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Fiduciary Principles: Corporate Responsibilities to Stakeholders

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INTRODUCTION

The lack of trust in American corporations and in corporate management over the recent scandals and financial crisis has increased public and legislative outcry for accountability in business decisions. Frustration is rampant, with “seemingly unending examples of mismanagement, ethical misconduct, and patterned dishonesty of a society dubbed ‘the cheating culture’.”¹ International competition created tremendous risks and rewards but forced companies to attract investors through creative accounting practices to raise share value. As a result, three decades of corporate greed, inappropriate financial risk-taking and personal misconduct eroded trust in corporate decision-making.²

Corporate governance reform initiatives beginning in 2002 were designed to increase financial disclosure and responsibility; however, such legislation is insufficient to rebuild public trust in business. Restoring trust requires that those individuals who manage corporations, i.e., the board of directors and senior officers, comply with requirements for greater accountability and transparency, and abide by the legal norms to which boards of directors and management are already subject, as directors and officers are legally bound as fiduciaries owing duties of care and loyalty to the corporation.³ However, centuries of legal and religious formalization and codification have diminished the actual meaning and purpose of fiduciaries, with the result that modern corporate fiduciaries have limited responsibility toward stakeholders and the greater society. Restoring the original definitions and roles of fiduciaries may legitimize and guide the corporation in developing new relationships with stakeholders.

This paper does not focus on illegal conduct by corporate individuals, although many criminal violations of fiduciary norms involve intentional assessment of the risk of penalties versus potential profits.⁴ Rather, the paper examines the limitations of today’s corporate fiduciary duties given the original intent of the fiduciary relationship. In particular, we examine the definitions of fiduciaries and fiduciary responsibilities to determine the extent to which formalization and codification have led to avoidance of corporate responsibility. We then revisit the historical and religious origins of fiduciaries in commercial transactions that defined and shaped the integration of moral and ethical duties in

¹ See David Callahan, The Cheating Culture: Why More Americans are Doing Wrong to Get Ahead (Florida: Harcourt, Inc., 2004), 12.
business today yet were so narrowly defined that corporate liability became increasingly limited. We propose a modest but well-defined, consistent and universal definition of “fiduciary duties,” that could offer corporate managers guidance in developing new approaches to stakeholder relationships – relationships built on expectations of corporate trust and decision-making that maximize shareholder wealth while protecting stakeholders.

**The Modern Fiduciary**

Most business students and executives today are introduced to the concept of a “fiduciary” in the context of agency law, where a fiduciary is defined as “one who has a duty to act primarily for another person’s benefit,” and agency is generally defined as “the fiduciary relation that results from the manifestation of consent by one person (a ‘principal’) to another (an ‘agent’) that the agent shall act on the principal’s behalf and subject to the principal’s control, and the agent manifests or otherwise consents so to act.”

Restatement (Third) of Agency states that proof of an agency relationship requires the existence of the manifestation by the principal that the agent shall act for him; the agent’s acceptance of the undertaking; and, the understanding that the principal is in control of the undertaking. The agency relationship that results is founded on trust, confidence, and good faith by one person in the integrity and fidelity of another, creating certain duties owed by each party established in the agency agreement and implied by law.

Within the relationship, fiduciaries have a duty of loyalty – the duty to act primarily for another in matters related to the activity and not for the fiduciary's own personal interest. Fiduciaries also have a duty of good faith – the duty to act with scrupulous good faith and candor; complete fairness, without influencing or taking advantage of the client. The fiduciary relationship, as defined by history and case law, exists in every business transaction. Moreover, the relationship is defined by the specific role or function of the agent toward the principal, i.e., the relationship of corporate management and boards of directors to shareholders, lawyer to client, or broker to client, and governed by the laws associated with those transactions, including criminal and labor law, securities and corporate law, contracts, partnerships, and trusts.

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5 Restatement (Third) of Agency, 3rd Ed. §1(1). (2006), Restatement Third of Agency is a set of principles issues by the American Law Institute, frequently cited by judges as well as attorneys and scholars in making legal arguments.


