Cowton, Christopher J.

Governing the corporate citizen: reflections on the role of professionals

FEGReG Working Paper 08/04

Governing the corporate citizen: reflections on the role of professionals

Christopher J Cowton
University of Huddersfield

Contact information:

c.j.cowton@hud.ac.uk
+44 (0)1484 473063

Financial Ethics and Governance Research Group

The Business School
University of Huddersfield
Queensgate
Huddersfield HD1 3DH
United Kingdom

Forthcoming in C. Luetge, J. Conill & T. Schoenwaelder-Kuntze (Eds.),
Corporate Citizenship, Contractarianism and Ethical Theory: On Philosophical Foundations of Business Ethics (Aldershot: Ashgate).

Governing the corporate citizen: reflections on the role of professionals

Christopher J. Cowton

Introduction

Professions and their members (or 'professionals') are a conspicuous feature of modern capitalist societies. They operate in many arenas, including the business realm. The starting point for this paper is that the degree to which professions and their members act ethically can have an impact on the ethical quality or behaviour of business in general. In particular, given the focus of this volume, my contention is that 'true' professional behaviour has the potential to impact upon the degree to which large businesses are 'good corporate citizens'. The aim of this chapter is to explore the nature of that potential, and to identify some of the issues involved in determining the degree to which that potential is realized.

The chapter is structured as follows. The section following this brief introduction makes some remarks about the term 'corporate citizenship', outlines the position to be taken for the purposes of the argument being presented, and links corporate citizenship to corporate governance The second section reviews the nature of professions, examines the debate over whether professions can be trusted to serve the public interest, and suggests that professions can vary in the degree to which they fulfil their social potential. The third section outlines the essential features of John Coffee's analysis of professional ‘gatekeepers’ to the corporate governance process. The fourth section then discusses the value of his work and relates it to an appreciation of the nature of professions. The fifth section concludes the chapter.

Corporate citizenship

The term ‘corporate citizenship’ has recently enjoyed a conspicuous rise in popularity, emerging ‘as a prominent term in the management literature dealing with the social role of business’ (Matten and Crane 2005, 166). Like many neologisms, however, it perhaps raises more questions than it answers. How should it be defined?[1] What is the relationship with other, also vague, terms such as ‘business ethics’ (see Lewis 1985) and ‘corporate (social) responsibility’ (CSR). In particular, what sorts of vistas does a focus on corporate citizenship open up that are not available via the other terms, and what does it close off? What kinds of behaviours might be associated with being a good corporate citizen? Given that a corporation can be *un*ethical or *ir*responsible, can it be a *bad* corporate citizen? Given that political theory distinguishes the citizen from the mere subject (Kymlicka 2005), does corporate citizenship inadvertently point towards increased rights for corporations rather than requiring a greater contribution from them? Does it even make sense to talk of a corporate citizen, when a citizen is normally taken to be an individual person?[2] I do not

---

[1] Indeed, how much value is there in attempts at universal definition? I share with Popper and others a certain scepticism about the essentialist concern with precision, the so-called ‘Platonic-Aristotelian theory of definition’ (Popper 1966, 21) – which is not to say that we should never attempt to ‘fix’ a definition for a particular purpose.

[2] This resonates with the familiar debate on the ‘moral status’ of the corporation (see, for example, Moore 1999).

wish to pursue these questions in any depth here, but I will stake out below an initial position sufficient to motivate the remainder of the chapter.

Of course, much of the power of the term *corporate citizen* derives from the concept of *citizen*, but that not only varies from nation to nation, it can also have remarkably little content. For example, the UK Government has been raising the issue of citizenship and, especially, promoting a notion of citizenship in the school curriculum, but for the ordinary Briton – perhaps because we do not have a written constitution – the term seems vague and unimportant, less important than nationality (with which it is often confused) and hence associated with issues of immigration, asylum-seeking etc – often in a negative way. To a British author, therefore, *citizenship* does not seem an ideal starting point for making real progress in encouraging good behaviour on the part of corporations.[3] Nevertheless, *corporate citizenship* has entered the vocabulary of business as readily in the UK as anywhere else, and it is accordingly worth taking seriously. And citizenship has been subjected to sustained examination in political theory. Other authors, represented in this volume, have already subjected it to rigorous and useful analysis, and with their help I will clarify my position for the purposes of this chapter.

Matten and Crane (2005) note that the usage of the term *corporate citizenship* has been neither consistent nor clear. In seeking to develop a more robust conceptualization, they identify and set aside two, broad conventional views. The first, which they term the 'limited' view, portrays corporate citizenship as concerned with charitable donations and

---

[3] Of course, the cynic with regards to corporate responsibility and the like might suggest that it is therefore an ideal point of departure, since it has little hope of getting anywhere!

other forms of community action, albeit perhaps in a more strategic way than has sometimes been the case in the past. The second, the 'equivalent' view, is so named because it is little more than a re-statement of CSR and thus essentially conflates the two terms. Against this backdrop, Matten and Crane then develop an alternative conceptualization that attempts to use the term *corporate citizenship* to generate some novel insights. Building upon an understanding of liberal citizenship (the principal template for Western democracy) they argue that corporations have taken over considerable responsibility from governments – including some responsibilities, in some circumstances, that amount to supporting citizenship. Recognizing the move they have made from the conventional view of the corporation *as* citizen to a position where the corporation to some extent substitutes for or complements the nation-state with respect to the individual citizen, they acknowledge that their conceptualization might better be termed '*corporate administration of citizenship* (as it were, "CAC")' (Matten and Crane 2005, 175, italics in original).

