laissez-faire capitalism and the role of corporations within the economy and society.

Those debates challenged the assumptions upon which society was based and brought to the fore a discussion of what the guiding principles of business should be: the pursuit of profit or a contribution to public well-being.[1] Perhaps unsurprisingly, this debate has re-emerged today, with many of the same factors driving it: a major financial crisis in 2008, the low growth and high unemployment of the 'Great Recession', the failure of traditional economic policies such as austerity to address the issues, and now the Covid-19 pandemic. Both the original and the current debates are centred around how we see business institutions: as strictly private entities, transacting with their suppliers, workers and customers on terms agreed with or imposed upon these groups, or as part of society at large and therefore expected to contribute to what society deems to be its interests.

John Maynard Keynes's contributions to this debate are not widely known. Yet the principles he proposed have great contemporary relevance. His views on this matter are scattered throughout his writings and in a collectively written book, *Britain's Industrial Future*. It is our purpose to pull these together and to show that the modern debate, while narrower than Keynes's framework, has roots in those principles. We introduce *Britain's Industrial Future* here, as that, too, is not well known today. At the Liberal Party summer school in 1926, with the 1926 General Strike fresh in the imagination, it was decided to mount a research project on Britain's industrial structure and future. A committee, calling itself the Liberal Industrial Inquiry (here referred to as 'the Inquiry' and bibliographically as LII) was formed. It was chaired by Walter Layton, then editor of *The Economist*, and commanded some of the best economic brains in Britain at the time, including, of course, Keynes. *Britain's Industrial Future* (LII 1928), was their report, known for its cover as the 'Yellow Book'. Keynes wrote several chapters and oversaw production of the book as whole (Keynes, *Collected Writings* – hereafter *CW* – 19, pp. 731-2). Even where the words may not be his, we are confident in taking them as ideas he agreed with. Speeches and articles under his name and based on the report are included in *CW* 19, Part II.

In the United States, Adolf Berle's contributions, particularly as expressed in his famous debate with E. Merrick Dodd in the pages of the *Harvard Law Review* in 1931 and 1932, *are* well known. However, Bratton and Wachter (2008) argue that they have been widely misread: 'When modern scholars read the texts out of context, Berle appears to be the supporter of modern shareholder primacy, which is a position he did not hold' (pp. 134-5).[2] We thus revisit Berle's contributions which, like those of Keynes, have relevance for today.

Although Keynes did not live to see it, out of the crisis of the two World Wars and the interwar years, a post-war 'welfarist' vision of companies ultimately emerged (Bratton, 2017). This lasted until the crisis of the 1970s, which witnessed the rise to dominance of shareholder primacy. Thirty years later, starting with the corporate scandals of the early 2000s, recurring crises have re-ignited the debate about corporate purpose.

Today's debate challenges more recent ideas about the role of globalisation and liberalised finance, drawing attention to the excessive power and questionable culture of the corporate and financial services sectors, and raising the issue of public bailouts. As in the interwar years, the policy response has included severe and prolonged austerity, resulting in high levels of unemployment, recession and increased debt, both public and private. In this context, after ten years of low growth, the timing of the COVID-19 pandemic could hardly be worse, with the UK economy alone predicted to shrink by some 14 percent in 2020 (Monetary Policy Committee, 2020, p. 7). It is too early to know what new ideas will ultimately emerge from this debate, as well as how – if at all – they will influence policy. But revisiting the ideas about the economic role and social purpose of the corporation which informed the interwar debate has the potential to offer some much-needed perspective.

Section 2 explores Keynes's evolving interwar ideas about companies' responsibility to society, at a time when laissez-faire capitalism itself was being questioned; we then turn to his views about its employees and shareholders. At around the same time as Keynes's attention was shifting away from the questions of industrial structure, governance and purpose, Adolf Berle's was shifting to the newly discovered phenomenon of the separation of ownership from control in large publicly listed corporations, and, in this context, the problem of unrestricted management power, which is the focus of Section 3. Section 4 traces the modern debate about corporate purpose, as it evolved from the post-war welfarist view to shareholder primacy during the 1970s and 1980s. This is now being challenged by a return to the idea that companies should serve a broader public purpose. Section 5 concludes.

2. Keynes's views on business and society

The main debate about business and society in interwar Britain was between believers in laissez-faire, who maintained that businesses were purely private concerns that could do what they wished within the law, and advocates of what Keynes variously called 'state socialism' or 'Labour socialism', who favoured nationalisation. Many others, including most of the Liberal Party, to which Keynes was allied, preferred a middle way, which might be called 'reformed capitalism', 'social democracy' or 'liberal socialism' (Konzelmann, Chick & Fovargue-Davies, mimeo). Most of the modern debate excludes nationalisation and typically treats the business enterprise as a purely economic organisation, in isolation from its wider social context. By contrast, the signatories of *Britain's Industrial Future* were clear: 'Industry is not an end in itself; it exists to provide livelihood for the whole community' (LII, 1928, p. 181).

Keynes's objection to laissez-faire was that the evolution of business institutions had rendered it obsolete. Although he disliked its harshness, he acknowledged the great motivating force of a system which could yield attractive returns to those who were successful; and he appreciated the efficiency of its ruthless competition, which would quickly drive out of business the less astute and the unlucky. During the nineteenth century, failure, though an unfortunate consequence for the individuals involved, had little consequence for society overall, because firms were relatively small. In summary, the laissez-faire capitalist system, though objectionable in many ways, had yielded both great improvements in the standard of living and many life-enhancing innovations, at low social cost.

