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***Chester Barnard's Theory of the Firm:  
An Institutionalist View***

***Vladislav Valentinov and  
Steffen Roth***

**Abstract:** Chester Barnard's work can be shown to contain subversive elements which accord with the spirit of institutionalist scholarship. Barnard saw corporations as systems of power whose sustainability must be backed by moral resources which are becoming increasingly scarce today. This vision suggests that the core role of corporations may be found to be in mobilizing power and morality needed to maintain social cooperation. Even though Barnard failed to develop an adequate critique of corporate power and business enterprise, he advanced a set of innovative concepts which illuminate the contribution of corporations toward the coordination of the social provisioning process.

**Keywords:** Chester Barnard, morality, power, sustainability, theory of the firm

**JEL Classification Codes:** A13, D21, M14

Recent debates on the institutionalist theory of the business enterprise, appearing on the pages of this journal, have foregrounded at least two novel issues (Jo 2019; Atkinson, Hake, and Paschall 2019; Dean 2018; Jo and Henry 2015). One of them is related to sustainability of corporations under the current regime of money manager capitalism. Reflecting on the progressing financialization of the U.S. economy, Tae-Hee Jo and John Henry (2015, 24) argue that “financially oriented business behavior makes the social provisioning process more unstable,” with the implication that the economic sustainability of many individual corporations is thereby undermined. For that reason, the authors called for revising the institutionalist view of going concerns, whose life becomes shorter (Jo and Henry 2015, 33) and increasingly insecure. Responding to their call, Erik Dean (2018) proposed a modification of that view. He explained that in addition to the traditional dichotomy of going plant and going business, going concerns under money manager capitalism develop a new layer, “the non-practicing enterprise,” which enables the orientation of going concerns “toward[s] more purely financial (more broadly: intangible) interests and methods of control” (Dean 2018, 1093). The interesting implication of Dean’s argument is that “the interests in stability of the non-practicing enterprise are served at the expense of stability of the industrial or commercial enterprise” (Dean 2018, 1100). This means that many individual going plants and businesses face the risk of their sustainability being sacrificed for the sake of sustaining the controlling “non-practicing enterprises.”

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Another intriguing issue that surfaced in the recent debates is concerned with the nature of “the coordination of the social provisioning process” (Jo 2016, 338). While mainstream economists take little interest in the idea of social provisioning and see the price mechanism as a premier coordination device, institutionalists are highly critical of this approach. However, as Jo (2016) rightly notes, institutionalists still have to think about how the social provisioning process can be coordinated. Crucially, he suggests that “the continuing process of social provisioning requires interactive going concerns . . . [which] strive to reproduce themselves over time by creating internal structures . . . and working rules, and by taking strategic actions. Reproduction requires stability, yet, irreversible decisions lead unexpectedly to instability” (Jo 2016, 338). A key example of such going concerns are corporations whose ongoing reproduction is increasingly endangered by financialization pressures. Having outlined an institutionalist-heterodox framework of the economic decision-making of an industrial going concern, Jo (2016, 341) calls on institutionalists to explore the ways in which corporations make strategic decisions on “production, pricing, price, and investment,” each of which constitutes a key dimension of coordination.

Both of the highlighted issues, corporate sustainability and nature of coordination within the corporate going concerns, are interrelated, and neither of them can evidently be illuminated by neoclassical price theory. Key to understanding the relationship of these issues is the institutionalist vision of the precarious interaction between business and industry, the latter of which tends to be destabilized by the former. On the institutionalist view, corporation presents the master institution of the capitalist society (Jo 2019, 599). This means that corporations hold tremendous power over markets and indeed whole societies in which they operate. As Veblen acknowledged, they often use their power to disrupt the social provisioning process and to pursue interests contrary to those of the broader community. Under money manager capitalism, it becomes increasingly clear that the way corporate power is used puts at risk not only the social provisioning process but also the economic sustainability of many individual corporations, especially if they are governed as going businesses rather than as “non-practicing enterprises,” to follow Dean’s (2018) terminology.

