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ESSAY

Toward a New Social Contract Theory in Organization Science

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This article suggests that strategy research (and other management disciplines as well) should move beyond a neo-Hobbesian approach to contracting toward a new social contract approach. Work from an agency theory perspective in particular has generated utilitarian insights, but its description of agent behavior is too limited and its assumptions are not a useful guide to productive alliances among firms. Altruism, ethics, goodwill, moral sentiments, and trust need to be placed in the foreground of our vision, and society must be accepted as the ultimate principal to which both individuals and firms are responsible.

A neo-Hobbesian perspective permeates economics literature and is rapidly diffusing to strategy research and other management fields. Following Bowles (1985) we refer to the models developed in agency theory (Alchian & Demsetz, 1972; Eisenhardt, 1989; Jensen & Meckling, 1976), transaction costs theory (Williamson, 1975, 1985), game-theoretic reputation models, and narrow economic (functionalist) approaches to organizational culture (Camerer & Vepsalainen, 1988; Kreps, 1990) as neo-Hobbesian because they rely on opportunism as a key concept for understanding the internal structure of the firm. Forms of opportunism such as shirking and free riding give rise to the archetypal Hobbesian problem of reconciling self-interested behavior on the part of individuals with collective or group interests. Economic explanations of the functional nature of the modern hierarchy bear a strong resemblance to the original Hobbesian rationale for the state as a socially necessary form of coercion. Thus Alchian and Demsetz's (1972) agency argument that a team of workers would rationally hire a supervisor to monitor their work activities is an economic analogue to the Hobbesian position that asserts uncoerced citizens in a state of nature would in their own interests commit themselves to obey the dictates of the state.

According to Williamson (1985), "Opportunism refers to the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse" (p. 47). It is possible to make the devil an honest man despite these assumptions (Hill, 1990) because it pays to be honest under certain conditions. *Calculative trust*, however, is basically a contradiction in terms (see also Williamson, 1992).

In this article, we argue that a broader view of trust and human behavior is required. Trust is defined as an expectation that alleviates the fear that one's exchange

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partner will act opportunistically (Bradach & Eccles, 1989). This is a mind-set characterized by a leap of faith that calculated self-interest alone would not anticipate. Even though opportunism is possible and occasionally occurs, trust prevails. Even in situations where trust is not totally justifiable or groundable, it is nonetheless generated and sustained.

Broadening the scope of assumed behavior to include trustworthy conduct has several beneficial consequences for management theory. First, a broader perspective suggests new solutions for the problems of incomplete planning, monitoring costs, enforcement costs, and dispute settlement that have benefits for both internal and external transactions. Second, a more balanced view of human motivation reunites the study of management with the field of ethics. We will argue in this article that these two benefits have special relevance for understanding alliance as a strategic option.

ECONOMIC APPROACHES TO CONTRACTING AND THEIR LIMITS

In the absence of opportunism and measurement problems, the contractual hazards of small-numbers bargaining (e.g., contracting when specialized assets are involved) would disappear. Consider situations that involve imperfect measurement of individual output, the *nonseparabilities problem*. Alchian and Demsetz (1972) provide the example of two men loading freight onto a truck. Because observation of the outcome (i.e., the amount of freight loaded at the end of the day) is not sufficient for ascertaining individual productivity, the *classical capitalist firm* and the *manager as monitor* are proposed as solutions to the possibility of shirking or free riding. The risk is that this neo-Hobbesian approach may lead to monitoring with excessive zeal. Given long study of human relations (Dalton, 1959; Mayo, 1945), we should know better. It is a rudimentary management principle that excessive monitoring reduces productivity.

Situations in which highly specialized assets are being exchanged in an ongoing contractual relationship between firms (Klein, Crawford, & Alchian, 1978; Williamson, 1985) are subject to even greater problems than intrafirm contractual agreements. When such exchanges involve bilateral monopoly, they are risky to undertake by definition because each party runs the risk of being "held-up." The amount that a party could theoretically appropriate is the difference between the first-best value and the second-best value of the asset—the so-called quasi-rent. The contractual problems between Fisher-Body and General Motors that ensued once the dies were cast are illustrative, and economists suggest that the eventual merger of Fisher-Body and General Motors was undertaken to avoid the contractual incentives to opportunistically appropriate available quasi-rents (Klein et al., 1978).

The solution offered by economists to interorganizational contractual hazards such as imperfect measurement and asset specificity once again boils down to the idea that the firm can mitigate opportunism through incentives, improved monitoring, increased auditing capabilities, and more refined compensation and dispute-settling mechanisms. The firm thus reduces opportunism at a cost. The alternative strategy of transferring transactions out of the market into the firm reduces these costs, but is attended by a loss of high-powered incentives (Williamson, 1985).

Broadening the scope of relationships to the difficult field of strategic alliances (Borys & Jemison, 1989) exacerbates this dilemma. The problem of interfirm cooperation from transaction costs theory and related perspectives is that alliances take place in a complex environment that precludes the possibility of writing a comprehensive agreement (Williamson, 1975). Real-world coordination difficulties between heterogeneous firms that possess differentiated products, dissimilar production processes, varied financial strategies, and organizational structures make complete planning unattainable. Theoretically, the implementation of contractual agreements between firms thus requires high monitoring costs that can easily dissipate benefits, whereas enforcement costs often involve costly court disputes between firms when unforseen outcomes occur.

It has been argued that these problems are so strong in the case of interfirm alliances that the solutions of classic industrial economics (Scherer & Ross, 1990) are insufficient. Williamson (1985) and others (Hennart, 1982; Walker & Weber, 1987) provide a persuasive case that internalization (e.g., internal growth, acquisition, merger) is required to overcome the contractual hazards involved in interfirm agreements. Internalization is favored on the grounds of the greater incentive, adaptability, monitoring, reward-refining, and dispute-settling capabilities of firms when compared to contractual arrangements.