But by the time Keynes was writing, the nature of companies and industrial organisation had changed dramatically. Laissez-faire industry had begun as small sole proprietorships or partnerships, but they grew in response to economies of scale and ready markets for mass-produced goods, until a small number of people were unable to furnish adequate capital. The creation of the easily registered joint-stock, limited-liability company in Acts from 1844 to 1856 resolved this problem and resulted in yet further growth, such that, by the beginning of the First World War, many firms were very large, some of them occupying oligopolistic or monopolistic positions in their industries (Pollard, 1983, pp. 98-107). Their failure would thus have repercussions not only for their owners but for society at large; and their size gave them scope to devote resources to self-preservation by means other than their core purpose. Many firms now wielded too much power, tended to be inefficient when in operation and had consequences well beyond themselves should they fail. They could no longer be viewed as a purely private matter.

2.1 Profit

Under laissez-faire, it was an article of faith that private profit meant industry was producing something society wanted; it was an indicator of public benefit. Keynes rejected this idea: 'It is *not* a correct deduction from the principles of economics that enlightened self-interest always operates in the public interest. Nor is it true that self-interest generally *is* enlightened ...' (Keynes, 1926, p. 288, emphases in original).

Yes, there should be profit sufficient to keep the firm going, but profit should not be the sole objective, to the exclusion of other considerations. In Keynes's view, when the profit motive becomes all-consuming, it distorts priorities:

> *'[When the] rule of self-destructive financial calculation governs every walk of life, [w]e destroy the beauty of the countryside because the unappropriated splendours of nature have no economic value. We are capable of shutting off the sun and the stars because they do not pay a dividend' (Keynes, 1933, pp. 241-2).*

At its worst, profit represents the love of money for its own sake rather than the good it can do:

> *'The love of money as a possession – as distinguished from the love of money as a means to the enjoyment of realities of life – will be recognised for what it is, a somewhat disgusting morbidity, one of those semi-criminal, semi-pathological propensities which one hands over with a shudder to the specialists in mental disease' (Keynes, 1930, p. 329).*

In the nineteenth century, concentration on profit was understandable, given the fierceness of competition; and social priorities – progress, prosperity, alleviation of hardship – were achieved almost by accident. That system, combined with the size and power of the typical interwar joint-stock company, did not, from Keynes's perspective, justify the continuation of the single-minded pursuit of profit to the exclusion of public goals. But there was a problem of persuasion:

> *'To suggest social action for the public good to the City of London [i.e. finance] is like discussing The Origin of Species with a bishop sixty years ago. The first reaction is not intellectual, but moral. An orthodoxy is in question, and the more persuasive the argument, the graver the offence' (Keynes, 1926, p. 287).*

This way of thinking was not confined to the City: it was fundamental to the doctrine of laissez-faire, held not only in industry and finance, but even the state.

2.2 Profit and the state

If any entity should be reliably focused on the public interest, it is the state. But the carry-over of laissez-faire thinking from the nineteenth century was such that the state itself could be found adopting the commercial criterion of return. At this, Keynes was scathing: 'It is the state, rather than the individual, which needs to change its criterion. It is the conception of the Chancellor of the Exchequer as the chairman of a sort of joint-stock company which has to be discarded' (Keynes,

1933, p. 243). Instead, he argued that the state should focus on broader objectives which serve a public purpose, such as 'what, broadly speaking, shall be produced within the nation and what shall be exchanged with abroad' (ibid.), so as to provide both full employment and other benefits associated with national self-sufficiency and international trade.

For Keynes, if the state could not be relied upon to look after the public interest, what hope was there to persuade private companies, accustomed to having their own way, to take account of the common weal?: 'It is curious how common sense, wriggling for an escape from absurd conclusions, has been apt to reach a preference for *wholly* "wasteful" forms of loan expenditure rather than for *partly* "wasteful" forms, which, because they are not wholly wasteful, tend to be judged on strict "business" principles' (Keynes, 1936, p. 129, emphasis in the original).

There follows the famous satirical attack on the Treasury about putting bottles in holes in the ground and digging them up again. Keynes knew he could not *prove* the case against the laissez-faire view and the reliance on profit to the exclusion of public purpose: He remarked in another context that you cannot convict your opponent of error; you can only convince him. Satire and exaggeration were an attempt to jolt people out of their accustomed ways of thinking: 'Words ought to be a little wild, for they are the assault of thoughts upon the unthinking' (Keynes, 1933, p. 244).

2.3 The 'public concern'

During Keynes's time, the British state was an organisation which, given the institutional structure of the day, was rather larger than 'government' as usually understood. It included many sorts of 'public concern': 'a form of organisation which departs in one way or another from the principles of unrestricted private profit and is operated or regulated in the public interest' (LII, 1928, p. 63). These were organisations which did the work of business firms but were governed differently, such as autonomous bodies with a publicly accountable Board to oversee them, or run by local authorities. These were considered an arm of the state, with a few concerns being run directly by the state. In addition, there were private organisations, such as charities, cooperative societies and building societies, which belonged to the private sector but shared their aim to serve a public purpose rather than profit.