Partners, corporate boards of directors, and corporate officers held fiduciary duties originating with the formation of modern partnerships and corporations, as did majority shareholders, while union leaders held fiduciary roles only when unions were granted power by statute to represent workers in negotiations with management. While modern definitions of these duties remain intact, the scope of the duties greatly varies based on the fiduciary’s role, which increases the complexity of analysis required to understand violations of those duties.

The modern definition of “agent” as a fiduciary was first rationalized and clarified as a legal doctrine in 1933:

“When the person acting is to represent the other in contractual negotiations, bargainings or transactions involved in business dealings with third persons, or is to appear for or represent the other in hearings or proceedings in which he may be interested, he is termed an ‘agent,’ and the person for whom he is to act is termed the ‘principal.’” The element of continuous subjection to the will of the principal distinguishes the agent from other fiduciaries and the agency agreement from other agreements. This implies that corporate officers and directors are also agents. However, in law and practice today, the fiduciary roles of corporate officers and directors are not “continuous subjection to the will of the principal (shareholders)” but more flexible as officers and directors make many decisions not approved by shareholders.

Further, the duties of officers and directors are distinct from those of other corporate employees. Corporate officers and directors owe fiduciary duties to shareholders (as defined by state case law and Delaware corporate law) while employees as agents owe duties to employers, suppliers, vendors, or customers in a wide variety of relationships involving trust. This distinction has created a two-tiered definition of fiduciaries, each with different duties, and varying liabilities for breaches of those duties, and is supported by economic theory. Such differentiation in fiduciary roles does not appear to be the intention, either historically or in modern corporate law. In 1928, Judge Benjamin Cardozo, then Chief Judge of the New York Court of Appeals, eloquently recognized the significance and sanctity of fiduciary principles in Meinhard v. Salmon.

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10 Deborah A. DeMott, “The First Restatement of Agency: What Was the Agenda?,” 32 S. Ill. U. L.J., (2007). Restatement (Second) of Agency, 1958, the American Law Institute, is now out of print and has been completely superseded and replaced by Restatement of the Law Third, Agency, 2006. However, some courts will continue to cite to The Restatement of the Law Second, Agency.
[J]oint adventurers, like copartners, owe to one another…the duty of the finest loyalty… and the level of conduct for fiduciaries has been kept at a higher level than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.

Cardozo’s opinion reflects three important principles that reinforce a long line of precedent in defining a *special level of fidelity for all fiduciaries*: 1) fiduciary matters demand a higher standard than normal marketplace transactions; 2) exceptions to the fiduciary standard undermine the duty of loyalty; and 3) neither courts nor regulators who interpret, enforce or modify the fiduciary standard should consciously weaken it. Supreme Court Justice Brandeis later noted that a fiduciary "is an occupation which is pursued largely for others and not merely for oneself… in which the amount of financial return is not the accepted measure of success." 15

*Fiduciary Duties: The Required Triad*

The Delaware Supreme Court, renowned for its corporate governance decisions and the source of the primary legal standards for the duties and liabilities of corporate officers, ruled in 1993, re-affirmed in 2006, and again in 2010, that the “triad” of duties includes the duty of loyalty, due care and good faith, where “good faith” and “full and fair disclosure” are considered to be the essential elements of, or prerequisites for proper conduct, by a director. 16 Violation of the duty of good faith could remove directors’ protections from liability. The Delaware Court also ruled that corporate officers owe the same fiduciary duties as corporate directors, noting that it is not possible to discharge properly either the duty of care or the duty of loyalty without acting in good faith with respect to the interests of the companies’ constituents. 17 Major legislation such as The Sarbanes-Oxley Act of 2002 18, or The Dodd–Frank Act 19 of 2010 support these legal

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15 See Kenneth M. Rosen, “*Meador Lecture Series 2005-2006: Fiduciaries.*”
18 Sarbanes-Oxley Act of 2002, PL 107-204, 116 Stat 745. Sarbanes-Oxley requires corporate officers to be responsible for earnings reports, prohibits accounting firms from acting as consultants to accounting clients (a conflict of interest) and increases penalties for fraud.
standards and require that directors and their corporations return to these fundamental principles to which they were formally subject already: individual integrity and responsibility in corporate governance; and, accountable and transparent disclosure of important financial and other information on which investors and the stability of the capital markets depend.\textsuperscript{20}

