

**Sen's capabilities and stakeholders' entitlements in the firm:  
A new foundation of corporate governance**

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**ABSTRACT**

This paper provides a new foundation of corporate governance based on Sen's capability approach. As the hierarchical nature of the firm and its corporate governance (intended as the configuration of a firm's entitlements) impact stakeholders' capabilities, the paper shows the nexus between capabilities and entitlements (that we call capabilities-as-entitlements) within the firm, identifies the criterion for the allocation of capabilities in the corporate domain and for solving potential conflicts among stakeholders' capabilities within firms, and provides examples of capabilities-as-entitlements and measures of capabilities within firms.

**Keywords:** Hierarchy; Capability; Corporate governance; Corporate social responsibility; Economic democracy; Stakeholders.

## 1. THE ISSUE: CORPORATE GOVERNANCE, STAKEHOLDERS' ENTITLEMENT, AND SEN'S CAPABILITY

Corporate governance (hereafter CG) represents “*the structure of rights and responsibilities among the parties with a stake in the firm*” (Aoki, 2000:11, italics added).<sup>1</sup> This definition raises some questions: Does CG (as rights, duties, responsibilities and so on) affect the well-being of stakeholders?<sup>2</sup> And, how *should* such entitlements be allocated, preventing an unequal well-being distribution? This paper seeks to answer these questions by exploiting the capability approach (hereafter CA), which was originally formulated by Amartya Sen and Martha Nussbaum (e.g., Sen, 1992, 1999, 2009; Nussbaum, 2011).<sup>3</sup> As it has been underlined on this journal very recently, CA

offers a perspective of a person's or agent's freedom to choose the life they want to live so that they prosper and enjoy freedom according to their wishes. [...] [CA] introduced a broader perspective by arguing that well-being, justice, human rights, and development should be considered in the light of people's capabilities to function [...] [W]ell-being freedom and development are not realized through economic freedom alone or by measuring feelings or possessions; rather, they are considered through broader sociopolitical freedoms that enable one to live under conditions of at least basically functional economic, physiological, and psychological well-being (Chowdhury et al. 2023, 9).

According to the CA, a person's well-being stems from her agency, i.e., “what a person is free to do and achieve in pursuit of whatever goals or values she regards as important” (Sen, 1985:203). In this approach, agency is embodied in the effective freedoms to achieve valuable *functionings*, which are states of being and doing (what a person is or does) that a person has reason to value. Examples of functionings include being adequately nourished, moving about freely, taking part in community life, being literate, being in good health, and avoiding escapable morbidity.

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<sup>1</sup> Similarly, for the OECD, CG is “the system by which business corporations are directed and controlled. The corporate governance structure participants in the corporation, such as the board specifies the distribution of rights and responsibilities among different, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs” (OECD, 2005).

<sup>2</sup> We adhere to the definition of stakeholders as parties who has a stake in the sense that they expect a return from their own specific investments in the firm (cf. Aoki, 1984; Blair & Stout, 1999; Sacconi, 2006, 2007).

<sup>3</sup> In the management literature, references to “capabilities” most often mean organizational dynamic capabilities (e.g., Teece et al., 1997). We instead refer to Sen's human capabilities for achieving the kind of lives that people have reason to value.

In this paper, we employ the strict nexus (which is often neglected) between capabilities and entitlements, referred to as capability-as-entitlement (see also Nussbaum, 2003). For instance, being well nourished relies on the entitlement to access food, which is understood as *legal liberty*.<sup>4</sup> To borrow an example from Sen (1981), although food was available in shops during the Bengal famine of 1943, people still died because they had no legal liberty to access it. Our interpretation of this argument is that capability as legal liberty may limit the claim(s) of another person such as owner's property right, e.g., the ability to exclude someone from the food—of course, the capability to access food would generally not extend to trespassing offenses.