There existed a rich variety of these concerns, governed in many different ways and most with a special, rather than general, public purpose, for example to provide water or electricity. At the time, they were a substantial part of the British economy. The Inquiry had found that the capital administered by public concerns amounted to around £4 billion (LII, 1928*,* p. 75). This was 'of the same order of

magnitude as the aggregate capital of all joint-stock companies [in the UK]' (Pollard, 1983, p. 100). Most of these institutions have long since disappeared during subsequent waves of deregulation and privatisation.

The Inquiry raised concerns about inefficiency in some of these bodies, but not that their hearts were in the wrong place. They proposed leaving the sector at its then-current size and scope for the near future. This experience of a large sector devoted to the public interest may have been a significant influence on differences between British and American points of view (see also note 4, below).

The Inquiry made one surprising prediction. The 1921 Railways Act took steps to curb the railways' profits, foreshadowing Keynes's later (1936) call for the euthanasia of the rentier:

> *'If the railways are successful in earning their standard revenues[3] as a regular thing, the functions of the private shareholders will have atrophied as much as those of the shareholders of the Bank of England. ... Generally speaking, the functions of private shareholders must tend to atrophy as soon as it has proved necessary to adopt the principle of limiting or of fixing profits' (LII, 1928, p. 82).*

The Inquiry thus advocated exchanging railway shares for fixed-interest bonds and having the railways governed by a public Board (of the sort that Water Boards used to be). 'The choice between a Public Concern and a Private Concern then resolves itself…' (ibid.).

2.4 The large enterprise

Despite all that has just been said, Keynes in 1926 looked favourably on some large companies. His ideal was a form of organisation and control somewhere between the level of the individual and the state – autonomous bodies governed rather like the mediaeval corporation.[4] Some institutions, he argued, already approximated that form of governance: the universities, the Bank of England, the Port of London Authority, 'even perhaps the railway companies' (Keynes, 1926, p. 289). He saw the same trend in joint-stock companies: '[W]hen they have reached a certain age and size, [they] approximate to the status of public corporations rather than that of individualistic private enterprise. One of the most interesting and unnoticed developments of recent decades is the tendency of big enterprise to socialise itself' (ibid.). Owners – the shareholders – become divorced from management; and managers, who are salaried, are not motivated by profit in the manner of nineteenth century proprietors. They are instead, he argued, concerned with the 'general stability and reputation' of their

organisations and, once shareholders are ‘satisfied with conventionally adequate dividends’, avoiding criticism from their customers and the public.

But after nearly two years of studying the structure of UK industry for the Inquiry, Keynes seems to have changed his mind. *Britain’s Industrial Future* gives a great deal of thought to the problem that many large firms occupied a position of monopoly or oligopoly. The Inquiry proposed certain criteria in relation to concentration, diffusion of share ownership and size which, in their view, should cause a firm to be registered not as a Public Company but as a Public Corporation, which ‘should be required to conform to conditions appropriate to … a semi-public concern’ (p. 95).

This recommendation was not implemented. Nor did large companies evolve as envisaged in 1926! Under pressure from shareholders and exacerbated by the partial remuneration of top managers in share options, coupled with the intense competition brought about by globalisation, many companies today have engaged in a variety of sharp practices, such as ‘teaser’ mortgages, a higher tariff for loyal customers, low wages, zero-hours contracts, and the like, in order to boost profits and share values – quite the opposite of Keynes’s prediction. We will argue later that the widespread acceptance of shareholder primacy in the neoliberal years bears some blame for this behaviour.

2.5 Social Responsibility within the Firm

Having explored the responsibility of the business firm to the society in which it operates, we now turn to those who are part of the organisation: its employees and shareholders. In *Britain’s Industrial Future*, the firm is viewed as a social organisation brought together to produce something they expect the public to value. Its function is not solely economic. This attitude is in sharp contrast to that of laissez-faire, in which the obligation of owners or managers toward employees ends when the wage bargain is struck and safety regulations put in place.

2.5.1 Workers

Britain’s Industrial Future was written against a background of bitter industrial strife. Trades unions had acquired considerable power, to counterbalance that of autocratic management. But relations had reached a point where capital and labour were seen as having no common ground. Labour relations had become a zero-sum game. The Inquiry argued that quite the opposite was the case: each ‘side of industry’ needed the other. Contrary to the thinking of ‘capital’, high wages and low prices were *good* for business, at the macroeconomic level.

The Inquiry proposed a number of remedies for the comparative powerlessness of workers (as opposed to unions), all of which were governed by one principle: to ensure that 'the worker may have a personal interest in the concern for which he works, and feel that he is treated as a partner and not merely a tool' (p. 199). Comparing the position of the worker with his role as a citizen, the Inquiry pointed out that as a worker, '[h]e may be dismissed at a week's or a day's notice … without redress or appeal … [w]hile, as a citizen, he has an equal share in determining the most momentous issues …' (p. 148). The factory life in which 'workers tramp in in the morning, and after their allotted tale of work hasten out in the evening to find their real life elsewhere, never once feeling that they are members of an organised company [which is] mutually interdependent' (p. 237) was not acceptable.

