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Agency theory and the paradoxes of contemporary work[1]

Helena Lopes

DinamiaCET- IUL, ISCTE-Instituto Universitário de Lisboa

Abstract: The paper draws on the distinction between the concepts of *individual* and *person* to show how management rhetoric addresses workers as persons whereas actual management practices organize work as if workers were self-interested individuals. We argue that this paradox is partly due to the widespread influence of agency theory whose conception of the firm, based on the agency problems generated by supposedly non-cooperative workers, became an influential normative model. Our argument is that agency theory's basic assumptions powerfully contributed to further and legitimize the deterioration of work life witnessed in the last decades. We end by sketching some of the theoretical and institutional changes in corporate governance regulation and labor law that would be required to make firms' behavior consistent with their rhetoric.

Keywords: individuals vs persons, agency theory, cooperation, management paradoxes, quality of work, social interactions at work

"… men, not Man, live on the earth and inhabit the world" (Arendt, 1958:7)

1. Introduction

The several paradoxes that always marked the world of work had critically grown deeper in the last decades. Pressured by markets and shareholders to simultaneously innovate and reduce costs, firms' management took on a schizophrenic turn. Being aware of the extent to which organizational efficiency depends on the workers' motivation, firms attempt to mobilize the workers' commitment through a trust-

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building and cooperative rhetoric. But the management practices they actually developed in the last years, based on tightened control and individualized incentives, can but undermine trust and cooperation (Drago and Garvey, 1998).

A close examination of this state of affairs makes one realizes that, whereas management rhetoric addresses workers as *persons* – that is, relational, socially embedded beings endowed with moral capacity (Harris, 1989), actual management practices address workers as *individuals* – that is, non-cooperative beings predominantly driven by self-interest. Since real workers are increasingly educated persons rather than mere self-interested individuals, their subjective involvement at work and expectations regarding work have tended to increase which, combined with the paradoxical injunctions referred above, are bringing about an unprecedented deterioration of the quality of work life.

The argument of the present paper is that what underlies the increase in the gap between management rhetoric and practice is the prevailing influence of agency theory on both academics and practitioners. Indeed, all mainstream economic theories of the firm came to adopt the micro-foundations provided by agency theory in the 1970s (Jensen and Meckling, 1976), and agency theory now also dominates other firm-related academic fields (corporate governance, law and economics, accounting and finance). Beyond, or because of, this huge academic influence[2], agency theory became a powerful normative model with pervasive real-world consequences.

The roots of agency theory's influence lie in its few but powerful basic assumptions. Firstly, agency theory conceives firms as a cascade of principal-agent relationships in which amoral agents seek to maximize their self-interest and act opportunistically whenever possible. The management prescriptions that logically derive from such a behavioral assumption focus on individualized incentives and tight monitoring. Secondly, following Friedman (1970)'s seminal paper, agency theory assumes that i) "shareholder value" is the only legitimate goal of the corporate firm because ii) shareholders are the owners of the firm. Whereas assumption i) has since long been debated in the literature, assumption ii) is less disputed though

[2] Jensen and Meckling (1976) is the third most cited paper in economics among those published since 1970; Michael Jensen is the fourth most cited author (Kim et al, 2006).

questionable, notably on legal grounds (Chassagnon and Hollandts, 2014; Robé, 2011, 2012; Blair and Stout, 1999).

Our argument is structured as follows. We begin in section Two by highlighting the differences between the concepts of individual and person. We then draw on this distinction to argue that cooperative behavior, which ultimately distinguishes firms from markets, cannot be accounted for without the social and moral abilities of persons. Section Three presents first the management rhetoric aiming at mobilizing "persons" and then the actual management practices aiming at motivating and controlling "individuals". Section Four examines agency theory's conception of social interactions at work and highlights the extent to which it departs from a person-based conception of behavior at work. Section Five relates the argument developed about the behavioral assumption to the two other assumptions of agency theory and briefly sketches the institutional framework that would necessarily accompany a theory of the firm based on micro-foundations other than that of agency problems. Section Six concludes.

2. The concepts of the individual and the person – application to the sphere of work

Distinguishing between the person and the individual

All heterodox economists emphasize the need to replace the mainstream atomistic conception by a socially embedded conception of the individual, but a change in terminology has not been suggested yet. Though, in philosophy and anthropology different terms and concepts are employed to single out these two different views of human beings. While the concept of *individual* refers to the internal attributes and uniqueness of humans primarily conceived as separate beings, the concept of *person* adds to these substantive characteristics the recognition that humans are constitutively social and relational (Roger, 2012; Harris, 1989). Whereas individuals are possessors of qualities indigenously describable in abstract and "divisible" terms (see the representation of the utility-maximizing individual by his indifference map or utility function), persons are agents-in-society inextricably shaped by the context in which they live and the persons with whom they interact

The supremacy of mainstream economics succeeded in imposing the atomistic, Hobbesian view, in which humans are able to survive and grow outside the world of social interaction. However, other philosophical strands argue that humans are constitutively relational beings since the genesis of the human mind is not *mono-logical* - something each person accomplishes on her/his own - but *dia-logical*, something that comes out of the exchanges with others, namely through language (Taylor, 1989). This tradition consequently characterizes the human condition by its gregariousness and its struggle for social recognition; persons enter into relations with others because of their need for relatedness and social esteem (Honneth, 1995). By contrast, rational choice theory retains the Hobbesian struggle for self-preservation as the basic human condition; individuals enter in relation with others when and if they need them to reach their goals, not for the relation itself.