Broadening the scope still further to encompass contractual relationships between firms and states, we find similar assumptions that the firm will indulge in opportunistic behaviors (polluting, hazardous work conditions, etc.) that are not specifically controlled by contract, whereas states tend to monitor with excessive zeal. Extreme forms of exploitation that endanger the life chances of citizens coming in contact with the firm can result (e.g., see "Manville Corporation," Chapter 35, in Snyder, Rowe, Mason, & Dickel, 1991), but allocating responsibility and bearing the costs of proposed solutions to such large-scale difficulties are unsolved problems.

Even in economic models, it is true that opportunism is not the only behavior possible. Empirical evidence shows that cooperation is often found in nonrepeated games (Sen, 1987), and is even more likely to emerge among self-interested agents in iterated games (Axelrod, 1984). Cooperation is also more likely to occur when knowledge is imperfect, for example, when cost characteristics of rival firms are not known or when the game has an indefinite end (Sen, 1987).

We argue in this article, however, that cooperative behavior can have a quite different explanation than that of the calculative self-interested man that emerges from such work. Egoistic incentives (reputation, reciprocity) are not necessary to create cooperation and altruism (Etzioni, 1988). In fact, examples of unselfish acts are ubiquitous. Long ago, Kropotkin (1924) pointed out the vast amount of mutual aid given in times of need. Etzioni (1988) gives more recent evidence of the existence of altruistic behavior; people mail back lost wallets, donate blood and bone marrow to strangers, support public television, and vote despite the incentive to free ride. We in strategy and related management fields need to keep in mind that managers and workers similarly do not regard transactions in a strictly neutral and instrumental way. Workers feel commitment to their employers, sales people track down needed information over their lunch hour, and managers initiate beneficial but time-consuming activities without salary incentives. In short, our experience supports a wider view of human behavior than is assumed in a number of the theories that are currently gaining favor.

Research along the lines of the neo-Hobbesian approach is certainly appropriate to strategic management as a scientific and pragmatic field (Barney, 1990; Mahoney, 1992), and recent empirical work in many other social science fields indicates the predictive power of theories of self-interest in certain circumstances. For example, Sears and Funk (1990) cite several studies of tax paying that show significant self-interest effects. Overall, however, Sears and Funk (1990) conclude "that self-interest doesn't usually have a major or significant effect on US public opinion" (p. 164). They cite both unclear means-ends relationships and the tendency of individuals to think at personal rather than system levels that go beyond calculations of self-interest in the voting booth. We argue that the prescriptive advice of neo-Hobbesian economics is of limited and declining usefulness for similar reasons. In complicated organizations it is often difficult for individual workers to carry out systemwide analysis or calculate the personal impact of their actions.

In short, the egoistic assumption drawn from economics allows for parsimonious models and predictive power, but is not scientifically established as a universal fact of human nature. This distinction should be emphasized to business students. Most business students are not instructed carefully on the distinction between self-interest as an empirical claim and self-interest as a simplifying premise (Bowie, 1991b); in fact, a number of business school graduates appear to adopt self-interest as the standard certified by their professional education (e.g., economics students). Both students and theorists need to consider the implications of more realistically portraying human actors.

This is not to say that self-interest should be ignored. Okun (1975) suggests that "efforts to suppress the tendencies toward self-interest by the individual—in societies as noble as monasteries or as base as Fascist dictatorships—have also severely restricted the rights of the individual" (p. 49). Our objection is to the modern tendency of teaching students that any action beyond that of narrow self-interest is irrational and invites being labeled a sucker. We argue instead that the allegory of self-interest is basically an unreflective story; it does not capture the range of our experience and it helps enact a world not worth living in.

REIFICATION OF THE MISTAKEN FOUNDATIONS OF ECONOMIC THEORY

It is quite ironic that overzealous admirers of the premise of self-interest have made Adam Smith their guru. A passage written over 110 years ago is still apposite:

> The isolation of the theory of political economy is peculiar to our own day. In more recent times, we find this study confounded with the other moral sciences,

> of which it was an integral part. When the genius of Adam Smith gave [economics] a distinct character, he did not desire to separate it from those branches of knowledge without which it could only remain a bleached plant from the absence of the sunlight of ethics. (Wolowski, 1882, p. 23)

Smith (1790/1976) actually champions benevolence, sympathy, and moral sentiments in his writing, although this emphasis tends to be lost in quotations by modern economists and business scholars (for exceptions, see Coase, 1976 and Viner, 1991). His central concept of the invisible hand regulating economic activity rests on the individual's adherence to human virtue and a common social ethic (Evensky, 1993), and his view of the individual is rich and complex. In fact, Sen (1987) notes that Smith chastised Epicurus for trying to reduce everything to one motivation:

> By running up all the different virtues, too, to this one species of propriety, Epicurus indulged a propensity, which is natural to all men, but which philosophers in particular are apt to cultivate with a particular fondness, as the great means of displaying their ingenuity, —the propensity to account for all appearances from as few principles as possible. (Smith, 1790/1976, p. 474)

Many modern economists have similarly ignored the human breadth Smith recognized, using him instead as the foundation for narrow assumptions about human behavior. Solow's (1993) observation is that:

> There is an important element of sheer daredevil athleticism in the attachment of economists . . . to the model of greed and rationality. "Show me anything, anything, and I will produce a model that derives it from greed and rationality."[1] (pp. 155-156)

McPherson (1984) is perplexed by the same behavior: "What is odd . . . is the desire to derive everything from self-interest as if that were a natural or necessary starting point. It is a peculiar feature of the sociology of the present-day economics profession that this odd ambition should be so prevalent" (pp. 77-78). In fact, Etzioni (1988) reminds us that efforts to explain away altruism have been advanced since the ancient Greeks. It seems that each generation must answer the challenge anew.

