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Stakeholder Theory and Business Economics (Economia aziendale)¹

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Abstract

In this paper a theoretical model is proposed with the purpose of exploring, from an ethical point of view, the relations between the Stakeholder Management Theory (SMT) and the Firm System Theory (FST). The latter is part of the Italian studies of *economia aziendale*. From this perspective *azienda* (any private and public organization) is seen as an open, synergetic system where any constituent part and function is strictly connected each other. Proposing a theoretical model where the SMT is included in the FST is useful in order to gain a better understanding of the explanatory power of the FST. Indeed, the FST could provide both to face the problem of dichotomy between economic success and ethics and to enlarge the perspective of SMT towards a systemic view of economic organization. In this way a four-principle model of extended SMT is derived. This could be useful to understand ethical position and view of any stakeholder of a company without undermine specific nature and working of original SMT

¹ This paper (a slightly modified version to that presented at conferences) has been presented at Rome, on 5-7 October 2006, for The Good Company Symposium organized by Pontificia Università San Tommaso (Angelicum) for the VI^o International Symposium on Catholic Social Thought and Management Education. It is an English modified version of the paper: “Stakeholder theory ed economia aziendale, spunti sulla relazione fra etica ed equilibri aziendali”, presented to the IV “European Symposium of University Professors” at Rome on 22-25th June 2006 and published in “Responsabilità Sociale d’Impresa e Nuovo Umanesimo (Bettini E. and Moscarini F., editors), published by San Giorgio Editrice, Rome, 2008. Thanks to the publisher of this Italian first version for the kind permission and to Dr Silvana Signori for her helpful comments, although it should be understood that I take sole responsibility for what is written here. The Italian term *economia aziendale* has been here translated as business economics. The Anglo-Saxon academic world contains no discipline that corresponds exactly to the Italian *economia aziendale*, a term that has been translated in a variety of ways. For this reason, the Italian term will be used at times.

1 – Introduction²

Although the stereotype of so-called “business amorality” has long been superceded³, two fundamental questions regarding the role of ethics⁴ in company management remain to be examined:

1. To what extent are there economic advantages in being ethical?
2. Which theories best describe such situations (descriptive aspect) and what are the implications regarding management choices (normative aspect)?

The relationship between ethics and competitive success lies at the very heart of a number of theories explaining and guiding entrepreneurial decision-making. This is especially true of SMT⁵, which rejects any separation between ethics and business (Freeman 1994).

Given the tendency nowadays to speak of stakeholders, the implications of SMT regarding the relationship between ethics and business should be examined in depth. It is particularly important to avoid making the identification of competitive success and ethics into a kind of generic “slogan”, vague and adopted uncritically, and thereby going the way of so many distorted interpretations of both the approach and the definition itself of stakeholder⁶.

The intention of this work, for the most part normative, is to show how the concept of a company as a “stakeholder system”⁷ may help in dealing better with the relationship between company ethics and SMT. This is undertaken using certain aspects of

² Any analysis of company management will have aspects that are both normative and descriptive. In the present work, empirical-descriptive analyses have been left in brackets, though in the full knowledge that all considerations put forward here constitute a starting-point for essential empirical investigation in the future.

³ This development has been simple enough at a methodological level and within the historical analysis of economic thinking. However, it has been more difficult in terms of real-life application, not simply because a stereotype cannot always be easily attacked by logic but also due to business at times being undertaken in degraded contexts where ethics and/or legality are frequently not respected.

⁴ Ethics are here referred to in very general terms, covering any form of ethical duty with a doctrinal basis. Moreover, the details of the distinction between ethics and morals (starting with Hegel’s observations) are not entered into here.

⁵ Starting with Freeman and Reed (1983) and Freeman (1984).

⁶ “The term “stakeholder” is a powerful one. This is due, to a significant degree, to its conceptual breadth. The term means many different things to many different people and hence evokes praise or scorn from a wide different variety of scholars and practitioners of myriad academic disciplines and backgrounds. Such breadth of interpretation, though one of stakeholder theory’s greatest strengths, is also one of its most prominent theoretical liabilities as a topic of reasoned discourse. Much of the power of stakeholder theory is a direct result of the fact that, when used unreflectively, its managerial prescriptions and implications are nearly limitless.” Phillips, Freeman and Wicks (2003), p.479.

⁷ This concept has also been put forward in Rusconi (2006a) in connection with unions as stakeholders. It is used again to examine the ethics of accountability documents in Rusconi (2006b), in Arena (2006). This approach is also in Rusconi (2009), in order to examine the relationships between ethics and competitive success.

SMT as well as with reference to the system-based approach in the classic Italian tradition of *economia aziendale*⁸.

Having dealt with the general characteristics of SMT and, in greater depth, their relationship to ethics, the intention is to propose, metaphorically speaking, a type of *merger*, inasmuch as FST allows for a broader view of business studies when compared to managerial theories such as SMT. Continuing in this way, the relationship between competitive success and ethical values in the area of FST will be examined, drawing a distinction between strategic and absolute ethics.

The successive systemic extension of SMT theory, while maintaining the central role of top management as “upholding equilibrium” among stakeholders, will also examine the ethical problems arising for individual stakeholders when relating to others. Such intellectual operation proves additionally useful in aiding a better understanding of business systems by top management itself.

Finally, attention is drawn to the need to carefully evaluate concepts and suggestions put forward here on the basis of empirical research.

2 – Remarks on SMT in the context of business ethics

In recent years, there has been an exaggeratedly widespread, frequently confused, use of the word “stakeholder”. With regard to this also Freeman, who has widely employed this concept in his studies, has called for avoiding “misleading interpretations” of the stakeholder concept⁹.

The relationship between ethics and business represents a key issue of the SMT. As it has seen SMT has arisen out of the context of managerial studies. Further, it consti-

⁸ In this instance discussion is limited to the company, but, *mutatis mutandis*, the process could also be extended to cover the entire complex of economic organizations.