Focusing on humans as persons draws attention to a feature crucial for our purpose: all concepts of person explicitly emphasize the moral/judgmental capacities of humans. Whereas mainstream economics highlights the calculative abilities of individuals – required for utility maximization - the inter-subjective ontology of persons emphasize their interpretative and normative abilities (Favereau, 2008). Persons are capable of submitting their conduct to shared values and, thus, of committing themselves to common goals and complying with commitments. Only the concept of person, because it breaks with ontological isolation, is theoretically compatible with the idea of a common good, which supposes a commonly shared set of standards and values.

The need to render behavior predictable - and thereby prone to modeling - led mainstream economists to adopting a view of the individual primarily self-centered and self-sufficient. Even in the models that introduce social and moral motives into utility functions, individuals are calculative rather than gregarious beings. Relating with others and following behavioral norms result from individualistic, possibly enlightened, calculations rather than moral capacity: “We do *not* assume that people follow a social norm for its own sake, but we investigate how such a rule is sustained by self-interested community members” (Kandori, 1992:63). Individuals as conceived by economists ultimately seek to maximize their utility; they form groups to further their particular interests, not to fulfill any requirement of their flourishing as human beings.

The relational and moral requisites of cooperative behavior

This view logically assumes that individuals do not spontaneously engage in cooperative endeavors. Instead, cooperation acquires a social dilemmatic nature in that every individual would be better off if all cooperated, but each individual finds in his self-interest to shirk on his contribution (Olson, 1971)[3]. Yet, the well-functioning of modern production processes, characterized by high levels of uncertainty, strong interdependence, and limited monitoring possibilities, requires that workers effectively cooperate. In most workplaces, workers are constantly entering into social interactions because it is through social interactions that they are able to establish the common understandings and the routines necessary for each to contribute his/her part.

Cooperating implies (a) giving up on one’s desire to cheat or exploit cooperative partners and (b) expecting that others will cooperate too. Requisite (a) means that workers must commit themselves to the pursuit of the previously set goal rather than the one-sided pursuit of self-interest. Yet, separate, independent and self-interested individuals would have no incentive to contribute their part if it happens to diverge from their private interest. Requisite (b) means that compliance with commitments and expectations about others’ behavior acquire crucial importance. Individuals who do not abide by social norms for their own sake would not expect co-workers to cooperate. In fact, it is the social needs and moral abilities of persons that both establish and enforce mutual expectations.

[3] Some models show that spontaneous cooperative equilibria are sustainable among self-interested individuals, but the conditions required, namely complete information about past behavior, efficient sanctioning and continuing interaction, are seldom met in real-world.

More precisely, workers cooperate because cooperating provides the opportunity to enter into interactions which satisfy the human need for gregariousness. It may be said that cooperating gives rise to “relational goods”, defined as the outputs of a communicative, cognitive and affective nature generated by the interpersonal relations one enters into (Bruni, 2008; Gui, 2000; Uhlaner, 1989). A given interaction gives rise to (positive) relational goods only if and when the interacting workers jointly value it. That is, relational goods (friendship, camaraderie, reciprocal helping) are more than just a combination of private goods; to the extent that they require a common valuation, they go beyond the individualistic derivation of utility. Relational goods explain why workers do not systematically exploit cooperative partners (requisite (a)).

Cooperating involves a series of mutual obligations that, depending on whether they are fulfilled or not, result in moral goods/bads (e.g. feeling fairly treated and respected versus deceived and humiliated). Moral goods are hence defined as the outputs of a moral nature generated by the social interactions in which workers enter (Lopes et al, 2009). Moral goods involve and require the common valuation of the norms that guide the actions of the interacting workers. The normative appeal of moral norms derives precisely from them being commonly shared. The fact that moral norms prescribe actions that may lead to acting contrary to self-interest is of special importance. Indeed, only persons abiding to moral norms can expect others, whom they know share the same norms, to also abide by them even when it runs counter to their interest. The existence of moral goods explains how requisite (b) is met.

To sum up, cooperative behavior at work cannot be accounted for without considering the role that relational and moral goods play in motivating and sustaining cooperation. If cooperation undoubtedly entails a calculative facet, it also inevitably calls for the relational and moral capacity of persons. Only morally able and gregarious persons, not calculative individuals, can effectively enter into moral obligations with others. It is important to note that relational and moral goods stem from both horizontal and vertical interactions, that is, from relations with colleagues as well as with superiors. Relational and moral goods may obviously also be “bads” (animosity, disrespect, resentment, etc), in which case they can be destructive for the workers’ well-being and organizational performance. The fact that human beings are persons as defined above does not obviate that they do often behave as self-interested, indeed immoral individuals. It is therefore of prime importance that work environments allow the nurturing of relational/moral goods to avoid the losses and inefficiencies caused by relational/moral bads.