The Court has long held that the board of directors is ultimately responsible for the management of the corporation,\textsuperscript{21} although boards often delegate major decisions to corporate officers with more expertise and information on a particular subject. Under Delaware corporate law, officers are granted titles and duties through the corporation’s bylaws or the board’s resolutions and employees who are not granted this power are deemed agents.\textsuperscript{22} Additionally, Delaware law dictates that the terms “officers” or “agents” are by no means interchangeable: officers are the corporation, but an agent is an employee and does not have the equivalent status of an officer.\textsuperscript{23} Agents’ specific duties include loyalty, performance, obedience, notification, and accounting.

Again, we see this distinction between officers as managers of the corporation and agents as employees as contrary to the historical and case law definitions espoused by two leading Chief Justices. It is noteworthy that agents as employees (and fiduciaries) are not required to act in a manner that ensures that organizational activities are conducted in good faith and with care for stakeholder’s interests. Also noteworthy is the omission in corporate law of the duty of obedience (to obey the law), which appeared to occupy a recognized place in corporations through 1946 but eventually was eliminated. As recent courts have made clear that corporate actors cannot consciously violate, or permit the corporation to violate, corporate and non-corporate norms, even when it may be profitable for the corporation, this duty may be resurfacing.\textsuperscript{24} The recent \textit{Disney} decision specifically defines the current required triad of fiduciary duties.\textsuperscript{25}

\begin{footnotesize}
\begin{enumerate}
\item Kilpatrick Stockton LLP, \textit{Directors Fiduciary Duties After Sarbanes-Oxley} (Atlanta: Kilpatrick Stockton LLP), 2003.
\item Delaware General Corporation Law section 141(a) provides that “[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation.” DEL. CODE ANN. Tit. 8, § 141(a)(2006).
\item See Michael Follett, note 57.
\item Michael Follett, note 57.
\end{enumerate}
\end{footnotesize}
The Duty of Loyalty

“[T]he duty of loyalty mandates that the best interests of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and... is not limited to cases involving a financial or other cognizable fiduciary conflict of interest. It also encompasses cases where the fiduciary fails to act in good faith.”26 The duty of loyalty is often described as an obligation of directors to protect the interests of the company and its stockholders, to refrain from decisions that would injure the company or deprive the company of profit or an advantage that might properly be brought to the company for it to pursue, and to act in a manner that he or she believes is in good faith to be in the best interests of the company and its stockholders.27 Recent case law also adds that the duty of loyalty requires boards to act “affirmatively and in good faith.”28

The Duty of Care

The duty of care is defined as ‘... that amount of care which ordinarily careful and prudent men would use in similar circumstances.’29 Courts review the standard of care in directors’ decision-making process, not the substance of decisions thus limiting director liability for failure in risky decisions. A breach of the duty of care may be found when a director is grossly negligent if the substance of the board’s informed decision cannot be “attributed to any rational business purpose.”30 In response to the financial crisis, legislation has specifically addressed the need for increased risk assessment in our financial institutions, requiring increased disclosure to ensure that effective reporting systems are in place and that all relevant information has been evaluated to ensure financial and systematic failure’ to assure existence of reporting systems that identify illegal corporate conduct, e.g., medical referral kickbacks, 459.

25 In re Walt Disney Co. Deriv. Litig., 907 A.2d 693, 753 (Del. Ch. 2005), aff’d. 906 A.2d 27 (Del. 2006).
28 See Thomas A. Uebler.
29 In re Walt Disney Co. Deriv. Litig., 907 A.2d 693, 753-57 (Del. Ch. 2005), aff’d, 906 A.2d 693 (Del. 2006).
30 In re Walt Disney Co. Deriv. Litig., 907 A.2d 693, 753 (Del. Ch. 2005), aff’d, 906 A.2d 27 (Del. 2006), quoting Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971), and Smith v. Van Gorkom, 488 A.2d 858, 873 (Del. 1985),
economic stability. The duty of care is often perceived as a minimal standard, but addressing the impact of risk could increase the importance of this standard.