⁹ See especially:

Table 2 – What Stakeholder Theory is NOT

Critical Distortions	Friendly Misinterpretations
Stakeholder theory is an excuse for managerial opportunism (Jensen 2000; Marcoux 2000; Sternberg 2000)	Stakeholder theory requires changes to current law (Hendry 2001 a; 2001 b; Van Buren 2001)
Stakeholder theory cannot provide a sufficiently specific objective function for the corporation (Jensen 2000)	Stakeholder theory is socialism and refers to the entire economy (Barnett 1997; Hutton 1995; Rustin 1997)
Stakeholder theory is primarily concerned with distribution of financial outputs (Marcoux 2000)	Stakeholder theory is a comprehensive moral doctrine (Orts and Strudler 2002)
All stakeholders must be treated equally (Gioia 1999; Marcoux 2000; Sternberg 2000).	Stakeholder theory applies only to corporation (Donaldson and Preston 1995)

(Phillips et al., 2003: 482).

tutes a theory of management, often defined simply as “a good idea”¹⁰, that sets out to widen the perspective in which corporate strategies are formulated, shifting the focus from increasing shareholder wealth to the maximized well-being of everyone who is in some way involved in the enterprise¹¹.

More recent papers have also overturned the concept of globalization geared exclusively to realizing more or less immediate profits, proposing instead that in the long run this process necessitates an approach aimed at maximizing the well-being of all stakeholders, obviously including shareholders, rather than maximizing company value for shareholders alone¹². From its very beginning, the basic idea of SMT was that *company survival and development is conditional upon an awareness of everyone involved in some way in the company*.

In the area of the theory under consideration, the following questions arise regarding the relationship between ethics and business success:

1. do possibly divergent interpretations of the stakeholder concept exist?
2. how might stakeholders be identified?
3. how does SMT relate to shareholder rights?
4. how is it possible to bring about the deeply significant blending of ethics and success-based strategy that for Freeman and others is fundamental to overcoming the “Stakeholder Paradox”?
5. does an ethical hierarchy exist for stakeholders and, if so, what is it?
6. what would be the “sound philosophical foundation” of SMT?

3 – The relationship between ethics and strategy in SMT: interested parties or with legitimate expectations?

3.1 – Different basic interpretations of the stakeholder concept

Insofar as it concerns itself with the behavior of top management relative to all stakeholders, SMT represents a *descriptive* study, though it includes a *normative* aspect as well. This is because, to put it simply, SMT also tells the manager “what to do”¹³. This normative aspect may assume a character of *instrumental hypothesis*¹⁴ or *uncondi-*

¹⁰ A concept repeated by Freeman also during conferences in Bergamo (2004) on the “History, development and problems of the stakeholder approach” and in Catania (see note 7).

¹¹ Freeman proposes a new concept of Capitalism, based upon an entrepreneurial approach aimed at maximising “stakeholder well-being”, a concept wide in value. Freeman, Wicks and Parmar (2006).

¹² Freeman, Harrison and Wicks (2006), Chapter 2.

¹³ A characteristic common to all management theory and business theory in general, is to link descriptive and normative approaches so as to become simultaneously a study in behaviour and politics as well as a guide to action.

¹⁴ Consider this type of statement: “if you *want* to obtain certain results you must implement your choices in this way”.

tional ethics, linked to a scale of values. However, stating that the best route to competitive company success is to respect the legitimate needs of all stakeholders, could well imply that ethics are no more than good business, setting aside any ethical principles of company management: this is very different to saying that ethics should be respected and may **also** be considered good business.

In the former case, it is possible to speak of an *instrumental* interpretation by the stakeholder, while in the latter, an *ethical* interpretation.

If an *instrumental* point of view is carried to extreme, though potentially logical, consequences, the stakeholder approach may become “no more than” the best route to maximizing shareholder profits: effectively becoming a new tool for maximizing wealth for shareholders, though of greater efficiency than other approaches.

Such an interpretation may lead to two consequences:

- a) should there be compatibility between ethics and business success, long term “goodness and earnings” keep step with each other. The end result is that shareholders, as well as other stakeholders, are happy and everyone lives in the “best of all possible worlds”, to paraphrase the optimism of Leibnitz, the 17th-18th Century German philosopher¹⁵;
- b) if such compatibility is lacking in business decisions, everything becomes more complex. Therefore, should this second possibility not be taken into account, there is a risk of having to deal with reality on the basis of insufficient knowledge and inadequate means of analysis.

On the other hand, the aim of an *ethical interpretation*¹⁶ is to explain how the top manager, also a stakeholder, may carry out his ethical duties; from this point of view, the pursuit of legitimate stakeholder interests/expectations becomes a moral value in itself.

However, if such an approach is interpreted badly, it runs the risk of “tying up” management in a tangle of rules and prohibitions. To avoid this, there should be an appropriate scale of values and effective use of the specific technical skills of whoever works within the company.

The presence of potential differences in values and/or related technical decisions should not be viewed as off-putting: consider, for example, the ethical and political/trade-union debate regarding greater or lesser powers of dismissal. Especially in today’s pluralistic society, it would effectively lead to paralysis to think that the stake-

¹⁵ About theoretical implications and faults of this “optimism” see Rusconi (2009).

¹⁶ “Thesis 3: Although Theses 1 and 2 are significant aspects of the stakeholder theory, its fundamental basis is **normative** and involves acceptance of the following ideas: (a) Stakeholders are persons or groups with legitimate interests in procedural and/or substantive aspects of corporate activity. Stakeholders are identified by **their** interests in the corporation, whether the corporation has any corresponding functional interest in **them**.

(b) The interests of all stakeholders are of **intrinsic value**. That is, each group of stakeholders merits consideration for its own sake and not merely because of its ability to further the interests of some other group, such as the shareowners” Donaldson e Preston (1995), p. 67

holder approach can function only in those instances where everyone shares the same system of ethical values in its entirety: SMT must also be able to deal with situations in which stakeholders differ over certain values.

3.2 – *The “boundaries for stakeholder identification”*

The difference between instrumental and ethical interpretations also influences the answer to the question: who are the stakeholders involved in the company?

Contrasting tendencies between a “narrow” or “broad” view¹⁷ have been present since the very beginnings of SMT. An instrumental approach would tend to consider the stakeholder as anyone with whom it is necessary to reach a deal in order to favor the competitive success of the enterprise, while an ethical approach identifies stakeholders as being linked exclusively to specific legitimate interests and/or rights. Taking the instrumental approach to an extreme, even a terrorist group or a criminal organization involved in extortion could be viewed as stakeholders to be satisfied, whereas an abandoned child or a worker with no legal-contractual protection might fail to be considered one!