Whatever the merits of Matten and Crane's substantive point about corporations supporting citizenship,[4] their use of the term 'corporate citizenship' to denote their description of corporate activity supporting rather than *being* (or being like) citizenship seems misleading, as their invocation of "CAC" implicitly concedes. Moreover, their analysis leaves no room for the corporate citizen as such, since the corporation is now standing in for the nation-state rather than for the individual when a comparison is made with conventional understandings of citizenship. So can we still say something useful

[4] See van Oosterhout (2005) for a comment and Crane and Matten (2005) for the response.

about the *corporate citizen*? Matten and Crane's analysis would suggest not. First, their descriptions of the *limited* and *equivalent* views, where the corporation does stand in for the citizen, suggest that those views have nothing novel to offer – and may even be counterproductive as they contribute to conceptual confusion. Second, 'usage of the term *citizenship* here seems to be at least stretched, if not an outright misnomer' (Matten and Crane 2005, 174, italics in original).

Nevertheless, the term *corporate citizen* is widely used, and even if it does not appear to offer anything novel to our understanding of the social role of business, that does not mean that it is devoid of content. Moreover, in a separate paper for which both Crane and Matten were co-authors, the idea of corporations as citizens is explored in some depth via four models of citizenship from contemporary political theory[5] (Moon et al. 2005). The different models generate different perspectives on what might be meant by the term *corporate citizen*, but an underlying issue for any model of citizenship with respect to corporations is, as Moon et al. acknowledge, whether it is intended merely as a metaphor for what corporations are *like*, or whether corporations actually *are* citizens in some sense. It seems to me that the second is contentious, to say the least, but that the metaphorical usage is likely to enjoy wider and more easily justifiable support; it will also prove sufficient for this chapter.

Although Matten and Crane (2005) focus on the rights (social, civil and political) of citizenship, as van Oosterhout (2005) points out in his critique of their paper, obligations

---

[5] The four models are liberal minimalism, civic republicanism, developmental democracy and deliberative democracy.

are entailed too (see also Moon et al. 2005). This is where the citizen metaphor might have something novel or powerful to offer to the understanding of the social role of business. But this tends to beg the question: first, because concepts of citizenship and the obligations associated with them vary (again, see Moon et al. 2005); and second, if a corporation is only metaphorically a citizen, the metaphor cannot be used to force some set of obligations upon it, suggestive though such an analysis might be. Nevertheless, at the core of any conception of the citizen in a properly ordered nation-state is the obligation to abide by the rule of law, by which the rights of fellow citizens are in turn protected. Such law may be formalized and written down, or it might be conceptually extended to include unwritten expectations, such as widely accepted customs that have no need of legal underpinning. However, this is not an issue to be addressed here. The point is that adherence to standards enshrined in law, and perhaps custom, represents the minimum that should be expected of both individual citizens and corporations.

This is clearly a somewhat narrow formulation, consistent with the lower levels of Carroll's well-known pyramid (Carroll 1991) and even Friedman's dictum that a corporation should use its resources and engage in activities designed to increase its profits *so long as it stays within the rules of the game*. Nevertheless, adherence to the rules of the game is a necessary foundation for any more highly developed conception of corporate citizenship or responsibility. And, crucially for the concerns of this chapter, it is a foundational standard that is not always met. Of course, many corporations engage in misdemeanours from time to time, just as many ordinary citizens do, but what has been striking about the recent past has been the occurrence of cases where something rather more systematic seems to have gone wrong. Like the state of Denmark in Hamlet, there has been found to be something rotten in the corporate world. I am referring, of course, to notorious cases such as Enron, WorldCom and Parmalat, to name just three. What we have in these cases is not isolated examples of management negligence but, rather (according to most commentators), a more systematic failure of corporate governance.[6]

In recent times, much has been written about corporate governance (Stiles and Taylor 2001). As might be expected, attempts to define corporate governance are marked by difference and vagueness, and different writers draw very different boundaries around the subject (Keasey et al. 1997). However, for the purposes of this chapter, the well-known definition proposed by Monks and Minow (2001, 1) is a good starting point: 'the relationship among various participants in determining the direction and performance of corporations'.[7] Although attention might be paid to other stakeholders,[8] those focused upon tend to be what Monks and Minow refer to as the three 'legs' of the corporate 'tripod' of 'primary' or 'direct' participants – the shareholders, the management (led by the CEO) and the board of directors. This aligns well with Klein and Coffee's (1988, 118) three 'basic groups' of shareholders, directors and officers, and with many other discussions of corporate governance. However, they are not the only parties relevant to corporate governance; as Coffee (2006) notes, they are surrounded by professionals who act as 'gatekeepers'. The following section examines the nature of professions and what might be

[6] This is not to imply that there have not been failures of corporate governance before, of course.

[7] This may be amplified with reference to Tricker, who usefully distinguishes governance from the management of a company: 'If management is about running business; governance is about seeing that it is run properly' (Tricker 1984, 6).

[8] For example, creditors – see Cowton (2006) and Davies (2002).

expected from them, before presenting and discussing Coffee's particular analysis of their gatekeeping role in corporate governance.

Professions

The term 'profession' is generally employed quite loosely in everyday speech,[9] being used to refer to any, or almost any, occupational group. However, it has a narrower, more technical sense when used by sociologists. In distinguishing professions proper from other occupational groups, sociologists highlight some characteristics that professions are expected to possess. Even though the list of features, their relative importance, and hence the related criteria for demarcating between professions and other occupational groups, are subject to considerable debate in the literature, there is enough agreement to provide a basis for taking forward the argument of this chapter.

A good starting for present purposes is the definition provided by Jary and Jary (1991, 501): 'A profession is any middle class occupational group, characterised by claims to a high level of technical and intellectual expertise, autonomy in recruitment and discipline, and a commitment to public service.' The idea of a commitment to public service represents an opening for relevant professions to play their part in ensuring sound governance of the 'corporate citizen', but it should be noted that the first three elements also have potential implications – positive and negative – for the way in which professions operate and the degree to which they might come to meet the public interest.

[9] I am not suggesting that such ordinary language usage is necessarily wrong and in need of correction, but for the purposes of this paper a more restricted sense will be more appropriate.