3. From mobilizing persons to managing individuals

Firms' appeal to the workers' commitment and subjective involvement

Firms know that workers are morally-endowed persons willing, for the most part, to behave cooperatively rather than opportunistically. To achieve profitability and foster innovation, they then try to draw workers into a cooperative endeavor by asking them to invest themselves at work cognitively but also affectively. In other terms, the prevailing management rhetoric requires the mobilization of the "whole person". Indeed, the workers' loyalty might be more efficiently achieved through internalized commitment than through obedience, technical prescriptions and bureaucratic control.[4]

The attempts of firms to bind workers to the firms' interests have their academic expression in several strands of literature, among which corporate culture and the human resource commitment model (Francis and Keegan, 2006). Corporate culture is broadly defined as a set of values, norms and beliefs shared by the members of an organization that control and guide how individuals and groups interact with each other. Shared norms - as opposed to technical rules – are not and cannot be directly enforced by hierarchical control but may be fostered by a strong corporate culture. Shared norms are enforced by the members of the group themselves because

[4] This raises a crucial issue: the fact that workers as persons need to nurture good relationships at work and are prone to behave cooperatively is often used by firms to manipulate them and perpetuate oppression in the name of overcoming it (Alvesson and Willmont, 1992). The rationale of the present paper is that firms must acknowledge the social and moral abilities of workers but not use them to further exploit workers.

they encompass behaviors that are essential to effective group functioning. Workers who violate shared behavioral norms may be subject to expulsion or ostracism, which generate affective and cognitive suffering (relational bads). Similarly, the “commitment model” prone by human resource scholars intends to empower workers and induce them to display self-driven initiative and take more responsibility for monitoring their own behavior (Francis and Keegan, 2006).

These management models explicitly acknowledge that behavior at work is driven by internalized moral norms; they then advocate that firms use the workers’ moral capacities in the interest of the firm. The social control resulting from the alignment of workers with organizational values would help firms operate like well-oiled machines without the need for extensive monitoring. Instead of relying on conformity and obedience, contemporary management is supposed to yield high levels of motivation and commitment through the building of strong corporate cultures and high performance work practices. Because work is not only a means to survival but also an opportunity for workers to realize their potential and satisfy their need for social esteem, workers are expected to subjectively engage in their work and devote great amounts of cognitive and emotional resources. Many management models now recognize that the economic world depends on the social and moral abilities of persons, not simply the pecuniary motives of individuals, for its functioning.

Note that strong corporate cultures and commitment models imply giving greater leeway to workers, which means enhancing autonomy at work, decentralizing and involving workers in decision-making, stimulating initiatives and risk-taking,[5] promoting team work, allocating above-market pay (efficiency wages) and ensuring job security. These practices would foster a kind of relation between workers and the organization based on “partial-gift exchanges” (Akerlof, 1982), in which workers reciprocate in effort and dedication the good working conditions offered by the firm. If firms fail to comply with their engagements, workers disengage from the moral obligations that such practices are supposed to generate.

[5] Actually, mainstream models show that providing workers with large decision rights promotes initiative but results in a loss of control for managers (Aghion and Tirole, 1997).

Firms' actual practices: the depersonalization and individualization of work

In fact, evidence shows that actual firms' practices break the "psychological contracts" presumed in the corporate culture and human resource rhetoric (Thompson, 2013). In the last decades, firms came to manage workers more as if they were maximizing individuals than morally able social persons. The trends that characterize the world of work to-day are in plain contradiction with the rhetoric of trust-building and empowerment of workers and closely follow instead agency theory's prescriptions. To minimize the agency problems supposed to originate from the workers' opportunistic behavior, agency theory prescribes two kinds of arrangements (Jensen and Meckling, 1976): i) compensation schemes aimed at aligning the principal and agents' interests (particularly recommended for high corporate executives) and ii) control devices aimed at keeping self-serving behavior in check and providing information about what agents are actually doing. Both arrangements would curb agents' opportunism since they reduce the conflicts of interest and prevent agents from deceiving principals. Their underlying rationale is that competition, rivalry and envy are more favorable to organizational efficiency than are mutual trust and reciprocity.

As for incentives, schemes such as performance-related pay, individualized and quantified appraisal systems, performance rankings and rising wage differentials are implemented to stimulate competition between workers at all levels of the hierarchy. The subsequent growing inequality of earnings is naturalized by the widespread diffusion of a meritocratic and elitist discourse. In what concerns monitoring, direct types of control, such as surveillance and giving orders, are replaced by "unobstructive" controls like standardization, involving workers in the setting of their individual performance targets, extensive reporting procedures and sophisticated monitoring devices that, thanks to the new management technologies, often conceal their true nature.