3.3 – *The stakeholder approach and shareholder rights*

The ethics-stakeholder relationship also significantly impacts on the position of shareholders¹⁸. For some theorists this carries implications regarding the so-called “Stakeholder Paradox”, and thus: “Managers who would pursue a multi-fiduciary stakeholder orientation for their companies must face resistance from those who believe that a strategic orientation is the only *legitimate* (author’s note: in italics in the original text) one for business to adopt, given the economic mission and legal constitution of the modern corporation. This may be disorienting since the word “illegitimate” has clear negative ethical connotations, and yet the multi-fiduciary approach is often defended on ethical grounds. I will refer to this anomalous situation as the *Stakeholder Paradox* (author’s note: in italics in the original text)...I call this a paradox because it says there is an

¹⁷ **“Broad or narrow view?”** Windsor (1992) correctly points out that stakeholder theorists differ considerably on whether they take a broad or narrow view of a firm’s stakeholder universe. Freeman and Reed (1983) recognized early on that there would be serious differences of opinion about broad versus narrow definitions of “Who or What Really Counts”. Their broad definition of stakeholder as an individual or group who “can affect the achievement of an organization’s objectives or who is affected by the achievement of an organization’s objectives (1983:91) is virtually identical to Freeman’s (1984) definition. And their narrow definition reverted to the language of the Stanford Research Institute (1963), defining stakeholders as those groups “on which the organization is dependent for its continued survival” (1983:91)”. Mitchell, Agle e Wood (1997), p.856.

¹⁸ No problem of this type exists for the instrumental view, because, all things considered, it is focussed upon applying the stakeholder approach specifically so as to maximise company value for shareholders.

ethical problem whichever approach management takes. Ethics seems both to forbid and to demand a strategic, profit-maximizing mind-set”¹⁹.

Goodpaster’s viewpoint (1991), quoted here, still makes use of the stakeholder concept and confirms the existence of ethical duties towards them. However, he distances himself from the original interpretation of SMT, stating that: “Taking business ethics seriously need not mean that management bears *additional* (author’s note: in italics in the original text) fiduciary relationship to third parties (non stockholder constituencies) as multi-fiduciary stakeholder synthesis suggests. It may mean that there are morally significant *nonfiduciary* (author’s note: in italics in the original text) obligations to third parties surrounding any fiduciary relationship (see Figure 1). Such moral obligations may be owed by private individuals as well as private – sector organizations to those whose freedom and well-being is affected by their economic behaviour. It is these very obligations in fact (the duty not to harm or coerce and duties not to lie, cheat, or steal) that are cited in regulatory, legislative, and judicial arguments for constraining profit-driven business activities. These obligations are not “hypothetical” or contingent or indirect, as they would be on the strategic model (author’s note: here Goodpaster is referring to an exclusively instrumental view of stakeholder theory), wherein they are only subject to the corporation’s interests being met. They are “categorical” or direct. They are not rooted in the *fiduciary* (author’s note: in italics in the original text) relationship, but in other relationships at least as deep.

Figure 1. *Direct managerial obligations*²⁰

	Fiduciary	Non-fiduciary
Stockholder	X	
Other stakeholders		X

On the other hand, Freeman notes that the “Stakeholder Paradox” is a logical consequence of the “Separation Thesis”, to which he contrasts the statement that any entrepreneurial action inevitably possesses an ethical aspect²¹.

Thus, the profit-unconditional ethics dualism that emerges from the above statements is dealt with by SMT according to the logic of the absolute interdependence of

¹⁹ Goodpaster (1991), p.63.

²⁰ Ibid, p.67.

²¹ Freeman (1994) states (p. 410) that Goodpaster quite rightly points out that neither a wholly strategic stakeholder approach can exist, “business without ethics”, nor one that is exclusively ethical-multifiduciary, in that it would bring the private sector of the economy to an end, through “ethics without business”. However, Freeman refutes the so-called “Separation Thesis” which states that “The discourse of business and the discourse of ethics can be separated so that sentences like, “x is a business decision” have no moral content, and “x is a moral decision” have no business content”. On the contrary, he holds that “ ... There is always a context to business theory, and that context is moral in nature. In is only by recognizing the moral presuppositions of business theory, refining them, testing them by living differently, and revising them that we can invent and reinvent better ways of live”. Freeman (1994), p.412.

ethics and business success. In placing SMT within the FST of the Italian tradition of business studies, an attempt will be made, beginning with the above-mentioned view, to deal with several critical aspects requiring analysis.

3.4 – Problems arising from the concept of an essential unity between ethics and success strategy

The following, closely connected, questions should be asked:

- a) In what way does the strategic approach to ethics by SMT differ from one that is entirely instrumental?
- b) What action should be taken in the event of social and environmental degradation?
- c) How should ethical pluralism be handled?

SMT and any purely instrumental generic approach share the idea that there is inherent complexity in the analysis and search for equilibrium regarding stakeholder requirements. It should not be limited just to whatever is involved in maximizing shareholder wealth. The key difference is that a purely instrumental approach does not question the ethical value of what is done for stakeholders, whereas SMT insists on the existence of a close link between ethics and business.

However, the statement that in the long term there is an inevitable coincidence of ethics and business can become little more than a simple slogan, impeding an in-depth understanding of SMT and its problems. An examination of points b) and c), above, should help in dealing better with these problems.

Regarding b), consider the context of a degraded socio-economic-civil environment in which ethics play a negligible role and where there may even be a widespread disregard for law itself, leading to competitive disadvantages for law-abiding citizens. This is the case, for example, with black-economy labor, tax evasion and corruption, when they are systematic and go unpunished. In such instances, a superficial and instrumental approach to stakeholders might even risk “eroding” the respect for law and current ethics indicated by Friedman (1970) in his article in which he proclaims the exclusiveness of maximizing shareholder profits!

What would become of SMT instead? There is no immediate answer, but the problem can be expressed in this way: even the developers of SMT²² state that the theory itself does not give rise to ethical principles, such principles being pre-existent and potentially of varying types. Therefore, if certain principles can be seen as fundamental, general, pre-existent and possibly of varying types, there is no reason not to allow for the

²² “Stakeholder theory is not intended to provide an answer to all moral questions. Stakeholder-based obligations do not even take precedence in all moral questions in an organizational context. Violations of the human rights of a constituency group by commercial organizations and the gratuitous destruction of the natural environment are morally wrong, but such judgements rely on concepts outside of stakeholder theory as herein delimited”. Phillips, Freeman and Wicks (2003), p. 493.

existence of strategic choices that may be considered immoral according to the conscience of top management, but which “deliver financially”.