The contribution of the present article is to contribute to the institutionalist literature by reconstructing Chester Barnard’s organization theory insights contained in his 1938 classic *The Functions of the Executive*. Barnard certainly cannot be called an institutionalist, yet he “was a pioneer in organization theory whose book left us a rich heritage of practical insights and theoretical constructions” (Dugger 1991, 893). It is noteworthy that his experience as a top executive of the New Jersey Bell Telephone Company, as well as his notable contributions to public service, led him to develop skepticism toward contemporaneous mainstream economic science which tended toward “the exaggeration of the economic phases of human behavior” (Barnard 1938, xxx). According to him, this exaggeration “was conjoined with an exclusion of adequate consideration of motives in pure economic theory, a materialistic philosophy rooted in utilitarianism, and a prevalence of highly erroneous conceptions of the place of the intellectual, as distinguished from the emotional and physiological, processes in social behavior” (Barnard 1938). Reflecting on Barnard’s contemporary relevance, management scholars Paul Godfrey and Joseph Mahoney (2014, 363) note that he saw corporations as systems which exert “power over individuals in mandating certain actions for the good of the system; authority works to clarify and legitimate those needs in the minds of organizational participants.”

Barnard's conceptualization of corporations as systems of power and authority has been prominently popularized, among others, by Oliver Williamson (2010) who ascribed to them unique coordination and adaptation properties which pose considerable challenge to the neoclassical production function view of the firm. Even though this reading of Barnard has not gone unchallenged (cf. Walsh and Brady 2019), it certainly strikes a chord with much institutionalist thought. What may be particularly interesting in the light of the recent institutionalist debates on corporate sustainability is that Barnard considered corporate power systems to be basically fragile, with their key sustainability condition being the existence of morality, both organizational and personal. As he explained, "[o]rganizations endure . . . in proportion to the breadth of the morality by which they are governed. This is only to say that foresight, long purposes, high ideals, are the basis for the persistence of cooperation" (Barnard 1938, 282). From today's point of view, a key function of this morality is to induce corporate managers to do justice to their fiduciary responsibilities which are supposed to minimize those risks of financial speculation that put the economic sustainability of corporations on the line (Godfrey and Mahoney 2014, 367). Thus, from a moral point of view, one possible effect of money manager capitalism is in undermining precisely this type of morality, whereas Barnard clearly believed corporate managers to be directly responsible for not running their corporations against the wall.

An institutionalist assessment of Barnard's vision of "the foundational role of morality in the effective practice of management" (Godfrey and Mahoney 2014, 260) may be aided by William Dugger's (1988, 107) comparison of Barnard's 1938 classic with a post-war book written by another corporate executive (Geneen and Moscow 1984). Dugger (1988, 107) explains that "while Barnard stressed the system-wide, cooperative behavior needed in large corporations, Harold Geneen stresses the need to meet the immediate profit targets. The difference in emphasis between the two is indicative of a profound shift in how U.S. corporations are managed. That shift has involved a narrowing of focus, a shortening of horizon, and, paradoxically, also an intruding of corporate interest into other spheres of life." Dugger's comment is highly significant, for it identifies a number of evolutionary changes in the U.S. capitalism which Barnard had no chance to witness, and which he most likely would have disapproved. In view of this comment, Barnard's view of corporations as power systems whose sustainability rests on organizational morality may appear too optimistic to fit the conditions of the present-day money manager capitalism. Yet, on the other hand, Barnard's work reinforces the institutionalist position that, given the deleterious influence of money manager capitalism on organizational morality, corporate endeavor may be ultimately unsustainable.

The following sections introduce a number of Barnard's core concepts, assess their institutionalist relevance, and contrast the institutionalist reading of Barnard's work with the mainstream approaches to the theory of the firm. Concluding remarks follow.

### ***Barnard's Core Concepts***

At the beginning of his 1938 book, Barnard shows that formal organizations have a clear economic justification. The cooperation enabled by formal organizations "justifies itself . . . as a means of overcoming the limitations restricting what individuals can do" (Barnard 1938, 23). From an institutionalist perspective, the overcoming of individual limitations may be read as a functional contribution of formal organizations to the social provisioning process which rests on the development and utilization of the community stock of knowledge. The

individual limitations Barnard had in mind are of physical and biological nature; they are however situational rather than fixed and can be determined only with reference to “the total situation viewed from the standpoint of a purpose” (Barnard 1938). By cooperating with each other in the framework of formal organizations, individuals are able to overcome some of these limitations, until the point when “the limiting factor becomes cooperation itself” (Barnard 1938, 25). Individual contributions to the cooperative scheme maintained by formal organizations require coordination which is to Barnard “the creative side of organization” (Barnard 1938, 256). It is because of coordination that the joining of individual efforts “creates a surplus” (Barnard 1938).