Jary and Jary's definition captures many of the important features of a profession. Although it is not easy to be comprehensive in describing either 'a profession' or 'professional work', the literature (e.g. Abbott 1988) tends to agree on the importance of the following characteristics, all or most of which will need to be present for an occupational group to be considered a profession:[10]

- there exists a widely agreed and extensive specialist skill and knowledge base, the latter often of a relatively theoretical or abstract/intellectual kind;
- acquisition of the requisite skill and knowledge base involves a long period of training, with formal certification of competence (usually involving written examinations) and, frequently, some form of licence to practise;
- the deployment of the knowledge base involves the use of discretion and (professional) judgment, not just the application of rules to routine circumstances;
- independence and self-regulation are jealously guarded, with control over the requisite knowledge base, setting of entry standards and criteria for membership, and responsibility for the disciplining of members;
- there are ethical codes (often formal, but not exclusively so), independent of contract or state law, and these are self-enforced;
- in many cases, high levels of personal and financial reward.

The classic examples of professions that meet the above criteria are medicine and the law, but the increased complexity and level of development of societies and economies has

[10] It might be better to view this list as being indications of family resemblance (see Wittgenstein 1958) rather than providing the basis for an essentialist definition.

thrown up new occupational groups that have aspired to professional status. A good business-related example, of clear pertinence to corporate governance, is accountants. Although accountancy in some form or other can be considered to be as old as writing itself, and although during the Renaissance in double-entry bookkeeping it reached a level of sophistication that has continued to prove invaluable into the modern era, the 'professional project' of accountants can be seen to have begun with the formation of professional associations in the UK in the nineteenth century. It was with the establishment of such bodies that many of the professional characteristics listed above came to be claimed and enacted by accountants.

It is worth noting that, in addition to the abstract notion of a profession, there are other, related concepts that will prove useful in the development of the argument of this paper, especially the 'professional association' or 'professional body'. This is the institutional form of a profession, responsible for things like the stipulation and examination of a requisite body of knowledge and the disciplining of its accredited members. In some cases there will be a single body covering a profession, although there may be complementary, more specialist professional associations to deal with particular sub-disciplines; both medicine and engineering provide good examples of this. In other cases the situation may be rather more complex. For example, in the case of accountancy, in spite of some mergers over the years, there are still several different UK-based professional bodies which differ, to some extent, in their geographical or professional focus but which, nevertheless, overlap considerably.[11]

[11] The membership of the Consultative Committee of Accountancy Bodies (CCAB) in the UK is:

Professional bodies also differ in the extent to which they control their domain of activity. In some cases they have *de jure* control, through legislative or other regulatory backing. In these cases, regulations will state that only members in good standing with a particular professional body (or bodies) will be qualified to undertake a particular task (e.g. the audit of a particular type of organization). In other cases professional bodies will have *de facto* control or very strong influence. On the other hand, some professional bodies – perhaps representing occupational groups which still aspire towards generally recognized, full professional status – might represent their members and provide services and a level of desirable accreditation etc, but their control over areas of activity and jobs will be much more limited. In a UK business context, examples might include the Chartered Institute of Purchasing and Supply (CIPS) and the Chartered Institute of Marketing (CIM).

Note, however, that both CIPS and CIM have managed to acquire the word 'Chartered' in their title; a feature of the 'professional project' is emulation. Just as the British Chartered Accountants of the nineteenth century sought to form professional partnerships akin to those of doctors and lawyers and thereby avoid being employed or 'in trade', so occupational associations with professional aspirations have sought the prestige in the UK of being 'chartered', which involves a successful petition to the Privy Council. Professions therefore may have social aspirations and projects, though these are likely to be

---

ACCA Association of Chartered Certified Accountants

CIMA Chartered Institute of Management Accountants

CIPFA Chartered Institute of Public Finance and Accountancy

ICAEW Institute of Chartered Accountants in England and Wales

ICAI Institute of Chartered Accountants in Ireland more culture-specific than their economic aspirations. Thus the notion of being 'chartered' means little or nothing in many countries, whereas it is hard to imagine a professional body in any country not being interested in the earnings potential of its members.

A further, more universal element in aspiring to professional status is the claim to public service, mentioned earlier as a key characteristic of professions. Such a claim is typically backed up by the presence of ethical codes of practice or similar statements of behavioural expectations, in addition to the required technical aspects of functioning as a professional expert. There are connected, since the technical expertise of the professional provides opportunities for exploitation of the lay person.. This would appear to make professions ethically admirable and socially advantageous, and therefore ideally suited to promoting and supporting good corporate citizenship. However, not all writers on professions view their actual contributions in such a positive light.

As indicated earlier, there is much debate about the definition of a profession, but it can be argued that the interesting question is not whether an occupation *is* a profession, but why and how an occupational group *turns itself into* a profession and its members into 'professional people' (Johnson 1972, 31). According to many commentators, a major part of the professional 'project' is the pursuit of economic advantage. Indeed, as noted earlier, one common feature of professions is the earning power of their members. This may involve an attempt to secure monopoly in the market through the establishment, protection and extension of an effective monopoly jurisdictional claim (Reed 1992); or, at least, a profession might seek to secure a privileged position in a market or markets, even if an

---

ICAS Institute of Chartered Accountants of Scotland exclusive monopolistic position is not attainable.[12] Professions also tend to secure control of entry into the profession itself, thus ensuring not only quality – which might be a reasonable justification – but also restricted supply. Given the demand for its services – which many professions will also seek to stimulate – the restriction of supply of accredited professionals serves, as prices would behave in any market, to push up remuneration.

Thus not all observers are convinced that professions really do serve the public interest; quite the contrary. For example, there have been sustained Marxist and, more recently, consumerist critiques of professions' protection of their privileged position to their own advantage.

Moreover, as mentioned earlier, the professional project is pursued not only in the economic order but also in the social order (Macdonald 1995; and see the reference to 'class' in Jary and Jary's (1991) definition, quoted earlier). The aim is 'upward social mobility' (Parry and Parry 1976), with an occupational group seeking to attain collective social status (Larson 1977) and respectability. Thus, for example, both expertise *and* respectability were central to launching the British professional accountancy project in the late nineteenth century (Macdonald 1995).