These practices made workers actively contribute to the intensification of work observed in the last two/three decades and resulted in increasing levels of stress and emotional exhaustion, substitution of extrinsic for intrinsic motivations and the dissolution of collective solidarities. Intensification of work is reported to being accompanied by a decrease in the time available to socialize - less “non-productive” moments; less time to learn, teach or help; less opportunities to meet and communicate; increasing feelings of isolation – as well as by a general depersonalization and deterioration of work relations. (Le Gall, 2011).

These trends in the evolution of work are reinforced by those observed in the evolution of employment, marked by depressive labor markets and a decline in the security of employment. Together, these evolutions can but contribute to the dismantling of communal values, like trustworthiness, cooperative dispositions and community building, that ground the management models referred above.

Because it lies at the core of the commitment and corporate culture models, which recommend giving workers more influence and discretion over their job, the evolution of autonomy at work as perceived by workers is worth mentioning. Instead of increasing over time and space, as could be expected, perceived work autonomy decreased or remained stable in most European countries over the 1995-2010 period (Lopes et al, 2014). Work autonomy declined markedly for workers in low-skill jobs in all but Nordic countries while it remained more or less stable for high-skill clerical workers in the 15 studied countries. These findings suggest that, overall and in spite of the higher educational level, the changes in work organization of the last two decades led to a decrease in the influence most workers now perceive to have on when, how and what to do at work when compared to the early 1990s. The widespread implementation of agency theory’s prescriptions may well be at the root of the observed decline in perceived autonomy at work.

A double paradox

The trends in the evolution of work, combined with the considerations developed in previous sections, delineate two paradoxes. The first concerns managerial practices: contemporary capitalism needs the cooperation and subjective involvement of workers but firms’ actual practices prompt competition rather than cooperation. The second paradox concerns workers: in spite of the worsening of their working conditions, workers do not seem to reduce their attachment to work[6].

Let's begin by the first, managerial paradox. The observation of unfulfilled "psychological contracts", that is, of a gap between managerial words and deeds, is nothing new. Management rhetoric advocates risk taking, personal commitment and trust-building, but in practice firms invest in ever more sophisticated surveillance and control devices. This paradox meets the person-individual distinction: firms want workers to involve themselves at work as *persons* but they organize work as if workers were opportunistic *individuals*, in need of being tightly directed and monitored. By individualizing incentives, controls and rewards, firms rely on the narrow self-interest of workers and their competitive dispositions rather than on their trustworthiness and cooperative dispositions.

The paradox confronted by workers is particularly cruel. Work became in our societies a powerful generator of identity and self-respect. Many sociological studies testify that the workers' expectations of self-actualization and recognition at work increased notably in the last decades, due to increasing educational levels but also to the commodification of other spheres of social life (Carvalho and Rodrigues, 2008). The individualization and depersonalization of work environments hence creates a tension between the need for a meaningful work, which necessarily includes feeling to contribute to a common goal and being part of a social community, and the pressure to enter into a competitive, zero-sum game. On the one hand, workers involve themselves as persons in work[7] but, on the other hand, they are compelled to behave as self-centered individuals to meet the quantitative objectives fixed by management, contributing hence to eroding the collective and cooperative spirit needed for their psychological well-being. If relational and moral goods could be observed, one would certainly see them regressing.

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[6] The data collected by the European Working Conditions Survey in 2010 shows that, though overall job satisfaction slightly declines, satisfaction with social relationships at work increased in most European countries (see http://www.eurofound.europa.eu/surveys/smt/ewcs/ewcs2010_10_05.htm).

[7] It must be noted that workers may be committed towards their work but not towards the organization in which they work (Cushen and Thompson, 2012), which further amplifies the paradoxical situation and its deleterious effects.

This state of affairs has considerably intensified the workers' vulnerability and psycho-social disorders (Siegrist, 2006). Burn-out and stress, feelings of culpability when performance targets are not met, and feelings of isolation became prevalent phenomena of contemporary workplaces (Le Gall, 2011). Firms are exploiting the person-side of workers without respecting it more intensely to-day than ever before in the past. Our argument is that this evolution of the world of work does not merely result from myopic managerial choices; it stems from the dominance of agency theory and the transformation of its basic assumptions into a dominant ideology and normative model.

4. Social interactions at work: costly contractual exchanges or efficient drivers of cooperation?

Social interactions as seen by agency theory

It is a particular kind of social interactions at work, namely principal-agent relationships, that grounds the whole theoretical apparatus of agency theory. Firms are conceived as a cascade of sequential principal-agent contracts in which principals delegate work to agents to act and decide on their behalf. Because agents are assumed to be utility-maximizers, effort generates disutility and is unobservable, and the parties' interests may diverge, this delegation allows agents to opportunistically further their interest at the expense of the principal's[8].

Firms are "nexus for a set of contracting relationships among individuals" (Jensen and Meckling, 1976:310) and ex-post violation of contracts is considered their root problem. The core concept of agency theory is hence agency costs and its core aim is to design contractual arrangements that minimize the problems brought about by human agency. The contractual relationships that take place within firms are of the

[8] Before the 1970s, the relationship between employer and employee was not seen as particularly problematic in standard economics. Employees were simply to be remunerated according to their marginal productivity. The notions of agency costs and moral hazard were introduced in the theory of the firm by agency theory.

same nature than market transactions: employers are not supposed to have any contractual obligation to long-term relationships with employees and the latter are assumed to be morally insensitive individuals who eventually renege on commitments. Social interactions within firms do not differ from social interactions in markets.