Barnard explains that the coordination of individual efforts is achieved through the operation of power and authority. He defines authority as “the character of a communication (order) in a formal organization by which it is accepted by a contributor to . . . the organization as governing the action he contributes; that is, as governing or determining what he does or is not to do so far as the organization is concerned” (Barnard 1938, 163). Remarkable in this definition is the emphasis on the voluntary acceptance of authority by individuals. This emphasis resonates with Dugger’s (1980, 897) observation that “individuals, often physically and mentally stronger than their rulers or leaders, willingly obey orders or instructions.” The moral concern raised by institutionalists is that the voluntary acceptance of corporate power may go too far, especially in the regime of corporate hegemony maintained by invaluation processes such as subreption, contamination, emulation, and mystification (Dugger 1980, 901; Waller 2017, 3). In analyzing corporate hegemony, institutionalists may draw inspiration from Barnard’s (1938, 167) seminal concept of the individual’s zone of indifference “within which orders are acceptable without conscious questioning of their authority.” Corporate hegemony evidently has the unfortunate effect of inflating the zone of indifference of many individuals, within and outside corporations, on a massive scale. Reflecting on the Barnard’s concept in the light of the ongoing financialization of the U.S. corporate world, Godfrey and Mahoney (2014, 369) plead for “the revival of critical thinking and questioning that would shrink our collective zone of indifference to business decisions with opaque, but very real risks. The public must narrow the zone of business behaviors we see as ‘unquestioningly acceptable.’”

Despite Barnard’s (1938, 152) encouragement of corporate propaganda (which he called “the inculcation of motives”), he lived at a time when corporate hegemony had not yet reached the levels of the late twentieth and twenty-first centuries. Accordingly he considered individual corporations to be subject to multifarious sustainability risks which they had to manage and navigate. In exploring the capability of corporations to survive in a precarious environment, he advanced the idea of organizational equilibrium which includes two terms: “first, the effectiveness of the organization, which comprises the relevance of its purpose to the environmental situation; and, second, its efficiency, which comprises the interchange between the organization and individuals” (1938, 83). Efficiency, in Barnard’s idiosyncratic interpretation, is secured if individuals are subjectively satisfied with the conditions of their membership in the organization. This satisfaction is multidimensional and is by no means reducible to the material remuneration that organizational members may receive.

From the institutionalist perspective, two aspects of the idea of organizational equilibrium deserve note. First, contrary to the connotations of the term in mainstream economics, organization equilibrium in Barnard’s work by no means implies organizational passivity or inertness. Barnard (1938, 83) explains that organizational equilibrium must be

continually maintained, and that this maintenance requires continual efforts by executive personnel. In that sense, “equilibrium” is a misleading term which could be advantageously replaced by the open systems theory notion of “steady state” (cf. Wolf 1974, 55; cf. Adkisson 2009). As Ludwig von Bertalanffy (1968, 143) explained, open systems “maintain themselves in a state of high statistical improbability, of order and organization” by engaging in “exchange of matter with its environment, presenting import and export, building-up and breaking-down of its material components” (Bertalanffy 1968, 141). Through metabolic exchange with their environment, open systems maintain steady state which is different from “true equilibrium and therefore is capable of doing work” (Bertalanffy 1968, 142). To Bertalanffy (1950, 23), true equilibrium presents a time-independent state marked by “maximum entropy and minimum free energy” (i.e., a state of death and decay). This state must be eventually reached by closed systems in accordance with the second law of thermodynamics. Barnard’s work is widely acknowledged to be anchored in the theory of open systems which maintain steady state (Valentinov and Roth 2021; Godfrey and Mahoney 2014; Wolf 1974).

Second, efficiency in Barnard’s understanding is subjective and does not yield itself to an easy measurement. However, institutionalists wishing to appreciate this concept may note its parallels with what Marc Tool (2001, 173–174) identifies as the limiting conditions of institutional adjustment, such as “the ability of a people to understand and accept the change,” and a minimal dislocation of extant instrumental functioning. It is clear that the validity of these conditions in specific cases depends on the subjective assessment of the affected individuals and communities, and the same can evidently be said of Barnard’s idea of efficiency. A further crucial parallel is that efficiency in Barnard’s understanding is not limited to satisfactions of managers, financial speculators, or any controlling group. In discussing efficiency as a component of organizational equilibrium, Barnard did not exclude or privilege any specific group of organizational participants.

