

Book Review

**The Form of the Firm:  
A Normative Political Theory  
of the Corporation**

by Abraham A. Singer.

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Writing as a political theorist, Abraham Singer begins his book, *The Form of the Firm* on the premise that despite public and political fixation on corporations, historically, there has been a dearth of literature on the subject from the disciplines of political theory and philosophy. Singer attempts to fill this void with an interdisciplinary overview on how modern corporations ought to be governed. Readers like myself, who come from outside the field of political theory will appreciate this contemplative contribution to corporate law and business ethics scholarship.

The book provides a thought-provoking critique of the law and economics perspective of the corporation that arose at the University of Chicago throughout the 20<sup>th</sup> century (the “Chicago School”). The Chicago School views the corporation as a nexus of contracts in which efficiency is improved through the bundling of freely-chosen arrangements between corporate constituents. Essentially, the corporation is entirely the product of market forces. Singer challenges the Chicago School’s assumption that corporations are purely economic and contractual entities that are justified in using all legal means to maximize profit. He contends that the Chicago School overlooks the role of the business corporation as an institution that depends on the cultivation of norms and social relationships.

Singer’s overarching argument is that economic theories of the corporation (or the firm), such as those conceived of by the Chicago School are important, but ultimately lacking for understanding the modern corporation in today’s liberal democracy. While this is a laudable contribution to the field on the political theory of the firm, Singer leaves out some important aspects. As discussed at the end of this review, the most notable of these omissions is the stakeholder perspective of E. M. Dodd, who laid out the groundwork for modern notions of corporate social responsibility.

Singer’s book is set out in three parts. In Part I, Singer articulates and assesses the economic justification of the corporation and explores the legal and economic theories associated with the Chicago School. In Parts II and III, he sets out various critiques of the Chicago School

*The Form of a Firm:  
A Normative Political Theory of Corporation  
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and offers a counterproposal that he calls the ‘relational’ theory of the firm. With certain exceptions outlined below, I am persuaded that Part I has the most compelling insights.

Singer begins by exploring the history of the firm in economic thought. He sets out the different ways theorists have tried to understand the corporation, ranging from Adam Smith to Karl Marx. Moving into the 20<sup>th</sup> century, Singer explores the ideas put forward by Ronald Coase in his foundational work on transactional costs, with a coherent articulation of Coase’s article “The Nature of the Firm” (1937).

According to Singer, Coase emphasizes in his 1937 article that in contrast to markets, firms are able to efficiently allocate goods and services (p.56). This is because firms internalize the “cooperative exchange of goods without sale” in a way that “replaces a series of contracts with an open ended contract” (p.57). Stated another way, firms are efficient and go against market forces because their goods and services are produced by employees, as opposed to a series of outside contractors.

This insight of Coase is set apart from the ideas of Adam Smith, who also characterized firms as instruments that suppress market forces (pp.41-44). However, in contrast to Smith’s pessimistic view that firms, or joint-stock companies as they were known in his time, stifle competition; Coase contends that firms increase efficiency as a consequence of circumventing market forces.

Additionally, Singer also provides a thorough explanation of Coase’s theory that directly led to the founding of the Chicago School and its law and economics approach, which subordinates legal analysis to preferences of economic theory. For example, the core concept of economics is efficiency, whereas in the law, efficiency is a secondary goal relative to fairness (ie. equity).

One such origin of this law and economics approach is Coase’s other influential article “The Problem of Social Cost” (1960). In this article, what has become known as the ‘Coase

*The Form of a Firm:*

*A Normative Political Theory of Corporation*

*by Abraham A. Singer*

Theorem' is established, that if four individually necessary but not sufficient conditions were satisfied, then market-based outcomes are optimal as compared to contrasting conditions (e.g., government regulation). Those four conditions are: [1] relatively few transactions required to internalize all material costs; [2] all transactions are voluntary; [3] individual transaction costs are small relative to the size of the transaction; and [4] the aggregation of all transaction costs is small relative to the aggregation of all transactions. Critically, routinely one or more of these four necessary conditions are missing and, thus, market outcomes are not necessarily superior to other outcomes.

More specifically, the Coase Theorem holds that if the four necessary conditions are present, then it does not make a difference whether one deals with externalities through contracts or through legal assignment (p.88). In other words, only markets with those four necessary conditions efficiently allocate the legal right to receive remedy in tort law and the duty to pay those remedies (p.120). Thus, a rational actor is paying approximately the same costs by settling a lawsuit as compared to participating in a judge-decided trial.