Yet, in 1972, Alchian and Demsetz had claimed that firms have a specific advantage when compared to markets: firms allow for the generation of cooperative surpluses, which are only attainable through joint cooperative effort – an argument long defended by institutional economists. Although Alchian and Demsetz (1972) elaborated on the importance of cooperation, they formulated the team production problem in terms of a vertical principal-agent problem (without using those terms, though, which only disseminate after Jensen and Meckling's 1976 paper), thus sidestepping the crucial question of horizontal social interactions. All the relationships of interest in the production process were deemed to be vertical, ie., of a principal-agent nature, each supervisor acting as a principal in relation to his subordinates and an agent to his own supervisor.

Horizontal interactions[9] among co-workers were nonetheless soon acknowledged in the agency literature, under the label of side-contracting. In the eyes of the then leading agency theorists, side-contracting takes the form of "bribes, personal relationships and promises of reciprocation" (Holstrom and Tirole, 1989:94). These "contracts" agents enter into cannot be fully controlled by principals, which generate agency costs and add "costly constraints to the owners' optimization problem" (Holstrom and Tirole, 1989:3). Side-contracting is hence considered undesirable and firms must take measures to prevent it. Suggested measures include the limitation of personal relationships, through isolation, for example, and the restriction of reciprocity through the promotion of short-term relationships (Holstrom and Tirole, 1989). Though, these authors comment in passing that the measures they recommend may have organizational drawbacks since they may undermine the development of trust, which they view as crucial for cooperation. In subsequent papers, side-contracting is considered as taking two possible forms, collusion or

[9] Observational studies reveal that most workers spend the majority of their time interacting with peers rather than with supervisors and subordinates. This illustrates the crucial role of horizontal coordination/social interactions and relational goods for cooperation.

cooperation, depending on its effect on the organization. The incentive and organizational structure should then regulate the degree of cooperation in order to limit collusion. In short, employers should consider social interactions among workers with suspicion.

These radical assumptions about horizontal interactions at work smoothen somewhat when the findings of experimental and behavioral economics are taken into account. Some recent principal-agent models explicitly acknowledge that workers derive utility from cooperation (defined as reciprocal helping) and that cooperative behavior among workers is a source of competitive advantage for organizations (Rob and Zemsky, 2002). It is recognized that “preferences for cooperating” are partly endogenous, which means that cooperative behavior may and should be fostered by appropriate incentive systems.

Likewise, if the first agency models assumed that workers behave a- or immorally towards principals, in recent years some agency theorists began to elaborate on Akerlof (1982)’s view of labor contracts as partial gift exchange. Dur et al (2010) call attention to the many benefits good relationships between principals and agents may yield to the firm and emphasize the fact that such relationships may motivate workers more powerfully than pecuniary incentives. Employees’ effort and employer’s benevolent treatment of workers are modeled as reciprocal gifts, and the signaling of good intentions on the part of principals, though costly, appears as a possibly efficient strategy (Non, 2012).

We might also refer the “relational contracts” literature, which emphasizes the role relational contracts have in enforcing incomplete contracts and compliance with commitments. Because the relationships are valuable in the future, the contracting parties do not wish to renege. Relational contracts are defined as informal agreements and unwritten codes of conduct established within and between firms (Baker et al, 2002). This type of contracts may be efficient when outcomes are not contractible ex ante and are observable ex post only by the contracting parties.

Social interactions as a major distinguishing feature of firms

Although these developments of agency theory denote an improvement in the way social interactions at work are envisaged – they explicitly/formally recognize the cooperative dispositions of workers, their efficiency-enhancing character, the self-enforcing nature of long-term relationships-, they differ to a great extent from the perspective endorsed here.

To begin with, cooperation is not considered by agency theory as an outcome of continued social interactions; that is, it is not viewed as a collective endeavor. Rather, agency theorists introduce social preferences into the individualistic theoretical apparatus and consider cooperating as a residual kind of behavior, not a constitutive trait of human behavior: "voluntary cooperation is defined as the difference between actual and privately optimal effort" (Non, 2012: 322). The decision to cooperate is taken separately by each worker depending on his/her preferences rather than emerging from the fact that workers are engaged in a collective productive venture. We consider instead that cooperation is associated to the relational goods stemming from the social interactions associated to joint production. As argued by Hodgson (2013), cooperating cannot be accounted for by introducing ad-hoc preferences into individualistic utility functions, but in agency theory the legitimacy of the utility-maximizing assumption is never questioned.

Secondly, instead of relational *goods*, sought and *valued* for their own sake by both employees and supervisors, social interactions are considered socio-emotional *resources* that are *costly* to produce and regulate. Good relations at work are always envisaged instrumentally, as a tool to foster efficiency, rather than an end in itself. Despite of the use of the term "relational", relational contracts are deprived of any kind of personal or social ties. They are impersonal relationships – established within or between firms - in which the honoring of contracts is exclusively based on self-interested calculations. The aim of relational contracts models is to design the incentive payments that comprise the "necessary and sufficient condition for the relational-employment contract to be self-enforcing" (Baker et al, 2002:74-75). The social constitution and moral endowment of workers is therefore not necessary for contracts to be honored.