In Barnard’s view, the essential mechanism employed by corporations to maintain their organizational equilibrium is organizational morality, which he defines as “that which is governed by beliefs or feelings of what is right or wrong regardless of self-interest or immediate consequences of a decision to do or not to do specific things under particular conditions” (Barnard 1958, 4). A key ingredient of organizational morality is executive responsibility for “securing, creating, inspiring of ‘morale’ in an organization. This is the process of inculcating points of view, fundamental attitudes, loyalties, to the organization or cooperative system, and to the system of objective authority, that will result in subordinating individual interest and the minor dictates of personal codes to the good of the cooperative whole.” An essential moral function of corporate leadership is to inspire “cooperative personal decision by creating faith: faith in common understanding, . . . faith in the superiority of common purpose as a personal aim of those who partake in it” (Barnard 1958, 259). Naturally, all these manifestations of organizational morality can only be upheld on the basis of loyalty and responsibility of individual organizational members. Godfrey and Mahoney (2014, 367) remark that, according to Barnard, “the primary moral responsibility of the executive resides in the work of maintaining the organization, creating a homeostasis that ensures the survival of the organization.” A brief reflection suggests that this responsibility requires avoiding financial risks and dubious practices that have gained currency under money manager capitalism.

***An Institutional Assessment***

For all its cursoriness, the overview of Barnard's key concepts indicates that his way of thinking is partly akin to and partly at odds with the spirit of institutionalist scholarship. Some of his differences with institutionalism may be rightly considered to be fundamental. In view of his primary interest in management and organization theory rather than institutional economics, Barnard has not given much attention to the long-term "changes in the financial and legal institutions supporting production for large-scale markets" since the late nineteenth century in the United States (Atkinson, Hake, and Paschall 2019, 1). Thus his work provides almost no insight into the evolutionary dynamics that transformed the corporation into a vehicle for advancing financial and vested interests; neither does it illuminate the origins of the financialization process. While acknowledging the centrality of power within corporations, Barnard did not see the pervasiveness of corporate power throughout the contemporaneous U.S. society; he is extremely far from understanding the phenomenon of corporate hegemony (Dugger 1989). To the contrary, he saw corporations as essentially constrained by the outer environment, natural and societal alike. According to Barnard, "the executive . . . faces limitations and prohibitions that restrict his range of activity. His environment places physical, biological, and social restraints upon his power of choice and ability to act" (Wolf 1974, 67).

Accordingly, he was not in the right position to acknowledge close associations between economic power and political power (Brady 1943). Obviously he was far from sharing the Veblenian insight that "business ends have taken the lead of dynastic ends of statecraft, very much in the same measure as the transition to constitutional methods has been effectively carried through. A constitutional government is a business government" (Veblen 1904, 284–285). Being unwilling to pay attention to corporate power in society, he would not have been likely to share the view of the economy as system of power based on the "interrelation between legal and economic processes" (Samuels 1971, 435). His work does not comprise a solid analysis of concepts such as "technology, class, capitalist state, and an economy that is capable of producing a surplus" (Lee and Jo 2011, 869) and thus cannot inform institutionalist debates on the creation and distribution of surplus (cf. Dugger 2006; Adams 1991).

Perhaps most importantly, Barnard lacked the Veblenian (1901) critical insight into the distinction between industrial and pecuniary employments. Barnard's ideas on organizational morality indicate that he could not have shared the view that "the interest of managers of a modern corporation need not coincide with the permanent interest of the corporation as a going concern; neither does it coincide with the interest which the community at large has in the efficient management of the concern as an industrial enterprise" (Veblen [1904] 1975, 157). The Veblenian view of corporations being controlled by captains of industry and finance seems to be fundamentally at odds with Barnard's idea of organizational equilibrium. To Veblenian institutionalists, the corporation provides a means for predatory elites to exploit the majority by extracting societal surplus, whereas Barnard saw corporations as arenas for "system-wide cooperative behavior" (Dugger 1988, 107). Obviously, the current regime of money manager capitalism reinforces Veblenian concerns, while highlighting the incompatibility of business success (or even survival) with what Barnard called "satisfactions" of the vulnerable organizational stakeholder-contributors, such as workers and local communities.



Whereas the suggested institutionalist critique of the Barnardian idea of organizational equilibrium is potentially devastating, one implication of this idea is likely to be appealing to institutionalists. This implication is related to corporate sustainability which was a key Barnardian concern. Under the contemporary money manager capitalism, the successful operation of business enterprise may indeed be incompatible with organizational equilibrium, yet this incompatibility accentuates the very real economic, societal, and ecological sustainability problems to which this enterprise is inexorably subject. In this line, management scholars Godfrey and Mahoney (2014, 260) rely on the idea of organizational equilibrium to diagnose “a systemic failure of the moral dimension of organization.” On their account, it is precisely the systematic violation of organizational equilibrium that is at the heart of “the scandals and financial crises of the early 21<sup>st</sup> century” (Godfrey and Mahoney 2014, 260). Seen in this light, Barnard’s idea of organizational equilibrium presages the present-day investigations of the multifarious corporate sustainability problems. Even though these problems seldom result in immediate breakdowns, they make the continuation of “business as usual” impossible in the long term. Whereas Barnard would have likely predicted the violations of organizational equilibrium to give rise to immediate corporate breakdowns, his view needs adjustments reflecting the influence of the current regime of money manager capitalism.