The Duty to Act in Good Faith

In the Disney case, the court stated that “Good faith has been said to require an “honesty of purpose,” and a genuine care for the fiduciary’s constituents…”31 A director acts in “subjective bad faith” when his actions are “motivated by an actual intent to do harm” to the corporation, and bad faith can take different forms with varying degrees of culpability.32 The court clearly ruled that the duty of good faith cannot be satisfied if directors act in subjective bad faith, consciously disregard their duties, actually intend to harm the corporation, or cause the corporation to knowingly violated the law.33

Most legal scholars disagree as to the practical importance of the duty of good faith, but proponents of managerial accountability in corporate governance look to the doctrine of good faith because the traditional duties of care and loyalty do very little to discipline boards, even if allegations of self-dealing were made (i.e., violations of duty of loyalty).34 The Disney decision was critical for corporate governance since the court recognized that conduct that benefits the corporation must be done with proper motives in order to satisfy the duty of good faith, thus making boards and senior managers more accountable for their decisions. Implicit in these recent cases is the assumption that new rules of “conduct” may be useful in restoring trust to a doubting public. To more fully understand these new rules of ethical conduct we must turn to the historical origins of fiduciary principles.

Origins Of Fiduciary Principles

Biblical and Early History

If you would understand anything, observe its beginning and its development.

31 In re Walt Disney.
32 In re Walt Disney, at 55.
34 See Peter C. Kostant, 426–427.
Aristotle, 4th Century BCE

The historical definition of a “fiduciary” was stated in terms of “an essential code of conduct for those who have been entrusted to care for other peoples’ property,” carry out transactions, work for another, or aid persons who were vulnerable and dependent upon others. The breadth and complexity of early trust relationships is implicit in today’s corporate organizational structure and business relationships. As early as 1790 B.C., the Code of Hammurabi (a Babylonian code of laws) established rules of law governing business conduct, or fiduciary considerations, for the behavior of agents (employees) entrusted with property. For example, a merchant’s agent was required to keep receipts and to pay triple damages for failing to provide promised goods, although an exception was allowed if losses were due to enemy attack during a journey. The insightful research of several scholars traces the religious roots of the fiduciary principle to the Old and New Testaments. For example, the Lord told Moses that it is a sin not to restore that which is delivered unto a man to keep safely, and penalties must be paid for the violation, (i.e., duties of loyalty and due care); the right to fair treatment in the marketplace, implying a responsibility to conduct transactions in good faith; and the unjust steward who, expecting to be fired, curries favor with his master’s debtors by allowing them to repay less than their full debts, illustrating the precept that one cannot serve two masters. Additionally, the law on pledges obligates everyone to establish his own trustworthiness by carrying out the agreements he has made and by being sensitive to the needs of those who depend on him to meet

38 Kenneth Silber, “Fiduciary Matters.”
42 John H. Walton notes that the precept that one cannot serve two masters in Luke 16:1-13 was later cited by scholar Austin Scott in an influential 1949 paper “The Fiduciary Principle,” which describes boards’ and officers’ responsibility to shareholders and not to other constituents.
their needs (i.e., loyalty of master to servant, employer to employee, seller to buyer, powerful to vulnerable). 43

Fiduciary roles were likened to the roles of stewards in early religious and business history as well as in later corporate development. In this context, “Fiduciary law secularized a particular religious tradition and applied it to commercial pursuits,” where the shepherd tending his flocks may be likened to a fiduciary (steward or employer) or an agent (servant or employee) tending the sheep for the owner of the flock. 44 The ‘steward,’ may be described as a moral agent or representative of “God,” a corporate partner or stakeholder whose profits could be distributed by the steward to the poor at year’s end. 45 Also, the King (as steward) was described as God’s representative responsible for administering the covenant (agreements) for the people, and who must avoid preoccupation with the trappings of office while observing the law. 46 Thus, the king may be described as a model of godliness to the people by governing in a way that conforms to the requirements of the covenant. 47