Lastly, the principal-agent models that take non-pecuniary motives into account exhibit a feature that deserves examination: they always end recommending low-powered incentives, that is, reduced wages. Two explanations are advanced. Firstly, as cooperating increases the workers' utility, firms may offer lower wages – relational goods substitute for incentives and allow for a reduction in compensation. Secondly, since monetary incentives are acknowledged to crowd-out intrinsic motivations, such as spontaneous cooperative behavior, incentive pay schemes are "inefficient". In brief, though cooperating is crucial for the efficient functioning of firms, the workers who cooperate receive lower pecuniary compensation - which means invalidating Akerlof (1982)'s insight that gift-exchange relationships result from above-market wages.

This prescription is both empirically perverse and theoretically consistent with agency theory's assumptions. In agency theory, like in the compensating wage differentials theory, workers have to "pay" for the relational goods they enjoy at work, which amounts to assume that relational goods or cooperative behavior is a cost to firms. Indeed, in Non (2012), the good treatment of workers by managers is modeled as a cost. Though cooperation is efficient for the firm, it is workers who have to support its cost in the form of reduced wages, that is, in terms of reduced means of subsistence. This could logically lead to workers engaging less in cooperative behavior, a perverse empirical effect that adds to the counterproductive effects brought about by the other agency theory prescriptions (see below). If cooperative behavior enhances efficiency, it should be positively valued by the firm who should attempt to maximizing it rather than assigning it a negative value.

But this downplaying of cooperative behavior is consistent with agency theory's analytical framework which, in reducing social interactions to contracts and defining firms as "privately owned markets" (Alchian and Demsetz, 1972: 795), is in fact claiming that the well functioning of firms does not require morally-driven behavior (actually, the agency models that consider cooperative dispositions remain an exception). The argument developed in this paper, namely that relational and moral dispositions are the basis for well-functioning organizations, claims just the opposite. One of the basic distinguishing features of firms when compared to markets is that firms provide the opportunity for intensive interpersonal relationships. It is precisely the unspecified *obligations* and the exchange of socio-emotional benefits deriving from social interactions that contribute both to generating the desire to cooperate and to rendering cooperation sustainable. In short, while mainstream economics assumes that relationships established within firms are like those established between firms, that is, contracts between self-centered *individuals*, we consider that within firms workers engaged in productive activities establish relationships as *persons*.

Agency theorists discard the social and moral dimension of behavior because they want to free economic theory, and economic agents, from moral obligations and social ties. As is the case in markets, in firms the contracting parties are supposed to be responsible for anything but themselves - which frees employers and shareholders, in particular, from any moral obligation.

5. What is at stake is the agency theory conception of the firm

The ownership and governance/responsibility assumptions

We have seen that the world of work progressively tends to conform to the way in which agency theory conceives of economic behavior and social interactions at work. Definitely, agency theory became more than a purely positive conception of firms; as a normative model, it influences the way in which work is organized (Goshal, 2005). Two other basic assumptions of agency theory also contribute to explain the way in which firms are governed, namely: i) the ultimate goal of principals/managers is the maximization of shareholders' interests (measured by the market value of the shares) because ii) shareholders are the owners of firms.

The ownership assumption (ii)) supports the principal-agent view of corporate firms, as stated by Friedman (1970:2): "a corporate executive is an employee of the *owners* of the business". A few agency theorists, though, do not endorse this assumption: "ownership of capital should not be confused with ownership of the firm" (Fama, 1980:290). Indeed, the *firm* and the *corporation* must be distinguished: the firm is an organized economic activity with no juridical personality – it can hence not be owned – while the corporation is a legal subject used to legally structure the firm – it cannot be owned either, only the shares it issues can be[10]. Shareholders enjoy the privileges of the owner only towards what they own – the shares -, they cannot have these privileges towards the corporation having issued the shares, and much less so towards the firm. The ownership assumption is founded on a misunderstanding of the actual content of corporate law (Robé, 2011, 2012; Favereau and Robé, 2012; Blair and Stout, 1999).

Since the ownership postulate does not hold, postulate i), also uttered by Friedman (1970) - the primary responsibility of managers is to shareholders -, must be questioned. Actually, corporate law never refers to any legal duty to maximize profits; it only establishes the duty to manage in the "corporate interest", not the shareholders' interest.

Faced with this ownership problem, agency theorists developed in the last years an economic justification for the principle of shareholder value maximization, according to which the best way to ensure economic efficiency is to consider managers the agents of shareholders. The "nexus of principal-agent contracts"' definition of the firm would then be preserved and the issue of ownership is deemed irrelevant. However, the fact that shareholders own the shares issued by the corporation but not the corporation itself has very significant normative consequences, since the responsibility of managers then go beyond that of maximizing shareholders' interest to encompass the interests of all resources contributors[11], first and foremost workers (Roger, 2012).