It is a particularly important time for U.S. business schools to reconsider the intellectual basis of our research and teaching. Mitchell and Scott (1990) forcefully argue that the ethic of self-interested, outcome-oriented individualism is a contributing factor of American decay. American leaders' lack of stewardship and management abuses of trust have had a devastating effect on American productivity. Productivity and trust are in fact inextricably linked (Ouchi, 1981), as forcefully explained by Arrow (1974):

> Now trust has a very important pragmatic value, if nothing else. Trust is an important lubricant of a social system. It is extremely efficient; it saves a lot of trouble to have a fair degree of reliance on other people's word. Unfortunately this is not a commodity which can be bought very easily. If you have to buy it, you already have some doubts about what you've bought. Trust and similar values, loyalty, or truthtelling are examples of what an economist would call "externalities." They are goods, they are commodities; they have real practical value; they increase the efficiency of the system, enable you to produce more goods or more of whatever values you hold in high esteem. But they are not commodities, for which trade on the open market is technically possible or even meaningful. (p. 23)

Beyond this argument, the critical importance of abandoning the classic economic assumption of opportunism to incorporate trust is that "the more people accept the neoclassical paradigm (of economists) as a guide for their behavior, the more the ability to sustain a market economy is undermined" (Etzioni, 1988, p. 250). This argument has received recent corroborating empirical evidence (Carter & Irons, 1991; Frank, Gilovich, & Regan, 1993; Guth, Schmittberger, & Schwarze, 1982; Marwell & Ames, 1981) as well. At the extreme, if all people behaved in the calculative, self-seeking manner described in economic theory, the market economy would collapse (Arrow, 1974). The underlying idea is that:

> Our beliefs about human nature help shape human nature itself. What we think about ourselves and our possibilities determines what we aspire to become; and it shapes what we teach our children, both at home and in the schools. Here the pernicious effects of the self-interest theory have been most disturbing. (Frank, 1988, p. xi)

The important ancillary argument is that high performance does not require a focus on opportunistic behavior. It is not true that apparently altruistic behavior must under closer scrutiny be revealed as reflecting egoistic motives (Piliavin & Charng, 1990). Stakeholders can see corporate social responsibility as indicating management skill (Freeman, 1984); firms can value reputation, including the reputation for being socially responsible (Bowman & Haire, 1975; Gatewood & Carroll, 1991; Wood, 1991); individuals known for being trustworthy are desirable partners (Frank, 1990).

Macneil (1980) notes that agency theory's quest for a noninstitutional, noncontextual, ahistorical explanation of contract de-emphasizes such effects. Similar criticism has also been articulated in the management literature by Eisenhardt (1989), and in the economics literature by Coase (1988), who chastises modern "blackboard economics" because "exchange takes place without any specification of its institutional setting. We have consumers without humanity, firms without organization, and even exchange without markets" (p. 3).

The alternative Macneil (1980) describes is a new social contract approach that can be integrated into the "conversation of mankind" (Habermas, 1979; Kahn, 1990; Mahoney, 1993; McCloskey, 1985; Oakeshott, 1933/1962; Rorty, 1979). The contract continues to be the important means of projecting exchange into the future in this much broader perspective on human activity. Macneil's view is new, however, in that it is neither the neoclassical contract of positive economics nor the contract of law. The new social contract approach assumes that "actors pursue two or more goals (utilities): [they] seek pleasure (and hence self-interest), and seek to abide by their moral commitments" (Etzioni, 1988, p. 254). The emphasis of this new view is not on individual actions, however, but on the social setting.[2] It is only in a social context that one actor can trust another to abide by moral commitments, a trust that leads to a satisfying exchange relationship. The social relationship is thus the institution which must be society's basic socioeconomic tool.

In the rest of this article we champion the new social contract approach as a means of uniting organization theory, strategic management, organizational economics, law, and ethics. As the fields of management inquiry mature, we have additional capacity to speak in these broader terms. As the economy globalizes and reaches more deeply into human life, it is increasingly important that we do so.

IMPEDIMENTS TO A BROADENED ETHICAL AGENDA

Before considering the new social contract approach we pose the following question: If the attenuation of opportunism and the development of business ethics is at the heart of responding effectively to management problems, then why are they not discussed more in our research and teaching? The answer is that one of the more damaging by-products of logical positivism and the empiricist movement is the assumption that ethical propositions lie outside the purview of science. For some time we have been in the position that social scientists may rationally discuss means but not ends.

Pragmatic philosophers such as Emerson and Dewey soundly reject the Cartesian dualism of ends and means that underlies this separation. Dewey (1929) suggests instead a means-ends continuum: We climb a peak only to find other peaks beyond us; no matter when we stop our Sisyphean climb, other peaks remain. Adopting a similar point of view, Emerson wrote:

> Causes and effect, means and ends, seed and fruit cannot be severed; for the effect already blooms in the cause, the end preexists in the means, the fruit in the seed. (Quoted from Bourgeois, 1984, p. 594)

These philosophical arguments from the beginning of the century are more and more compatible with the globalizing world in which we live. Accepting a pragmatic perspective, the key to successful management must be the journey more than the destination. We must become far more concerned with means than we have been in the past, recognizing the temporal brevity of the ends we can envision.

Anyone who suggests that the best direction for management research is toward "disinterested social science" is advocating, in fact, both an unattainable goal and an unprofitable journey. No such social science is humanly possible. As Giddens (1984) notes: "The theories and findings of the social sciences cannot be kept wholly separate from the universe of meaning and action which they are about" (p. xxiii). We can make our conversation more rational only by facing our valuations, not by evading them. To have evaluation, we cannot eliminate valuation.