The increasing complexity in fiduciary relationships over time is equated to the increasing complexity in the relationship between man and God (as owner) in early biblical history. The relationships change as a function of the increase in the complexity of the duties demanded of the steward (manager of covenants). Similarly, the steward is the precursor to the modern professional fiduciary as well as to those corporate directors or officers who owe a duty of care to the owners (shareholders) of the corporation as well as a duty of loyalty to all

46 John H. Walton, quoting Deuteronomy 17:14-20, 216.
47 Stephen B. Young details the link between fiduciary and ethical duties in the four covenants, or agreements, between God and man in the Old Testament that establishes and expands man’s duties of care. These covenants allow stewards to impose ethical duties on those who obey them (i.e., agents or employees) and reflect the core of modern agency and fiduciary relationships: 1) The first covenant establishes Noah as steward of God’s will to care for creation, and if Noah and his descendants take good care of creation it would not be destroyed (duty of care for the owner’s property); 2) The second covenant requires Abraham to accept the duty to behave according to a code of holy behavior in return for protection (protection from liability for accepting the responsibilities of duty of loyalty and care); 3) The third covenant requires the children of Israel to behave morally with religious devotion in return for protection of all of society (extending fiduciary duties of loyalty and care from an individual to society, i.e., to all stakeholders); The fourth covenant expanded these promises – if the conduct of all mankind is ethical and moral and not based on material temptations, Jesus will protect them on earth and grant them entry into heaven (fiduciary duties are deeply rooted in moral principles).
stakeholders and to the larger society. Stewards, or fiduciaries, “hold offices with authority, power and privileges set by law or custom, separate from individual personalities, and such office demands moral duties in private conduct, requiring new decision-making habits and reflective capacities that transcend selfishness.”

Similar to the descriptions of fiduciaries by Justices Cardozo and Brandeis, the description of stewards implies an inherent willingness to serve others (a moral duty), and a willingness to subordinate one’s interests to that of others by acceptance of the duty to serve. Both in early law and today, the fiduciary, or steward, is evaluated and compensated for his performance and understands that failure to fulfill his duties will result in penalties. While today’s corporations seldom attribute morality to a deity in fiduciary law, acceptance of fiduciary duties does require selflessness and a willingness to subordinate the fiduciary’s interests to that of another. Aristotle, who lived from 384 B.C. to 322 B.C., influenced the development of fiduciary principles, recognizing that in economics and business, people must be bound by high obligations of loyalty, honesty and fairness, and that when such obligations aren't required or followed, society suffers.

**Fiduciaries in Ancient Law**

Modern fiduciary law is traceable to developments in Ancient Roman law and early English law. Ancient Roman law defined fiduciary relationships as both moral and legal relationships of trust. For centuries until the end of the 18th Century, Roman law refined and formalized fiduciary law, recognizing various “trust” (fiducia) contracts in which a person held property in safekeeping or otherwise acted on another’s behalf (the core duties of loyalty and due care), and acted in good “faith” (fides) (core duties of honesty, full disclosure and applied diligence). Failure to uphold such trust could result in monetary penalties as well as a formal “infamy” (infamia), in which one lost rights to hold public office or to be a witness in a legal case. These fiduciary relationships in early Roman law were later incorporated into British courts of equity and then into Anglo-American law, providing standards for modern corporate law.

Early English law established the role of steward or agent with the granting of the Magna Carta, an English legal charter issued in 1215 which allowed the King to grant charters (companies) yet retain sovereignty (ownership)

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48 See Stephen B. Young and Joseph F. Johnston, Jr.
50 See Kenneth Silber, “Fiduciary Matters.”
in the charter while recognizing the recipient’s limited rights. The King served as steward, with fiduciary rights (ownership) in the management of his property but was required to place the interests of his subjects (inferior rights) above his own – a fiduciary relationship. Increasing population growth caused the King to transfer his role as steward to town leaders, creating an early form of agency (master to servant). Scholars describe the king’s stewardship duties as similar to the legal or fiduciary duties ascribed primarily to boards of directors and senior officers. Town leaders were similar to “agents” or employees who owed duties to their “stewards” or employers (managers). The continued development of Charter companies and later private companies, during the era of industrialization and specialization in business of the 1700-1800s, formalized the role of fiduciaries and their specific duties.