Notwithstanding the intense debates surrounding the ownership and governance/responsibility assumptions, the latter conferred academic legitimacy to the growing adoption of the "shareholder value governance model" over the last thirty

[10] These considerations only apply, obviously, to public corporations, not individually-owned firms.
[11] There is a huge literature on this issue. We limit ourselves to very simplistic inferences here.

years. By pressuring managers to focus on creating value for shareholders, this governance model submitted firms to the imperative of financial profitability, thereby neglecting workers' well-being and bringing about the dramatic loss of power labor is presently undergoing (Fligstein and Shin, 2004). The prevalence of shareholders' interests over workers' rights and the attempt to minimize labor costs reinforced the negative effects on the quality of work life partially caused by the implementation of agency theory's prescriptions. The next sub-section provides further evidence of such negative effects.

The perverse effects of agency theory's prescriptions – when a false theory threatens to become true

There is a large amount of empirical evidence, collected by social psychologists and experimental economists, showing that agency theory's prescriptions – enhanced control, pecuniary incentives - may have deep deleterious and counterproductive effects. Instead of mitigating opportunistic behavior, they may actually create and enhance such behavior (Goshal, 2005; Roberts, 2005). The use of strict control devices signals to workers that they are not trusted, which may result in them becoming less trustworthy. Indeed, strict monitoring is shown to threaten the sense of personal autonomy, thereby damaging self-esteem and decreasing intrinsic motivation (Gagné and Deci, 2005). When workers are excessively controlled, intrinsic motivation is supplanted by defensive or self-protective processes such as the tendency to withdraw concern for others and focus on oneself (Deci & Ryan 2000). Workers then tend to adhere to more materialistic values and behave less cooperatively. Sheldon et al (2004) show that workers involved in controlling environments appear less satisfied at work and more focused on pay and benefits.

In the same vein, the use of monitoring tools by managers leads them to distrust workers and triggers a pathological spiral. These processes are well-known by psychologists: "Surveillants come to distrust their targets as a result of their own surveillance and targets in fact become unmotivated and untrustworthy. The target is now demonstrably untrustworthy and requires more intensive surveillance, and the increased surveillance further damages the target. Trust and trustworthiness both deteriorate" (cited in Goshal, 2005: 85). This problem also concerns top executives whose compensation schemes are recommended to be aligned with shareholder's interests. Many of the reforms set up to curb top executives' opportunism in the last decades ended up augmenting rather than diminishing the governance problem (Roberts, 2005). As Hannah Arendt (1958) brilliantly put, the danger with theories is not so much that they are false, it is that they may become true. In assuming that people behave opportunistically and are primarily motivated by pecuniary motives, agency theory may contribute to make people be just like that.

The management prescriptions that derive from agency theory, in which the relevant problems are those of agency costs and the relevant prescriptions are the design of devices able to restrain opportunism, may hence produce the opposite effect, undermining cooperative dispositions and intrinsic motivations. An alternative theory of the firm is needed, based on micro-foundations other than that of agency costs.

Elements for an alternative theory of the firm and required institutional framework

In accordance with the theoretical considerations made above, a meaningful theory of the firm would conceive it as a "system of cooperative services of *persons*" as well as the "sum of services of *individuals*", to use Barnard's terms (Barnard, 1938: 110, our italics). That is, the behavioral assumption to be put at the core of the theory of the firm should consider both the cooperative dispositions and the self-interested dimension of human behavior. The principal-agent relationship concept in particular must be revised: it must be assumed that it involves power (see later) and the (i)moral abilities of both parties.

Because it is considered a-moral, that is, rational as defined by mainstream economics, self-interest with guile is presumed compatible with a value-free theoretical framework. But there is in fact a hidden moral assumption behind the principal-agent model: workers are supposed to be loyal to principals (which they sometimes fail to be). By emphasizing opportunism, agency theory disguises the fact that morally-driven behavior is actually required on the part of workers. This moral dimension is explicitly acknowledged in labor law. Upon entering an employment relationship, the employee endorses the duty of loyalty and the obligation of obedience – within reasonable limits. Accordingly, the employer is entitled to "recover damages from a *disloyal* or *uncooperative*" employee (Masten, 1988:189, our italics). More generally, the law tends to impose fiduciary obligations in all principal-agent relationships, not only employment relationships. Recognizing that limiting agents' discretion, monitoring them, and aligning interests through incentive-compatible devices, does not suffice to enforce contracts, fiduciary law assigns agents the duties of loyalty and care (Sitkoff, 2011). Note that some duties and obligations are imposed on employers and principals as well.

This runs counter to agency theory's theoretical attempt to free principal-agents relationships from moral obligations but is consistent with firms' management rhetoric. Contrary to what agency theory assumes, real-world firms do expect workers to be loyal, conduct themselves in a trustworthy and cooperative manner and honor the non-contracted obligations inherent in incomplete contracts.