Entitlement in this respect involves *freedom*—rather than an obligation, as in a paternalistic intervention—to achieve a valuable functioning. Indeed, the two chief aspects of choice in the CA are (i) the range of valuable and meaningful options (capabilities to function) and (ii) the power to choose and act. In this regard, the agency is the active role that the agent plays in bringing about the achievement of any functioning.<sup>5</sup> This paper extends this idea, till now mainly limited to public institutions—where the aim of the public intervention is to create capabilities—to the design of private economic institutions. Indeed, we exploit the strict nexus between capabilities and entitlements to propose an analysis of CG: Entitlements provided by CG represent a fundamental component of stakeholders' capabilities and may limit residual control rights (*à la* Hart, 1995). This paper contributes to the literature on Business Ethics by extending the current theoretical perspective on stakeholders' capabilities, building upon previous works such as Westermann-Behaylo et al. (2016), Fia and Sacconi (2018), and Chowdhury et al. (2023), and providing a new foundation for CG inspired by Sen's CA.

The CA that we propose to apply to firms also has some practical implications. Indeed, our paper identifies some measures of stakeholders' capabilities and, consequently, some indicators for assessing CG according to CA. These practical implications are particularly topical when viewed from the perspective of CG reforms, at least at the European level, as for instance envisaged by the proposal of the Directive on Corporate Sustainability Due Diligence (CSDD). CSDD aims to ensure that companies, in particular, large companies, active in the internal market contribute to sustainable development and the sustainability transition of economies and societies through the identification and minimization of potential or actual adverse human rights and environmental impacts connected with companies' own operations, subsidiaries, and value chains, such as a violation of the right to

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<sup>4</sup> We will develop the consolidated taxonomy based on the jural positions and relations of Wesley N. Hohfeld (1917). Cf., in particular, Sumner (1987).

<sup>5</sup> Notably, while famine in Bengal stemmed from the lack of this liberty and related capability, Ramadan fasting and hunger strikes are *choices* and therefore do not represent a lack of capabilities.

enjoy safe and healthy working conditions.<sup>6</sup> Using our perspective based on CA, it may reflect a functioning of “being in a healthy and clean environment” and a capability (particularly for workers) representing the freedom to work in a healthy place. As we argue below, the capability related to “being in good health” can be measured by the number and types of policies for workers that outline safety procedures and prevent work-related accidents. According to our perspective, moreover, such (workers’) capability implies a limit of residual control rights à la Hart. That is, the “boss” in the enterprise is limited to pursuing corporate profit if it implies unhealthy or unsafe (working) conditions. Similarly, in line with our CA approach, CSDD redesigns the manager’s duties by considering and supporting what we call stakeholders’ capabilities. Our new foundation is then able to enrich the theoretical bases of the CSDD, provide measures for its due diligence, and assess capabilities-as-entitlements that compose a CG regime.

The remainder of the paper unfolds as follows: The next section presents the state of the art on the CA applied to the business domain. Section 3 explains why applying the CA as an idea of justice is needed to address the issues deriving from the economic theory of the firm. Section 4 shows that Sen’s capability can be seen as a structure of entitlements which is based on Welsely Hohfeld’s classification of jural relations. Section 5 introduces a formalization of capabilities that considers various conversion factors. Section 6 discusses Anderson’s sufficientarian criterion of equal citizenship within the corporate domain. Section 7 provides some examples of capabilities-as-entitlements within the firm. Section 8 presents our conclusions.

## 2. LITERATURE REVIEW

A limited number of works have emphasized capabilities' role in the business domain. Westermann-Behaylo et al. (2016) used the CA to develop the idea of stakeholder capability

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<sup>6</sup> Adverse impact in the CSDD results from the failure to comply with obligations such as a violation of: (i) the right to enjoy just and favourable conditions of work including a fair wage, a decent living, safe and healthy working conditions and reasonable limitation of working hours; (ii) the right to freedom of association, assembly, the rights to organize and collective bargaining; (iii) the prohibition of unequal treatment in employment (it includes, in particular, the payment of unequal remuneration for work of equal value); (iv) the prohibition of causing any environmental degradation, such as harmful soil change, water or air pollution, harmful emissions or excessive water consumption or other impact on natural resources (see Annex of CSDD). Moreover, in order to gather information, identify and assess actual and potential adverse impacts as well as to prevent, cease or minimize such adverse impacts, the company shall develop in consultation with affected stakeholders an action plan. In this respect, stakeholders include workers and other relevant stakeholders such as other individuals, groups, communities or entities whose rights or interests are or could be affected by the products, services and operations of that company, its subsidiaries and its business relationships.