It is not sufficient to relegate business ethics to a separate field of inquiry, and descriptive statistics of behavior cannot be the focus of our academic involvement. We need to integrate *practical* business ethics (Arthur, 1984) into our research and teaching. Conversation that discusses the criteria that are used in evaluating organizational interactions on some scale of goodness or badness is inescapable. It is apparent that many academics at present question whether ethics, even in this restricted sense, is a proper subject for management study. Our argument is that the ethical beliefs and the ethical practices of managers and workers are part of the data that must be considered in our research. What constitutes a fair employer is thus as important a variable for academic study as the entropy measure of related diversification.

The suppression of normative values may be deemed as "good" by some researchers, but this stance rests on a normative value as well. Myrdal (1970) argues against suppressing value judgments in the interests of science. He also rejects the sharp distinction made between positive and normative theory. His solution to the concerns expressed by positivists and those they have influenced is to suggest that the scientist boldly declare value judgments at the outset of the analysis:

> There is no other device for excluding biases in social sciences than to face the valuations and to introduce them as explicitly stated, specific, and sufficiently concretized value premises.... Emotion and irrationality in science . . . acquire their high potency precisely when valuations are kept suppressed or remain concealed in the so-called "facts." (Myrdal, 1944, pp. 1043-1044)

Our argument, to summarize, is that positivist philosophers were wrong in asserting that all ethical propositions are meaningless (Sen, 1987), and their legacy has negatively affected management research. Research that sidesteps ethics is problematic (Nelson, 1991). Boulding (1953) contends that most influential writers in social science (e.g., Adam Smith, Marx, Freud) have been moralists. They knew what they liked and especially what they didn't like, and they had no hesitation in giving their work a persuasive tone. In this spirit, we agree with Freeman and Gilbert (1988) that "we must put ethics in its rightful place at the very center of discussions about corporate strategy" (p. 7), and add that this change applies to all management studies. Management researchers and company executives each have an unavoidable role as "moralist"—not merely as describers of moral ideas and ideals, but as the creators and propagators of ideas and ideals (Barnard, 1938; Schumacher, 1973).

Bringing an ethical perspective to this work is critical because relinquishing the single-minded assumption of self-interest requires that we acknowledge malevolence as well as benevolence. In his essay "The Recent History of Self-Interest," Stephen Holmes (1990) does a good job of cataloging the darker regions beyond self-interest. He notes, for example, Adam Smith's list of disinterested passions which include "malice, the longing for revenge, . . . irrational avarice, zealotry, caprice" (p. 277). Social science and management science must take account of such human complexities, and can do so only by more directly discussing ethical behavior.

BASIC BEHAVIORS OF A NEW APPROACH TO SOCIAL CONTRACTS IN STRATEGIC MANAGEMENT

Arguments for the importance of ethics in management research are not new. Focusing explicitly on the field of strategic management, a narrow economic view of managerial obligations (Friedman, 1962) is rejected emphatically by Andrews (1980), who regards coming to terms with the morality of choice as perhaps the most strenuous undertaking in strategy. The "Harvard School" (Andrews, 1980) long argued for a broad definition of strategy that includes "the kind of economic and human organization (the company) is or intends to be, and the nature of the economic and noneconomic contribution it intends to make to its shareholders, employees, customers and communities" (Andrews, 1980, p. 18). Recent trends, however, have moved many strategy researchers away from this perspective toward definitions that are more tractable for empirical research and theoretical modeling.

In trying to reassert the importance of a broad, socially connected definition of strategy for empirical and theoretical work, we find Macneil's (1980) commentary on the basis for a new social contract to be particularly insightful:

> The fundamental root, the base, of contract is society. Never has contract occurred without society; never will it occur without society; and never can its functioning be understood isolated from its particular society. (pp. 1-2)

The implication is that businesses are inextricably bound to each other in a complex web of ongoing interdependencies that would not be possible outside the confines of society.

In many ways the problem of understanding the firm's place in its historical, institutional, social context is analogous to Rousseau's (1762/1952) original arguments about the social contract over two centuries ago:

> The problem is to find a form of association which will defend and protect with the whole common force the person and the goods of each associate, and in which each, while uniting himself with all, may still obey himself alone and remain as free as before [i.e., in the original state of nature]. (p. 391)

> What man loses by the social contract is his natural liberty and an unlimited right to everything he tries to get and succeeds in getting; what he gains is civil liberty and the proprietorship of all he possesses. (Rousseau, 1762/1952, p. 393)

The relevant scope of social contracts today involves a complex three-cornered set of relationships, outlined by Stopford and Strange (1991) and by Dicken (1993). There is mutual dependence among firms, among states, and between firms and states. In addition to these relations among corporate bodies are the relationships between individual actors, the firm, and the state. Although relations at all levels are of vital importance to business concerns, in outlining the emerging elements of a new social contract, our focus will be on individual-firm and firm-firm relations. The general issue the social contract must address, we argue, is not different from Rousseau's original outline, substituting "the firm" for the prefeminist use of "man" (Ferber & Nelson, 1993):

> The passage from the state of nature to the civil state produces a very remarkable change in [the firm], by substituting justice for instinct in [its] conduct, and giving [its] actions the morality they had formerly lacked. Then only, when the voice of duty takes the place of physical impulses and right of appetite, does [the firm, which] so far had considered only [itself], find that [it] is forced to act on different principles, and to consult . . . reason before listening to . . . instincts. (Rousseau, 1762/1952, p. 393)

> In fact, each individual [firm] may have a particular will contrary or dissimilar to the general will which [it] has as a citizen. [Its] particular interest may speak . . . quite differently from the common interest: [its] absolute and naturally independent existence may make [it] look upon what [it] owes to the common cause as a gratuitous contribution, the loss of which will do less harm to others than the payment of it is burdensome to [itself], and [thus] . . . *[the firm] may wish to enjoy the rights of citizenship without being ready to fulfill the duties of a subject. The continuance of such an injustice could not but prove the undoing of the body politic* [italics added]. (Rousseau, 1762/1952, p. 393)