In commenting on Coase's 1960 article "The Problem of Social Cost", Singer argues that the Chicago School ignores the insight from Coase's 1937 article, "The Nature of the Firm". In fact, Singer himself suggests that the theoretical underpinning of Coase's two articles do not align (p.89). In "The Nature of the Firm", Coase argues that the efficiency of the firm is due in part to its differences from the market. However, in "The Problem of Social Cost", Coase sees the market as potentially, but not necessarily, optimal in accurately assessing the inherent costs of settling a lawsuit through a private contract as compared to proceeding to litigation, legislation, or governmental regulation.

Put another way, in "The Nature of the Firm" Coase argues that firms exist in order to reduce transactional costs. In "The Problem of Social Cost", Coase's argument rests on the opposite assumption that smaller transactional costs only are assured when these four stringent conditions are satisfied (p.120).

According to Singer, the Chicago School grabs onto the Coase Theorem and conflates it with Coase's argument in "The Nature of the Firm" to suggest that the firm is essentially a market, and this minimizes the distinction between the firm and private contracting (p.89). Singer views this as a misinterpretation or misuse by the Chicago School of Coase's theory. Singer's insight on the conflation by the Chicago School of Coase's work is quite perceptive.

What is noteworthy besides Singer's reformation of Coase's 1960 article is Singer's criticism of the Chicago School in general. It is clear that Singer has several objections to the implications of the Chicago School and its impacts on contemporary theories of the firm. A leading premise of his book is that the ideas of the Chicago School must be taken seriously if one seeks to understand the economic justification of the corporation. However, Singer clearly deviates from the models put forward by the Chicago School.

For instance, the Chicago School treats the corporation as a purely economic and contractual entity. According to Singer, this conception misunderstands the fundamental nature of the firm. Singer agrees that the Chicago School is highly relevant and influential in understanding a business corporation, but a corporation must also be viewed as a political entity if one is to properly examine its theoretical underpinnings as an institution. Thus, Singer argues that firms also upholds social and political values which enable their existence as opposed to solely seeking profit maximization. These social and political values include individual autonomy, social equality and other norms associated with liberal democracy.

In Part III of the book, Singer offers a counterproposal to the Chicago School perspective on the firm, which understands the firm only in terms of private contracts and as a creature of markets. Instead, in Chapter 9 Singer begins the development of what he calls a 'relational' theory borrowed from feminist legal theories on "relationality" (p.161). His aim is to bring corporations in line with liberal democratic norms. Singer relies on terms from Eric Orts's institutional theory of the firm in asserting that corporations connect to law is both "jurisgenetic" and "jurispathic" ways (p.174). That is to say, corporations are given internal power by the state

to generate their own norms, while still being subject to broader state regulation.

In Chapter 10, Singer focuses on strengthening corporate governance to render corporate relationships more legitimate. He proposes a pluralist approach where corporations are required to govern themselves in accordance with their own norms and values. Singer also posits a second, contrasting, approach that he characterizes as “more rationalist”. The aim of the second approach is to promote liberal values in governing corporations such as moral equality, individual liberty and a belief in democratic decision-making (p.191). As part of his arguments, Singer endorses cooperative enterprises over the corporate form. In his view, decisions in a cooperative will be allocated to those whose investment gives them a relational stake in business. Therefore, the business is governed by those who are most closely aligned to the enterprise, such as its labor force, customers and suppliers (p.202). Singer then goes on to discuss various disadvantages and advantages of corporations and cooperatives. He seeks to address the advantage of corporations having access to the stock market with a proposal for an alternative cooperative stock market. This alternative would mimic a stock exchange through the use of “mock” money and “mock” shares in a way that maintains the democratic and participatory ethic inherent in cooperatives (p.212). However, Singer’s cooperative analysis is as alien to existing corporate law as is the Chicago School’s subordination of that law to economic theory.

In Chapters 11 and 12, Singer sets out a theory of business ethics aligned with egalitarian justice. This theory aims to impose ethical responsibilities on corporations, one of which is to avoid profiting from market failures. According to Singer, under the market failures theory, more than mere efficiency is taken into account in making ethical business decisions (p.222). Examples include businesses refusing to sell faulty or harmful merchandise to the public, or treating pollution as an externality, even when polluting activities are deemed more efficient (p.226). Instead, corporations should seek to combat problems of racial exclusion by supporting affirmative action programs (p.246) and respecting the collective bargaining rights of workers (p.250).

