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**Corporate Social Responsibility and the ‘Game of
Catallaxy’: The Perspective of Constitutional
Economics**

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Corporate Social Responsibility and the ‘Game of Catallaxy’: The Perspective of Constitutional Economics

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1. The issue.

- Milton Friedman (1962: 133) on the “social responsibility of business” in a market economy: “In such an economy, there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase profits **so long as it stays within the rules of the game**, which is to say, engages in open and free competition without deception or fraud.”
- The CSR issue: Are there other “social responsibilities of business” than **to seek profits within the rules of the game?**
- The purpose of this paper: To examine the **arguments on CSR** from the perspective of **constitutional economics**.

2. The Perspective of Constitutional Economics.

- **The research program of constitutional economics:**
 - Inquiry into the systematic relation between the ‘**order of rules**’ (the **constitutional level**) and the ‘**order of actions**’ emerging within the rules (the **sub-constitutional level**).
 - Inquiry into the procedures for **choosing rules**.

Rules / procedures for choosing the rules of the game



Rules of the game



Playing of the game

- Applied constitutional economics: Providing advice on “gains from joint commitment” (mutual gains from constitutional choice).

2. The Perspective of Constitutional Economics.

- Constitutional economics and the **game metaphor**.
 - Distinction between:
 - Playing a given game (within defined rules).
 - Choosing / changing the rules of the game.
 - The **individual players' perspective**: How can a given game be played better, more successfully?
 - The **community's perspective**: How can a given game be improved? What changes in the rules of the game might make a better game?

3. The Market als the „Game of Catallaxy“ and the Role of Profits.

- The market economy as “exchange and competition game”, as the “**game of catallaxy**” (F.A. Hayek).
- The “game of catallaxy” as “wealth creating game”
 - Hayek: “The individuals have reason to agree to play this game because it makes the pool from which the individual shares are drawn larger than it can be made by any other method.”
- Profit (i.e. the difference between the revenue earned from offering services/goods for exchange in the market and the costs of providing these services/goods) as indicator of success in the market game.
- The rules of the market game as the constraints within which profit or success may be sought.
 - Hayek: “How well the market will function depends on the character of the particular rules.”

3. The Market als the „Game of Catallaxy“ and the Role of Profits.

- **Dual capacity of individuals:**
 - As ‘players’ in the market game.
 - As citizens-members of the political community that defined the rules of the market game (or, more generally, of the ‘economic constitution’).
- In their individual and separate capacity as players in the market game: Responsibility to seek their success (profit) within the rules of the game (‘fairness’).
- In their joint capacity as citizens: Joint responsibility for defining and enforcing suitable rules of the game.

4. The Corporation as a Constitutional System.

- **The market game and the role of corporations:**
 - The “game of catallaxy” played among individuals as ‘natural persons’.
 - It would be inconsistent for individuals to agree to play the market game (because of its wealth-creating capacity), but then to require the participants not to strive for profits, i.e. for success, in playing the game.
 - Does the operation of corporations as ‘legal persons’ in markets make a difference in this regard?

4. The Corporation as a Constitutional System.

- Corporations as “constitutional systems”.

- Distinction between “stakeholders” who are participants in the team production process (and, thus, parties to the “social contract”) and other “stakeholders”.
- **“Social contract”** among the participants in the team-production process.
 - Recipients of contractual income (employees).
 - Recipients of residual income / profits (owners, shareholders).
- **Exchange relations** of the corporation to suppliers and customers.
 - Disciplining role of competition.
- **Political relation** to political community as rule-setting and –enforcing entity.
 - Responsibility for acting within the rules of the game.

4. The Corporation as a Constitutional System.

- **Profit as indicator of successful operation of the corporation within the market game.**
 - Profit = The difference between revenue earned from services / goods offered for exchange in the market and the costs of producing these services/goods.
- **The terms of the “social contract” among the participants in the team production process are subject to the test of market-competition (within the constraints defined by the rules of the market game).**
 - Alternative “constitutional contracts of the firm” as ‘conjectures’ of what is a more successful arrangement in market competition.
 - Lorenzo Sacconi’s model of “extended corporate governance” subject to market test.

5. Varieties of Corporate Social Responsibility.

- Classification of the demands voiced in the name of CSR:
 - The soft version.
 - The hard version.
 - The radical version.
- **The soft version:**
 - The most common variety, characterized by the slogan “Corporate social responsibility is good business”.
 - No conflict between profit seeking and CSR demands.
 - CSR demands as a matter of prudential business behavior.
 - An issue of strategy. - It is the function of competition to discover what is “good business”, i.e. what are successful strategies in the market game.
 - “CSR” as business consulting?

5. Varieties of Corporate Social Responsibility.

- **The hard version.**
 - CSR-demands that require corporations to act in ways that decrease their capacity to earn profits, given the rules of the game as they are.
 - They require corporations to act within rules / constraints that are different from or go beyond the 'official' rules of the game.
 - **A constitutional issue:** Under what rules / constraints should the market game be played?
 - Distinction between:
 - Constraints implied in informal rules of good and decent conduct, on which a general agreement exists in society.
 - Rules / constraints on which such general agreement does not exist.

5. Varieties of Corporate Social Responsibility.

- In cases where a general agreement exists on informal rules, compliance with such rules may be encouraged by informal sanctions, such as CSR-campaigns. Where compliance erodes beyond a tolerable threshold, formal enforcement may be needed (formalization of the previously informal rule).
- In cases where general agreement does not exist it should be the task of the formal legislative process to consider a change in the 'official' rules of the game, following the deliberative procedures defined for this process.
 - Deficiencies in the 'official' rules of the game cannot be remedied by individual 'social responsibility'. They require a change in the rules.
 - CSR-campaigns can contribute to the political debate on legislative reforms, but they should not become substitutes for the formal legislative process.

5. Varieties of Corporate Social Responsibility.

- The radical version.

- While the 'hard version' is about the rule-constraints under which corporations should be allowed to seek profit, the 'radical version' is about whether profit-seeking should be allowed to play a role at all in the economy.
- CSR-demands of the 'radical' variety amount to calls for abandoning the market game in favor of an alternative 'economic game' (as a rule, though, without specifying the 'economic constitution' of the alternative game).
- The 'radical' version is not about **how** the market game should be played, but **whether** it should be played at all.
 - Advertising a different game than the market game is, of course, legitimate, but it should be done under its 'true colors', not as a matter of 'corporate social responsibility' within the market economy.

6. Summary and Conclusion.

- Summary:
 - The soft version: Issue of strategy, about how to play the market game.
 - The hard version: Constitutional issue, about under what rules / constraints the market game should be played.
 - The radical version: About what game to play.
- Conclusion:
 - As players in the market-game, the social responsibility of corporations is, as Friedman argued, to seek business success (i.e. profit) **within the formal and informal rules of the game.**
 - As 'corporate citizens' that operate within political communities, corporations share in the joint responsibility for defining and maintaining rules of the game that serve the common interest of the community.
 - This joint responsibility may be more aptly called "**constitutional responsibility**" rather than social responsibility.