Stockholders, Stakeholders, and the Ethics of Universities

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Abstract *— Business schools teach stockholder and stakeholder perspectives for ethical decision-making, but what are the implications of those perspectives for the management of universities themselves? From the stockholder perspective, faculty are agents in an organization financed by two types of principals—private donors and governments—with goals based on education's social and economic benefits. The essay addresses the stockholder perspective's issues of open and free competition, deception and fraud, and the role of required or desirable objectives. Some university competition is open and free yet some is not. Deception and fraud do not appear significant. Objectives not specified by the principal may be required or desirable in pursuing educational objectives. Next, the stakeholder perspective suggests further parallels between business and academia. Three market failures—externalities, moral hazards, and monopoly power—are readily found in academia. Decisions do not incorporate all costs, there are numerous moral hazards, and monopoly power may arise.*

Keywords — academia, universities, ethics

1. Introduction

In 1970, economist Milton Friedman published his famous *New York Times Magazine* essay "The Social Responsibility of Business is to Increase its Profits". Friedman was concerned with the twin questions of why and how businesses operate. The title of the present essay is a play on his title, since the object of this essay is to apply concepts from Friedman and others to the operation and administration of universities. In so doing, I will demonstrate that there are numerous areas that have the potential to pose significant ethical concerns.

Business schools teach stockholder and stakeholder perspectives to help students make ethical decisions, but what are the implications of those perspectives for the management of universities schools themselves? Ethics and integrity are a central theme in business debates about corporate governance and corporate social responsibility (CSR), and may refer to concepts like property rights, agency, stakeholders, and market failures. Universities already address ethics and integrity in terms of course content, programs, and research, but this paper has a different purpose—to apply the basic concepts and arguments of those two primary social responsibility perspectives—the stockholder and stakeholder views—to the workings of universities.

Universities address social and ethical issues in teaching and research, but the extent to which they create ethical environments remains a topic for investigation (Cornelius, Wallace & Tassabehji, 2007).

2. Applying the Two Views to Universities

2.1 The Stockholder View

The stockholder perspective (Friedman, 1970) and the stakeholder perspective (e.g., Freeman, 1984; Donaldson & Preston, 1995; Friedman & Miles, 2002) address business goals and decision-making criteria. In the stockholder view, property-rights and agency mean business should pursue owners' goals (typically, profits). In the stakeholder normative view, managers ought to be concerned about interests beyond those of stockholders, due in part to market failures within capitalism.

Friedman's first stipulation is that managers work for owners. In the stockholder view, university administrators and faculty are classic wage agents working for principals (government and government) who invest in education by creating universities. The obvious stockholder concerns that arise are whether the principal's objectives are articulated, whether they are known by faculty and administrators, and whether they are pursued.

Friedman's second stipulation is the need for open and free competition. Certainly, universities compete for students, tax dollars, donations, jobs for graduates, and reputation. In the quest to attract students, they appear to compete openly and freely on many factors, including programming, instructional quality, location, facilities, network opportunities, and placement resources/record. There is evidence, however, that schools do not always compete openly and freely on price but, rather, form cartels to engage in collusive price-fixing. They may, for example, agree to standardize prices (tuition and board) or discounts (financial aid).

Friedman's third stipulation is that deception and fraud are unacceptable tools. Although universities may not have significant opportunity to engage in deception and fraud, the tools and training provided to their students clearly may be put to illegitimate use.

Finally, the stockholder perspective requires the organization to invest in non-primary objectives only when they are beneficial. Universities typically enjoy substantial freedom when defining educational objectives and how to pursue them. For example, spending on athletics and infrastructure may be only loosely linked to education.

2.2 The Stakeholder View

University stakeholders include taxpayers, donors, students, employers, faculty and staff, communities, and high schools. There are academic parallels of three particularly significant free-market failures identified in the stakeholder view: externalities, moral hazards, and monopoly power.

Traditional economic externalities are costs like pollution, which is created by transactions but borne by neither party. There are parallels in university growth, including the fully-loaded cost of faculty and the impact on real estate, taxes, and infrastructure.

Moral hazards (failing to disclose known or foreseeable shortfalls or costs to buyers) are numerous in academia—adulteration, false weight, substitution, and stimulation of excess demand. Costs are not fully disclosed. Quality is hard to define and measure—students may get less than they expected, and employers may get less than they expected. Substitute courses also may give less—the depth and effectiveness of online courses, for example, continue to be debated. The desire to maintain enrollment may be at odds with the demand for a school's graduates. Another form of moral hazard appears in the form of free-riding, or pursuing one's own objectives at the expense of another. The central values of academia mean that faculty have great freedom. Interestingly, many faculty decisions—course content and methods, research topics, conference attendance, and sabbaticals—rarely are required to be justified to an outside audience.

The third market failure is monopoly power. Universities have monopoly power as gateways to many careers, such as accounting, law, nursing, and engineering. This power protects schools from competition and requires students to be relatively insensitive to the price of education. Further, by developing bundled and specialized curricula, schools effectively lock their students into sole-supplier contracts for education. Monopoly power also exists in department structures, which essentially define the turf of what faculty may teach or study, and what students may learn.

3. Conclusions

The preceding discussion used well-known views of organizational responsibility to look at universities.

From a stockholder perspective, in contrast to Friedman's stipulations for a healthy system, universities do not always compete openly and freely. Price collusion occurs, as might other anti-competitive behavior.

The stakeholder view reveals a variety of potentially troubling issues in university governance. Particularly strong groups like faculty or administrators may dominate decision making. It is not clear that other stakeholders have strong voices in governance. There may be externalities associated with operation and growth. There are numerous moral hazard possibilities. And, monopoly power has its analogue in academia.

Various topics for further study and discussion come from this process of drawing parallels between business and universities, and from exploring the applicability and meaning of business governance concepts to the institutions which educate people.

The concepts of central interest to stockholder theory include property rights, agency, the need for open and honest competition, and the role of objectives mandated by society or seen as desirable by business. The focal points of stakeholder theory include the groups affected by business decisions and actions and the nature and consequences of market failures such as externalities, moral hazards, and monopoly power. Each of these topics has an extensive body of empirical research, theoretical analysis, and philosophical debate in areas of literature ranging from law to economics to management.

There is a remarkable opportunity to apply those bodies of research, analysis, and debate noted above to the study of universities. Universities can and—I believe—should pursue a greater role in discussions of governance issues of social and ethical/moral importance. Indeed, social and ethical/moral dimensions and implications are often found in our teaching, research, and outreach. Nonetheless, for universities to be viewed as leaders teaching, discussing, and acting on ethical issues, perhaps schools first should explore the ethical implications of their own governance structures, mechanisms, and norms.

It is important to pursue this form of self-analysis, not only so that higher education can operate effectively, but to help fulfill our educational role in society, to strengthen our shared values of intellectual integrity, and to create and share knowledge, ideas, and beliefs.

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