Towards an Ethical Wealth of Nations: An Institutional Perspective on the Relation between Ethical Values and National Economic Prosperity

Peter L. Jennings
Manuel Velasquez
Santa Clara University

ABSTRACT: In this paper we examine how ethical values contribute to national economic prosperity. We extend the concept of an ethical wealth of nations first introduced by Donaldson in which he proposed four categories of ethical values—fairer distribution of goods, better government, ingrained social cooperation, and inculcation of economic duties—that can drive economic performance, but only if citizens ascribe "intrinsic value" to them independent of their economic interests. Our analysis draws on institutional economics and sociology research to show that if ethical values are to drive economic performance, they must also be supported by the institutional fabric of the nation. We embed an expanded set of ethical values in a set of democratic, free market and civil society institutions spanning three sectors of society—political, economic and cultural respectively. We conclude by discussing the implications of our institutional framework for moral education.

KEY WORDS: Ethics, values, institutions, wealth of nations, responsible leadership, moral education

HOW, IF AT ALL, are ethical values related to national economic prosperity? In "The Ethical Wealth of Nations" (2001) Donaldson attempts to answer that question. Donaldson claims that successful economies rely in part on the collective values of their participants. He points out that economists have provided some evidence that certain values, when embraced by a society's population, promote economic prosperity. Some of these values, he claims, are ethical values, which he organizes into a "typography" of four categories: *fairer distribution of goods* that enables everyone, especially the economically disadvantaged, to develop and employ their talents which increases economic productivity; *better government* that is more open, democratic and "market-compatible" to provide the freedom necessary to fuel innovation and economic activity; and *ingrained social cooperation* and *inculcation of economic duties* to avoid destructive economic interactions and support the efficient functioning of the economic system. Donaldson claims that when a political economy possesses these ethical factors, national economic performance will be higher, not only because they help remedy market imperfections, but also

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because they contribute to the broad political and social conditions that drive economic performance in ways that even idealized perfect market conditions cannot.

Donaldson is not the first to claim that ethical values are instrumentally important to economic prosperity (e.g., see Frank, 1996; Sen, 1985, 1997; and more recently, Porter & Kramer, 2006; and Porter & Rivkin, 2012). However, Donaldson's distinctive contribution is the paradoxical insight that ethical factors can drive economic performance only to the extent that individuals see them as having "intrinsic value" that is independent of "their usefulness in attaining some additional object that satisfies the individual's self-interest" (Donaldson, 2001: 32). If an individual's commitment to ethical values is based on self-interest, he argues, those values will be abandoned when it is in the individual's interests to do so. Those values will then not provide the trust and cooperation that successful economic transactions require, particularly in certain economic situations, such as prisoner's dilemmas and commitment problems.

Though less well known than many of his other contributions, returning to Donaldson's article, we believe, will yield valuable and timely insights. First, the relation between ethical values and economic prosperity and, more broadly, the role of ethical values in a modern commercial society, is a fundamental issue for research on the political economy going back to Adam Smith. Second, revisiting Donaldson's article is timely in light of calls in business ethics research for a better balance between research focusing on individual ethical decision making—the Moral Manager Model—and research focusing on the moral aspects of the political economy—the Moral Market Model (Boatright, 2010). Third, Donaldson's insights into the role and importance of ethical values to national economic prosperity has proven prescient in light of the emergence in recent decades of a new form of capitalism—what some have called "investor capitalism" (Useem, 1996)—and the ensuing fallout from what Carroll (2010: 717) described as the "two business ethics eras"—the Enron era accounting scandals and the Wall Street era financial crisis. The ethical failures stemming from this new form of capitalism extended beyond individual wrongdoing and involved systemic institutional failures that have caused many to question the moral consequences of economic growth (Friedman, 2005; Picketty, 2014). Indeed, some have argued that we are now in a "battle for the soul of capitalism" (Bogle, 2005). Thus, we believe that revisiting Donaldson's notion of an ethical wealth of nations is important to advancing our understanding of how ethics is related to national economic prosperity.

Although Donaldson's typography of ethical factors establishes a compelling conceptual foundation for his notion of an ethical wealth of nations, we find his analysis lacking in that he does not explicitly address how his ethical factors and economic prosperity are related, if at all, to institutions. Institutions have long been recognized as important to economic prosperity. Indeed, Adam Smith devoted significant portions of his books, *Wealth of Nations* and *Theory of Moral Sentiments*, to analyzing the nature of an appropriate institutional framework that would not only promote economic prosperity, but do so in a way that harmonizes individual self-interests with the broader interests of society (Hanley, 2009). Since Donaldson's article appeared, much research has examined the role of institutions in advancing economic prosperity. So we begin our extension by reviewing recent scholarship in institutional economics (e.g., Acemoglu & Robinson, 2012; North, Wallis, & Weingast, 2009; Rodrik, Subramanian & Trebbi, 2004) as well as research from the sociology of institutions (e.g., Bellah, Madsen, Sullivan, Swidler, & Tipton, 1991; Heclo, 2008; Selznick, 1957, 1992).

This research highlights that national economic prosperity depends significantly on a particular combination of institutions across three sectors of society—political, economic and cultural. Political institutions favorable to economic prosperity are generally characterized as democratic; economic institutions linked to economic prosperity are characterized as supportive of free markets; and cultural institutions conducive to economic prosperity include a diverse array of civil society institutions. These findings allow us to restructure Donaldson's typography of ethical factors by embedding them in a tripartite institutional framework involving an interlocking set of democratic political, free market economic and civil society cultural institutions. Overall, this research establishes that institutions not only play an instrumental role in mediating the relationship between ethical values and economic prosperity, but also embody the fundamental ethical values constitutive of what Bellah et al. (1991) call "the good society" —a society characterized by the open access institutions of democracy and by inclusive economic institutions, in and through which not only prosperity, but peace, freedom, equality and rights and justice flourish. We therefore extend Donaldson's "intrinsic values thesis" and propose what we refer to as our "institutionalized values thesis" which posits that to contribute to economic performance and realization of a good society, ethical values must not only be intrinsically valued by citizens as Donaldson argues, but they must also be fully embedded in and supported by the institutional fabric of society.

Second, we critically examine the ethical factors Donaldson identifies and propose additional values that address certain institutional tensions within each sector that impact economic prosperity and societal flourishing. In the political sector, we focus on the tension democratic governments face in promoting distributional fairness while preserving access to opportunities that support economic freedom and productivity but create inequalities. We extend Donaldson's *fairer distribution of goods* to include *fairer access to opportunities.* Then we focus on the defective incentives created by democratic institutions that can undermine the effectiveness of public policies important to economic performance and we refine Donaldson's *better government* to emphasize *better executed government*. In the economic sector, we focus on the tension between market competition that underlies productivity and the ethical values that restrain opportunism and support the system and thereby sustain economic prosperity. We extend Donaldson's *ingrained social cooperation* and *inculcated economic duties* to include *internalized aspirational morality*. Lastly in the cultural sector—a sector that Donaldson largely ignores—we emphasize the importance of cultural institutions, specifically civil society institutions, as the vital source of ethical values and focus on how these can be "crowded out" by markets and government. We propose a new ethical factor, *respect for civil society*. Figure 1 graphically depicts the conceptual logic of our extended framework.