Point c), on the other hand, relates to the pluralism of current ethics²³. Speaking of “current” ethics, as in the case of Friedman (1970) for example, could lead to a particular “moderated” relativistic position, stating that moral principles hold true for everyone but only within a defined cultural context. Moreover, this would be in contrast to “radical” and individualistic relativism²⁴, as well as to the existence of objective and universal moral values. There are strong objections to this form of “cultural” relativism, including those based on the so-called “fallacy of naturalism”²⁵. But setting aside the logical criticism of moderated relativism, the fact remains that the coexistence of various “current” ethics within a single environment²⁶ means that individuals with differing moral principles operate within the same economic world. In certain cases this could lead differing competitive results in relationship to the ethical principles followed. Thus the instrumental approach runs analogous risks to those at point b), while the question needs to be asked as to what happens to SMT when the company decision-maker’s current ethics differ to those of others within the same environment. An attempt will be made to answer this question further on, but for the moment the problem of the ethical hierarchy of stakeholders should be considered.

3.5 – Does an ethical hierarchy exist for stakeholders and, if so, what is it?

The instrumental approach finds no particular problem with any possible “hierarchy” among stakeholders. In this instance, it is actually the search for competitive equilibrium that determines the behavior of whoever is obliged to maximize stakeholder benefits, albeit from a viewpoint not focused shortsightedly on short-term profits.

In the case of an ethical interpretation, on the other hand, it might well happen that the top manager, in laying out a stakeholder “map”²⁷ and formulating his strategies, finds himself having to give more weight to the legitimate expectations of a stakeholder with little or no voice, than to the demands of a more powerful stakeholder: for example, a community might pressure a company not to employ, at a managerial level, people discriminated against for reasons of sex, religion or being from a particular ethnic-linguistic group. In what way, here, does SMT differ from the straightforward instrumental application of the stakeholder approach?

²³ Consider the differing positions held by bioethics or religious differences.

²⁴ Regarding these comments, see Rusconi (1997), pp 36-38.

²⁵ The “fallacy of naturalism” (see the philosopher Moore (1903)) exists whenever a logical path is followed, transforming a statement of a fact (such as: “this group of people hold these moral principles”) into a general truth. Regarding moderated ethical relativism, see Bowie (1993).

²⁶ A fact that is increasingly marked these days, also as a result of globalisation.

²⁷ Regarding the stakeholder map, see Freeman (1984).

Essentially, this problem represents an aspect of what has been noted previously as to how, and under which conditions, SMT is able to build strategies in which ethics and success are intrinsically linked. It should especially be taken into account that:

1. if there is complete coincidence between competitive success and respect for those stakeholders considered legitimate, avoiding conflict with those not considered such, no problems arise, although this is also true in a purely instrumental context;
2. if satisfying the demands of non-legitimate stakeholders conflicts with meeting those of legitimate ones, it should be borne in mind that foregoing the satisfaction of non-legitimate stakeholders could bring about competitive disadvantages, especially in a context of social and environmental degradation²⁸;
3. in the event of conflict between legitimate stakeholders of differing “weight” and influence, should mediation not prove possible, recourse should be made to a hierarchy of ethical values. Such values should be objective and uninfluenced by competitive success, even if helped by those with technical skills within the company²⁹.

Therefore, SMT is distinguishable from a purely instrumental interpretation provided that:

- a. there is no prior assumption that a convergence between ethics and strategic success exists in all cases;
- b. the ethical role in competitive success strategies is evaluated in a way that is not ethically self referential;
- c. in any case, space is left for stakeholder freedom of initiative in pursuing their own interests by means of such technical skills as are useful to a civilized society.

All of the above, and in particular point c), yet to be dealt with, bring to mind the relationship between *economia aziendale* and ethics as proposed within Firm System Theory (FST). However, it should first be determined whether or not SMT represents an ethical theory in a real sense and, if so, to what extent.

3.6 – What would be the “sound philosophical foundation” of SMT?

Certain studies have underlined the lack of a sound philosophical foundation on which to base the stakeholder concept, proposing the use of various theories as a remedy³⁰.

²⁸ A company that rejects corruption and agreements with organized crime might find its survival seriously at risk.

²⁹ To give two simple examples: it is perfectly legitimate for shareholders to expect high dividends, but not at the expense of basic human rights; an employee is quite right to expect a pay rise, but this should not impact negatively upon the basic legitimate expectations of consumers or subcontracted workers.

³⁰ Argandona (1998) holds that the stakeholder approach is sufficient in dealing with the dichotomy between ultraliberal individualism and collectivism. However, it lacks a sound ethical foundation, which for him is identifiable as the theory of the Common Good as developed in the context of the Catholic Church’s Social Doctrine. Rusconi (2002) subscribes to what is stated above, although it limits the area of

Freeman (1994) notes regarding the presence of a “reasonable pluralism” of “normative cores” to which the manager may refer when applying the stakeholder approach³¹. The stark statement that SMT is not “a comprehensive moral theory”³² should also be kept in mind, since it is specifically an instrument for management and ethical strategies.

This has certain significant implications:

- a. to be considered such, an ethical approach to stakeholders should be conditioned by those theories (such as the Common Good) in which it is possible to avoid considering stakeholders simply as interested parties to be evaluated on the basis of their “weight” in competitive success;
- b. the question arises as to how, and to what extent, ethics interact with SMT. Although this theory views competitive success as usually linked to a respect for ethics, that does not render it an “a priori” factor, true in all instances, but rather involves an articulated process. In the final analysis, this process implies an understanding of what is meant by a company system in terms of synergy and how the socio-economic-cultural system functions, of which it is part;
- c. in particular, not only should the ethics of the decision-maker regarding company strategy be considered, but also those of all stakeholders within the company system.

All of this, though especially points b) and c), indicate how important it is to consider ethics in relation to the theory of the company as an open system³³, which has been developed within the context of Italian *economia aziendale*.

study to the right to information of stakeholders who are “weak” or “without voice” in compiling the company’s social accounts.

³¹ Freeman (1994), p. 414. In the same work there is a table with three differing “normative cores” possible for SMT, according to “A Reasonable Pluralism”: Doctrine of Fair Contracts, Feminist Standpoint Theory and Ecological Principles.