Of course, different cultures will have different symbols to indicate social standing, and it is likely that the UK has been focused more than many other countries on social symbols rather than just earning power. Even within the UK, there are variations. As Parry and Parry (1976) note in their study of the rise of the medical profession, in the USA and Continental Europe the dominant image of professionals has been that of successful, expert money-earners. In England, they argue, professions have stressed the notion of acting as

[12] See the earlier reference to de jure and de facto control.

the elevated servants of their fellow-men, an emulation of the 'gentleman of private means', resulting in a gradual claim to that status. Macdonald (1984) argues that the achieved status of the accountancy profession in Scotland was endorsed by the respectability of ascription because its leaders were associated with the gentry, the legal profession and the more respectable (commercial, as opposed to manufacturing) part of the bourgeoisie. That they achieved recognition and 'professional' status earlier than in England can be attributed, in part, to the culture, social structure and stratification system of Scotland in the eighteenth and early nineteenth centuries. For example, the landed gentry and the legal profession were closely related.

Thus the balance of economic and social objectives within 'professional projects', and the manner in which the social objectives are pursued, will vary from one culture to another. Nevertheless, the negative assessment of professions – whatever the particular intellectual form it might take – is that they are fundamentally self-interested endeavours focused upon attaining privilege, and that claims to ethics and serving the public interest are either fallacious or, at best, a misleading 'sideshow'.

Such critical views of professions can be set against not only the claims of professions themselves to serve the public interest, but also earlier sociological analyses of the professions, which seemed content to accept them largely on their own terms and which painted a positive picture of their contribution to society. Indeed, many of the critical analyses were, at least in part, a reaction to the functionalist analysis of professions, which dominated the sociological literature until the early 1970s (Macdonald 1995). As such, they were probably a useful challenge and corrective, but I think there are reasons why they might be considered to be problematic in some important respects. I wish to make three connected points. The first is that the critical perspectives on professions often carry intellectual baggage, or argue from a general perspective, that might itself be considered to be flawed. However, I do not wish to pursue that issue here, not so much because it is beyond the scope of this paper (though it is), but because some of the problems of professions to which they point are nevertheless plausible risks, even if some of the implications might be less attractive. Second, notwithstanding some fascinating and insightful studies of individual professions, particularly more recently, much of the traditional debate treats professions in a homogeneous manner. Such 'totalizing' discourses leave little or no room for considering whether some professions, in some places or circumstances, at some times, are less prone to abusing their privileged position or, indeed, are even of significant public benefit – albeit that members continue to reap considerable economic and social rewards. My contention is that the actual contribution of a particular profession is a contingent matter, not an inevitability. Third, if there can indeed be variation in the social contribution that professions make, then it is worth considering how that can occur and how it can be encouraged – a strategy that general sceptical arguments about professions will tend to suppress or ignore. Thus it is necessary to overcome the intellectual barrier of seeing professionals themselves gaining, at some level, from the professional project if not from each individual action; it is vital to recognise the importance of positive-sum games in modern economic life, rather than viewing everything in terms of zero-sum games, which might be said to have characterised pre-modern economies (Luetge 2005).

Thus, the relation between professions and the public interest is a contingent, not a necessary, one. It is to be empirically assessed as well as theoretically informed. There might be pressures or temptations that push professions towards or away from adequately serving the public interest, but the actual outcome is not uniform and inevitable. If professions do live up to their rhetoric on ethics and public interest, at least to a significant degree, then so much the better. If we are to have professions, that seems to me a desirable position to aim for. One of the important reasons, as Davis (1997) makes clear, is that a code of professional ethics must require something that ordinary morality merely permits in order to have real value. It should be 'higher' or more demanding than ordinary morality. 'Professions carry with them *special* obligations that members of that profession take on, both individually and collectively.' (De George 2006, 93, emphasis added). This seems to open up the possibility of professionals making a distinctive contribution, or set of contributions, to the governance of the corporate citizen.

However, a recent influential analysis casts doubt on this positive vision. Indeed, it sets the shortcomings of professionals firmly at the centre of some of the most notorious corporate failures of recent years. It is to John C. Coffee Jr.'s book, *Gatekeepers: The Professions and Corporate Governance*, that I now turn.

Coffee's gatekeepers

The starting point for Coffee (2006) is that, useful and necessary though previous research by scholars of corporate governance has been, it leaves a blind spot: namely, the professional agents who inform and advise boards of directors. His thesis is that all boards are prisoners of their professional advisers. For this reason, focusing on the board of directors when things go wrong, or calling for higher ethical standards, is almost to miss the point. Boards of directors have been extensively reformed and, in Coffee's opinion, are now more independent and hard-working than ever. While there is room for improvement, they are probably the party 'least responsible' for the corporate scandals that erupted in the early years of this century. A more productive focus is the professional advisers who act – or should have acted more effectively – as 'gatekeepers'.

In employing the term 'gatekeeper', Coffee is referring to an independent professional who plays one of two distinct roles: preventing wrongdoing by withholding necessary cooperation or consent; and – a superior conception, according to Coffee – acting as a reputational intermediary to assure investors regarding the quality of the 'signals' sent by the corporation. The intermediary pledges the reputational capital that it is has built up over the years through repeated episodes with different clients.

An auditor expressing a professional opinion on the corporation's annual accounts is an obvious example – indeed, auditors have received much criticism in relation to the recent cases that exercise Coffee's interest – but he also has in mind attorneys, securities analysts, credit-rating agencies and investment bankers. All these parties are in a position to alert investors and others to inadequacies in the governance of a corporation. In observing and commenting on the corporation (e.g. through opinion, rating or even just being willing to work with it), the gatekeeper is lending or pledging its own reputation. Its reputation is, in effect, a hostage. Since reputation is central to the adviser's ability to earn money in relation to a larger set of corporations, its 'comment' on the individual corporation may be taken seriously. Its self-interest in relation to its reputational capital gives a degree of confidence in the quality of the signals it provides about the corporation. 'The gatekeeper is trusted to the extent that it is a repeat player who possesses significant reputational capital that would be lost or depreciated if it were found to have condoned wrongdoing.' (4) This will be expected to happen as long as the reputational loss exceeds the one-off gain from connivance, and this can take place in the absence of legislation. The stronger the reputation, the more highly sought will be the adviser's services as a gatekeeper.