The message is clear: The rights and benefits of participation in the socioeconomic context rest on fulfilling the responsibilities of being a part of that context (Etzioni, 1993). Similarly, the quid pro quo of organizational involvement is the partial subjugation of individual will. The individual worker must sacrifice immediate self-interest to coordinate with others (Barnard, 1938); the manager's task is to articulate a general vision that inspires this subordination of individual will (Barnard, 1938; Simon, 1945; Ulrich & Lake, 1990). Unfortunately, we are in danger of coming to believe recent models of egoistic and atomistic behavior and we are now proceeding to enact a world in accordance with these models—the amoral world of the "rights of appetite" Rousseau warned against. Such a world is not worth living in over the short term and is unsustainable in the long term.

We have outlined several critical assumptions on which an alternative world can be built. In summary:

- All actors (individuals, firms, states) have some impulses which can harm other actors.
- Society provides security and the possibility of proprietorship in this context.
- These rights of citizenship (security, proprietorship) are accompanied by responsibilities to the common interest.
- Society thus must be the ultimate beneficiary of all contractual behavior.

Five behaviors form the basis for successful contractual relationships in this framework. These behaviors must be the focus of both descriptive and prescriptive work. We cannot understand the function of behavior that we do not catalog, but by focusing attention on behavior that supports the new social contracts we can hope to encourage its increasing practice.

Recognition of Unity

Especially as the world economy becomes more dominant we must recognize the detrimental effects of us-versus-them thinking that pervades the world of agency theory and perceived zero-sum games; we must, in particular, redefine the boundaries of care. Boulding (1953) notes that "almost every organization . . . exhibits two faces—a smiling face which it turns toward its members and a frowning face which it turns to the world outside" (p. 10), but this distinction will be increasingly difficult to maintain:

> As competition becomes keener we need to remind ourselves and colleagues that management is not a gladiatorial contest, it is rather a process which tries to ensure that all involved—customers, suppliers, sub-contractors, agents, employees, shareholders—are satisfied. (Davis, 1991, p. 101)

Macneil (1980) suggests that in a world of stakeholders and constituencies, the complex economic actors of Adam Smith's (1790/1976) *Moral Sentiments* are more descriptive than a simplistic view of principals and agents locked in a world of individual self-interest.

Once we relinquish a blackboard worldview of two-dimensional "economic men," recognition of connection becomes possible. In a world of increased interdependence:

> One flat tire on a busy superhighway and traffic can be blocked for miles; one defective bolt and an airliner crashes; a gasoline shortage—shortage, mind you, not stoppage—and the whole national economy is thrown into turmoil. (Macneil, 1980, p. 104)

In his book *The Greening of America*, Reich (1971) argues more broadly for nothing less than the goal of "species solidarity" where harmony is maintained between individual freedom and social consciousness. This perspective draws more on the study of the humanities than the social sciences (Burrell & Morgan, 1979; Zald, 1993). It asserts that the genuine good for any individual in society rests with the good of all (Bowie, 1991a). From this perspective, a lack of social consciousness can be shown to generate distinct economic loss as well as the loss of essential human qualities. Alternatively, a sense of solidarity can enhance the welfare of the individual. We agree with Chester Barnard (1938), who ended his classic book *The Functions of the Executive* with the observation: "I believe that the expansion of cooperation and the development of the individual are mutually dependent realities, and that a due proportion or balance between them is a necessary condition of human welfare" (Barnard, 1938, p. 296).

Convergent Expectations

The sociologist Durkheim (1933) anticipates Boulding's (1953) internal/external distinction by using the terms *mechanical solidarity* (solidarity of likes, more likely to be found intrafirm) and *organic solidarity* (solidarity of unlikes, the task now required for interfirm cooperation). Solidarity is difficult to achieve in a world in which respect for the individual is fragile and perishable (Bauerschmidt, 1993; Rorty, 1989); it ultimately hangs by the narrow thread of "convergent expectations" (Arrow, 1974).

The convergence that makes an intellectually understood commonality real is not easy to understand or influence. Long ago Chester Barnard (1938) noted that:

> Organizations endure . . . in proportion to the breadth of morality by which they are governed. This is only to say that foresight, long purposes, high ideals, are the basis for the persistence of cooperation. . . . Inspiration is necessary to inculcate a sense of unity, and to create common ideals. Emotional rather than intellectual acceptance is required. (pp. 282, 293)

Ultimately, "the social solidarity making exchange work" (Macneil, 1980, p. 14) is derived from the "complex webs of interdependence created by the relation itself" (Macneil, 1980, p. 23), and organizations whose managers can build a culture that inspires members to transcend short-term interest will have a distinct advantage (Miller, 1992).

Work on culture and the possibility of positively affecting culture is especially useful here (Allaire & Firsirotu, 1984; Smircich, 1983). Culture can be defined as an interdependent set of socially acquired shared understandings, values, ideologies, tacit knowledge, metaphors, stories, specialized language, socialization, myths, symbols, rituals, organizational routines, and systems of belief (Geertz, 1973; O'Reilly, 1989; Pettigrew, 1979; Polanyi, 1958; Wiener, 1988). A strong culture involves convergence at sociological, psychological, artificial (e.g., routines and structures), and historical levels (Saffold, 1988; Schein, 1985).