The Inquiry proposed several remedies, including consultation, improved collective bargaining, profit-sharing, share ownership, and Supervisory Councils. The latter would work alongside Boards of Directors to look after the interests of both workers and shareholders. A large employer told the Inquiry that profit-sharing, in particular, encouraged workers to feel that 'the prosperity of the business was their concern … and that the effect of this in improving relations and making real cooperation was marked' (p. 200). The Inquiry foresaw a 'new order' which would be 'quite unlike the harsh individualism and employer autocracy of the nineteenth century' (p. 205).

2.5.2 Directors and shareholders

Shareholders get little attention in *Britain's Industrial Future*, although the Inquiry did recognise that shareholders have the ability to exercise some control over management. Thus it is perhaps unexpected that they favoured worker ownership of small amounts of shares and proposed a channel for the shareholders' voice, as mentioned above. In general, however, shareholders were regarded as ignorant of the work of their companies and generally passive. This evaluation is not new: it was voiced by Adam Smith:

> *'This court [of directors], indeed, is frequently subject, in many respects, to the control of a general court of proprietors [the shareholders of his day]. But the greater part of those proprietors seldom pretend to understand anything of the business of the company, and when the spirit of action happens not to prevail among them, give themselves no trouble about it, but receive contentedly such half-yearly dividend as the directors think proper to make them' (Smith, 1904 [1776], p. 107).*

The last clause has echoes in Keynes (1926, p. 289), quoted above.

Directors, in the Inquiry's view, too easily saw themselves as in post for life – a not unreasonable expectation in the light of shareholder dispersion and passivity. They therefore did not take the view that Boards of Directors, 'as at present constituted, of Public Companies of diffused ownership are one of the strong points of private enterprise' (p. 91). But the problem was difficult to address through legislation. To deal with it, they could only propose 'publicity' – transparency in today's language – to inform potential investors. Of interest in the light of later developments is their singling out of an 'increasingly frequent' abuse by directors, 'for which the secrecy of accounts is at least partly responsible': the publication of balance sheets that conceal as much as they reveal, putting a premium on 'insider information' (p. 85). They also deplored 'the growing practice of directors dealing directly or indirectly in shares of their own companies' (p. 86), against which they proposed that directors' holdings of shares be published.

Britain's Industrial Future was in effect the Liberal Party's manifesto. But the Liberal Party did not win the election – indeed they were in the process of being eclipsed by Labour – so the industrial policies they espoused were not implemented. A year after *Britain's Industrial Future* was published, the American stock market crashed, and the Great Depression and World War Two followed. Keyes's attention thus turned away from the questions of industrial structure, governance and purpose, never to return.

3. Meanwhile, in the USA …

During the 1920s and 1930s, the general consensus was that the period's economic difficulties were a consequence of inherent instabilities of laissez-faire capitalism, and that modern corporate institutions, as an important part of the system, were part of the problem (Bratton & Wachter, 2008, p. 102). The question was whether corporations had obligations extending beyond the pursuit of private profits. At the same time, recognition of the separation of ownership from control in large joint-stock, limited-liability corporations, caused some, including Adolf Berle, a Wall Street lawyer and Columbia University Law School professor, to question the resulting increase in managerial power. Traditionally, this power had been restricted by a company's articles of incorporation or by owner-shareholders. But public corporations had general charters without this restriction, giving management powers to enter new businesses, and issue stock to fund them.

Berle was concerned about the problem of unrestricted management power and shareholders' inability to control it. He saw this as a governance problem to be treated within the financial community; and he advocated that managerial discretion be constrained by 'businessmen themselves', through self-regulation,

monitoring by investment institutions and stricter stock market rules (Berle, 1928, pp. 37-9). At the time, he did not believe that the courts could serve as agents of reform. But Berle's attitude towards regulation – and corporate purpose – would change even before the Wall Street stock market crashed.

The catalyst was Gardiner Means, his statistical and economic research assistant on a five-year project funded by the Rockefeller Foundation that would ultimately produce *The Modern Corporation and Private Property.* Means's empirical research revealed that two thirds of the national wealth was held by the 200 largest US corporations; and he predicted that by 1950, this figure would rise to seventy percent. This would further concentrate power in the hands of a small cluster of corporate managers, whose level of responsibility had already come to worry Berle greatly. Means's projection would later prove wrong; but it sent a clear message that something had to be done about corporate power, causing Berle to change his views accordingly. He now saw a case for judicial control in the name of shareholder interest (Berle & Means, 1932, p. 9, 37, 40).

The gestation period of *The Modern Corporation* spanned five years, beginning in 1928, at the end of the long American boom and a year before the Wall Street stock market crashed. It was published in 1932, in the throes of the Great Depression, and on the eve of the election of President Franklin Delano Roosevelt, and the progressive legislation of the New Deal. In the rapidly changing context of the 1920s and 1930s, Berle's ideas (like those of Keynes) were evolving in response to unprecedented political, economic and societal developments. Bratton and Wachter (2008) point out that understanding this context – and Berle's political viewpoint – is crucial for understanding what he *actually* meant in his writings of the early 1930s. Otherwise, it is easy to interpret Berle as advocating shareholder primacy, in the now familiar form that is understood today.