		Ethical Wealth of Nations	
	Extractive Institutions • Ethically Regressive • Limited access	**Inclusive Institutions** • Ethically Progressive • Open access	**Typography of Ethical Values** Plain text: Donaldson's typography • *Bullets/italics: Extended typography*
Political Sector	Small centralized government operating without consent Social relationships organized along personal lines, special privileges, social hierarchies, laws enforced unequally, insecure property & contract rights	Large, decentralized democratic government operating with consent Social relationships governed by impartial forces, rule of law, secure property & contract rights	Fairer distribution of goods • *Fairer access to opportunities* Better government • *Better executed government*
Economic Sector	Closed, controlled markets Limited freedom to pursue economic opportunities Restricted movement of goods & services Social stagnation	Open, competitive markets Freedom to pursue economic opportunities Free movement of goods & services Social mobility	Ingrained social cooperation Inculcated economic duties • *Internalized aspirational morality*
Cultural Sector	Few non-state civil society organizations	Many vibrant civil society organizations	• *Respect for civil society*
Wealth of nations	Economic privation: • Slow growing, fragile economy in which wealth is concentrated in the hands of an elite few	Economic prosperity: • Fast growing, stable economy in which wealth is widely distributed with a large middle class	*Good society:* • *Prosperity, peace, freedom, equality, rights and justice flourish*

Figure 1: Extended institutional framework for the ethical wealth of nations.

In the final section of our paper, we discuss what our institutional perspective implies for Donaldson's conclusions about the necessity of moral education. Donaldson argues that getting citizens to see these ethical factors as having intrinsic value requires moral education, and so moral education is a requirement of economic prosperity. Our analysis of the tensions inherent in the various political, economic and cultural institutions highlights that these institutions are imperfect human constructions and the values they embody and support are always at risk and subject to displacement, attenuation and corruption (Selznick, 1992). Therefore, moral education, especially of business leaders, should not only generate the commitment to the intrinsic worth of values as Donaldson argues, but should also develop a sense of responsibility for promoting and protecting the ethical character of society's institutions.

AN INSTITUTIONAL FRAMEWORK FOR THE ETHICAL WEALTH OF NATIONS

Institutions are the basic building blocks of society and are intimately associated with the realization of values (DiMaggio & Powell, 1991; Selznick, 1992). Institutions take many forms including organized social structures (e.g., family, church, corporations, Congress) and social practices (e.g., weddings, religious rituals, corporate financial reporting, public elections) that together constitute the ways by which we organize ourselves for life in society (Searle 1995, 2005, 2010). They are made up of formal constraints (rules, laws, constitutions), informal constraints (roles, norms of behavior, conventions) and their incentive structures and enforcement characteristics

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(North, 1990). To say that some organization or social practice is an institution means, at a minimum, that there is an authoritative way of doing things to which people are expected to conform (Heclo, 2008). Institutions are thus normative structures and patterns that provide the "rules of the game" for coordinating the political, economic and social interactions of people in society (Bellah et al., 1991; North, 1990).

Research from institutional economics finds that institutions are the decisive factor in explaining the comparative wealth of nations, more decisive than natural forces like weather, geography, disease, or even culture (Robinson et al., 2005; Acemoglu & Robinson, 2012; North et al., 2009; Rodrik et al., 2004). Further, this research finds that it is not any one particular institution that explains the wealth of nations, but the combination of many different institutions spanning political, economic and cultural sectors of society. This combination creates a political economy characterized by a structure and pattern of institutional relationships that falls along a continuum from ethically regressive to progressive (Ferguson, 2013; North et al., 2009).

On the regressive end of the continuum is a political economy structured around extractive institutions that extract income and wealth from the broader society to the benefit of a narrow elite (Acemoglu & Robinson, 2012). Extractive institutions create what North et al. (2009: 12) call a "limited access pattern" characterized by: a small and centralized government operating without consent of the people; social relationships organized along personal or dynastic lines that treat people unequally, including social hierarchies, unequally enforced laws, and insecure property and contract rights; relatively few non-state civil society organizations; and a slow growing fragile economy in which wealth is highly concentrated. On the progressive end of the continuum is a political economy structured around inclusive institutions that encourage participation by many in economic activities of their choice that make productive use of their talents and whose benefits they are able to keep (Acemoglu & Robinson, 2012). Inclusive institutions promote what North et al. (2009: 11-12) call an "open access pattern" characterized by: a large but decentralized government operating with consent of the governed; social relationships governed by impartial forces that treat people equally, including the rule of law and secure property and contract rights; many vibrant civil society organizations; and a fast growing stable economy in which wealth is widely distributed.

Moreover, North et al. (2009) find that an inclusive open access society emerges from certain changes in political and economic institutions that go hand in hand and strengthen one another. In the political sector, these changes involve a move toward more democratic forms of government based on the rule of law, suffrage, separation of powers and political rights that ensure greater participation by citizens and more open and transparent decision making processes. In the economic sector, these changes involve a move toward a more free market-based economy based on secure property and contract rights, competition and freedom to create new businesses and pursue economic opportunities, social mobility, free movement of goods, and prohibitions on the use of force to obtain resources and goods or to coerce others.

But not only do changes toward democratic political and free market economic institutions tend to be mutually supporting, both emerge and depend on a diverse and vibrant base of civil society cultural institutions—e.g., marriage, family, religion, church, schools and the full range of private associations—that nurture the social relationships, ethical values and norms of civic life that underpin these changes (Bellah et al., 1991; Patterson, 1991, 2008). In Western societies, these cultural institutions are rooted in Judeo-Christian and classical Greek and Roman traditions that in the early modern era, provided the moral impetus for people to seek freedom from the oppression of feudal society, liberation from social inequality, and the gradual move toward democratic government and free market economies (Kirk, 2004; Novak, 1991).

This interlocking structure of inclusive democratic political, free market economic and civil society cultural institutions creates an institutional "moral ecology" that in turn, explains what economic historians call "the great divergence"—the growth in wealth, standard of living, health and longevity of western European nations and their colonies in the New World that occurred between 1500 and the late 1970s (Bellah et al., 1991; Ferguson, 2013). But this institutional moral ecology is not just instrumental to national economic prosperity. It also embodies ethical values that are constituent of what Bellah et al. (1991: 9)—building on the earlier work of John Dewey (1927) and Walter Lippmann (1937)—call "the good society" (see also Galbraith, 1996), which they characterize as:

> a widening of democratic participation and the accountability of institutions; an interdependent prosperity that counteracts predatory relations among individuals and groups and enables everyone to participate in the goods of society; a peaceful world. . . . Freedom must exist within and be guaranteed by institutions and must include the right to participate in the economic and political decisions that affect our lives . . . [And so includes] the great classic criteria of a good society—peace, prosperity, freedom, justice.

Based on these research insights, we extend Donaldson's "intrinsic values thesis" and propose what we refer to as our "institutionalized values thesis" which posits that if ethical values are to drive economic performance and contribute to the realization of a good society, they must not only rise to the level of being intrinsically valued by citizens as Donaldson argues, but they must also be fully embedded in, and supported by, the institutional fabric of society.

Restructuring Donaldson's typography of ethical factors

To align Donaldson's typography with this research and our institutionalized values thesis, we restructure his ethical factors by embedding them in a tripartite framework of political, economic and cultural institutions. Political institutions provide the democratic systems of governance that establish the legal and regulatory conditions for economic prosperity, and include Donaldson's ethical factors related to fairer distribution of goods and better government. Economic institutions, such as markets and corporations, are responsible for the production and distribution of the goods and services that create economic prosperity, and include Donaldson's ethical factors related to ingrained social cooperation and inculcated economic duties. Cultural institutions constitute the structures of civil society that govern social life and shape and articulate the civic relationships, values and norms that underpin both political and economic institutions. We propose one ethical factor important to this sector, respect for civil society.

A final insight from our review of the institutional economics and sociology research emphasizes the complexity and fragility of this institutional moral ecology that enables economic prosperity and constitutes the good society. As human constructions, these institutions are highly imperfect. They often fail to function effectively and the values they embody are often in conflict and at risk of displacement, attenuation and corruption from a variety of forces, both external and internal to the institutions themselves (Heclo, 2008; Selznick, 1992). Indeed, Ferguson (2013) argues that systemic institutional tensions and conflicts within Western societies are causing what he calls "the great degeneration" characterized by: political regression in the debilitating expansion of government combined with a lack of fiscal discipline and increasing public debt; economic regression in the erosion of the rule of law and the ability of certain business elites to exploit the economic system to their own advantage; and social regression in that for the majority of people income is stagnant and social mobility greatly diminished. In the following sections, we critically examine Donaldson's ethical factors and propose additional ethical values important to preserving and protecting this fragile institutional moral ecology. We begin with the political sector, followed by the economic sector and end with the cultural sector.