Organizational (distinct from societal) culture displays these spontaneous features, but also has more intentional features (Williamson, 1992). It is thus affected both by intended strategy and emergent strategy (Barney, 1986; Gordon, 1991). Although it rarely reaches the depth and richness of anthropological cultures (Allaire & Firsirotu, 1984), some evidence suggests it is more adaptive and more easily developed than one would expect given the anthropological metaphor (Deal & Kennedy, 1982; Van Cauwenbergh & Cool, 1982; Wilkins & Dyer, 1988; Wilkins & Ouchi, 1983). Intended strategy, for example, may involve the creation of symbols, the management of shared organizational values, and corporate identification processes (Trice & Beyer, 1991, 1993). A key idea is that as supplying a satisfying exchange relation becomes a part of the strategic management agenda, the possibility of future unity is increased. The atmosphere surrounding a transaction (Williamson, 1975) is of increasing importance; and the exchange process itself becomes an object of value (Knight, 1921, 1935).

Commitment Over Time

Durkheim (1933) suggests that organic solidarity may ultimately be ungroundable or based on the flimsiest of grounds and yet continue to exist. Similar themes may be found in philosophy (Rorty, 1989), economics (Arrow, 1974), law (Macneil, 1986), politics

(Etzioni, 1993) and organization theory (Ouchi, 1980). This experience seems to show that generating and sustaining a sense of unity and solidarity requires ongoing cooperative relationships and conversations. The best known examples of the kind of interfirm and intrafirm associations we are talking about involve the Japanese Keiretsu and the Korean Chaebol.[3] The benefits found within these associations are now legendary and appear to have played a strong role in the phenomenal economic growth of the region: The network acts like a living organism, producing products quickly and cheaply. It explains why Hong Kong has superseded Italy as the world's top producer of fashion goods. And it explains how small companies in Taiwan run circles around big companies in the personal-computer market ("Survey," 1991).

In our view the arguments that the Keiretsu and Chaebol economize on transaction costs and overcome market imperfections (e.g., Chang & Choi, 1988; Leff, 1978) are accurate but incomplete. Asian alliances have been in place over a much longer time frame than most Western companies contemplate. They encompass a multifaceted context that is more complex than considered by most Western firms. The result of this framework is that any given exchange is only a small part of the total relationship, and the social context places a constraint on short-term, self-interested behavior.

Because these forms of alliance are tied to culture (Casson, 1991), it is foolish to think that Western firms can directly adopt them. The way they function is nevertheless instructive. First, they show there are quite different ways to establish a social context that controls the human tendency to maximize self-gain or engage in "unsocial passions" (Smith, 1790/1976). Second, they illustrate a way of interacting in which the formal contract plays a supporting role, rather than a primary one. The basic point is that the basis for relational contracts is a social connection among actors that goes beyond legal connections, and recognizes that this fabric exists over time (Granovetter, 1985).

Moral Criteria

We have argued that the spirit of market capitalism is based on the invisible institutions of altruism, ethics, goodwill, morality, and trust (Arrow, 1974; Dore, 1983; Nielsen, 1989), and that the broader cohesion of the global economy, which mixes different forms of economic activity, ultimately requires the same moral base. These invisible institutions are fragile and yet profoundly vital. As Durkheim (1933) writes: "Altruism is not . . . an agreeable ornament in social life, but it will forever be its fundamental basis. How can we really dispense with it?" (p. 228).

In direct contradiction to the basic assumptions of classic economics, a new social contract approach recognizes that:

1. one act has implications for other acts in the past and future;
2. any given action has implications for many actors;[4]
3. action outcomes for others ultimately impinge on the originator of the action.

These assumptions are much more complicated than the assumption of systematic self-serving behavior. Decisions based on them must be more content specific; they will recognize the unique nature of the time and the actors involved in the exchange. Although theory is thus made more complicated, a social contract perspective also allows the development of a social context that in turn makes it more likely that individuals will make moral (socially serving) decisions.

The old golden rule "do unto others as you would have them do unto you" is not a sufficient guide to moral behavior under the new social contract. The competent, healthy, forceful manager can be lured into thinking "of course I could deal with this if it happened to me." The world in contrast is peopled by a much more diverse set of actors—old and young, in various states of health and wealth, with a consequently broader range of adaptive ability at any point in time.

The guiding principle of the new social contract can be expressed as a more socially connected variant of the golden rule: "Do unto to others as you would do to a member of your own family." The critical ethical stance is to abandon the "faceless" agent (Foucault, 1977). The new golden rule shifts the locus of responsibility and the motivation for action—it's not what *they* might do to me, but what *I* want to do in the presence of those to whom I am related.

Expressing the new golden rule in terms of the mature family participant[5] does not mean a return to paternalistic management. In families, broadly conceived, patriarchy is not the only model and no one tops the hierarchy forever. In these complex ties, we have all been subordinate, we have all recognized our own need for sustenance.

Evolving family relations also hint at the enormity of the task before us in articulating the new social contract—for we must admit that even at our best we do not always know what to do when interacting with those we love, and we must admit that even in these closest connections we do not always have the will to do what we know we should do, or desist from doing what we know we should not do.

Participation in a New Dialogue

Recognizing our insufficient ability to generate new social contracts requires that the firm become a nexus of ethical conversation. MacIntyre (1984) and Etzioni (1993) argue that the language—and therefore to some large degree the practice—of morality today is in a state of grave disorder; what is needed is a Schumpeterian innovation in language. As with all innovative activity, sometimes a particular innovation will be a success, other times undesirable and unforeseen consequences emerge from new perspectives. The important thing is to recognize the need to bring together broader views of human motives. The conversation should be unbounded, diverse, undistorted, continuous, and at times argumentative (Kahn, 1990; Rorty, 1979). For example, to make ethics training effective in organizations, executives must insure that employees feel free to question directives when ethical problems are encountered (Harrington, 1991).