enhancement, incorporating the notions of dignity and exploring normative responsibilities and consequences with regard to human capabilities and dignity. Finally, they define stakeholders' specific capabilities. Quite similarly, Spangenberg (2016) developed a Corporate Human Development Index that translated the United Nations Human Development Index (HDI) to corporations as a strategic management tool. However, neither paper considered the role of CG in creating and sustaining (or destroying) stakeholders' capabilities. These authors focused on the effect of firms' behaviour on stakeholders' capabilities, but the firms' actions were largely detached from the concept of entitlements. We depart from this literature by advancing a framework that focuses on stakeholders' rights, duties, and responsibilities.

Our paper also represents a further step of several papers published on this journal. Chowdury et al. (2023) use capabilities to design a model of firm that considers marginalized stakeholders, namely those who belong to vulnerable social identities or lower social classes and that are often subject to racial profiling, generate very low incomes relative to their locations, and are stigmatized for their sexual orientations, physical disabilities, and mental health problems. By considering CA, authors study marginalized stakeholders' capabilities "as agents' pursuit of different functionalities within and outside organizations to achieve their freedom, which, in effect, contributes to their societal and well-being freedom" (Chowdhury et al., 2023, p. 9). Basing on Westermann-Behaylo et al.'s (2016) model, Goodstein (2019) sheds light on the relationship between rights and capabilities by studying the employee-worker relationship in the hiring practices of ex-offenders. Capabilities provide a normative criterion for balancing the rights of employees to protect property and individuals, the rights of ex-offenders to uphold their dignity, and the benefits for external stakeholders such as families and residents. Syed and Van Buren III (2014), compare the capability approach (as a representation of the mainstream Western liberal individualist view of freedom and equality) with an Islamic view on gender equality. In particular, they contest the notions of well-being inherent within the capability approach. However, these papers focus solely on a limited number of economic relationships (i.e., worker-employer relationships) or stakeholders (marginalized stakeholders), while our paper proposes a (more) comprehensive view that can be applied to all relationships and stakeholders in a firm.

Our paper contributes to the stakeholder approach, and specifically to the problem of distributing stakeholders' entitlements—namely, how to shape CG. In fact, the stakeholder approach advances a more complex view of CG that goes beyond the idea of a hierarchy that grants univocal and exclusive rights to the hierarch/boss (Donaldson, 1982; Donaldson & Preston, 1995). However, outside of some relevant exceptions (Blair & Stout, 1999; Sacconi, 2006, 2007, 2011a, 2011b), proponents of the stakeholder approach have not specified a consistent alternative structure of CG. Here, we recall the wise warning of Adolf Berle (1932:167, italics added): "You cannot abandon

emphasis on the view that business corporations exist for the sole purpose of making profits for their shareholder *until* such time as you are prepared to offer a clear and reasonably enforceable *scheme of responsibilities* to someone else”. We believe the CA can offer such a scheme, paving the way for a CG built around the idea of capabilities-as-entitlements.

This paper also relates to the literature on CSR. Renouard (2011) examines how Nussbaum's concept of relational capability can provide insights into CSR practices. Relational capabilities serve as a measure of individuals' actual opportunities and well-being. Therefore, corporate social performance can be evaluated based on the extent to which it maximizes the relational capability of individuals affected by a company's activities. This concept enables the assessment of the genuine impact of the behavior of multinational companies. Also, González-Cantón et al. (2019) used the CA to identify the content of CSR concerning human rights and dignity. The CA helps to define firms' human rights in a more comprehensive manner (and in a cross-country perspective when dealing with multinational corporations). This concept of human rights applied to business mirrors our notion of capability-as-entitlement, but it is applied solely to workers. We add to that literature by arguing that the CA can be used to design and evaluate different CG regimes and their effects on multiple stakeholders (and not only workers). Similarly, Sacconi (2006, 2007, 2011a, b) analysed CSR as an extended model of CG that results from a fair social contract among all corporate stakeholders, which recalls Rawlsian principles of justice. Fia and Sacconi (2019) went further by advancing an enlarged social contract model of the corporate constitution that focuses on the distribution of Rawlsian primary goods and Sen's capabilities.