A meaningful alternative theory of the firm should hence explicitly acknowledge the moral dimension of human behavior – for the worst and the best, which has substantial normative consequences for how work is to be organized. While the norm of self-interest calls for devices aimed at restraining opportunism, the norm of cooperation requires that monitoring and control devices, though necessary, do not undermine trust and intrinsic motivations. It requires in particular that workers are entrusted with power and enjoy broad discretion to carry out their tasks.

Because it is the possibility of cooperation that justifies the existence of firms in the first place, prescriptions should focus on fostering cooperative dispositions rather than trying to economize on, and indeed discard, agents' moral and social capacities. Organizational studies show that the conditions that foster trust and cooperation rather than narrow self-interest include the existence of continuing and sustained interactions, collective along with individual rewards and moderate wage structures (Perrow, 1986). Such prescriptions differ radically from agency theory's.

But managerial perspicacity cannot be relied upon to prevent firms and workers from being caught ever more deeply in the paradoxes described above. There is no robust evidence showing that cooperative or participative firms are more profitable than exploitive ones. It may well be the contrary since the externalization of social costs may compensate for motivational losses. In fact, evidence shows that the failure of commitment models to yield the expected positive outcomes on productivity and workers is due to workers having insufficient decision-making power (Godard, 2004). Actually, a full implementation of the commitment model, if it is not to be manipulative, demands that much voice and power is given to workers. Which most employers are not prone to do since firms ultimately are means of controlling workers in the pursuit of their owners' interests. This asymmetry of power is overlooked in the principal-agent relationship, just as is the moral dimension.

The solution to the contemporary degrading of work can therefore not be purely organizational. Institutional changes that foster the workers' rights and challenge the shareholder primacy norm are called for. The required institutional innovations must reinforce the workers' rights rather than dismantle them - as is the case in the newly created "employee shareholder contract" in the UK (Prassl, 2013), for example. Entering into an employment relationship implies accepting inequality of power, which legitimates being controlled - *within certain limits* - but not being systematically distrusted. Just as workers can shirk on their effort, managers can shirk on their responsibilities. Institutional changes should be introduced in labor law that would be grounded on the recognition of the plurality of goals which legitimately exist in any organization and on how to organize voice in constructive ways. This would mitigate the imbalance of power embodied in the employment relationship with positive effects on the vulnerable condition of workers. It must be kept in mind that the workers' needs go beyond the extrinsic dimensions of work to encompass the whole psycho-social work environment.

To be effective, these changes in labor law should be necessarily accompanied by changes in corporate law that would i) challenge the ownership postulate and consequent legitimate goals and scope of responsibility and ii) promote the workers' participation in the corporate governing structures. Questioning the behavioral assumption that underlies mainstream economies of the firm hence leads to questioning also the two other agency theory's assumptions. It further leads to recognizing the need for juridical and economic institutions that would regulate firm governance - which is precisely what the launching of agency theory wanted (and succeeded) to avoid in the seventies (Gindis, 2013).

6. Conclusion

Our starting point was the observation of an increasing contradiction between management rhetoric - which tries to draw workers into a collective, cooperative endeavor - and management practices - which continually reinforce control and rely on individualistic, market-type incentives. We argue that the increase in this contradiction – itself inherent to capitalism - is associated to the widespread influence of agency theory, and specifically to its success in turning into influential normative models the basic assumptions on which it is grounded. Its conception of human agency, based on the assumption of self-interested, opportunistic, behavior, combined with the ownership postulate and the related governance prescriptions powerfully contributed to enhancing the pressure for financial profitability and labor costs reduction, thereby weakening the power of workers and degrading the psychosocial work environments.

We draw on the distinction between the concepts of *individual* and *person* to show that management rhetoric addresses workers as persons but actually organizes work as if workers were opportunistic individuals. While the concept of individual defines humans as unique and separate beings engaged in the pursuit of self-centered goals, the concept of person defines them as constitutively social, morally-endowed beings prone to cooperative behavior because of their need for gregariousness. We then show that cooperation, on which the well-functioning of modern productive processes depends, as management rhetoric indicates, requires the social and moral abilities of persons to be effectively established and sustained.

Agency theory's disregarding of the relational and moral dimensions of workers is consistent with its definition of firms as nexus of contracts, which equates social interactions at work to market interactions and denies the collective character of production. Like neoclassical economics, agency theory wants to free economic agents from – the vulnerability of – moral obligations and social ties. Its prescriptions, aimed at constraining and aligning self-interested individuals, powerfully molded the processes of individualization and depersonalization that mark contemporary work. Beyond their deeply deleterious effects on the workers' health and well—being, these processes are fostering the opportunism they were supposed to restrain.

Agency theory has profoundly shaped managerial practices; it has further contributed to disseminate a deeply negative vision of human intentions and behavior which, if not false, is neither true. Recognizing that the good working of firms and their creativity necessitates treating workers as persons rather than individuals, combined with accepting that shareholders cannot be said to own corporate firms, leads to questioning the legitimacy of the power of the owners of capital in corporate firms and thereby their governance structure and responsibilities. In order to coerce firms to be more consistent with their own rhetoric, major institutional changes are required.

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