Conversation can provide both the text and context (i.e., information and meaning) for achieving reliable organizational learning and mutually satisfying interfirm and intrafirm transactions (Hurst, 1991). It can mediate the deep-level assumptions and the surface-level behavioral manifestations of organizational culture (Fiol, 1991) to construct a new sense of our rights and responsibilities as global citizens. Most important, it can reaffirm our unity with one another. The chemist and philosopher Polanyi (1958) notes that:

> The main reason for which people talk to each other is a desire for company. The torment of solitary confinement is that it deprives one not of information but of conversation, however uninformative. The fostering of good fellowship within small groups of people . . . is a direct contribution to the fulfillment of man's purpose and duty as a social being. But the process is also of practical use in making the joint activities of the group more effective. (pp. 210-211)

Now we must recognize that the dynamic of making the group more effective goes far beyond "good fellowship within small groups of people." Through conversation, we argue, we will more broadly understand our common global fate and begin to develop a convergent, moral sense of how we can improve our common condition.

NONSEPARABILITY IS THE SOLUTION, NOT THE PROBLEM

Arrow's (1974) central insight is that there is a moral and social basis to our contractual institutions. An important corollary is that the individual cannot be the central unit of economic analysis, even though it is imperative to sustain and nurture the individual morality that must inevitably confront collective immorality (Niebuhr, 1960).

The key for developing the new social contract approach is Rousseau's *with rights and privileges come duties and responsibilities*, and at the heart of the tension between the individual and the firm and between business and society is the interpretation of what citizenship entails. At issue is whether businesses are shirking their moral obligations as responsible citizens in the name of competition, bargaining, and responsibility to stockholders, and whether individual decision makers are similarly avoiding their duties and responsibilities in pursuing self-interest (Etzioni, 1993).

In developing this theme, Macneil (1980) goes right for the heart of agency theory by calling for the "death of principals." The principal-agent view is attacked on two fronts. First, the narrow view of *economic man* is called into question because "everyone is a mix of selfish and social interests melding in kinship and other social patterns precluding agency-principal differentiation" (Macneil, 1980, p. 80). Then, Macneil reminds us that the world of organizations is multifaceted:

> The constituency with the best claim in the Western world to being a principal (the stockholder) is far from it. We . . . find ourselves in a world of agents of contractual relations, rather than agents of principals, relations organized in hierarchical, bureaucratic structures. The hierarchies are subject not to a single constituency brooding over them, but to many constituencies interpenetrating the hierarchy and bureaucracy at all levels. (Macneil, 1980, p. 79)

Rather than calling for the death of principals, we respond to these observations by calling for the recognition that agency theory and other neo-Hobbesian approaches have been defined far too narrowly. What managers and stockholders have lost sight of is that society is the ultimate principal of economic contracts. Agency theory has misspecified the ultimate beneficiary of economic behavior and in the process has undermined the benefits of economic transactions.

Returning to the possibility that one of two men unloading a truck may shirk his responsibilities, we observe that social interaction is more likely to be an efficient corrective than the elaborate contracting, diligent monitoring, and hierarchical organizational forms recommended by agency theory. The people doing the work are close enough to it to make reasonable judgements about realistic effort, and they also have the greatest knowledge of the many reasons (clumsiness, illness, age, heartache, hangover, etc.) why input may vary among workers. In many, although not all, collaborative efforts of our experience, the promise of a sustained and productive working relationship with others (a social contract) is a more effective inducement to effort than legal promises and managerial oversight.

The new social contract approach, in other words, directly contradicts agency theory prescriptions (Arrow, 1985). Rather than seeing nonseparability as a problem, connections among individuals and organizations become an intrinsic and necessary part of the social context that help generate moral behavior. More specifically, because mutual dependence between exchange partners promotes trust (Shell, 1991), the prescriptions to the manager will often be exactly the opposite of those made by agency theorists.

The most important of these reversals involves *separability*. Whereas nonseparability invites free riding from an agency perspective, possible opportunism from a new contract perspective is more likely to be mitigated by establishing and emphasizing the links in time and space that bind people together. An important externality, in the language of economics, is that efforts to establish and maintain links among actors from the new social contract perspective will not have the recurring costs associated with incentives, monitoring, auditing, and dispute settling. Monitoring and the like are unfortunate costs in a world of principals and agents, but managerial investments in the context of social contracts have benefits in the future because they make it more likely that moral acts will be followed by moral acts (Etzioni, 1988).

INDIVIDUAL AND ORGANIZATIONAL DEVELOPMENT CAN BECOME AN ALTERNATIVE TO SATISFYING INDIVIDUAL INTEREST

We have argued throughout this article that the assumption individuals will act to maximize their personal self-interest is a simplistic, and ultimately a dysfunctional, view of human motivation. Laying aside for the moment the possibility that some acts that do not reflect self-interest nevertheless can be malevolent (Holmes, 1990; Smith, 1790/1976), we now want to concentrate on the possibility that human acts can be motivated by community and self-development.

In his work on a *theory of commitment* Robert Frank (1990) considers the usefulness of emotion and reputation:

> A person who is known to "dislike" an unfair bargain can credibly threaten to walk away from one, even when it is in her narrow interest to accept it. By virtue of being known to have this preference, she becomes a more effective negotiator. . . . Consider, too, the person who "feels bad" when he cheats. These feelings can accomplish for him what a rational assessment of self-interest cannot, namely, they can cause him to behave honestly even when he knows he could get away with cheating. And if others realize he feels this way, they will seek him as a partner in ventures that require trust.

The key idea is that "in order to appear honest, it may be necessary, or at least very helpful to be honest" (Frank, 1990, p. 95).

It follows that it is sensible for the individual to make choices, not on the basis of immediate reward or punishment, but on the basis of developing character. This is a sensible choice for the individual because there is some ultimate use to having made a commitment to socially oriented behavior. Thus we are not forced to argue that self-interest is totally abandoned. As Jane Mansbridge (1990) argues, a viable world based on altruism will not be sustained if the cost to self-interest is too great.