THE POLITICAL SECTOR

As Adam Smith taught, the wealth of nations is ultimately determined by their productivity, and free and competitive markets spur productivity. But markets are not perfect. They are prone to certain failures that reduce economic productivity and can also yield distributive outcomes that society deems inequitable. Government policies are often considered the proper correctives for these problems. However, government suffers its own imperfections and its attempts to remedy market failures and ameliorate economic inequalities often exacerbate them. In this section, we focus on how the values related to the fairness of political institutions can affect economic performance and social well-being. First we extend Donaldson's notion of *fairer distribution of goods* to include what we call a *fairer access to opportunity*. Then we complement Donaldson's notion of *better government* with *better executed government*.

Fairer distribution of goods: Fairer access to economic opportunity

Donaldson points out that "some data" and research by the World Bank suggest that increased distributional fairness is an ethical factor that enhances economic productivity. According to Donaldson, distributional fairness involves a reasonably equitable distribution of what Rawls (1971) called society's "primary goods"—income and wealth, healthcare, as well as basic rights and liberties such as property rights and economic freedom and opportunity. Large distributional inequities imply that a few people receive a disproportionate share of the economic rewards while a greater share of the population gets little or no reward. Under such circumstances,

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the economically disadvantaged find it difficult to develop their talents and skills and succeed in the market. Thus society develops less human capital and achieves less optimal economic development.

Democratic societies, which tend to value equality in all its forms, view such economic inequality as a kind of social injustice to be addressed by political institutions. However, government efforts to ensure the fair distribution of wealth can instead have negative implications for economic performance and important values related to economic freedom and independence. One way that government may seek to ensure a fair distribution of wealth, for example, is through progressive taxation. Yet, beyond certain levels, this can undermine incentives for business investment and entrepreneurial activity, which in turn can reduce employment and wealth creation (Zingales, 2012). Another way that government attempts to promote a fair distribution of wealth is through the provision of welfare benefits such as unemployment, food stamps, disability and various entitlement programs. However, these redistributive programs have an inherent "moral hazard" which incents economic dependence that can also undermine human capital development and economic productivity (Schuck, 2014: 145). Overall, when government wealth redistribution is pushed too far, it can have significant regressive effects that undermine productive economic activity and compromise important values related to economic freedom and independence.

Towards a fairer access to opportunity. This is not to suggest that distributional equality has no place in the political economy. It is to suggest, however, that government efforts to promote the value of a fairer distribution of economic rewards and benefits can become a cure that is worse than the disease, and so must be restrained by a countervailing value that avoids the adverse effects of government wealth redistribution. To preserve the incentives that underlie business investment, development of people's talent and skill, and productive economic activity, we propose what we call the value of *fairer access to opportunity*, which refers to economic opportunities and rewards that are widely available to all, and access to which is not determined by birth, political connections, economic or social class or status (Schuck, 2014; Zingales, 2012). Whereas government wealth redistribution can distort economic incentives and undermine economic freedom and self-development, fairer access to economic opportunities and rewards incentivizes individuals to take personal responsibility for their economic well-being and encourages self-reliance, which is integral to economic freedom and independence. This in turn promotes human capital development and greater economic productivity and prosperity.

Allowing institutions to embody fair access to economic opportunity implies that the resulting distribution of economic rewards may not be perfectly equal. Real differences in individuals' endowments of intelligence, talent, effort, aspiration, industry, etc., will inexorably differentiate people economically (Gregg, 2007). Yet in a market economy that values wide and nondiscriminatory access to economic opportunities, such distributional inequalities are not necessarily unfair. Indeed, given human diversity, no economic system can possibly achieve equal distributional outcomes. Some distributional inequality is therefore justified if, as we assume, a just society is one that balances distributional equity with fair access to opportunity. For fair access to opportunity is itself a moral value insofar as it is part of a conception of justice that prohibits discriminatory access to economic opportunities, and favors fair access to positions that are not only economically rewarding, but allow individuals to achieve economic self-reliance and independence that comes from developing and employing one's own endowments. To deprive individuals of fair access to these would be to deprive them of one of the main forms of human good (Rawls, 1971: 84).[1]

What does the value of fair access to opportunity imply for political institutions? We highlight two requirements that are widely recognized as essential. Foremost is formal equality before the law, which refers to laws that are applied without regard to the person(s) involved, especially with regard to property and contract rights (Gregg, 2007; North et al., 2009). Related to this is the absence of legally privileged or protected social classes based on race, religion or social status or preferential treatment given to any special interests. Equality before the law reflects the democratic moral animus against unfairly privileging any particular social class or special interest group. The law's impartiality can also promote greater economic freedom by enabling more people to take advantage of economic opportunities and rewards, and thereby also reducing extreme distributional inequalities.

A second requirement for fair access to opportunity is government policies that support the kind of educational system that enables more people to take advantage of the economic opportunities and rewards available to them. Education is widely recognized as the key to economic opportunity and prosperity, especially in the modern technology-driven economy. It also helps promote what Sandel (1998: 68) called "fair meritocracy" in which socio-economic disadvantages are mitigated by educational opportunities. Indeed, Piketty (2014) highlights education as a critical driver of economic growth and the most effective way to reduce inequalities of income and wealth.

Better government: Better executed government

Donaldson points out that some economists have claimed that democratic forms of government are not only better in that they promote political participation and transparency in political processes, but also in that they can correct market failures and promote the kind of economic freedom that is a catalyst for economic growth. However, democratic governments with their separation of powers and complex systems of checks and balances are notoriously inefficient and prone to imperfections that can render public policies ineffective. Indeed, a significant majority of studies of government performance highlight the ineffectiveness of public policies in correcting market failures (see Winston, 2006). In a recent comprehensive analysis of US federal government performance, Schuck (2014: 4) concludes that "*the federal government does in fact perform poorly in a vast range of domestic programs*" (italics in original).

Government policies that fail impose economic as well as social costs. Schuck (2014) highlights four major categories: (1) wasting scarce social resources; (2) suffering by those who depend on government programs for primary goods; (3) reducing future economic growth, especially through accumulation of public debt; and (4) compromising government's legitimacy through a loss of public trust

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and confidence. Moreover, these costs often exceed the costs of market failure. Winston (2006: 3-4) in his review notes: "Thirty years of empirical evidence on the efficacy of market failure policies . . . suggests that the welfare cost of government failure may be considerably greater than that of market failure." Bok (2001: 120-1) in his review concurs: "Again and again . . . , the operative legislation is burdened by unrealistic objectives, inadequate funding, clumsy implementing machinery, and poor targeting of funds. The costs in terms of waste, frustrated expectations, and harmful side effects are virtually incalculable."

The virtues of better executed government. Though democratic forms of government are better than say, authoritarian regimes, such chronic poor performance suggests that badly executed democratic government can create serious social and economic liabilities. As Alexander Hamilton said: "A feeble execution is but another phrase for a bad execution; and a government ill-executed, whatever it may be in theory, must be, in practice, a bad government" (cited in Light, 2008: 1). To become a social and economic asset and to realize the values intrinsic to democratic institutions, government—as the institutional designer, implementer and enforcer of public policies—must embody certain institutional virtues that enable it to close what we call the "execution gap"—the gap between the benefits of better government and the costs of government failure. Such virtues constitute what we classify as *better executed government*, an extension to Donaldson's notion of the values that make for *better government*.[2]

Schuck's (2014) analysis, which focuses on the U.S. federal government, found that the causes of government failure are many and systemic. However, he stresses that the legislative branch—Congress—is "the single greatest *institutional* source of government failure" (Schuck, 2014: 380, italics in original). He attributes this failure to what he calls the "dysfunctional aspects" of legislative policy-making (Schuck, 2014: 34). We highlight three institutional virtues important to Congress whose absence creates the dysfunctional aspects of legislative policy-making and prevents democratic government from closing the execution gap. These three are: restraint in policy-making, commitment to the public good, and discipline in fiscal spending.