That, at least, is the theory. Of course, Coffee is interested in how this reputational model has come not to work, or to work much less successfully than it once did, and hence has led to, or permitted, the kind of corporate governance crises that we have witnessed in recent years. For example, in the 'iconic' cases of Enron and WorldCom, what happened to the gatekeepers? Why did the watchdogs not bark? As he sums up towards the end of the book, the central mystery is: 'Why did gatekeepers risk, or even willingly sacrifice, reputational capital that they had diligently amassed over decades?' (317) He groups his answers under: competitive environment; conflicts of interest; and the market for reputational capital.

Although they face incentives to do so, gatekeepers will not always seek to protect their reputational capital.

> Circumstances can arise in which it is rational to risk that capital. Particularly in concentrated markets, the rational gatekeeper may recognize that it does not need an unblemished record, but only one not significantly worse than its rivals. Indeed, if its rivals have tarnished records, while it instead resembles Snow White, it arguably has made an excessive investment in reputational capital on which it will realize little return. (333)

Coffee is pointing out that, since reputation is, competitively speaking, a relative thing, rather than competing to enhance their reputations, gatekeepers might permit their reputations to become noisy and indistinct, as long as entry of new competitors is restricted.

This is clearly a problem in terms of credit-rating agencies, which are few in number. It also applies, perhaps more worryingly, to auditors. Coffee comments: 'From an industrial organization perspective, the most striking fact about accounting as an industry is the degree to which it has recently consolidated' (158); the Big Eight of the 1980s has, twenty years later, reduced to the current Big Four,[13] responsible for the audit of most large corporations. 'Indeed, because each of the Big Four tends to have a different specialization, focusing on different industries, there is even less competition than the name 'Big Four' implies. Within a particular industry, the dominant firm may have only one true rival – if that.' (159) Thus the demise of Arthur Andersen following the Enron debacle has served only to reduce competition still further. It has also shown in graphic terms how reputational incentives can become overwhelmed by other forces.

Reputational self-interest is limited, according to Coffee, especially because the party paying the gatekeeper is typically the party being monitored – not the parties that have most to gain from the gatekeeping function being performed well. This hasn't always been the case, at least not for all gatekeepers. For example, credit rating agencies now receive most of their revenue from the corporation being rated rather than from the user of the information. One of the factors that brings this about is that – through its influence on the corporation's cost of capital – the credit-rating agency creates value for the corporation. This leads to pressure on the rating agency 'because of the devastating consequences of a rating downgrading' (35). It is thus no surprise that the pattern in ratings downgrades often resembles more 'obituary' than 'prophecy'. Indeed, credit-rating agencies maintained a high rating for Enron until the last days.

In the case of auditors, they are notionally appointed by the shareholders, but in practice it is senior management that is primarily responsible for their engagement. The

13 PricewaterhouseCoopers (PwC), KPMG, Deloitte and Ernst & Young.

role and independence of audit committees has been strengthened over the past decade or so (Enron had one that looked good on paper), but against that, the audit has become just one of a package of services provided by the firms. This is Coffee's principal concern about auditors.

Coffee points out that, as early as 1984, consulting revenues were greater than auditing revenues at Arthur Andersen. In other words, non-gatekeeping services were earning more money that auditing, and this helped to replace an older 'professional' culture with a 'business' culture. Audit partners had strict targets for cross-selling non-audit services – making them more salesman than watchdog. The firm's Professional Standards Group, which provided guidance on whether or not certain accounting treatments were permitted, was downgraded to the extent that local partners could overrule it. Some have used empirical evidence to suggest that non-audit services don't have a negative effect on audit quality, because no statistical relationship has been found linking the two. However, Coffee argues that 'the real conflict lies not in the actual receipt of fees, but in their expected receipt' (66). In other word, a firm *hoping* to sell non-audit services, not just fearing their loss, might not be as rigorous in its audit as it should be. Thus, accountancy having successfully distinguished itself from the more clerical task of bookkeeping only by stressing its need for independence and its duties to third parties, and thus becoming the 'paradigmatic gatekeeping profession' (103), accounting firms increasingly turned themselves into information consultants, with deleterious implications for their independence.

Coffee naturally asks, ‘Why were such obvious conflicts tolerated?’ (163) The only answer that he finds plausible is that the major firms feared neither regulatory sanctions nor reputational injury from violation of ‘technical’ rules.

> Reputational injury was less of a consideration because their business strategy was to develop their relations with existing clients, rather than market themselves to new clients based on a reputation for high integrity. In this light, accounting firms had little to fear from the disclosures that they had grown too close to their clients. This would not offend their clients, who by definition already know of these relationships. (163)

Such an environment favoured the audit partner skilled at marketing but provided less favourable conditions for the more technically skilled[14] partner. Coffee notes that, in a context where growth was through non-audit revenue, auditors also faced a decline in expected liability costs because of legislative developments and legal decisions, at the same time as they experienced an increase in managerial pressure because of the massive increase in equity-based compensation for executives. Hence the diligence with which they carried out their gatekeeping role was compromised.

Coffee also notes the impact of the stock market bubble, which tends to affect all gatekeepers: they become less relevant and experience a decline in their leverage over clients and the value of their reputational capital. Gatekeepers and their warnings tend to be valued more when investors are more cautious and sceptical. This helps to explain why other gatekeepers, including securities analysts, did not provide an effective substitute for auditors or were not able successfully to call attention to their apparent shortcomings. Indeed, stock market bubbles pose a special problem for securities analysts, for the cautious ones will be outperformed for as long as the bubble lasts.