> Arrangements that make unselfishness less costly in narrowly self-interested terms increase the degree to which individuals feel they can afford to indulge their feelings of empathy and their moral commitments. (p. 137)

The key difference in this perspective from more calculative arguments is that self-interest is established as a general outcome of participation in a social context. Moment-by-moment behavior is based on broad, convergent, enduring, and moral expectations rather than continually calculating maximum individual gain. But here again there are some interesting uses. Two immediate benefits of shared expectations are decreased calculation time and increased certainty for the individual decision maker. Calculating individual benefits is a time-consuming and uncertain business. In complex settings no single individual has enough knowledge to do it well, even if he or she is motivated to take the time to try. With shared expectations, in contrast, and a societal perspective, the work of understanding complexity is shared. Following collective wisdom also increases confidence in the likely result of an action taken. In a society capable of delivering security and proprietorship, individuals trust that, on balance, their own concerns and self-interest will be taken into account; they will not suffer unduly while their fellows gain. Even when the immediate outcome is not beneficial, the individual knows that the *real* game is a larger one and has faith that continuing protective community-wide adjustments will be made.

There are examples of groups and organizations that have achieved this ideal, at least for a time. Pick-up basketball games, improvisational jazz, good conversation, and many responses to disaster offer the flavor of exchange without the intrusion of self-interest. Good marriages, close friendships, cohesive sports teams, a few neighborhoods, hand-shake partnerships, intensive work efforts, some energy and war-time projects suggest that this kind of exchange can endure. The larger argument, however, is that the more individuals act to create such circumstances, the more viable and enduring they become. Given the sober realities of today's world, with its evidence of broken contracts and untrustworthy partners, this commitment seems great. However, the risks of not working to develop a world of trustworthy alliance (individual and organizational) is far greater.

CONCLUSION

The basic thesis of this article is that by operating with neo-Hobbesian assumptions to assure short-term gains, the firm undermines the longer term benefits of alliance—not only with other firms, but among its own employees. Opportunism undermines the spirit of cooperation that is essential to business success (Bowie, 1988). More specifically, contracts that assume the other can not be trusted in the present are unlikely to lead to trust in the future. Therefore attempts to constrain opportunism along the lines suggested by agency theory and other similar economic theories will have continuing economic as well as human costs.

We have argued that we cannot make sufficient progress as academics in developing an alternative perspective as long as we concede to the artificial restraints on ethical discussion imposed by logical positivists and other arbitrators of the scientific. Contracts are social connections with ongoing social consequences. Understanding this context requires an integration of law (Fuller, 1969; Macneil, 1980), economics (Arrow, 1974; McCloskey, 1985), sociology (Durkheim, 1933; Swedborg, 1987), political science (Etzioni, 1993), and organization theory (Eisenhardt, 1985; Etzioni, 1988; Ouchi, 1980). We claim that developing an integrative, interdisciplinary approach to management research is imperative if we are to remain relevant to current and future managers. This interdisciplinary, pluralistic approach is also arguably the best way forward for the intellectual development of each academic field (Bowman, 1990; Huff, 1981; Jemison, 1981; Zajac, 1992).

The compelling reason to develop better understanding of the social context of contractual behavior is Etzioni's (1988) argument that moral behavior supported by the social context is likely to beget further moral behavior. The existence of trust gives one reason to trust. Trust builds optimism about others' behavior which can lead to further gains based on mutual cooperation (Frank, 1990; Orbell & Dawes, 1991). Conversely, distrust begets distrust (Banfield, 1958; Nussbaum, 1989).

In an chapter titled "A City of Green Thoughts," Giamatti (renaissance scholar, former president of Yale, and former baseball commissioner) noted that one of our strongest desires is to conserve purpose in a world of confusion (Giamatti, 1988). By developing new ideas about the contractual relationship, the contemporary business school academic and the modern business executive may share similar dreams and hopes of developing and nurturing organic solidarity. In some instances we may continue to view strategy in the narrow economic sense of "a continuing search for rent" (Bowman, 1974, p. 47), but in loftier moments we should be persuaded that strategy and its sister management sciences are also a continuing search for morally satisfying ways of interacting with other human beings.

NOTES

1. Allison (1971) refers to this as the " 'Rationality Theorem': there exists no pattern of activity for which an imaginative analyst cannot write a large number of objective functions such that the pattern of activity maximizes each function" (p. 35).

2. Although our main argument is that the social setting informs the study of economic institutions, we acknowledge that institutional economics also informs our understanding of the social setting. Institutions make people more confi-

dent that they can use trust and ethics as alternative ways to structure relationships (Shapiro, 1987; Zucker, 1986). We thank Tom Roehl for this observation.

3. Observers have pointed out that the basis for these two kinds of cooperation are somewhat different; whereas some Keiretsu have their roots in long-established trading companies, the Chaebol is more firmly rooted in family connections (Oh, 1992). In domestic Chinese-owned firms, a similar form of interfirm alliance is apparently more closely linked to individual entrepreneurs (Komiya, 1987). The content of exchange also tends to differ. In Japan, intergroup networks involve cross-shares, loans, and joint ventures whereas in Korea coordination is primarily through banks and government (Orru, Biggart, & Hamilton, 1991).

4. This observation is reflected in Frank Capra's classic movie *It's a Wonderful Life* and is discussed by Scott and Hart (1979) under their theme of the indispensability of the individual. A similar conviction is also articulated by Norton (1976).

5. Raghu Garud is also working on the idea that useful guidelines for contractual relations can be expressed in family terms, whereas Virginia Held (1990) argues more radically that mothering provides a paradigm for human relations that avoids contracts altogether.

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