In defense of Barnard, it is good to note that similar adjustments are needed today even for concepts with a genuine institutionalist pedigree, such as the concept of the going concern which was important in the work of Veblen and Commons. Jo and Henry (2015) question, for example, whether this concept retains its full validity under money manager capitalism, given that “increasing instability of the economy renders going concerns more vulnerable, and vice versa” (Jo and Henry 2015, 29). They conclude that the concept is still viable, because “a viable provisioning process requires the going concern, and vice versa” (Jo and Henry 2015, 43). They recommend however that “Veblen’s theory of the going concern needs to incorporate the current economic environment and institutions” (Jo and Henry 2015). Obviously, Barnard’s concept of organizational equilibrium can benefit from the same recommendation, which, if followed, would help to arouse the interest of management and business ethics scholars in corporate sustainability concerns voiced by institutionalists. The more radical of these concerns are aptly formulated by Jo and Henry (2015, 44) who ask, perhaps rhetorically, whether it is “conceivable that the recent evolutionary process of modern capitalism has so distanced the business enterprise from its supposed task of satisfying of the requirements of the provisioning process that the latter itself is endangered.”

While Barnard’s work falls short of the institutionalist standards of the critique of corporate power, it remains relevant for those institutionalists who believe that an adequate organization of the social provisioning process calls for “system-wide cooperative behavior,” noted by Dugger (1988, 107). A key reason why the social provisioning process poses non-trivial organizational challenges is that it rests on the utilization of community knowledge which is, by definition, beyond the grasp of individual community members (Valentinov 2013). Veblen ([1919] 1990, 325ff.) explained that “the mass of technological knowledge possessed by any community, and necessary to its maintenance and to the maintenance of each of its members or subgroups, is too large a burden for any one individual or any single line of descent to carry.” The organizational challenges are magnified by the fact that, in Veblen’s ([1904] 1975, 10) words, “none of the mechanical processes carried on by the use of a given outfit of appliances is independent of other processes going on elsewhere. Each draws



upon and presupposes the proper working of many other processes of a similarly mechanical character. None of the processes in the mechanical industries is self-sufficing.”

If “an individual can know only a tiny fraction of the total stock of knowledge” (McCormick 2006, 35) needed for the organization of a specific production, then a crucial part of the organizational task will be the coordination of numerous individual contributions (Foss 1998). The contribution of Barnard is in elaborating a rich conceptual toolbox for making sense of the way this coordination occurs in formal organizations. Central concepts occupying pride of place in his 1938 magnum opus, *The Functions of the Executive*, are power and authority which can obviously be used for coordination purposes. However, as documented by Aidan Walsh and Malcolm Brady (2019, 951), in his later work, Barnard focused “less on authority and more on ‘responsibility’ and on the spontaneous nature of coordination within the firm.” In a conversation with his biographer William Wolf, he expressed regret that his 1938 book did not “deal adequately with responsibility and its delegation” (Wolf 1973, 15). In the same conversation, he averred that “you couldn’t run a college, you couldn’t run a business, you couldn’t run a church, couldn’t do anything except on the basis of the moral commitments that are involved in what we call responsibility. You can’t operate a large organization unless you can delegate responsibility, not authority but responsibility. Authority comes second” (Wolf 1973, 35).

Walsh and Brady (2019) report on Barnard’s correspondence with liberal thinkers such as Friedrich A. Hayek and Michael Polanyi, whose work led him to identify important elements of autonomy, spontaneity, and self-organization in the coordination within the firm. There is room to argue that all these elements are required by the Veblenian argument that “an individual can know only a tiny fraction of the total stock of knowledge” (McCormick 2006, 35) needed for the organization of production. Obviously, the cognitive limitation suggested by Veblen applies also to expert power-holders, whose understanding of the production process remains necessarily imperfect. Thus the use of power and authority can be only limitedly effective. Much more importantly, from the Veblenian point of view, the organization of production requires “the cooperation of an industrial community. This industrial community . . . always comprises a group, large enough to contain and transmit the traditions, tools, technical knowledge, and usages without which there can be no industrial organization and no economic relation of individuals to their environment. The isolated individual is not a productive agent . . . There can be no production without technical knowledge . . . and there is no technical knowledge apart from an industrial community” (Veblen [1898] 1934, 34).