First, closing the execution gap requires the exercise of political restraint in the economic policy-making agenda. A fundamental value of democracy is the idea that political authority cannot rightly dominate the full range of human life (Galston, 2009). A restrained government is not only instrumental to a productive economy, but also integral to preserving the values of economic freedom and independence (Galston, 2009). Yet, Wilson and DiIulio (2011: 467-8) identify a fundamental institutional change from what they call the "Old System" of government characterized by a small federal policy agenda in which checks and balances restrained legislators from starting new programs, to a "New System" characterized by a large and growing policy agenda in which the threshold for government expansion is markedly lower. This expansion of the legislative policy agenda is driven in part by external pressure from the public who demands that government "do more" to solve social and economic problems (Schuck, 2014), and by the proliferation of highly organized and well-funded special interest groups dedicated to active policy advocacy (Heclo, 2009).

Moreover, due to defective incentives internal to the institution (which we discuss below), legislators have responded to these expansionary pressures by giving in to them, thereby expanding the reach of the federal government so it has become increasingly interventionist over time (Schuck, 2014).

The lack of institutional policy restraint not only compromises the value of limited government and threatens the values of economic freedom and independence, but also contributes to government failure in several ways. First, it leads policy makers to intervene in markets when no real market failure exists. Winston (2006) found that legislators often exaggerated the extent of market failures and adopted corrective programs that created government failures of greater magnitude. Second, government expansion has a crowding out effect not only on market solutions, which can be more efficient and more conducive to an inclusive and open access economy, but also policy solutions by sub-national government bodies—e.g., states, counties, municipalities—which are often more efficient and vital to effective democratic governance (North et al., 2009; Schuck, 2014). Moreover, federal policy expansion has caused business to depend increasingly on lobbying and "rent-seeking" rather than on competing in the market, which is a major driver of crony capitalism (Zingales, 2012).

The expansion of government can lead it to intrude not only into the market but into all aspects of social life, such as education, health care, housing, transportation, urban development, environmental protection, human and civil rights, consumer affairs, gender relations, etc. (Heclo, 2009). Such an expansive policy agenda results in more comprehensive and complex policies that are difficult for administrative agencies to manage. Indeed, bureaucratic mismanagement—including muddled policy implementation (e.g., the initiation of the Affordable Care Act), debilitating rules and "red tape" (e.g., the accounting requirements of the Sarbanes-Oxley and Dodd-Frank Acts), poor policy enforcement and systemic fraud, waste and abuse (e.g., the Medicare reimbursement system)—is an endemic source of policy failure that imposes significant social and economic costs (Schuck, 2014). In addition, the moral hazard inherent in these programs contributes to the proliferation of what we call an "opportunistic dependence"—the tendency of people to "game the system" by taking undue advantage of free or low cost government benefits at the expense of productive economic activity. Opportunistic dependence helps explain, for example, why federal disability insurance has expanded sixfold since 1970 and tripled since 1990—and much of this involves young people (in their thirties and early forties) despite a much healthier working age population (see Eberstadt, 2012: 52-58).

The second institutional virtue critical to closing the execution gap is a strong commitment to the public good. Democratic government, for all its advantages, subjects legislators to incentives that can undermine this virtue. One set of such defective incentives involves election cycles. Congress is populated for the most part by career politicians who seek to maximize their chances of reelection and so have strong incentives to court the support of groups with money and resources necessary for their re-election campaigns (Wolf, 1979). This can lead to what political scientists call "client politics" where legislators adopt policies whose benefits target a narrow group but whose costs are borne by the broad public (Wilson, 1995).

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Reelection also creates powerful incentives for legislators to devise policies that benefit their constituents—i.e., "bring home the bacon"—to the neglect of more systemic, longer term issues that affect the broader public. Further, given voters' reluctance to pay for programs through higher taxes, legislators' incentive is to exaggerate benefits of such programs while hiding costs. Indeed, legislators use an array of cost-hiding techniques including: simply ignoring the costs or delaying or delegating cost decisions to executive agencies; disguising or concealing costs as off-budget programs or deferring costs with deficit financing; and using unfunded mandates and pork barrel projects to shift the costs to non-constituent or future taxpayers (Schuck, 2014). In short, defective institutional incentives related to election cycles cause legislators to yield to the short-term demands of narrow interest groups and neglect broader long-term problems and costs, resulting in policies that compromise the public good and increase federal spending and public debt (Schuck, 2014). Indeed, federal spending has grown fivefold since 1960 and tripled in just the last two decades, accounting for the highest share of gross domestic product since World War II (Ferguson, 2013; Schuck, 2014).

This leads to the third and arguably the institutional virtue that is the most important factor to closing the execution gap: fiscal discipline. The deleterious effects of fiscal profligacy are well known. We highlight that failure to avoid excessive spending and debt not only undermines efficient government functioning *now* by increasing interest payments needed to service the debt—public money that might otherwise be spent for more productive uses. But it also imposes an unjust economic burden on *future* generations, such as the massive unfunded entitlement liabilities, which represent a vast taxation and redistribution of wealth from future generations to the current generation (Ferguson, 2013).

In sum, external expansionary pressures and defective internal incentives combine to undermine three institutional virtues—policy restraint, commitment to the public good, and fiscal discipline—important to effective government policy making and closing the execution gap. The decline of these institutional virtues contributes to policies that compromise the value of limited government; crowd out markets, sub-national governments and civil society; redistribute wealth in ways that favor narrow short term special and localized interests at the expense of broader long term public good; incentivize economic dependence and undermine economic freedom; and contribute to unjust spending and debt. To this end, Heclo (2009) argues that the decline of these virtues represents a gross failure in the institutions of democratic government.

THE ECONOMIC SECTOR

At the heart of a market economy is competition. By offering products or services that fulfill a need or desire, businesses compete for customers and in turn, society's resources are developed and allocated towards productive uses to the benefit of society. However, competition in market economies is not perfect. Prisoner's dilemmas, commitment problems and other market imperfections can lead to opportunism and destructive forms of competition that undermine economic performance. Ethical values such as social cooperation and economic duties are often considered necessary correctives to such destructive economic activity. But ethical values often prove too weak to avoid these problems. In this section, we focus on how ethical values can affect destructive competition inherent to market economies. We extend Donaldson's *ingrained social cooperation* and *inculcated economic duties* to include an ethical factor foundational to these, which we call *internalized aspirational morality*.

Social cooperation, economic duties and market imperfections

Donaldson's "ingrained social cooperation" includes a disposition among market participants to cooperate with others by behaving in socially responsible ways. Relying on the work of Robert Frank (1996), he claims that such a disposition to "take ethics seriously" can avoid common forms of self-destructive market interactions and thereby, will increase economic productivity. Donaldson makes a similar argument for the value of inculcated economic duties, which can remedy imperfections inherent in market systems. Donaldson lists eight such duties including: the duties to avoid bribery, anti-competitive behaviors, nepotism and "crony capitalism" as well as duties to respect intellectual property and environmental integrity, provide accurate information to the market, and honor contracts, promises and other commitments. Donaldson claims that several economists have argued that failing to take these market-related duties seriously negatively affects economic performance.

Underlying Donaldson's analysis of the necessity of social cooperation and economic duties are neo-classical economic assumptions that attribute self-interest and competition to market participants and presume no preexisting cooperation among them. These assumptions create important theoretical and practical problems. Theoretically, they imply an inherent opposition between the self-interested competitive motivations assumed to operate in markets, and the ethical values of social cooperation and economic duties that are assumed to provide external moral restraints on these market motives. But as external restraints, ethical values are seen as costly to self-interest in the short run and as causing socially responsible individuals and firms to lose out to less scrupulous competitors in the long run (Quinn & Jones, 1995; Frank, 1996). Consequently they are weak and susceptible to displacement (Selznick, 1992).