3.1 The Berle-Dodd Debate

In a very influential article, 'Corporate Powers as Powers in Trust', published in the *Harvard Law Review* in 1931, Berle developed his trust model of corporate law. In it, he focused on the problem of managerial power, arguing that managers, as the trustees of shareholders, owed them a fiduciary duty to maximise the company's wealth, and that that duty should be enforceable at law.

In May 1932, E. Merrick Dodd, a Harvard Law Professor, attacked Berle's position, arguing that the view that corporations exist for their shareholders' financial benefit made no sense in the context of the Great Depression. Corporations should instead act as social institutions, providing economic security for their employees, quality products for consumers and contributions to

broader society; and managers could be relied upon to undertake these responsibilities. According to Dodd, the public corporation was a legal entity, created by the state for public benefit, and run by professional managers seeking to serve not only shareholders but also stakeholders and the public interest (Dodd, 1932, p. 1148).

Taken at face value, these texts have been widely interpreted as positioning Berle as the father of shareholder primacy and Dodd of corporate social responsibility. However, Bratton and Wachter (2008) argue that this is to fundamentally misinterpret them:

> *'To understand the Berle-Dodd debate is to see Berle and Dodd participating in a national political discussion over the outlines of the new American corporatism ... This was the key political issue at the time ... The question went to the allocation of power as between corporate managers and the state' (p. 122).*

On one side of this debate were those like Dodd, who wanted to delegate authority to management to run the economy, with the government assuming a supporting role. On the other side were those like Berle, who wanted strict government oversight of the economic planning process, with labour also being brought to the negotiating table (Hawley, 1966, pp. 43-6). Thus, '[t]he Berle-Dodd debate emerges as a clash between the different visions of corporatism whose advocates were then vying to capture Roosevelt's attention' (Bratton & Wachter, 2008, p. 124).

By now, Berle was a member of Roosevelt's Brains Trust, advising him on policy which after the November 1932 election would influence the First New Deal. His response to Dodd, in the *Harvard Law Review's* next issue, thus avoided any mention of policy goals, focusing instead on weaknesses of the business model Dodd was advocating (Berle, 1932). In a context where unbridled management power was the problem, further management empowerment was *not* the solution. Rather, controls in the form of trust duties were needed. But Berle did not advocate shareholder primacy. Instead, he held that shareholders derived legitimacy from being passive recipients of the wealth created; and as such, they to some extent represented the welfare of the general public.

3.2 *The Modern Corporation*

In the Preface of *The Modern Corporation*, also published in 1932, Berle acknowledged that corporations are 'human institutions' that were being expected to take on 'a steadily growing degree of responsibility for our economic welfare' (Berle & Means, 1932, p. viii). The authors went on to argue that during the early twentieth century, in large joint-stock companies, the entrepreneurial function had been split between salaried executives, with control over large hierarchical organisations, and anonymous investors, holding relatively small amounts of equity, with an interest in liquidity rather than participation in management. Management had been empowered and shareholders, who for the most part were ordinary working people who relied on their dividend payments to make ends meet, had been reduced to passive collectors of dividends, with no productive role to play in the political economy.

In this context, as trustees of shareholders, managers owed them a fiduciary duty to prioritise their financial interests in the corporation's wealth; and because markets could not be relied upon to provide a stable economy, managers should cooperate with the government in regulation designed to achieve a social welfare function. Thus, what Berle had, in the 1920s, considered a problem for private actors in a world of finance, he now saw as a problem for government (Schwartz, 1987, p. 56). In the final chapter, 'The New Concept of the Corporation', Berle built upon the point that those who have power in society will inevitably come into conflict with the populace because the exercise of power impacts the public interest; and he went on to argue that managers' primary allegiance was to the national interest (Berle & Means, 1932, p. 356).

3.3 Evolving ideas about corporate purpose

In September 1932, Roosevelt gave his famous Commonwealth Club Address, a speech written by Berle and his wife, Beatrice. In it, everyday management practice was viewed as a political problem because corporate managers, the 'princes of property', had infringed the rights of ordinary citizens to economic security. To address this problem, Berle used his trust model, this time substituting, as the beneficiary, citizens for shareholders (Roosevelt, 1932). Roosevelt won the election; and New Deal legislation swiftly followed.

Dodd soon adjusted his thinking. The Securities Act of 1933, one of the first laws enacted under the New Deal, and the Securities Exchange Act of 1934, were enacted in response to abuses of the corporate system that had contributed to the 1929 Wall Street crash. These required disclosure by all publicly listed companies, of the financial condition of the firm as well as of the compensation (including stock options) received by their three highest paid executives. Failure

to do so would mean removal from the stock exchange. In Dodd's view, this new securities legislation was successful in rebalancing the power of managers and shareholders. In 1941, he published an essay abandoning his previous position and supporting the corporation's private profit seeking motive, arguing that the purpose of corporate law was to protect shareholders from powerful managers, who could no longer be trusted (Dodd, 1941).

After Dodd's death in 1951, Berle also returned to the debate. In a series of lectures entitled *The Twentieth Century Capitalist Revolution*, he made a famous concession: Dodd had been proven right over time; managers could be trusted after all. But this no more meant what it seems to than Berle's 1931 and 1932 *Harvard Law Review* articles did. Berle only admitted that later events had produced a corporate system that Dodd had described in his 1932 *Harvard Law Review* article, *not* that Berle had been wrong at the time of publication.