³² Phillips, Freeman and Wicks (2003), p. 493. In the same work there is a diagram summing up the various ethical-normative points of view that lie at the basis of stakeholder theory: “Figure 1 - Normative justifications for stakeholder theory

Author	Normative Core
Argandona (1998)	Common Good
Burton e Dunn (1996) Wicks, Gilbert e Freeman (1994)	Feminist Ethics
Clarkson (1994)	Risk
Donaldson e Dunfee (1999)	Integrative Social Contract Theory
Donaldson e Preston (1995)	Property Rights
Evan e Freeman (1993)	Kantianism
Freeman (1994)	Doctrine of Fair Contracts
Phillips (1997, 2003)	Principle of Stakeholder Fairness

³³ “The term open (author’s note: in italics in the original text) may be applied to a system interrelated with the environment (author’s note: in italics in the original text) in which it operates, the environment conditioning the functioning of the system and vice versa. Roughly speaking, the environment is identifiable with the market (or better, markets), technological progress (author’s note: in italics in the original

4 – Firm System Theory (FST) in the Italian business economics tradition and the ethics of business economics³⁴

From the 1920's onwards, Zappa proposed³⁵ a change in Italian business studies, developing, similarly to the German "Betriebswirtschaftslehre"³⁶, a discipline to be known as *economia aziendale*, which viewed business as a unitary institution coordinated so as to meet human needs. Business is, in fact, defined as an economic institution coordinating people and means, utilizing scarce resources economically, seeking to survive and develop in conditions of economic, financial and patrimonial equilibrium.

In general terms, this definition of *azienda* corresponds to what in international studies, especially Anglo-American, is defined as economic organization. This latter term covers the various realities that, while having differing institutional aims, share the same economic problem, which is to say, the management of resources that are in short supply. These may be profit and non-profit companies, public institutions, or families³⁷.

The present study limits itself to considering profit companies: in speaking of business, only entrepreneurial institutions focused on profit will be under discussion.

Returning to Zappa's theory, he states that a company is articulated into three essential aspects, being management, information (for example, accounting, both internal and external) and organization: "tripartition" as such is not intended, but rather the awareness that every action undertaken by business is conditioned by interdependent management, organizational and informational aspects, all of which are studied as specific interdependent disciplines (company management, organization and accountancy), linked to various business functions.

The various aspects and functions that make up business are integrated, so that any changes in, or generation of, a function will have repercussions on the others. For example, take the role of ethics in *economia aziendale*³⁸: from the moment the decision is made to give importance to an explicit consideration of ethics in business choices, and this was especially true of the 80's and 90's, an ethical business function is gradually generated, analogous, *mutatis mutandis*, to those of marketing or finance³⁹. This func-

text) and with the various institutions (author's note: in italics in the original text). the variability of these factors defining the variable structure of the environment itself". Antonio Amaduzzi (1988), p. 59. If the term "institutions" is widened (and since the focus is on open systems, this is in keeping with the spirit of the text) to include all types of relationship with whoever is in some way involved in the enterprise, it becomes clear, *mutatis mutandis*, that SMT may be introduced into FST.

³⁴ A specific study on the relationships between ethical stakeholder approach and historical Masters of *economia aziendale* is in Signori and Rusconi (forthcoming).

³⁵ Zappa (1926, 1950 e 1957).

³⁶ Regarding German theorists, see especially Ferrarsi Franceschi (1978), Chap 1, pp 11-90.

³⁷ Obviously, only the economic aspect is being considered.

³⁸ Studies of the relation between ethics and *economia aziendale* may be found in: Di Toro (1993), Riccaboni (1995), editor, Rusconi (1997).

³⁹ Company ethics are spoken of here as a "function" so as to indicate that management decision-making must take ethics into account as much as any other aspect of business system (marketing, finance, etc),

tion comprises aspects relating to management, organization (in relation to the company organization chart) and information (both internal and for public purposes, such as the social accounts⁴⁰).

From a starting point of Zappa's unified concept, it was then Aldo Amaduzzi who defined business as "...a system of economic forces that develop, in the field of which it is a complementary part, a process of production, or of consumption, or of both production and consumption, in favor of the major shareholder as well as individuals who cooperate in it"⁴¹.

Thus Firm System Theory was born, in which business is understood as a systematic and synergic unity of interacting elements and their relationships. This systematic extension of premises already present in Zappa's observations places particular importance on the "open" and "interdependent" character of business. This is both with regard to the link between its elements, which in general terms can be defined as "internal" (shareholders, manager, employees), as well as the relationship between these elements and those external to it (environment, institutions, etc). In this way, business institutions come to be considered as ultra complex subsystems of a wider socio-economic system⁴².

There is an increasing tendency for this interdependent system to link the solution to management problems to a broad, articulated, interrelated and dynamic consideration of all system elements. In this context, if company management wishes to be successful it must take into account the relationships between everyone who is some way involved in its activities, thereby coming back to the stakeholder concept. In fact, Freeman (1984), referring to SMT precursors, had already quoted systems theory⁴³, although he states that "The system model of stakeholder, by emphasizing participation, is a far reaching view of the nature of organizations and society. It has been quite useful in problem formulation, and represent an ongoing stream of research using the stakeholder concept. It

since specific skills are required and business choices are affected just as with finance, marketing or quality control. Therefore, the use of the term "function" does not imply any intention to make ethics subordinate to competitive success. Quite the opposite, since the ethical "function" opens the window for top management onto an ethical utilization of the various functions that are part of the business system.

⁴⁰ Social accounting was accepted from its very beginnings in the 1980's in the field of Italian business studies. This was also because it was felt that accounting systems, in this context, should be studied in a way that was strictly interdependent with aspects of management. The latter held that a correct and transparent relationship with all stakeholders was necessary, not only with respect to financial statements but also regarding ethical-social-environmental information. Concerning this, see Contrafatto and Rusconi (2005).

⁴¹ Aldo Amaduzzi (1969), p.20.

⁴² "in the business concept we include *all the economic units* (author's note: in italics in the original text) which are component parts of the general economy". Ibid, p. 18. Through taking this viewpoint further, thanks to an application of the organicistic view of general systems theory (Bertalanffy (1983)), adapted by Forrester (1974), it has been possible to arrive at Antonio Amaduzzi's definition of business as a system, quoted above in a previous note.