The practical problem is that the ethical values Donaldson identifies have indeed been weakened and displaced in recent decades by the institutionalization of neo-classical economic assumptions in a new form of "investor capitalism" (Useem, 1996). Investor capitalism emerged in the 1980s in response to investor demands for market returns that had languished throughout the economic crisis of the 1970s. By the 1990s, it became the dominant institutional logic governing the way corporations were managed and is widely acknowledged to be an important cause of the corporate scandals that have since plagued the economy (Ordonez, Schwietzer, Galinsky, & Bazerman, 2009).

First, investor capitalism narrowed the purpose of the corporation to the singular goal of maximizing shareholder value and displaced other important corporate ends and stakeholder interests. Second, to align corporate executives' interests with that goal, it institutionalized a new system of stock option performance incentives that increased pressure on executives to produce short term results, e.g., achieving quarterly earnings targets, and decreased attention to the longer term investment purposes for which the corporation was designed. Third, the narrow focus on maximizing shareholder value and short term performance incentives combined with intense global competitive pressures distorted executives' risk preferences and encouraged riskier business strategies. And fourth, because riskier strategies are likelier to fail, executives tended to adopt unsound business practices—e.g., earnings management, financial engineering, and moving risks off balance sheets—that ultimately led many executives to violate ethical standards (Schwietzer, Ordonez, & Douma, 2004).

Ordonez et al. (2009) refer to this combination of effects—narrow focus on maximizing shareholder value, short term performance incentives, inappropriate strategic time horizons, and excessive risk taking culminating in unsound business practices and unethical behavior—as "goals gone wild." It is the practical effect of the distorted logic of investor capitalism organized around neo-classical economic assumptions about profit maximization as the singular purpose of business, self-interest as its primary motive force, and the primacy of competition as the spur to business success. As these assumptions became widely institutionalized in corporate governance, they altered the "rules of the game" for business such that ethical considerations were significantly weakened. Indeed, in some high profile corporate scandals such as Enron, they were rendered moot, as a recent speech by convicted former Enron CFO Andy Fastow illustrates:

> Accounting rules and regulations and securities laws and regulations are vague. They're complex . . . What I did at Enron and what we tended to do as a company [was] to view that complexity, that vagueness…not as a problem, but as an opportunity. [The only question was] do the rules allow it—or do the rules allow an interpretation that will allow it? . . . I knew it was wrong. . . . But I didn't think it was illegal. I thought: That's how the game is played. You have a complex set of rules, and the objective is to use the rules to your advantage. And that was the mistake I made. (Elkind, 2013).

Fastow's opportunistic understanding of "how the game is played" illustrates the kind of ethical drift that the logic of investor capitalism injected into the business world. It reveals how a great deal of destructive behavior in business originates from an institutional logic that renders ethical values extraneous to business. But the more insidious effect was how investor capitalism contributed to the emergence of what Hambrick (2005: 106) described as a "new breed" of top corporate executive. Not only was this new breed more obsessed than their predecessors with shareholder value, but Hambrick claims they were fundamentally different kinds of people—"more money-minded, self-interested, and emotionally detached from their companies as living, breathing institutions" (2005: 106). He notes that this obsession with shareholder value was due to the new rules of investor capitalism and executives' narrow and ethically detached qualities merely reflected the qualities that it encouraged and rewarded.

Towards an alternative institutional logic for capitalism

Ideas have consequences and ideas about capitalism institutionalized in the market not only establish the "rules of the game," but shape in significant ways the beliefs

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and behaviors of market participants, including their disposition to take ethics seriously. Investor capitalism institutionalized a narrow set of neo-classical economic ideas that proved to be socially and economically destructive, moving the corporation from an institution for long-term value-creating investment and sustainable economic growth for the benefit of many, to an instrument for extracting short term profits out of the economy for the benefit of a privileged few. The problem, however, is not that neo-classical economic assumptions are wrong: profit is a desirable and indeed essential outcome of business, self-interest is an important motive force of capitalism, and competition is vital to a healthy and productive economy. The problem is that these ideas alone do not constitute the whole of capitalism; and by themselves, they created a false institutional logic, what Ghoshal (2005: 82) described as an "ideology-based gloomy vision," that compromised the institutional foundations of capitalism and weakened the role of ethical values to curb its destructive tendencies.

What is needed to restore the institutional foundations of capitalism and strengthen the role of ethical values in the economy is a richer, more holistic and more compelling institutional logic: one in which ethical values are not externally superimposed upon business, but internally emergent from within business itself; one in which those values do not serve only as negative restraints on destructive economic activity, but serve as a positive catalyst for constructive economic activity; and one that does not just enforce a minimal morality of obligatory duties to ensure that the market system functions efficiently, but embraces an aspirational morality that inspires those excellences and virtues that contribute to the realization of the system's ideals and the flourishing of people individually and collectively within it (Fuller, 1969; Solomon, 1993). This is what we mean by *internalized aspirational morality* as an ethical factor necessary to restore the institutional foundations of capitalism and strengthen the role of ethical values in the economy. Such a morality if institutionalized would help promote and preserve business and the market system in general as an inclusive institution for long-term value-creating investment and sustainable economic growth for the benefit of many.

What would such an internalized aspirational morality for business look like? Though investor capitalism is the dominant logic of capitalism, it is not the only logic. In recent years, a countervailing logic has been institutionalized by many leading companies. It finds its most compelling expression in a movement championed by John Mackey, co-CEO of Whole Foods Market, called *conscious capitalism* (see Mackey & Sisodia, 2013). Conscious capitalism is not grounded in abstract economic theory, but in Mackey's personal experience in which he started out in the non-profit food co-op movement as an anti-business "progressive" and went on to become a business entrepreneur and "free market libertarian" (Mackey & Sisodia, 2013: 2, 11). One defining moment from Mackey's experience illustrates three insights important to our notion of aspirational moral logic for capitalism.

A turning point for Mackey occurred towards the end of Whole Foods' first year when a record flood nearly wiped out the nascent business. Destroyed were all the equipment and the inventory and with no warehouse inventory, no savings and no insurance, the business was financially bankrupt. To survive this disaster, the business needed help. Mackey describes how an "avalanche of support" poured in from a "volunteer army" of Whole Foods' stakeholders (Mackey & Sisodia, 2013: 6): employees worked for free to clean up the store, suppliers offered to resupply on credit, investors provided urgently needed capital, even customers and neighbors from the surrounding community pitched in to help clean up the store. All these stakeholders gave help in the form of time, labor, inventory and capital without any assurance that their investments in rebuilding the business would pay-off. This had a galvanizing effect and in less than a month after the flood, the store reopened and Whole Foods has since gone on to become an enormously successful corporation with over $11 billion in annual sales.

The successful rebuilding of Whole Foods after the flood raises a question central to our analysis: Why would a business "attract a volunteer army" of stakeholders to help it in its "hour of need" without any assurance that their efforts would pay-off? To derive our insights about an aspirational morality for business, we contrast neo-classical economic assumptions with Mackey's own answer to this question.

First, neo-classical economics assumes that maximizing profit is the singular purpose of business. But for Whole Foods profit was a means to serving what Mackey calls a "higher purpose" —the positive "difference you're trying to make in the world" (Mackey & Sisodia, 2013: 47). Whole Foods is dedicated to the higher purpose of bringing whole foods to people to help them to eat well, improve the quality of their lives, and increase their lifespan. This higher purpose was institutionalized in the business through what Mackey calls "core values": selling the highest-quality natural and organic products available, satisfying and delighting customers, supporting team member happiness and excellence, creating wealth through profits and growth, caring about communities and the environment, creating ongoing win-win partnerships with suppliers, and promoting the health of stakeholders through healthy eating education (Mackey & Sisodia, 2013: 43). This higher purpose and core values infused the business with a value beyond the instrumental requirement of making profits (Selznick, 1957). The more a business is "infused with value" in this way, the more it is valued for the higher purpose and values it serves which in turn, evokes a willingness to invest and sacrifice to support the business (Selznick, 1992).