By this point, Berle believed that the New Deal had created a political economy in which corporate power had been rendered benign.

> *'The 1929 crash, the slow recovery of 1930, and the ensuing spiral descent into an abyss of unemployment, bank failures, and commercial paralysis was not corrected by market processes. ... [T]he public ... increasingly asked that the political state propose a program and act. Necessarily, this meant considerable reorganization of private business. ... Out of the crisis was born the American economic republic as we know it today' (Berle, 1963, p. 91).*

In Berle's new 'American economic republic', the state and economy were interdependent, with the state taking ultimate responsibility for economic outcomes and exercising a high level of political and economic authority (Berle, 1963, pp. 95-99). Managers, whether they liked it or not, were caught between the post-war regulatory state and the public political consensus, which, in turn, depended on corporate performance – the delivery of price stability and employment and income security. Failure to satisfy the general public meant new regulation; and avoidance of new regulation required satisfying the public. Thus, as a practical matter, managers could not avoid public duties. They thus emerged as quasi-public servants, caught inside a web of countervailing forces which served to restrain their use of power (Berle, 1954, pp. 172-3). In Berle's words: 'Since they are not owners but only managers, they really are a variety of non-Statist civil servant' (Berle, 1959, p. 8). By contrast, shareholders remained as they had been in 1932, passive collectors of dividends.

During the 1950s, the American corporate system did seem to approximate Berle's American economic republic. While other countries were setting up national health systems and generous state pension schemes, American corporations were taking responsibility for a significant part of the welfare burden. Powerful corporations, like General Motors, and their trade unions negotiated generous collective bargaining settlements, providing pension provisions and health insurance benefits. These set patterns that were copied across the industrial landscape and modified over time to labour's advantage (Davis, 2016, p. 42).

Thus, although Berle is remembered for having drawn attention to the separation of ownership from control in large publicly listed corporations, and the problem of corporate power being concentrated in the hands of a small group of senior managers, in the last chapter of *The Modern Corporation*, published in 1932, and for most of the rest of his life, he stood for the opposite proposition.

4. The modern debate about corporate purpose

By the middle of the twentieth century, the managerialist view of corporate purpose – that the corporation's purpose is to produce satisfactory returns for investors, good jobs for employees and reliable products for customers, and to be a good corporate citizen – was the dominant view. But this perspective began to be challenged during the 1960s, as shareholders reacted to a range of issues including recognition of the need to strengthen consumer protections and perceptions of environmental degradation (Wells, 2002). Another challenge came from the new phenomenon of the 'hostile takeover', the first of which was launched in 1964 by UK corporate raiders. This set off a wave of other takeovers due to the enormous financial gains that could be made (BBC, 1999, Parts 2 and 3). Hostile takeovers were typically followed by asset stripping to repay the debt used to finance them. This had a damaging effect on British and, soon afterward, American industry, as asset and cash-rich companies whose shares had been undervalued on the stock market became targets (Konzelmann, Wilkinson, Fovargue-Davies & Sankey, 2010; Lazonick & O'Sullivan 2000).

Berle had recognised that the legitimacy of management power depended upon economic performance, and that economic failure stripped management of legitimacy and triggered clear and forceful public demands for economic stability as well as employment and income security. Thus, once the economy was effectively regulated, management power disappeared as a political problem. Berle did not expect the problem to re-emerge, at least without an economic crisis.

But his death in 1971 meant that he would not live to see the economic crisis that followed, which proved him right.

During the 1970s, the discovery of widespread insider trading, market manipulation and corporate bribery of foreign officials by US corporations – which inside directors knew about but outside directors didn't – came to light. This resulted in board reforms, including improvements in transparency and disclosure, an increase in the number of non-executive directors, and creation of audit, nomination and remuneration committees (Cheffins, 2012). This mirrors both the concern of *Britain's Industrial Future* for greater 'publicity' and publication of directors' holdings of shares, and early New Deal securities legislation, which had been strengthened over time by increasing federal regulation of securities markets (Bebchuck & Hamdani, 2006).

At the same time, 'stagflation', failing stock markets, frontal attacks on organised labour and the perception of national economic decline – in no small part a consequence of the deindustrialisation triggered by corporate raiding – added to the evidence that managers could not be trusted with social responsibilities. But the remedy proposed was better education in the requirements of the job rather than oversight by shareholders. This resonates with Tawney's (2010 [1920]) assessment:

> *'The higher officers of the corporation', writes Mr. H. L. Gantt of a Public Utility Company established in America during the [First World] war, 'have all without exception been men of the 'business' type of mind, who have made their success through financiering, buying, selling, etc. ... As a matter of fact, it is well known that our industrial system has not measured up as we had expected. ... The reason for its falling short is undoubtedly that the men directing it had been trained in a business system operated for profits, and did not understand one operated solely for production. This is no criticism of the men as individuals; they simply did not know the job, and, what is worse, they did not know that they did not know it.'' (p. 175, emphasis in the original.)*

This comment follows a discussion of how 'business', i.e. financial matters, had taken over from production. A similar distinction between business (finance) and industry, as parts of the same company, was made by Thorstein Veblen.[5] Today we call it financialisation.