*The Form of a Firm:*

*A Normative Political Theory of Corporation*

by Abraham A. Singer

Singer tries to accomplish a great deal in Part III of the book. Despite his meandering into various differing subjects, his insights are intriguing and somewhat novel to the field. The only major shortcomings of the book arise in Chapter 4, where Singer explores the managerial approach of Berle and Means put forward in their seminal work, *The Modern Corporation and Private Property* (1933).

Singer correctly points out that Berle and Means highlighted the division between the ownership interest of shareholders from the control over the firm exercised by management. According to Berle and Means, because of this separation of ownership and control, managers should have a fiduciary responsibility to act in the best interest of the shareholders (p.79). The concern arises when Singer states that Berle and Means “famously concede” that the corporation is “a social institution and must be recognized as such” (p.80). In this way, Singer mischaracterizes the views of Berle and Means as stakeholder theorists. On the contrary, their endorsement for strong fiduciary duties towards shareholders represents the origins of the shareholder primary model of the firm.

It is true, as cited by Singer, that Berle and Means wrote that “demands are constantly put forward that the men controlling the great economic organisms be made to accept responsibility for the well-being of those who are subject to the organization, whether workers, investors, or consumer” (Berle and Means 1933, p. 353). However, Berle and Means are not subtle in their expectation that it is the responsibility of directors to protect the interest of shareholders as opposed to other stakeholder groups. These managerialists understood that a corporation belongs to “its shareholder, or in a wider sense, to its security holders, and theirs is the only interest to be recognized as the object of corporate activity.” (Berle and Means 1933, p. 354). Therefore, it is incorrect of Singer to suggest that Berle and Means support a duty of corporate managers to “take the interests of society as a whole into account” (p.179).

In a closely related second critique, Singer curiously does not mention an influential 1932 debate between Berle and an early stakeholder proponent, E. Merrick Dodd. This debate was a pivotal event that resulted in nascent theories that came to be known as the shareholder and

stakeholder model.

In the debate, Berle argued that a corporation should be run with the objective of serving the interests of its shareholders by enforcing a strict fiduciary duty for management. Dodd countered that corporations must be accountable to various stakeholders in society. Dodd's main point was that there is a community at large within which these corporations operate. For this reason, Dodd may be regarded as a forerunner of the stakeholder theory and modern conceptions of corporate social responsibility (Elson and Goossen 2017). However, Singer instead suggests that it is Berle and Means who are linked to corporate social responsibility, rather than Dodd (p.89). This is a suspect claim which I contend is without merit.

Perhaps Singer overlooked this debate, and Dodd's contribution to stakeholder theory, because it is most prominently cited today among legal scholars (which Singer is not). It also does not have a comparable impact as the law and economic theories of the firm, which Singer focused on. Despite this, Dodd's ideas on the responsibilities of business managers continues to have resonance. Take as one example the 2019 announcement of the Business Roundtable's *Statement on the Purpose of the Corporation*, in which 181 CEOs committed to leading their companies for the benefit of all stakeholders (Business Roundtable, 2019).

The themes raised by Dodd are parallel in many ways to the questions raised by Singer on the legitimacy of corporate power in a liberal democracy. Thus, it would have been engaging for the reader if Singer tied together his own ideas with those of Dodd in reaching normative conclusions on the modern corporation. Dodd's stakeholder conception of the corporation supports many of the same liberal democratic ideas, including legitimacy and equality, that are integral to Singer's proposal for a relational theory of the firm.

Finally, Singer has provided an underdeveloped review of the scholarship on the stakeholder theory of the firm. There is mention of the team production model put forward by Blair and Stout as a critique to the Chicago School (Blair and Stout 1999). However, little else is mentioned on the subject. Another conspicuous omission is the influential work of R. Edward

*The Form of a Firm:*

*A Normative Political Theory of Corporation*

*by Abraham A. Singer*

Freeman on stakeholder theory (Freeman 1994).

Despite Singer failing to incorporate certain aspects of stakeholder theory, reading *The Form of the Firm* is a worthwhile endeavor. It serves its primary purpose by injecting political philosophy into theories on governing business corporations. It is an insightful and interdisciplinary perspective that academic readers will appreciate. The book is of particular assistance to readers, like myself, who come from outside the realm of political theory and the thought-provoking application to corporate law and business ethics that comes with it.

*The Form of a Firm:  
A Normative Political Theory of Corporation  
by Abraham A. Singer*

Note: A similar version of this book review first appeared in *Law and Politics Book Review*

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