Second, neo-classical economics reduces the motive force of capitalism to rational self-interest. But this does not seem to capture the stakeholders' motives at work re-building Whole Foods. Indeed, the stakeholders gave help not out of some rational self-interest calculation, but because they "passionately believed in what [Whole Foods] was doing"—its higher purpose and core values. Mackey calls this motive force the "power of love"—the capacity of stakeholders to form close relationships with the business, to sympathize and empathize, and to care and commit intensely (Mackey & Sisodia, 2013: 7). Adam Smith in his *Theory of Moral Sentiments* recognized the importance to capitalism of similar motivations, including sympathy, empathy, friendship, love and the desire for social approval. Gilder (1981) went so far as to propose that such altruistic motives rather than self-interest are indeed the "essence of capitalism."

Third, whereas neo-classical economics assumes competition among market participants (buyers and sellers) and presumes no pre-existing level of cooperation, the rebuilding of Whole Foods points in the opposite direction: a community of stakeholders with a pre-existing shared commitment to the purpose and values embodied by Whole Foods and the absence of competition among them. Indeed, rebuilding the business required the investors, employees, suppliers, even customers and members of the community to cooperate towards that end. Stakeholders' commitment and loyalty in rebuilding the business in turn, inspired a reciprocal commitment and loyalty from Mackey: "These [stakeholders] love us so much and they have given us so much that we owe it to them to do everything possible to reopen and to serve them as well as humanly possible" (Mackey & Sisodia, 2013: 6). Mackey's sentiment is not an impersonal kind of abstract obligation to "support the system," but a more personal kind of duty emergent from a deeply felt moral debt owed his stakeholders. Moreover, this mutual spirit of cooperation was not imposed as an external restraint to avoid commitment problems, but emerged spontaneously from a shared value-laden attachment and loyalty to Whole Foods.

Suggestive in our analysis of Whole Foods is an aspirational morality that points toward the possibility of an institutional logic for business that contrasts sharply with neo-classical economic assumptions of investor capitalism. In this aspirational morality, the central unifying purpose of business is not narrowed to maximizing profit, but profit is understood as a necessary and beneficial means by which the business can fulfill a socially valued higher purpose. The dominant motive force is not limited to rational self-interest, but includes a full range of moral, even altruistic motivations. And the backbone of business success is not reduced to zero-sum competition among market participants, but mutually beneficial cooperation among a community of stakeholders. This kind of aspirational morality is gaining traction in the economy and can be found in several other companies, including, for example, Apple, Federal Express, Patagonia, Starbucks, Google and Genentech. These companies have institutionalized moral ideas similar to Whole Foods that involve a commitment to a higher purpose that inspires stakeholder commitment and cooperation.

In sum, the point of our analysis is not to falsely idealize business and capitalism, but to suggest an alternative to the institutional logic of investor capitalism that better integrates and strengthens the role of ethical values important to economic prosperity and a good society. One in which business is not reduced to an economic instrument for shareholders to maximize profit, but is a social institution for a community of stakeholders to realize intrinsically valued purposes; and one in which business as an institution has social and moral legitimacy not because it somehow transmutes base self-interest through competition into economic prosperity, but because it catalyzes noble moral qualities through social cooperation into a higher and more inclusive economic prosperity and human flourishing. In short, it is an institutional logic that can, not only, "deliver the goods" instrumental to economic prosperity, but also "deliver the Good" intrinsic to a good society.

THE CULTURAL SECTOR

Both democratic government and free markets institutions are grounded in the same set of cultural values and institutions (Patterson, 1991, 2008). However, democratic government and free markets have an ironic flaw—if not an Achilles heel—in that the more they flourish, the more they tend to crowd out the cultural values and institutions on which they depend (Novak, 1991). This self-destructive tendency has already been suggested in our analysis of government failure in the political sector and corporate corruption in the economic sector. In this section, we discuss how the cultural values and institutions on which economic prosperity and the good society depend, can also be crowded out by markets and government. We introduce an ethical factor—*respect for civil society*—that is a cultural value that is not only important to economic prosperity and a good society, but is also a check against socially and economically destructive expansion of the market and government.

Respect for civil society

Civil society refers to the diverse array of private relationships, associations and institutions established to serve some valued social purpose or solve some social problem for reasons other than profit (Ferguson, 2013). It includes marriage and family, church and school, and the full range of voluntary private charities and other non-government associations. Such civil society institutions provide the environment in which the social relationships, moral values and norms of civic life are nurtured—what researchers term "social capital" (North et al., 2009: 7). The social capital that participation in civil society generates in turn nourishes and supports the market and government institutions vital to a flourishing economy. Fukuyama, for example, emphasizes the centrality of social capital to the development of economic and political institutions (1995: 356-7): "A healthy capitalist economy is one in which there will be sufficient social capital in the underlying society to permit business, corporations, networks, and the like to be self-organizing. . . . The same propensity for spontaneous sociability that is key to building durable businesses is also indispensable for putting together effective political organizations." Similarly, Knack and Keefer (1997: 1252) found in their empirical study of the economic effects of social capital in 29 market economies, that "trust and civic cooperation are associated with stronger economic performance." A flourishing civil society, then, that generates high levels of social capital, will in turn promote a more productive economy.

A civil society that is flourishing affords citizens the social space to associate and manage their social relationships and problems as they choose. On the other hand, in an "uncivil society," political or economic forces encroach on this social space, crowding out civil society and the relationships, moral values and civic norms it nourishes (Ferguson, 2013). Civil society can flourish only if its domain is respected as one into which governments and markets should not encroach. This is what we mean by *respect for civil society*. Respect for civil society implies that the domain of civil society is not allowed to become the province of markets or government.

In recent decades, the vitality of civil society in the United States has diminished. Putnam (2000), for example, documented a marked erosion of civic engagement since the 1960s, including high double-digit percent declines in attendance at public meetings or town or school affairs, service on a committee for a local organization or as an officer of a club or organization, membership in national chapter-based

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associations, and membership in parent-teacher associations. Concurrent with the erosion of civic engagement is the expansion of government and markets into the domain of civil society (Sandel, 2012; Schuck, 2014). This is not coincidental but reflects a twofold market and government crowding out of civil society. We briefly analyze the effects of this twofold crowding out on the values of civil society and its implications for economic prosperity and a good society.

Market crowding out. In recent decades, markets and market incentives have increasingly been used to deal with issues once reserved for civil society. Sandel (2012: 3-5) in his analysis of the moral limits of markets illustrates. He highlights, for example, some "things money can buy" including a prison cell upgrade, the services of an Indian surrogate mother to carry a pregnancy, the right to immigrate to the United States, and admission of your child to a prestigious university. He also highlights some controversial "ways to make money" including fighting in Somalia or Afghanistan for a private military company, standing in line overnight on Capitol Hill to hold a place for a lobbyist who wants to attend a congressional hearing, and buying the life insurance policy of an ailing or elderly person, paying the annual premiums while the person is alive, and then collecting the death benefit when he or she dies. Sandel's concern is not the usual complaint about the corrupting effects of greed, but a broader and deeper concern about the remaking of social relations into market relations. He claims that we have drifted "from *having* a market economy to *being* a market society" (Sandel, 2012: 10; italics in original). He raises several moral concerns about the expansion of the market into the domain of civil society. We focus on his concern that certain social goods are degraded by their commercialization.