4.1 The 'Friedman doctrine' and the rise of shareholder primacy

The view that the proper purpose of the public corporation is to make money for its shareholder 'owners' found a happy home in the emerging Chicago School of free market economics, where one of the earliest contributions came from Milton Friedman. In *Capitalism and Freedom*, Friedman (1962) argued that public corporations should maximise wealth for the benefit of their shareholders, based on the contention that shareholders are the 'owners' of corporations. This idea was popularised in his 1970 *New York Times Sunday Magazine* article, which argued that because shareholders 'own' the corporation, the only 'social responsibility of business is to increase its profits' (Friedman, 1970, p. 32). This became known as the 'Friedman doctrine', which for the next half century would be a powerful concept defining business practice and government policies in relation to corporate governance and purpose.

The Friedman doctrine was bolstered by the newly developed 'agency model' of corporate governance, which first appeared in a 1976 paper by two economists, Michael Jensen and William Meckling. Jensen and Meckling identified corporate shareholders as 'principals' who, effectively, hire corporate managers to act as their 'agents'. Because the agent/manager does all the work while the principal/owner gets the lion's share of the profits, they argued that a self-interested manager could be expected to shirk (or even steal) at the owner's expense, giving rise to 'agency costs'. Their solution was to require managers to prioritise the purely financial interests of the corporation's shareholders.

During the 1990s and early 2000s, articles, mainly published by legal scholars, began to point out that, despite what the economists had to say, corporate law does not (and never has) required public corporations to maximise shareholder value.[6] A corporation could choose to mandate shareholder primacy in its company charter; but as far as the law is concerned, maximising shareholder value is just one objective out of many. It is *not* a managerial obligation; it is a choice.

Nevertheless, the principal-agent model was enthusiastically embraced by the emerging Law and Economics School for bringing the rigour of economic theory to corporate law; and a generation of academics in law, economics and business management accepted it as a simple way of understanding the complex reality of public corporations. Thus, by the close of the millennium, the Chicago School had won the debate over corporate purpose in the US; these ideas took hold in the UK as well. Shareholder primacy theory, in turn, influenced corporate practice; and the majority of scholars, regulators and businesspeople came to accept the Friedman doctrine.

4.2 Challenging the shareholder model: New thinking about corporate purpose

Despite its popularity, after each wave of corporate scandals since the 1960s and 1970s – and especially since the 2008 financial crisis – the shareholder primacy model of corporate governance and purpose has been challenged. But each time it rebounded, stronger than before, despite accumulating evidence that it had, in fact, contributed to the recurring crises (Cheffins, 2012). Out of all of this, traditional stakeholder and corporate social responsibility arguments re-emerged. With the benefit (if you can call it that) of experience, the critics of shareholder primacy focused on how it hurts stakeholders and/or society *per se* (Bratton and Wachter, 2008; Stout, 2012, 2013a, 2013b). In response, proponents of shareholder primacy maintained that the critics had not put forward a compelling alternative to replace it. What is compelling, of course, depends on your point of view.

However, things now appear to be changing, more than a decade after the 2008 financial crisis; and we expect the experience of the Covid-19 pandemic to accelerate this growing change of mind. With trust in both government and big business at an all-time low, growing concerns about environmental sustainability, and high levels of social and economic inequality, alternative ideas about corporate purpose are beginning to emerge and attract attention, not only in academia but also in business and policy-making circles (British Academy, 2018; Mayer, 2018; Business Roundtable, 2019). This resonates strongly with the economic climate and policy debates of the interwar period, when voters' confidence in capitalism was also severely shaken; this produced heated debate about corporate purpose, which ultimately led to positive reforms, decades of improved corporate and economic performance and improved social outcomes. Those debates provide the basis for the alternative that the advocates of shareholder primacy found wanting, if they would but look.

Arguably, emerging ideas about corporate purpose could still be accused of lacking the economic precision of the principal-agent model. But, as we know, 'precision primacy', though seductive, can lead one astray: 'It is better to be vaguely right than exactly wrong' (Read, 1898, p. 272). A step forward is 'enlightened shareholder' thinking, which would allow directors and executives to focus on the long-term interests of not only shareholders but all corporate stakeholders, as well as the corporation itself. But there is still a wider constituency that this thinking does not encompass. The new corporate purpose models are not only morally superior but much closer to the reality of corporate law, economics and organisation (Salter, 2019; Stout, 2012, 2013a, 2013b).

Prominent business leaders are also calling for companies to put ‘purpose’ before profit. A catalyst was a letter sent to CEOs in 2018 by Larry Fink, CEO of BlackRock, one of the world’s largest asset management companies. With ‘governments failing to prepare for the future’, Fink wrote, ‘society is increasingly turning to the private sector and … demanding that companies, public and private, serve a social purpose’. In his 2019 letter, Fink reiterated his argument about government failure and society’s demand for companies ‘to address pressing social and economic issues’, going on to explain the ‘inextricable link’ between corporate purpose and profit. Seven months later, in August 2019, the Business Roundtable, a group of CEOs of major US corporations, issued a ‘Statement on the Purpose of a Corporation’, signed by 181 CEOs. This expressed confidence in the ‘free market system’ but abandoned the idea that a corporation’s purpose is first and foremost to maximise profits for its shareholders. Instead they committed themselves to prioritising the long-term interests of all corporate stakeholders. In 2020, Fink repeated his call for companies to commit themselves ‘to embracing purpose and serving all stakeholders’, again connecting this with driving ‘long-term profitability’.