⁴³ "In the mid-1970s researches in system theory, led by Russell Ackoff and C. West Churchman "rediscovered" stakeholder analysis, or at least took Ansoff's admonition more seriously", Freeman (1984), p. 36.

is not, however, focused on solving strategic management problems which are narrower than total system design”⁴⁴. However, unlike systems theory in general, it is easier for FST to assimilate the stakeholder approach: by so doing, it modifies its configuration without losing any of its essential characteristics. These are actually enriched, thereby creating a more stable framework for SMT.

Having noted that SMT and FST share common characteristics, the relationship between ethics and strategy remains to be considered. Discussion of stakeholders operating within an open system leaves unanswered the problem of how to handle the relationship between ethics and strategy in company success, between stakeholders as parties with “interests” or with “legitimate expectations”.

The systematic view of Aldo Amaduzzi insists on the opening-up of business systems and on their interaction with all aspects of reality (whether historical, sociological, ethical/value-based, etc). Thus, with an extension of FST, it can be linked to SMT’s rejection of any separation between ethics and business⁴⁵.

If SMT is placed within a business system function dealing with ethics, obviously augmenting its role and importance, the various aspects of business are affected. At this point, the problem of the relationship between profit-motivated instrumentality and ethics arises and a solution must be sought in this new context.

It has already been noted that in instances of a divergence between success and ethics, a purely instrumental approach risks conditioning management analysis, and consequent decisions, on the basis of presumed future economic-financial-patrimonial results. On the other hand, a strong bias towards ethical principles will itself give greater weight to the consideration and application of moral principles.

SMT’s search for an intrinsic link between success strategy and ethics may therefore be handled by placing this theory into the context of FST’s ethical considerations, with especial regard to the dynamics of strategic ethics and absolute ethics⁴⁶.

Respecting this, an approach comprising two interacting stages might be proposed:

1. STRATEGIC ETHICS - consider “...all the moral choices that are to be made so as to maintain the long-term equilibrium of the business system; especially, here, in order to avoid behavior in which the need to maximize profits is acted upon by shortsighted management”⁴⁷. In this way ethical strategies are developed that are

⁴⁴ Ibid, p.38.

⁴⁵ It is essential not to forget that, even before SMT, an ethical company concept had arisen within FST, linked to satisfying everyone involved in the business system: this has certainly facilitated a stakeholder concept for FST that is not strictly instrumental. In particular, see Carlo Masini (1970) and Coda (1985 e 1989).

⁴⁶ Rusconi (1997), pp 154-161.

⁴⁷ Ibid p.154. Such “ethical short-sightedness” may be due not only to the single-minded pursuit of profit maximisation, but also to the results of certain functions being rendered unduly absolute; for example, giving too much importance to the size of turnover, or short term cash-flow.

able to maintain the equilibrium of business systems in the full light of the coincidence of ethics and business referred to by SMT.

2. ABSOLUTE, OR PURE, ETHICS - concern the basic moral principles to be dealt with by the Individual, or group of Individuals, occupied with business decision-making. In certain instances, such principles could possibly conflict with the development of a success strategy, in which case a suboptimal ethical strategy might be developed limited, with the aim of also taking binding ethical principles into consideration.

If this “two stage” proposal is accepted, then SMT is forced to admit a certain degree of separation between optimum success strategy and ethics. However, a large part of this theory’s area of activity remains unaffected, especially if it is considered that probably⁴⁸ *whatever appears suboptimum today in terms of success, could well turn out to be indispensable when everything is reconsidered in a few years’ time.*

In any case, it should be remembered that SMT is not an exhaustive moral doctrine, complete and self-contained. Since it may well reference differing “normative cores”, there is no reason not to suppose that certain instances exist in which a winning strategy from a competitive point of view is to be rejected on the basis of ethics.

Summing up, it is possible to identify certain common and differing aspects with regard to the interrelationships of SMT and FST relative to business ethics:

ASPECTS IN COMMON:

1. Ethics relate to the overall complex of business system activity and not “residual” aspects;
2. Strategic ethics are not self-referential at the level of principles;
3. The relationship between business and the socio-economic environment is bi-directional and open.

DIFFERENCES:

1. FST holds a general view of business that also includes management theories such as SMT;
2. Right from its very beginning, FST was not limited just to companies, whereas SMT developed as a study of profit-company strategies and became adapted only later, *mutatis mutandis*, to other organizations.

5. The company as a “stakeholders system” and the role played by ethics

There now follows an application of SMT arising from the *merger* of SMT into FST, bearing in mind that:

⁴⁸ Here there are ample possibilities for empirical research.

1. Evan and Freeman (1993) suggest there is no company-stakeholder dualism within SMT. Rather, the company is a complex of stakeholders to be coordinated⁴⁹;
2. Freeman (1994) states that a variety of ethical positions may represent the starting-point for SMT: for example, “feminist”, etc;
3. Recently, Freeman has defined the company as a “star map” in which every stakeholder has his own viewpoint⁵⁰;
4. The system concept is consistent with a systematic view of business, inasmuch as FST considers not only structural elements, but also their relationships, to be part of the system.

5.1 – *The principles of the proposed model*

1. The company is a stakeholder system

See what has been noted above.

2. Starting from SMT external ethical bases (the “cores” of Freeman 1994), all stakeholders tend to seek a dynamic equilibrium among themselves, based on “Minimal Mutual Acknowledgement (MMA)”

What is meant by MMA is a kind of lowest common denominator of stakeholder satisfaction, allowing them to reach a state of dynamic and provisional equilibrium with regard to the company. Thus companies tend to find themselves in a state of equilibrium

⁴⁹ In this work reference is made to a metaphysical director that “would be responsible for convincing both stakeholders and management that a certain course of action was in the interests of the long-term health of the corporation, especially when that action implies the sacrifice of the interests of all”, Evan and Freeman (1993), p.83. This concept was not subsequently developed, but the idea has remained that no company subject may act as a “neutral” counterpart in the name of the company itself. Top management itself is both stakeholder and in charge of stakeholder equilibrium, with the inevitable risk of a conflict of interests. Moreover, *mutatis mutandis*, such conflict also exists in the case of pure *profit maximization*, as is clearly indicated by agency theory. Evan and Freeman (1993) speak of “*both stakeholders and management*”, although the considerations in the following note clarify that no company constituent may be considered as outside of the stakeholders.