Barnard’s work sheds considerable light on the functioning of the Veblenian “industrial community.” In part, this functioning involves the use of power, as Barnard stressed in his 1938 treatise. But the rich Veblenian understanding of an industrial community makes clear that power alone is not enough. Barnard elaborated a plethora of additional concepts that potentially fill this gap. The concepts include “psychological and social factors in systems of cooperation,” the voluntary acceptance of authority, zone of acceptance, informal organization, organizational status systems, loyalty, moral responsibility, executive leadership, judicial process, faith, and the likelihood of conflict between moral codes. Perhaps most importantly, Barnard stressed non-logical thought processes, such as “intuition, know-how, hunches, and similar characteristics which are usually related to intensive experiences” (Wolf 1974, 51). Of particular interest to institutionalists, Barnard approvingly referred to John R. Commons’ (1934) distinction between limiting and complementary factors, and argued

that managers must be continually making and revising judgments on what constitutes the limiting factors in the evolving decision-making contexts. In order to be able to do so, Barnard tells us, managers must be able to sense the organization as a whole.

Walsh and Brady (2019) are certainly right to document the evolution of Barnard's theoretical foci from power in *The Functions of the Executive* to responsibility, autonomy, delegation, spontaneity, and self-organization in his later work, much of which was put together in his 1948 volume. It is instructive to reflect on the implications of this evolution from an institutionalist point of view. As Walsh and Brady (2019, 951) note, this evolution brought Barnard to argue for 'invisible hand' explanations of coordination within the firm and to compare coordination within the firm to market coordination, which was prominently described by Hayek in terms of self-organization and spontaneous order. Assuming that Walsh and Brady (2019, 951) are right, it is useful to reconsider the fact that Barnard was not a price theorist, but an organization and management scholar interested in the functioning of the Veblenian "industrial community." If Hayek (1945) succeeded in associating the growth of community knowledge with self-organization and spontaneous order embodied in the price system, the subversive contribution of Barnard is in undermining this association.

Barnard's work shows that whereas the industrial community indeed possesses much more knowledge than its individual members, it is not because the community relies on the price system in any form. Rather, it is because this community has access to unique features such as responsibility, loyalty, and organizational morality. In a sense, these features are grounded on the autonomous and spontaneous action of individual members of the industrial community. Yet, the key institutionalist message is that the driving of these features is precisely membership in the industrial community rather than any form of price system.

All in all, on an institutionalist reading, it seems safe to say that Barnard has largely neglected the critical implications of the ceremonial-pecuniary aspect of the business corporation, but has provided an original analysis of its instrumental aspect. From the instrumental point of view, a corporation presents an industrial community, which Barnard interpreted as a system of power whose sustainability requires considerable moral resources. Today, this interpretation is need of the fundamental institutionalist correction which would take account of the current regime of money manager capitalism, in which the instrumental role of the corporation is suppressed by its ceremonial-pecuniary role, in such a way as to put at risk the sustainability of the social provisioning process itself (cf. Jo and Henry 2015, 44). If this correction is undertaken, institutionalists may consider the vision of power-morality balance emerging from Barnard's work to offer a unique, if idiosyncratic, perspective into the internal workings of the black box that takes the place of the firm in the neoclassical price theory.

This could be an important input for the project of developing an institutionalist theory of the coordination of the social provisioning process (cf. Jo 2016). In a seminal work devoted to this project, Jo (2016, 339) elaborates on the institutionalist logic of economic decision-making in a going concern. As Barnard's work is not primarily economic, it does not imply specific modifications to this or other similar institutionalist perspectives, but it does suggest that such perspectives could be usefully complemented by a theoretical and empirical analysis of categories, such as authority, zone of acceptance, informal organization, loyalty, moral responsibility, executive leadership, judicial process, managerial judgment and "sense of the whole," and even organizational equilibrium. Lacking an economic focus, Barnard's work cannot be expected to yield direct insights into how corporations make strategic

decisions on “production, pricing, price, and investment” (Jo 2016, 341), but it does suggest that understanding this decision making may be usefully illuminated by the above categories, which may be summarized by the encompassing vision of the power-morality balance.