Standard economic analysis assumes that commercializing an activity does not change it (Radin, 2001). If a previously untraded good is made tradable, no harm is done. On the contrary, benefit is generated. However, following Hirsch (1976), Sandel (2012: 120-1) argues that the introduction of market incentives for certain social goods can result in "commercialization effects" that change people's attitudes and crowd out civic values (see also Costa-Font, Jofre-Bonet & Yen, 2013; Radin, 2001; Titmuss, 1970). For example, slavery commercialized human beings by treating them as commodities to be bought and sold. Such treatment fails to value human beings appropriately—treating them as instruments of gain and objects of use and utility rather than as persons with inalienable rights and inherently worthy of dignity and respect.

When social goods are bought and sold, it implies that it is appropriate to treat them as commodities—instruments of profit and use. Sandel argues that some social goods are not properly valued in this way because it corrupts them; they cease to be social goods exchanged on the basis of civic relationships, and become economic commodities exchanged in the market. This suggests that in a civil society there are certain goods that money should not be allowed to buy because they embody civic values and norms important to civil society that can be crowded out by market values and norms. This objection challenges the expansion of markets and market incentives into many aspects of social life, including motivating performance in education, healthcare, voluntary associations, civic life, and other settings in which moral commitments to civic values matter. To the extent that economic performance depends on social capital—the values and social relationships that civil society nourishes, it is indeed diminished, then, by the expansion of markets into the domain of civil society.

Government crowding out. We noted earlier how the expansionary dynamics of government have led it to intrude into all aspects of social life. Here we will only note the damaging effect this intrusion has had on civil society. Fundamental to civil society, especially as it emerged in America, is a civic character defined by a spirit of civic cooperation. This social trait provided the moral impulse that shaped our approach to civil society (Novak, 1991). Tocqueville, for example, in his visit to America in the 1830s, observed:

> If a stoppage occurs in a thoroughfare and the circulation of vehicles is hindered, the neighbors immediately form themselves into a deliberative body; and this extemporaneous assembly gives rise to an executive power which remedies the inconvenience before anybody has thought of recurring to a pre-existing authority superior to that of the persons immediately concerned. . . . In the United States associations are established to promote public safety, commerce, industry, morality, and religion. There is no end which the human will despairs of attaining through the combined power of individuals united into a society (1994: 191-2).

Important is Tocqueville's observation that when faced with life's difficulties, the moral impulse of Americans was not to look for help to "a pre-existing authority," i.e., government. On the contrary, it was first to cooperate with one's fellow citizens to solve the problem themselves. This spirit of civic cooperation that takes personal responsibility for solving social problems underlies the development of the associations and relationships of civil society and is precisely what government expansion into the domain of civil society has crowded out.

Civil society depends on civic cooperation fueled by a strong sense of public spiritedness and the willingness of citizens to exercise their civic duties. But this traditional emphasis on civic duty has given way in recent decades to rights-based activism aimed at compelling government to solve social problems. Indeed Finkel and Moghaddam (2005: 4) note that the clarion by which a multitude of groups have tried to get government to effect social change is "rights"—human rights, civil rights, Black rights, women's rights, gay rights, children's rights, employee rights, the rights of the mentally ill, disabled persons rights, patients' rights, and even animal rights. The cultural hegemony of rights over duties contributes to what Kagan (2003) calls an "adversarial legalism" in dealing with social problems that undermines civic cooperation.

First, the two cultural impulses are fundamentally different: civic duty affirms the public order over the freedom of individuals; rights affirm the freedom of the individual (or group) against the social system. Second, the very concept of a right has an inviolable quality that permits little compromise and makes social problems harder to resolve. Third, the adversarial impulse redirects civil society energies to using lawsuits and advocacy politics to force government to solve social problems through regulatory coercion or judicial fiat (Fukuyama, 2013). This results in the

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government expansion into the domain of civil society. Indeed, Rauch (1998: 2153) notes that "Never before has the government concerned itself so minutely with the detailed interactions of daily life."

But the most significant cost of such rights-driven adversarial legalism is the weakening of civic bonds. People come to see themselves more individualistically and atomistically—less morally bound to work with their fellow citizens for the benefit of the "commonwealth." People may feel linked with select others in certain causes, such as an ethnic minority community or environmentalism, but these do not represent the holistic sense of community. Taylor (1991: 112) called this a "fragmentation of society" in which people become less capable of forming a common purpose and carrying it out, which is the essence of the civic cooperation at the heart of civil society. Rights-based political activism has thus induced government expansion into the domain of civil society, weakening the bonds of civic cooperation. And just as the intrusion of markets into the domain of civil society can affect economic performance, so too can the intrusion of government damage the social capital that a prosperous economy and good society requires.

DISCUSSION AND IMPLICATIONS

Our main contribution to Donaldson's notion of an ethical wealth of nations is identifying the critical role of institutions in the relation between ethical values and economic prosperity. Drawing on research from institutional economics and sociology, we developed a tripartite institutional framework that embedded an expanded set of ethical values in an interlocking set of democratic, free market and civil society institutions spanning three sectors of society—political, economic and cultural respectively. Our analysis underscored that this institutional moral ecology not only plays an instrumental role in mediating the relationship between ethical values and economic prosperity, but also plays a constituent role in embodying the ethical values intrinsic to a "good society." Based on these insights, we extended Donaldson's intrinsic values thesis by proposing what we called our institutionalized values thesis which claims that, if ethical values are to drive economic performance and contribute to the realization of a good society, they must not only rise to the level of having intrinsic value by citizens as Donaldson argues, but they must also be fully embedded and supported as intrinsically valued parts of the institutional fabric of society. So although Donaldson's intrinsic values thesis is an important and powerful insight, we see it as a *necessary* though not a *sufficient* condition for explaining the relationship between ethical values and economic prosperity. In short, Donaldson's intrinsic values thesis, which we accept, is incomplete. Our institutionalized values thesis provides a critical institutional dimension missing from his notion of an ethical wealth of nations.

We conclude by discussing what our institutional perspective implies for Donaldson's conclusions about the necessity of moral education. Donaldson argues that since prosperous economies depend on the collective morality of their participants, moral education is necessary to generate an independent (i.e., intrinsic) commitment to the worth of ethical values (Donaldson, 2001: 34). Without such independent commitment, Donaldson argues that people easily fall prey to rational self-interest calculations. Indeed, our analysis of the failure of Congressional legislators in the political sector and corporate executives in the economic sector, suggests that if these individuals had taken ethical values more seriously—that is, had they ascribed intrinsic worth to ethical values—then much of the government failure and corporate corruption we highlighted could perhaps have been avoided.

However, our institutional perspective also suggests that the failure of the Congressional legislators and corporate executives was not just a problem of their not ascribing intrinsic worth to ethical values, but also a problem of their not ascribing appropriate worth to the institutions that embody those values. That is, it was a problem of their not just failing to *take ethics seriously*, but also their failing to *take institutions seriously* as the essential vehicles for realizing purposes and values important to economic prosperity and a good society. From our institutional perspective, prosperous economies and good societies depend on more than the collective morality of their citizens, and as Donaldson argues, they also depend on the moral ecology of their institutions. Yet, as our analysis of the tensions pervasive in political, economic and cultural sectors revealed, this institutional moral ecology is complex and fragile and is not created or sustained by an "invisible hand." On the contrary, the institutions that establish this moral ecology are imperfect human constructions and so the values and purposes they embody and serve must be preserved and protected from displacement, attenuation and corruption from a variety of forces internal and external to the institutions themselves. This is a critical function of leaders in institutionally responsible positions (Selznick, 1957), such as the Congressional legislators and corporate executives we analyzed.