⁵⁰ Replying to a question on stakeholder maps in which it was asked whether “...in reality, business is not an entity separate to its *stakeholders* (author’s note: in italics in the original text), but rather a kind of network of the relationships between them”. Freeman notes that: “This is also the model presented by Russell Ackoff in the 70’s, supporting systems theory. Organizations, described as open systems, are part of a wider network rather than being independent and self-contained entities. The identification both of *stakeholders* (author’s note: in italics in the original text) and the interconnections they make among themselves is of crucial importance for this approach. My own studies focus on *managers* (author’s note: in italics in the original text) and their ability to handle relationships. Therefore I prefer to concentrate on these subjects. The systems theory viewpoint is certainly wider and gives a more complete vision. But, according to which *stakeholder* (author’s note: in italics in the original text) is placed at the centre of this star map, the perspective changes and therefore the information that may be obtained. This is not to say that business lies at the world’s centre, but that we are looking this world from the business viewpoint.” English translation of the interview with Freeman in Baldarelli, Santi and Signori (2005), p. 231.

when MMA “base conditions” are respected for all stakeholders⁵¹, considered as corresponding to their legitimate expectations⁵².

It has to be mentioned that MMA does not involve basic ethics and inviolable rights of the “ethical core” of a stakeholder approach, see also to the above mentioned difference of strategic ethics from absolute ethics. In such a way it is also possible to avoid to jeopardize the rights of weakest stakeholder.

3. Each stakeholder (top management, consumers, dependent workers, etc⁵³) “draws up” his own specific stakeholder “map”, with varying degrees of precision

In the view of SMT, the business strategy formulator, usually top management, is also the specific stakeholder in charge of “balancing stakeholder equilibrium”. This is inevitable, since top management is **the administration leader**, *acting as the stakeholder-subject of the company decision-making and management process, whereas all other stakeholders (including top management with regard to its specific expectations) are stakeholder-objects of management decision-making.*

By studying the system starting with as many different subjects as there may potentially be stakeholder-subjects, the view of the company as a system put forward here widens this perspective. Not only is it possible to speak of the managerial approach to stakeholders, but also of an approach to stakeholders from the viewpoint of unions, ecology, consumers, etc, thereby also creating the conditions for an increased understanding of how business systems function.

⁵¹ Even those who are hostile to the existence of a company system have interests, the potential to apply pressure, contracts and also rights. However, they are not part of the stakeholder network, because the company might well be destroyed in the name of their interests, possibly following maximum exploitation, as happens at times in the case of organised crime or business fraud. It has also been noted, though, that it is possible to satisfy hostile stakeholders when this takes place in the interests of legitimate stakeholders, recalling, for example, the distinction made by Phillips (2003) between *normative* stakeholders (towards whom there are moral responsibilities) and *derivative* stakeholders (whose requests are not morally acceptable): “Managerial attention to these groups is legitimate, but this legitimacy is derived from their ability to affect the organization and its normative stakeholders. Consideration of these groups is justifiably limited to this ability to affect the organization and its normative stakeholders”. Phillips (2003), p.31. At an ethical level, the matter should refer back to a “scale of values”: for example, is it morally acceptable to submit to extortion in the interests of stakeholders, when this implies an offence to society as a whole and therefore to the Common Good? Furthermore, in such cases the answer does not lie with strategic ethics, but with absolute ethics and their principles, in the light of “technical” knowledge of the effects on business decision-making.

⁵² Since it is not a question of rights considered fundamental by stakeholders, there is little likelihood of an extreme conflict between them. Therefore, one method of combating a lack of respect for MMA in the context of a company might be to apply “heavy pressure” (consumer or employee strikes, gradual disinvestment by shareholders, being discredited, etc), without this leading to feeling definitively excluded from the stakeholder network that makes up the business.

⁵³ This is simply a generalised indication, since stakeholder analysis should always be extremely specific; in certain cases, linked to specific management choices, differentiation between stakeholders must be made in a much more analytical way: for example, the distinction among different categories of employees.

This perspective can also be utilized to study responsibilities of every stakeholder of the firm system (see Goodstein and Wicks (2007)).

To sum up:

- 1) each stakeholder has his own view of MMA;
- 2) the top manager seeks to interpret and balance the legitimate expectations of all stakeholders;
- 3) the analysis of each stakeholder's subjective point of view helps improve, amongst other things, the top manager's viewpoint, thereby facilitating future management;
- 4) each individual stakeholder-subject "adjusts" his requests until, having clarified varying positions, a dynamic and unstable equilibrium is reached. According to SMT, the guarantor for this equilibrium is whoever manages the company, which is to say, top management;
- 5) this theoretical model does not conflict with the fundamental properties and basic principles of SMT, but it actually increases its utility;
 - a. it should be underlined that in establishing the best possible equilibrium among stakeholders also requires the active involvement of all stakeholder-subjects;
 - b. the purpose is to place SMT within a wider context regarding business systems and their ethics, especially with regard to the individual stakeholder's ethics and not just that of the top management.

4. Whilst respecting MMA's principles and inviolable ethical constraints, each stakeholder negotiates so as to reach a state of strategic equilibrium most favorable to his own legitimate interests

The convergence on MMA allows for a lasting, ethical existence of the company as a stakeholder system, without unduly limiting the field of action of stakeholders themselves. Each of them also possesses a *free area of negotiation*.

Each stakeholder is free, *as a stakeholder-subject*, to act so as create a relative improvement in his situation, especially economic. This makes the business system dynamic and stimulates the other system elements in favor both of increasingly economic and efficient behavior, as well as respect for basic morals, law and MMA.

This view takes the fiduciary duties emphasized by Goodpaster into consideration while avoiding any form of separation between business actions and ethics. In fact, in seeking to obtain the largest possible profit, shareholders make use of the top manager's fiduciary obligations. However, all of this must take MMA into account (from which point of view, they are all "qualitatively equivalent" stakeholders in terms of relationship), as well as the absolute ethics of the Individuals involved⁵⁴.

⁵⁴ It might be thought that in this case the presence of ethical pluralism could easily lead to asocial choices. The reply to this is that "looking after one's own interests" is filtered here through various levels (basic principles, law and MMA). Opportunistic and asocial behavior can therefore be dealt with by the sys-

The process of reaching an equilibrium among stakeholders is thought of as being continuous, dynamic and cyclical, as well as in constant renewal. This fits in well with the dynamic instability of business systems, which continually renew and modify their equilibrium relative to the general economic-competitive environment.