For all its worth, this vision presents a clear alternative to the neoclassical view of “a standard production function that transforms scarce inputs into scarce outputs for the purpose of maximizing profit” (Jo 2019, 599). Neoclassical price theory conceals the role of power and neglects the significance of morality. Foregrounding the power-morality balance, as Barnard did, presents one way of removing the cloak of price theory over the inner workings of the firm. In effect, Barnard’s explanation of corporate organization shows price theory, as the foundation of modern economics, to be indeterminate, for corporate behaviors are largely determined by the discretionary maintenance of the power-morality balance. In Barnard’s work, corporations are no longer black boxes deterministically reacting to price changes. They are much better described as being “deliberately created, structured, and managed for the sake of survival and growth in size and power” (Jo 2019, 601). Just as Marc Tool (2001) explained the economy as being discretionary, Barnard elaborated the discretionary character of its premier organization. Both Barnard and Tool stressed accountability of human decision makers for their actions in a way that is unparalleled by mainstream economics.<sup>1</sup>

### ***Informing the Theory of the Firm***

In assessing the current state of the institutionalist theory of the business enterprise, Tae-Hee Jo (2019) undertakes a critique of the literature of the new institutional economics and evolutionary approaches to the theory of the firm. Jo (2019) explains, among other things, that contrary to the mainstream economic assumptions, firms do not optimize; instead, top managers employ their discretionary power in order to achieve strategic goals, such as firm “survival, growth, and reproduction” (Jo 2019, 607). The new institutional economics and evolutionary approaches suffer from a neglect of pervasive power relations within firms, and fail to grasp the way in which the firm navigates the precarious interface between business and industry (Jo 2019). The idea of power-morality balance, which can be derived from Barnard’s work, reinforces and expands Jo’s (2019) ground-breaking analysis. Barnard stressed that top management holds tremendous discretionary power which may or may not be used responsibly. In the latter case, the firm mutates into a predator or even a parasite (Dugger 2006, 667) on the body of the social provisioning process, and thereby sacrifices its own long-term sustainability.

On a Barnardian view, an adequate understanding of the firm must include an appreciation of the role of morality, whereas a major strand of the new institutional economics approaches to the theory of the firm, the so-called contract-based approaches, makes particularly dramatic assumptions about the egoism of economic actors. As a prominent representative of these approaches, Oliver Williamson’s transaction cost theory of the firm “pairs the assumption of bounded rationality with a self-interest-seeking assumption that makes allowance for guile. Specifically, economic agents are permitted to disclose information in a selective and distorted manner. Calculated efforts to mislead, disguise, obfuscate, and confuse are thus admitted. This self-interest-seeking attribute is variously

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<sup>1</sup> Key ideas and formulations of this paragraph heavily rely on the comments of one of the anonymous reviewers whose inputs we gratefully acknowledge.

described as opportunism, moral hazard, and agency” (Williamson 1989, 139). Barnard would have most likely concurred with Williamson that the prevention of opportunistic behavior could be a unique capacity of organizational morality. Yet, contrary to Williamson, he believed that organizations develop this capacity not merely through elaborate contractual safeguards which penalize opportunism, but primarily through instilling organizational morality, or “securing, creating, inspiring of ‘morale’” (Barnard, 1938, 259). If Barnard may be said to have offered a theory of the firm, this theory would locate the core function of the firm in the mobilization of power and morality needed for securing complex forms of cooperation among individuals, and thus for ensuring the sustainability of the social provisioning process.

This standpoint informs not only the contract-based approaches, but also the competence-based ones, which do recognize that dealing with “the tacit, idiosyncratic or group-bound knowledge” requires a social context marked by the existence of trust and loyalty (Thompson and Valentinov 2017, 1065). To stress this point, Bruce Kogut and Udo Zander (1992) refer to firms as “social communities” in which the tendencies to opportunistic behavior can be suppressed by the awareness of social embeddedness (cf. Zenger, Pelin, and Bigelow 2011, 106). In a similar fashion, Geoffrey Hodgson (2013, 140) believes that the “firm increases productivity by providing a relatively sheltered organizational environment that enhances social cohesion and fruitful interaction among workers.” Yet, even the competence-based approaches lack the Barnardian vision of power-morality balance, and shed little light on the origin and function of organizational morality. Most importantly, they do not see morality as a basic sustainability condition of anything that might characterize the firm as an emergent level of the social provisioning process relative to individual actors. Thus, a Barnardian perspective adds a new dimension to Jo’s (2019) critique of the competence-based and evolutionary approaches exemplified by the work of Richard Nelson and Sydney Winter (1982).