Securities analysts also failed to warn investors that auditors were conflicted because they, too, were not in a sufficiently independent position. For example, investment banks earned massive underwriting fees from Enron, which would have been put at risk by adverse comment. But there was more than this going on. For example, a bad opinion from an analyst can prompt a corporation to retaliate by excluding the 'disloyal' analyst from the steady stream of non-public material provided by the corporation, thus putting the analyst at a material disadvantage. Moreover, although securities analysts are critical gatekeepers in capital markets for testing and interpreting corporate disclosures, they are distinctive in several respects, such as having underdeveloped standards and facing limited regulation. On the sell-side, at least, there is a suggestion that they are little more than 'a conspiracy of snake-oil salesmen'.

In these and other ways, the lack of transparency surrounding Enron and other corporations seems attributable less to a single gatekeeper that failed and more to the 'absence of any true gatekeeper in the disclosure process with real responsibility and authority' (34). What was needed – and what was largely absent – was a professional able to express an *independent* judgment about the appropriateness of the company's financial statements. Coffee's analysis suggests that truly independent opinions on corporations were generally in short supply. His suggestions for dealing with this situation and my comments on his analysis and proposed solutions are the focus of the next section.

Discussion

The previous summary of Coffee's book did not seek to describe every avenue he explores: for example, it did not examine his comments on attorneys or investment bankers.

---

[14] and independent-minded.

However, it attempted to summarise the principal elements of his analysis, and in this section I wish to highlight briefly what I believe to be his most important contributions before moving on to discuss some respects in which his analysis might warrant further development, particularly bearing in mind the earlier section of this chapter dealing with professions.

Coffee's is a very persuasive analysis, displaying a keen awareness of legal, economic and historical factors. He recognises the difference that the structure of share ownership can make, focusing his attention on the dispersed ownership pattern characteristic of many large US corporations and acknowledging the different governance risks that the concentrated ownership traditionally associated with continental Europe tends to bring about. Of course, since he is working from a particular set of events, he is always likely to come up with an explanation that 'fits' his description of them. Nevertheless, there are real and useful insights. Undoubtedly, one of the key points that Coffee's analysis demonstrates is that more attention needs to be paid in both academic and policy discussions of corporate governance to the professionals who surround the parties normally focused upon – the shareholders, the board of directors, and management. Even if rhetorical flourishes such as describing boards as the 'least responsible' for governance failures and as 'prisoners' of gatekeepers might seem too strong, it is nevertheless the case that broadening the field of analysis in this way is a valuable step. Of course, auditors have – recently, and in the past – been much discussed in relation to corporate governance failures, but Coffee's analysis adds something in identifying them as just one gatekeeper among many. He performs a valuable service in pointing out that there is a whole set of highly expert occupational groups surrounding the corporation. Where one gatekeeper does not do its job properly, it might be hoped that another might make up for its inadequacies. Coffee, by taking a broader view of gatekeepers, both points to their importance for sound corporate governance and alerts us to the position that they have come to find themselves in.

Furthermore, while previous historical and economic work has demonstrated that legislation is not necessary to generate a demand for audit, Coffee succeeds in showing the importance of reputational capital,[15] which – in his hands – not only explains how audit quality can vary from firm to firm and over time, but also is something of relevance to other gatekeepers. Most important, he explains how gatekeepers can collectively come to fail.

Coffee's focus on gatekeeper failure might seem to bring him into line with the critical perspectives on professions, discussed earlier. In effect, he sees the professions' behaviour as being driven by private gain which leads, in due course, to damage to the public interest. He does not seem to doubt the expertise of the groups he examines so much as the manner in which that expertise is deployed. Yet in highlighting the particular problems of the recent past, he implicitly points to better times in the more distant past. Furthermore, his historical perspectives and, in particular, his understanding of reputational capital, show that he is not unremittingly negative about professions. Coffee recognises that the dynamics of reputational capital can accomplish a great deal – sometimes. In that sense, his analysis is more in keeping with the position reached at the end of the earlier section on professions: that the relation between professions and the public interest is a contingent, not a necessary, one. In pointing out the differences in gatekeeper behaviour

15 A concept familiar to many scholars of corporate citizenship, of course.

over time and the underlying dynamics relating to reputational capital, Coffee gestures towards the possibility of a better future. So what does he propose doing?

Given the detail and confidence of his earlier analysis, Coffee's proposals are surprisingly general and tentative – though perhaps that is a general feature of academic writing. For example, in the case of securities analysts he states:

> The bottom line then is that for the securities analyst to perform as an honest gatekeeper, two linked problems must be solved that have persisted …: (1) analysts must be protected from retaliation, including pressures from the buy-side and issuers, and not just from pressures within the investment banking firm (which is the only context that Sarbanes-Oxley addresses); and (2) a means must be found by which to subsidize research in the case of the smaller cap market without that subsidy distorting the research. (273)

At which point the chapter ends!

Coffee's general belief, though, is that 'gatekeepers work well only when their performance is subject to effective monitoring' (354). Given that much of his analysis, like most corporate governance work, draws on agency theory, even if only informally, it is perhaps not surprising that his main proposal is that the gatekeepers, as agents, should be brought under the control of stronger, more effective principals. Thus the most promising reform would be to re-establish a direct principal-agent relationship between investors and their gatekeepers, but where shareholdings are widely dispersed, he acknowledges that this is easier said than done. Since 'true' principals for the gatekeepers are hard to find, he suggests that the audit committee may be 'the strongest monitor one can find for the auditor, attorney, or investment banker.' This seems a somewhat half-hearted proposal, but this is understandable when it is remembered, first, that he earlier said that the board – of which the audit committee is a sub-committee – was probably the 'least responsible' for recent governance problems; and second, that he also pointed out that Enron possessed what appeared to be a good audit committee. It has to be admitted that he did criticise the operation of Enron's audit committee, but his criticism – based on time spent in meetings – is not entirely convincing (members might have done a great deal of preparatory work outside formal meetings) and, more significantly, if Enron's potentially strong audit committee was not effective, what is to give us any confidence that others will be? This is not to suggest that audit committees, and further development of their role, would not be worthwhile, but it seems more is needed from Coffee, particularly given his apparent lack of enthusiasm for his proposal – which he does not develop at any great length.