In the UK, since 2015, Will Hutton, Chair of the Big Innovation Centre, and Clare Chapman, then a director of BT, have co-chaired the Purposeful Company Taskforce. This engages with leading UK companies in gathering evidence that corporate purpose makes a difference, issuing guidance for putting it into practice, and pressing for changes in policy, regulation and law. One outcome can already be seen in the new UK Corporate Governance Code, which came into effect in January 2019, requiring all companies with a premium listing, whether incorporated in the UK or elsewhere, to declare and report on corporate purpose.

Whether all of this represents, on the part of those involved, a genuine commitment for change – which will ultimately produce a shift in corporate purpose akin to the one that followed the Second World War – remains to be seen.

5. Conclusions

We conclude by returning to Keynes and Berle, who saw companies as human institutions with an important role to play in the economy and society. Nearly a century later, the debate continues, with remarkable similarities. The modern debate is in no small part a consequence of the reappearance of ‘laissez-faire’ capitalism at the end of the 1970s, with its accompanying economic and financial instability, heightened levels of poverty and inequality, and damaging effects on an already fragile natural environment.

Much of this debate has been rooted in the relationship and balance of power between the private sector and the state, and the related question of regulation. Following the Second World War, to varying degrees, states played a key role in managing the economy; the problem of managerial power was tamed, and corporations served an accepted public purpose. Across the industrialised world, this was accompanied by generally rising living standards and virtually no financial crises. However, the 1970s and 1980s witnessed a decisive shift in favour of the private sector and markets. Whilst Berle would have seen his ideas about the sources of legitimacy of managerial and corporate power proven largely correct, it is doubtful he would have found much solace in that. In returning to 'laissez-faire' – whose time, in Keynes's view, had already passed by the turn of the twentieth century – all of the factors that had created the difficulties of the interwar years, were once again given free rein, with much the same result.

The contrasting perspectives on corporate purpose between the interwar years and today are also striking. Not only has the debate narrowed considerably; but concern about the relationship between business firms and society, which was centrally important to Keynes and Berle, has virtually disappeared. Today's business leaders make the link between companies and the economy; and they talk about the other stakeholders, alongside shareholders, although these are now conceived as purely economic, as opposed to social as in Keynes's and Berle's time. But they stop short of connecting corporate purpose with the broader interests of society as a whole. That is left to the advocates of corporate social responsibility.

The political motive behind current moves by large companies to embrace what they describe as corporate purpose could be an attempt to avoid further external regulation, as it was during the 1930s, in response to Roosevelt's New Deal policies. But history shows that significant and positive change is certainly possible, although achieving it will require a better balance between the private sector and the state.

The crises that have historically played a role in catalysing this sort of change are currently present. But it will take far more than that for genuine and lasting change to take place. The Covid-19 pandemic, which at the time of writing remains unresolved, has, however, produced some evidence that positive change is possible, at least in Britain. For the first time in half a century, the state and large sectors of industry faced an unprecedented public health crisis. The result was a call by government to manufacturing companies for a major boost in medical supplies, to which many responded. Teams of highly skilled people and organisations made themselves available to design and manufacture new products. In this context, cooperation between large and small manufacturers,

universities, medical companies and even Formula 1 motor racing teams – with their ability to rapidly design and produce prototypes – allowed the production of needed supplies to begin within weeks, if not days.

It remains to be seen how, if at all, current experience will change the way business is conducted in the UK, or indeed, who will benefit. But the current interest in and evidence of businesses assuming a social and public purpose – and in the context of the Covid-19 crisis, cooperating to deliver it – is reason for optimism.

Notes

1 See, for example, Tawney, 2010 [1920] and Veblen, 1923.

2 Shareholder primacy refers to the principle that managers should prioritise the financial interests of the company's shareholders over those of all other stakeholder groups.

3 The Railways Act required that charges be set, from 1928 onwards, at their 1913 level plus a 5 percent return on capital expenditure. Revenue for the system as a whole was set annually. This was the 'standard net revenue'. If exceeded, charges would be reduced. We are indebted to Edward Humphries for this information.

4 Note that this word is used in the USA to mean an incorporated private business. It has quite a different meaning in Britain, where the corporation is a form of organisation, usually of craft or trade guilds, which began in the late Middle Ages. Corporations had certain privileges: they were 'legal persons' whose life extended beyond the lives of its members and which could enter contracts. But as a condition, they were expected to engage in some form of public service. This meaning exists to the present day: for example, the BBC, originally an ordinary commercial business, was called the British Broadcasting Company Ltd. until transformed into a public service broadcaster, when it became the British Broadcasting Corporation. The link between incorporation and public purpose was broken in 1856 when the Joint-stock Company Act allowed incorporation without an Act of Parliament. In the USA, the corporation is simply a legally empowered business firm of indefinite life, 'public' if their shares are traded publicly, 'close' if held by a small number or by directors only. The word 'corporation' is used in this paper in both the UK and US senses. The reader must be alert to context.

5 See, for example, Veblen, 1904, 2009 [1921], 1923.

6 See, for example, Stout, 2012, Chapter 2.

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