It is noteworthy that the unrealistic view of human nature in the mainstream economic theory of the firm is noted not only by institutionalists but also by business ethics scholars, many of whom stress the pervasive nature of business-society tensions and thus come close to the Veblenian discrepancy between the interests of businessmen and those of the broader community (Pies, Schreck, and Homann 2021; Crane et al. 2019; Lee 2018; de los Reyes, Scholz, and Smith 2017; Donaldson and Walsh 2015; Jones and Felps 2013; van der Linden and Freeman 2017; Mitchell et al. 2016; Heath 2014; Boatright 1994). Many business ethicists concur in regarding the firm as a moral actor bearing wide-ranging responsibilities toward a variety of stakeholders, even though the nature of these responsibilities, as well as the criteria of stakeholder salience, continue to be debated (Crane et al. 2019). An eminent scholar stressed that the firm presents a moral community (Bowie 2017). Understandably, some business ethics scholars find the economic theory of the firm to be overly amoral (Néron 2015; Hendry 2004) or even immoral (Lee 2018). One might agree with Lee’s (2018, 153) assessment that “the widespread influence of economic theories of the firm may have had detrimental effects on society.” Business ethics scholars sharing these concerns may find consolation in the Barnardian argument that the long-term sustainability of corporations is predicated on the existence of organizational morality.

Contrary to the mainstream economic theory of the firm, Barnard saw a key role of formal organizations in mobilizing “willingness of persons to contribute efforts to the cooperative system” (Barnard 1938, 83; emphasis in original). Barnard notes several

synonyms of this willingness, such as loyalty, solidarity, and *esprit de corps* (Barnard 1938, 84). He explains that “willingness . . . means self-abnegation, the surrender of control of personal conduct, the depersonalization of personal action. Its effect is cohesion of effort, a sticking together . . . Without this there can be no sustained personal effort as a contribution to cooperation. Activities cannot be coordinated unless there is first the disposition to make a personal act a contribution to an impersonal system of acts, one in which the individual gives up personal control of what he does” (ibid). Naturally, in order to have the capacity to mobilize moral resources and to forge the individual willingness to cooperate, organizations must be “something much broader than a bare economic or political instrumentality or the fictional legal entity implicit in corporation law. As social systems, organizations give expression to reflect mores, patterns of culture, implicit assumptions as to the world, deep convictions, unconscious beliefs” (Barnard 1958, 2).

### **Concluding Remarks**

Chester Barnard was not an institutionalist. Yet he upheld at least two ideas which accord with the spirit of institutionalist scholarship: the ideas of power (Waller 2017) and of the cultural conditioning of human agency (Beal and Cavalieri 2019). He may be said to have developed a vision of power-morality balance which provides a tool to diagnose the long-run economic (but also social and ecological) sustainability of corporations. Having failed to develop an adequate critique of corporate power, as well as to discern the fundamental tensions between this power and organizational equilibrium, Barnard has nevertheless highlighted corporate sustainability risks which require paying more attention to responsibility and morality underpinning the use of discretionary power. A message that institutionalists may take from Barnard’s work is that the social provisioning process must be backed by moral resources that are corroded by the present-day money manager capitalism on a scale that Barnard had not imagined. This corrosion makes the social provisioning process unsustainable, and ultimately puts at risk the sustainability of many individual corporations. While institutionalists do not accept neoclassical explanations of the allocation of scarce resources through the price mechanism, Barnard’s ideas, such as the organizational equilibrium and zone of indifference, yield valuable alternative insights into the contribution of corporations toward the coordination of the social provisioning process (cf. Jo 2016).

While these insights shed little light on the economic logic of managerial decision-making per se, they foreground the fact that corporate contributions to the coordination of the social provisioning process rest on the navigation of precarious power-morality balances. In the light of the modern debates on the theory of the firm, the core role of corporations may be found to be in mobilizing power and morality needed to secure the complex forms of social cooperation as well as the sustainability of the social provisioning process. A key aspect of the coordination role of corporations is to minimize corporate sustainability risks, which constitute a major dimension of the disruptions that business can inflict on industry. This role is best achieved if morality is sufficiently pluralistic, and if managers are aware that corporate sustainability risks may be related to diverse societal problems, far from merely economic (Roth, Valentinov, and Clausen 2020). As Barnard explained, in order to bring this role to fruition, corporate managers need to make moral judgments, to see their organizations as a whole, and to discriminate strategic factors. If many corporate managers do not excel at doing so under money manager capitalism, a likely reason, on a Barnardian view, would be irresponsible and immoral use of corporate power. As Barnard explained,

in order to bring this role to fruition, corporate managers need to make judgments in a broader context, to see their organizations as a whole, and to discriminate strategic factors. If many corporate managers do not excel at doing so under money manager capitalism, a likely reason, on a Barnardian view, would be the narrow immoral use of corporate power.

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