One avenue that Coffee does not explore is dealing with the gatekeepers as professions. Although the title of his book refers to 'the professions', it will be apparent from the earlier discussion of this chapter that some of the parties that he analyses would not normally be viewed as true 'professionals'. Indeed, Coffee clearly recognises this. For example, he states that the credit-rating agency 'merits examination, *even if the few entities engaged in this work do not amount to a full-scale profession*' (103, emphasis added). If the matter were simply one of definition, perhaps not much would hang on this point. However, Coffee fails to take advantage of the possibility of paying some attention to proper professional bodies, which are associated with some of the parties he examines, as a possible lever for influencing behaviour. Instead, he focuses all his attention at the level of the firm. Given the lack of both specificity and confidence of his proposals, it seems worth exploring professional bodies, where they do exist, a little further.

This is not to imply that Coffee is unaware of professional bodies. He has a very interesting chapter on the history of the accountancy profession, for example. Indeed, it may be the case that his assessment of the behaviour of professional bodies leads him to conclude that there is no point looking in their direction for any help in improving the behaviours of the gatekeepers within their jurisdiction. 'In principle, professional discipline could substitute for private or public enforcement in order to maintain professional standards.' (156) However, in the case of accountancy – which is one of the more developed 'professional' groups he considers – he notes that it was always characterised by weaker professional control from the outset in the United States than in Great Britain, because it lacked control over both entry and exit.[16] This meant that 'from its earliest days, the profession undertook only a relatively toothless form of self-policing' (116).

Nevertheless, while he believes that the accountancy professional bodies have been weak watchdogs, he describes them as an effective guild. For example, he describes how the American Institute of Accountants (AIA) and the American Society of Certified Public Accountants (ASCPA), long fierce rivals, merged in 1937 in order to better resist the dangers of a federal takeover by the SEC. This helped the accountancy profession to achieve the two goals that it has consistently pursued over its century-long evolution. First, it has sought to acquire and preserve professional autonomy (though how many professions would not seek to do this? As explained earlier, it is one of the characteristics that serves to mark out an occupational group as professional.) Second, it has sought to limit its gatekeeping responsibilities.

Given this overall characterisation of the accountancy profession – that it resists demands from the state and yet poorly disciplines its own members to meet those restricted

[16] He also views peer review as ineffective, 'producing just review and more review, with no meaningful sanctions being imposed' (p.157).

demands – it seems surprising that the accountancy profession enjoys any status at all. This empirical observation must stand as a challenge to the completeness and fairness of Coffee's analysis. Another important point to note, particularly given the interest of this section in Coffee's proposals for improvement, is that his contrasting of the US and British accountancy professions reinforces the earlier insight that the contribution of professional bodies is a variable; and being variable, it is subject to influence. Moreover, although he does not describe it in such terms, it is clear that where true professional bodies exist that relate to his gatekeepers, he sees strategies and strategic choice at work. The outcomes are not determined wholly by the structural features of the context. Again, this points to the possibility of influence, presumably by the state or its representative.

Perhaps, though, Coffee would see little potential here. Although he does not examine this avenue in any depth, he does conclude from his analysis of the accountancy profession that professions are difficult to regulate, even when the political will to do so exists. His reasoning is that few agencies 'can claim to possess the broad expertise necessary to adopt comprehensive rules governing a profession, and thus regulators are predictably forced to defer to the profession on most technical questions' (130). This seems unconvincing. First, regulators can acquire expertise but, more important, they can and should work at a more general level, setting the agenda and monitoring outcomes; they don't need to get into the most abstruse technical detail. If 'out-sourcing' to professional bodies – for so it can be seen – is going to be worthwhile, regulators should not become involved in technical detail. Second, just because it is difficult to control professional bodies does not mean it is impossible to influence them. And since Coffee hasn't come up with a convincing solution to the challenges of corporate governance that he has delineated, it is worth thinking further about how this might take place.

In order to pursue the possibility of influencing gatekeepers through professional bodies, I suggest that a more sophisticated understanding of professions is needed than that offered by Coffee. Just as Coffee redrew the map of corporate governance to include gatekeeping professionals, so too, the complexity of the professional terrain needs to be appreciated. This should include insights from the sociology of professions, which was briefly reviewed earlier, and a more sophisticated appreciation of the way in which professional bodies operate. This should include a recognition of factors such as:

- the tensions that can develop between professional firms and professional bodies, which themselves suggest that professional bodies do put firms under pressure;
- the ways in which professional bodies' and professional firms' respective reputational capitals are mutually dependent; and
- the possibility that professions can, to some degree and in their own particular ways, act as substitutes for one another – which in turn opens up for regulators the option of playing one off against the other.[17]

Such an expanded understanding of professions should also recognise social as well as economic rewards. Coffee focuses on the economic, perhaps because of his US perspective or his dominant intellectual perspective, or both.[18] Yet, as explained earlier,

---

[17] There is much historical evidence of how professions have competed with each other as they have sought to redefine their domains of expertise and activity. Note, too, the overlapping – and hence, to some extent, competing – UK professional accountancy bodies referred to in an earlier footnote.

[18] One of the few purely social points that Coffee makes is that accountancy's middle-class, 'democratic' status means that it has 'little of the sense of noblesse oblige that characterizes a profession with more aristocratic aspirations' (p.146).

professional strategies take place in the social as well as the economic realm, which expands the range of levers that regulators are able to pull, though these are likely to be more culture-specific in their range and effects than economic levers.

One way of characterising what I am suggesting is that we ought to consider professional bodies as the gatekeepers' gatekeepers, thus responding to the ancient question "Qui custodiet custodiens?"[19] Or, to put it in other, Coffee-esque terms, I am suggesting that the state and its regulators should, if necessary, seek to be a stronger 'principal' to the professional body 'agents'. In doing so, rather than simply calling for professions to be more ethical, the most productive way will be to so structure conditions that they encourage behaviour which is in both the professions' own interest and the public interest (see Luetge 2005). No single measure, or even source of measures, will ever be sufficient. A perfect and permanent equilibrium is not achievable. But given the paucity of Coffee's own proposals, to ignore professional bodies as amenable to influence by the regulators seems a missed opportunity. Of course, some of Coffee's gatekeepers do not have associated professional bodies, but that just serves to emphasise one of the limitations of his analysis and the benefits of a fuller appreciation of the term 'professional'. Furthermore, it suggests the option for regulators not just to seek to influence existing professional bodies but perhaps also to encourage the establishment of professional standards and associations in those areas of gatekeeping not currently professionalised.