In contrast to conventional notions of organizational leadership that focus on a leader's instrumental effectiveness in motivating followers and achieving organizational goals, institutional leadership focuses on a leader's role in taking personal responsibility for the integrity and well-being of the institution as a "whole"—serving as the trustee and steward of the values and purposes the institution was designed to serve (Selznick, 1957). But it was precisely this sort of "institutional mindset" that Congressional legislators and corporate executives lacked. Instead, they possessed a kind of "instrumental mindset" that reduced the institutions in which they operated to mere technical instruments for achieving personal and organizational goals. The problem is that personal and organizational goals often do not serve the larger values and purposes of the institution (Selznick, 1957). Indeed, corporate executives' focus on the narrow organizational goal of maximizing shareholder value, especially in the short run, proved destructive to the corporation as an inclusive institution for long-term value creation for the benefit of many. Similarly, Congressional legislators' focus on the narrow personal goal of getting re-elected contributed to the dysfunctional aspects of legislative policy-making that rendered Congress a primary institutional source of government failure.

Combine this instrumental mindset with Donaldson's concerns about weak independent commitment to ethical values and strong tendency for self-interested calculation and it is a short step to leaders' abandoning their responsibilities as trustees and stewards of institutional values and purposes and engaging in opportunistic behavior. Indeed, Mitchell and Scott (1987: 449-450) in summarizing research examining how both public and private mangers view the responsibilities of their work, conclude: "the evidence suggests that public and private administrators as a class appear to care little about their obligations to be trustworthy stewards." And insofar as external demands from investors or special interests, internal performance pressures or dysfunctional incentives, or other short-run imperatives dominated the decision-making of corporate executives and Congressional legislators, the values and purposes of their respective institutions were vulnerable and dissolved easily in the face of such pressures (Selznick, 1992). The prevalence of such leadership failures has caused some to argue that the institutional crisis many Western societies are facing is at bottom, a crisis of leadership (Burns, 1978; Kellerman, 2012). Heclo (2008: 25-6) argues this point forcefully:

> Institutional failure and the distrust it engenders is the result of leaders continually failing to live up to legitimate expectations attached to their positions of responsibility. . . . When institutions become venues for expressing – and even facilitating – greed, lust, cowardice, and selfishness, . . . we are seeing something debauched. [Ultimately] the performance we care about is not simply a matter of leaders failing to "deliver the goods." In a larger sense, it is a matter of their failing to deliver the Good that was rightly expected of someone in an institutionally responsible position (Heclo, 2008: 32).

Given this institutional perspective, the kind of moral education we highlight must not only generate an independent commitment to ethical values as Donaldson argues, but it must also develop an independent commitment to promoting and protecting the ethical character of society's institutions. That is, it must develop, especially in leaders, what we described above as an "institutional mindset" as a moral counterforce to the prevailing and destructive "instrumental mindset." For business leaders specifically, this requires a fundamental restructuring of university-based business education.

Business schools, especially at the graduate level, were originally based on the model of professional education established for law and medicine (Khurana, 2007). This model involves three interrelated dimensions (Sullivan, 2005): an *intellectual dimension* that imparts a robust foundation of theoretical knowledge, usually with a strong scientific orientation; a *practical dimension* that trains the technical and practical skills necessary for expert practice; and a *moral dimension* that develops the requisite sense of responsibility and care for the purposes of the profession and the public good and welfare of those served by the profession. This moral dimension is central to the institutional mindset required of business leaders.

The institutional mindset emerges from a sense of professional identity and responsibility shaped by an understanding of business as more than an economic profit maximizing instrument, but as a social institution operating within a larger institutional moral ecology. This broad awareness is important to dealing with the moral complexities inherent in the political economy in which business is embedded, especially in an advanced, technology-driven global business environment. Business leaders need a moral horizon that includes, for example, a broad outlook on history, politics, economics, culture, religion and even literature, in order to think incisively about their own situation and that of business in relation to its defining institutional purposes. This broad perspective is traditionally the domain of the liberal arts (Donaldson & Freeman, 1994). The aim of a classic liberal arts education is to develop students' minds and character for a broad understanding of the world in order to take a responsible part in it (Donaldson & Freeman, 1994; Sullivan, 2005).

Classic liberal arts education was central to the original vision of university-based business education (Khurana, 2007). Such liberal learning was thought necessary because neither scientific knowledge nor practical skills provided an adequate understanding of business's role as an institution in society. This stress on liberal education recognized that business leaders were "trustees" of society's economic resources and so required that they be educated to "administer this trust" by not only being proficient in the techniques of business, but also by possessing a professional identity and character worthy of the responsibility (Khurana, 2007). This stress on liberal learning emerged from a larger set of concerns about the social significance of business in a society reeling in the early decades of the 20th century from the effects of rapid scientific, technological and material change. The fear was that modern industrial civilization might be outstripping society's capacity for moral self-governance and lacked the leadership needed to deal with the emerging problems. Such a sentiment was expressed by Wallace B. Donham, Dean of Harvard Business School in the 1920s:

> On all sides, complicated social, political, and international questions press for solution, while the leaders who are competent to solve these problems are strangely missing. These conditions are transforming the world simultaneously for better and for worse. They compel a complete reappraisal of the significance of business in the scheme of things. (cited in Khurana, 2007: 116).

The concerns that motivated the original vision of professional business education echo the challenges we face today and underscore the importance of the kind of moral education business leaders require: classic liberal learning aimed at shaping a professional identity and character that is responsible to the purposes and values served by business as an institution in society. Yet it is precisely this moral dimension of professional education that business schools largely abandoned over the course of their evolution (Khurana, 2007; Sullivan, 2005). Indeed, internal academic disciplinary pressures have biased business education towards the first dimension, stressing scientific and theoretical knowledge; and external market pressures have biased business education towards the second dimension, stressing technical and practical skills (Khurana, 2007). This imbalance reduces business education to imparting knowledge and skills instrumental to business success but neglects developing the requisite professional identity and institutional mindset that, we argue, must be integral to the aims of a business education. In short, business education requires a fundamental rebalancing to restore appropriate focus on developing leaders with a

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sense of responsibility for promoting and protecting the ethical character of business as an institution in society.

CONCLUSION

In the twentieth anniversary issue of Business Ethics Quarterly, Donaldson (2010: 728) argued that we are undergoing a "deep transformation in the logic of modern capitalism," an evolving shift in the values—the "tectonic plates"—of democratic capitalism. The first stage, according to Donaldson, involved the law, e.g., child labor laws, labeling and safety standards, and environmental requirements. The second, and he argues the more difficult stage ongoing today, is the transformation of private attitudes, mores, practices, and institutions. Our extension of his "Ethical Wealth of Nations" can inform our understanding of the ethical dynamics important to this second stage. Our analysis makes three fundamental claims. First, institutions are intimately associated with the realization of values and play a critical mediating and constituent role in the relation between ethical values and national economic prosperity and a good society. Second, if ethical values are to drive economic performance and contribute to the realization of a good society, they must not only rise to the level of having intrinsic value by citizens, but they must also be fully embedded and supported as an intrinsic part of the institutional fabric of society. Third, if moral education is going to be beneficial for the development of future business leaders, then it must not only generate a commitment to the intrinsic worth of values, but must also develop professionals with a sense of responsibility for promoting and protecting the ethical character of business as an institution in society.

NOTES

1. Note that Rawls distinguishes two kinds of "equality of opportunity," namely: "formal equality of opportunity" or "careers open to talents," and "substantive equality of opportunity." As our discussion here and later indicates, we are referring to substantive equality of opportunity, not formal equality of opportunity. See Rawls, pp. 65-75.
2. Attributing virtues and vices to institutions does not imply that they are moral agents of some sort. It is merely to say that the rules, roles, relationships, and practices that constitute the institution, are such that when people act in accordance with those rules, roles, relationships and practices, as well as the incentives these provide, they engage in behaviors that can be characterized as virtuous or vicious. As we explain in detail below, the rules, roles, relationships, practices, and incentives of our government institutions lead to behaviors that can be described as lacking in policy restraint, lacking commitment to the public good, and fiscal intemperance. It is important to note that it is not deficiencies in the individual members of government institutions that we are pointing toward with these terms, but deficiencies in the rules, roles, etc., that structure and shape the behaviors of the members of these institutions.

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