Early common law separated management from ownership (investors), creating the office of “manager” to protect the interests of investors and to prevent corporate self-dealing. Subsequently, fiduciary duties were attached to such office, and stewardship duties were borrowed from early law and applied to positions of responsibility to promote financial goals. Thus, although a “fiduciary” is a term described by legal statute, case law or professional codes of conduct, this term also describes ethical obligations and duties in a wide variety of business and personal activities and encompasses a “legal or moral recognition of trust, reliance, or dependence and of responsibility often ignored”

A MODEST PROPOSAL: NEW RULES OF FIDUCIARY CONDUCT

Legal standards for management behavior can be traced to “deeply rooted moral standards” that shaped the "fiduciary principle, a principle of natural law incorporated into the Anglo-American legal tradition underlying the duties of good faith, loyalty and care that apply to corporate directors and officers.” Scholars examined early fiduciary history as a potential solution to understanding corporate misconduct, suggesting that revisiting those early fiduciary principles might answer the questions: To what standards should managers be held?; and

56 See Joseph F. Johnston, Jr., “Natural Law and the Fiduciary Duties of Business Managers.”
What are the historical and conceptual bases for these standards?\textsuperscript{57} Alternatively, if one assumes that fiduciaries are responsible to the company’s shareholders as well as to a wider set of constituents, one might ask questions such as: In whose interests does the company presently function?; and, In whose interests should it function in the future?\textsuperscript{58} The latter set of questions not only asks who is served by the company, but also suggests that stakeholders bear some general rights as citizens, and should be protected against an abuse of power or violation that causes injury, as citizens.

If the role of a fiduciary is ascribed only to corporate boards and officers or to licensed professionals, corporate misconduct at other levels may go undetected. Despite this, corporate management argues that directors and officers are responsible only to shareholders, and that corporate management cannot serve two masters, i.e., multiple groups of stakeholders. To the contrary, history has demonstrated that fiduciary duties have been and can be the responsibility of all corporate members, and these duties may be extended to all stakeholders and the larger society. Research supports the theory that the corporation should have one set of duties for multiple stakeholders, an argument made by managers in the 1990s that managers had the skills and independence to mediate fairly among the firm’s stakeholders, and could assemble innovative teams capable of expanding wealth and economic opportunity.\textsuperscript{59} Managers sustained this claim well into the 1990s, both within their firms and within their major business associations but by 1997 pressure from the global commodity and national financial markets persuaded managers to revise their stakeholder standard. The perception is that managers moved from a focus on a single duty of loyalty to shareholders, to a narrower focus on making their principals (shareholders) and themselves rich, while disassociating themselves from the ideal of widening economic opportunity and improving living standards for the many.\textsuperscript{60} The Clarkson Principles, a set of principles for stakeholder management, are considered to be a critical academic effort to revive the idea that managers should be obligated to expand material opportunities for the many through economic growth.\textsuperscript{61} Additionally, compliance with fiduciary duties can reduce the principal’s costs of monitoring and disciplining agents and lessens the need for government regulation.\textsuperscript{62}

\begin{itemize}
  \item \textsuperscript{57} See Joseph F. Johnston, Jr. “Natural Law and the Fiduciary Duties of Business Managers.”
  \item \textsuperscript{60} Allan Kaufman, “Managers’ Double Fiduciary Duty,” 190.
  \item \textsuperscript{61} Allan Kaufman, “Managers’ Double Fiduciary Duty,” 190-93.
  \item \textsuperscript{62} Kaufman, “Managers’ Double Fiduciary Duty.”
\end{itemize}
Today, although most major corporations support the idea of corporate social responsibility (CSR), and believe that CSR and profit maximization work together, they continue to support the Freidman view that “The social responsibility of business is to increase its profits.” A top executive of a major oil company illustrates this view in the comment that “a socially responsible way or working is not… a distraction from our core business. Nor does it in any way conflict with our promise and our duty to deliver value to our shareholders.”