A distorted interpretation of SMT as a simple “static equilibrium” among business system elements could actually lead to “a corporative quagmire of economic, social and cultural dialectics among the various *stakeholders* (author’s note: in italics in the original text)⁵⁵”. Furthermore, this could create a “consociate cage”, potentially resulting in an Orwellian “Big Brother”-style company, though possibly “enlightened”, or one that is static, inert and in decline.

It is therefore possible to talk in terms of a general stakeholder theory (or extended SMT) within FST, bearing in mind that:

references to a “generalization” of approach might seem to imply an unjustified extension of SMT. Although the model above placed SMT within FST, it left unchanged its field of action, which is company management;

when the latter is described as a “stakeholder system”, this is not meant just as a nexus of contracts. Rather, the company is considered as a coordinated complex of relationships of varying natures (economic, social, ethical, environmental, etc) between stakeholder-subjects: that is, a synergic system of constituent elements and their relationships that continue over a period of time⁵⁶. By gradually acquiring “substantiality”, it comes to represent an institution with its own increasingly well-defined history, characteristics and identity.

6 – Conclusion

The *merger* proposed here between SMT and FST should, amongst other things, allow for a simultaneous consideration of:

1. ethics not subjugated to economic success;

tem structure itself. For example: the Common Good viewpoint might be pursued so as to induce the acceptance of behavior conforming to the Common Good, even by those who do not consider it to be an ethical principle but do not wish to violate MMA because certain stakeholders (NGO, religious groups, unions, etc) have decided to represent people who have little or no voice.

⁵⁵ Rusconi (2006a), p.194. As in, for example, the case of company suppliers. “...once top management has ‘agreed’ a particular policy regarding prices and conditions, suppliers are obliged to fall in with this and, vice versa, company is no longer able to “press a little” for qualitative improvement on the part of certain suppliers, possibly by requesting lower prices or considering alternative sources”. Ibidem.

⁵⁶ In *economia aziendale* a simple “take the money and run” activity is not considered as business, since a “tendency to last” is a fundamental characteristic of the latter. SMT also takes this tendency into consideration, inasmuch as it aims at the long-term maximization of well-being for all stakeholders.

2. questions of technical discretion and the decision-making autonomy of whoever is at the helm of a company, attempting to safeguard its equilibrium in the long term;
3. each individual participant's freedom of action;

Speaking very generally, it is possible here to think in terms of a series of concentric "ethical duties":

1. fundamental ethical rights-duties (linked to the basic principles of personal ethics) that need to be safeguarded in all instances, even when this might be seen as not consonant with the best possible strategy for competitive success;
2. a correct relationship between stakeholders on the basis of MMA, which should thereby allow the company a well-balanced development. This also represents an adequate ethical strategy in the face of entrepreneurial short-sightedness;
3. the potential, within the context of a basic respect both for absolute ethics and MMA conditions, for each stakeholder to "look after his own interests", thereby imparting a dynamic thrust to the company. This helps avoid using the stakeholder as an excuse to justify a management that is static, routine and, in the long run, lacking in competitiveness⁵⁷.

Exploring a little deeper, it may be noted that:

1. The business decision-maker's absolute ethics correspond neither to Friedman's current ethics, nor to objective morals imposed by any particular political authority⁵⁸. It develops within the subject's moral conscience and may at times lead *inevitably* to ethical ties greater than those for possible competitors who hold to other principles.
2. MMA involves aspects (higher salaries, certain characteristics of product quality, etc) that, while not considered essential from an ethical point of view, should be borne in mind in terms of stakeholder equilibrium.
3. *Success strategy also has an ethical value* inasmuch as it is morally positive to maintain business system equilibrium while simultaneously pursuing the socially legitimizing aim of all companies, profit or not, which is that of satisfying human needs in the long term.

⁵⁷ "This last principle is essential so as to avoid "tying up" *stakeholders* (author's note: in italics in the original text) in a consociate and bureaucratic network in which autonomy of negotiation and socio-economic dialectics are hindered. The principle here in play, as has been shown, is one arising from the very modality and context in which *stakeholder* (author's note: in italics in the original text) theory was developed)". Rusconi (2006a) p.199, note 13. Shareholders continue seeking to improve their situation, unions are busy working for improved living- and working-conditions, and consumers persist in looking for the same quality at a better price, although all of this takes place within a framework of the Individual's ethical rights and (the key innovation of SMT) the equilibrium of stakeholders' legitimate expectations. The company seen as aimed at the Common Good (Argandona (1998)) constitutes a solid foundation on which to develop this type of concept, both from the point of view of the stakeholder approach as well as business system theory.

⁵⁸ The respect for law alone is binding upon everyone, forming part of the absolute ethics of the good citizen with no wish to undermine the basic conditions for the civil and ordered coexistence of a socio-economic reality.

4. The existence of MMA as an area also facilitates a respect for the various basic rights insisted upon by certain stakeholders, rights that those having a differing ethical basis might otherwise not take into account.
5. Additionally, a situation such as the one mentioned in the previous point contributes to “raising top management awareness of virtue and excellence⁵⁹”. This means that whatever was originally respected for economic advantages alone, becomes increasingly accepted as a moral principle.
6. SMT operates more specifically in the area of MMA in terms of safeguarding against management shortsightedness, thereby aiding the conciliation of business and ethics.
7. In any case, stakeholder “boundaries” are conditioned by the presence of an ethical area of basic rights that cannot be set aside, safeguarding certain rights common to everyone.
8. Considering the proposed extended MMA from the subjective viewpoint of the “star map” (to use Freeman’s above-mentioned metaphor), it would be possible to undertake a study of the role, rights, ethics and choices related to stakeholders, including, for example, unions⁶⁰, the local community or consumers as equally valid stakeholder-subjects.

Finally, it should be stressed that the material presented here is intended as an initial proposal-hypothesis and as a stimulation to future studies of the phenomena in play, by means of careful and accurate experimental research.

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⁵⁹ Entrepreneurial shortsightedness is also the result of managerial diseducation, which may be challenged by pressure from certain altruistic stakeholders (for example, NGOs, religious groups and unions) committed to upholding the rights of stakeholders who are “weak” or “without voice”. It is possible to link this “awareness of virtue” to “virtue ethics” (of Aristotelian origin), even without fully sharing the philosophical structure. See Solomon (1992, 1993 e 1994).

⁶⁰ See Rusconi (2006a), pp 191-212.

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