[19] Who will guard/watch the guardians/watchmen?

Conclusion

This chapter has argued that, whatever corporate citizenship is normatively held to entail, sound governance is necessary. A good corporate citizen is a well governed corporation. Experience suggests that, even within the conventional system – focused on shareholders, boards of directors and management – good governance is far from guaranteed. John Coffee's work demonstrates the importance of 'gatekeepers' and reputational capital to the corporate governance process, and his analysis provides useful insights into how professionals have come to be less effective in their gatekeeping role than they once were. His suggestions for making those gatekeepers more effective in the future, though, are surprisingly vague and tentative.[20] It is argued here that a fuller appreciation of the nature of professions and their strategies offers the prospect of a complementary way forward, providing other options and hence more chance of success. Such an approach would take seriously both the rhetoric of professions and the risk that they don't live up to it. Perhaps, with the encouragement of *professional* citizenship, corporate citizenship will find itself on a firmer footing.

[20] A similar criticism might be made, I suppose, of my own suggestions, though in defence I would point out that they were simply the final part of a chapter-length argument, not the conclusion of a book-length analysis.

References

Abbott, A. (1988), *The System of Professions* (Chicago: Chicago University Press).

Carroll, A. B. (1991), 'The Pyramid of Corporate Social Responsibility: Towards the Moral Management of Organizational Stakeholders', *Business Horizons* July-August, 39-48.

Coffee, J. C., Jr. (2006), *Gatekeepers: The Professions and Corporate Governance* (Oxford: Oxford University Press).

Cowton, C.J. (2006), 'Creditors: The Forgotten Third Party in Corporate Governance Debates?', paper presented at the Fourth Transatlantic Business Ethics Conference, The Wharton School, University of Pennsylvania, 6-7 October 2006.

Crane, A. and Matten, D. (2005), 'Corporate Citizenship: Missing the Point or Missing the Boat: A Reply to van Oosterhout', *Academy of Management Review* 30:4, 681-4.

Davies, P. (2002), *Introduction to Company Law* (Oxford: Oxford University Press).

Davis, M. (1997), 'Professional Codes', in P. H. Werhane and R. E. Freeman (eds.), *Encyclopedic Dictionary of Business Ethics*, 514-5 (Malden, MA: Blackwell).

De George, R. T. (2006), *Business Ethics*, 6th Edition (Upper Saddle River, NJ: Prentice Hall).

Jary, D. and Jary, J. (1991), *Collins Dictionary of Sociology* (Glasgow: Collins).

Johnson, T. (1972), *Professions and Power* (London: Macmillan).

Keasey, K., Thompson, S. and Wright, M. (1997), 'Introduction: The Corporate Governance Problem – Competing Diagnoses and Solutions', in K. Keasey, S. Thompson and M. Wright (eds.), *Corporate Governance: Economic, Management, and Financial Issues*, 1-17 (Oxford: Oxford University Press).

Klein, W. A. and Coffee, J. C., Jr. (1988), *Business Organization and Finance: Legal and Economic Principles*, 3rd Edition (Westbury, NY: Foundation Press).

Kymlicka, W. (2005), 'Citizenship', in T. Honderich (ed.), *Oxford Companion to Philosophy*, 2nd Edition, 122 (New York: Oxford University Press).

Larson, M. S. (1977), *The Rise of Professionalism: A Sociological Analysis* (Berkeley, CA: University of California Press).

Lewis, P. V. (1985), ‘Defining “Business Ethics”: Like Nailing Jello to a Wall’, *Journal of Business Ethics* 4:5, 377-83.

Luetge, C. (2005), ‘Economic Ethics, Business Ethics and the Idea of Mutual Advantages’, *Business Ethics: A European Review* 14:2, 108-18.

Macdonald, K. M. (1984), ‘Professional Formation: The Case of Scottish Accountants’, *British Journal of Sociology* 35:2, 174-89.

Macdonald, K. M. (1995), *The Sociology of the Professions* (London: Sage).

Matten, D. and Crane, A. (2005), ‘Corporate Citizenship: Toward an Extended Theoretical Conceptualization’, *Academy of Management Review* 30:1, 166-79.

Monks, R. A. G. and Minow, N. (2001), *Corporate Governance*, 2nd Edition (Malden, MA: Blackwell).

Moon, J., Crane, A. and Matten, D. (2005), ‘Can Corporations Be Citizens? Corporate Citizenship as a Metaphor for Business Participation in Society’, *Business Ethics Quarterly* 15:3, 429-53.

Moore, G. (1999), ‘Corporate Moral Agency: Review and Implications’, *Journal of Business Ethics* 21:4, 329-43.

Parry, N. and Parry, J. (1976), *The Rise of the Medical Profession* (London: Croom Helm).

Popper, K. R. (1966), *The Open Society and its Enemies, Volume II, The High Tide of Prophecy: Hegel, Marx, and the Aftermath*, 5th Edition (London: Routledge and Kegan Paul).

Reed, M. (1992), *The Sociology of Organizations* (London: Harvester Wheatsheaf).

Stiles, P. and Taylor, B. (2001), *Boards at Work: How Directors View their Roles and Responsibilities* (Oxford: Oxford University Press).

Tricker, R.I. (1984), *Corporate Governance* (Aldershot: Gower).

van Oosterhout, J. (2005), ‘Corporate Citizenship: An Idea Whose Time Has Not Yet Come’, *Academy of Management Review* 30:4, 677-84.

Wittgenstein, L (1958), *Philosophical Investigations*, 2nd Edition, trans. G. E. M. Anscombe (Oxford: Blackwell).