We propose that adherence to a new understanding and rule of fiduciary principles goes hand in hand with CSR and profit maximization and is perhaps the missing link in today’s corporate governance. The essential definition of a fiduciary does not change – a fiduciary is a person who has a duty to act primarily for the benefit of another. However, the role of the fiduciary should extend to all corporate members, and the duties of the fiduciary should not differ regardless of the specific function or distinction in roles. The primary focus of all corporate members continues to be to the shareholders (owners of the corporation), but duties toward other stakeholders should be consistent with those duties to shareholders. Any differentiation lowers the high standard of fidelity required of fiduciaries. Thus, the duties of loyalty, good faith, due care and obedience to the law should be incorporated fully into all fiduciary relationships, regardless of role or function within the corporation.

**CONCLUDING THOUGHTS**

“Many of the most shocking examples of corporate misbehaviors involve conduct that violates existing law.” This result occurs when most cost-benefit analysis weighs the potential harm and subsequent penalties against the potential profits, resulting in an ethical question often ignored because of the focus on maximizing shareholder profitability. Therefore, reform initiatives for boards of directors and corporate governance “without proper attention to ethical obligations will likely prove ineffectual.” Schwartz et al. found that board and officer leadership by example and action are roles central to the overall ethical and governance environment of their firms, a leadership role that is reinforced by board members’ legal responsibilities to provide oversight of the financial performance of their

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64 See Allan Kaufman, 192.

65 See David Callahan, “The Cheating Culture: Why More Americans are Doing Wrong to Get Ahead.”

firms – based on the assumption that ethical corporate leadership results in the best long-term interests of the firm.

Thus, Schwartz et al.’s study of corporate boards of directors demonstrated that boards have a professional duty expressed as a fiduciary duty to make ethics-based decisions. We contend that ethics and morals in line with fiduciary principles must permeate the entire corporate culture, if corporate governance reform is to succeed. A return to those central values inherent in ethical and fiduciary duties extended to the greater community as well as to shareholders may provide more socially responsible guidelines for corporations in this period of stakeholder demand for increased government regulation. Defining and providing examples of fiduciary values of honesty, loyalty, integrity responsibility, fairness and citizenship can provide guidance for corporate fiduciary relationships with all stakeholders, and provide a more efficient voluntary control mechanism. Thus, we contend that consistent fiduciary principles should be implemented throughout the firm, regardless of the corporate member’s function or role.⁶⁷ This view is consistent with Friedman’s view, that a corporate executive is an employee of the owners of the business, owes responsibility to his employers to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of society, embodied both in law and ethical custom.⁶⁸

Our review of the historical and religious origins of fiduciary relationships demonstrates that the concept of fiduciary was intended to be both a societal and a legal principle, and this is consistent with Friedman’s view of obeying the law and social custom. The leaders of organizations, as stewards, were responsible to the whole organization, and to society, not just to themselves or shareholders. Perhaps a revitalization of the stewardship principle is part of the new perspective required to create sustainable competitive advantage in today’s economy. We believe that there is room for stakeholder-focused management that does no harm to shareholder interests while also benefiting a larger constituency, and that fiduciary duties require the exercise of care, loyalty, obedience and good faith

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⁶⁷ R. Edward Freeman, in “The Politics of Stakeholder Theory: Some Future Directors,” *Business Ethics Quarterly* (1994) 4:409-421, suggested that “multi-fiduciary stakeholder analysis is simply incompatible with widely-held moral convictions about the special fiduciary obligations owed by management to stockholders. At the center of the objections is the belief that the obligations of agents to principals are stronger or different in kind from those of agents to third parties.” This view is not supported by historical development of the fiduciary principle, and may be perceived more as a function of corporate management choosing those functions that support personal, not fiduciary, goals.

⁶⁸ See Milton Friedman, 51.
with regard to shareholders as well as to all stakeholders and the larger community.  

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