Furthermore, our paper shares some similarities with the works of Elinor Ostrom (in particular, Schlager & Ostrom, 1992; Cole & Ostrom, 2012), in which the property right regime is seen as a *bundle* of control rights, rather than a single and indivisible right. Ostrom's taxonomy identifies four control rights over a (common pool) resource: (i) access and withdrawal, i.e., the right to enter a resource and harvest resource units; (ii) management, i.e., the right to manage the resource; (iii) exclusion, i.e., the right to determine who has rights on the resource, and (iv) alienation, i.e., the right to sell these rights. They are cumulative and only available in functionally meaningful combinations. Interpreting the firm as a *common* resource, we can create a parallel between these four control rights on commons and entitlements within a firm to better interpret different models of CG. For instance, in the US public companies, shareholders have in the assembly the right to address fundamental changes in a corporation (management rights), such as a merger. Likewise, they have an exclusion right, e.g., the right to nominate or revoke the managers. Finally, each shareholder also has an alienation right on her share and, by extension, on her voting rights. Instead, these control rights are distributed differently in the co-determination model of large German corporations. Here, workers exert management rights—by electing representatives to the supervisory board and the work

councils—to counterbalance the power of shareholders. Through the notion of capability, we can “unpack” a firm’s control rights to highlight that a shareholder, a boss or, more generally, a stakeholder has no absolute rights but only a bundle of entitlements that gives her the legal liberty to do or not, to access or not, to alienate something or not, etc.

Recent contributions from lawyers about capabilities are also relevant to us. One seminal book (Langille, 2019) applied the CA to labour law through the contributions of leading scholars such as Langille, Salais, Deakin, Del Punta, and Nussbaum, to name a few. Here, we draw attention to Salais’s (2019) efforts to identify workers’ capabilities: capability to choose, capability in personal accomplishment, capability to do or to realize, and capability to deliberate (or voice). Our work goes further by incorporating other stakeholders’ entitlements into the analysis.

### **3. WHY THE CAPABILITY APPROACH SHOULD NOT STOP AT THE DOOR OF (THE THEORY OF) THE FIRM**

In this section, we discuss some of the main reasons for reconsidering the theory of the firm under the lens of the theory of justice, in general, and of the CA in particular: 1) the risk of abuse of authority, 2) the problem of a firm’s unaccountable hierarchy, 3) the significance of work as an end, and 4) the Penelope canvas paradox.

#### **3.1. The risk of abuse of authority (or residual control rights à la Hart)**

Transactions require contracting parties to write a state-contingent contract and rely on an external third party or enforcer to settle their conflicts ex post. However, in the parlance of incomplete contract theory (e.g., Williamson, 1985; Hart, 1995, see also Vatiello 2021), the parties’ conduct and the exact nature of their transaction are not ex ante completely predictable by the terms of the contract; unforeseen events can occur, or at least, cannot be verified upfront by the enforcer. This is particularly challenging when the transaction involves investments in asset specificity *à la* Williamson (1985), namely investments that are costly to redeploy in alternative economic relationships. In order to spur investments in asset specificity, the contracting parties might move to a hierarchical relationship, i.e., the firm, where one party is the boss and the other(s) the subordinate(s). The firm relies on authority, i.e., the power to decide on all contingencies that are not specified in a prior contract, custom, or law. Hart (1995) labelled this power as *residual control rights*.

In this view, a firm emerges as a solution to contractual incompleteness. However, the hierarchy imbues the boss with the power to protect her investment in asset specificity, but at the same time, by

means of team production, that boss's power can also siphoning the value created by other stakeholders' investments (Blair & Stout, 1999). Namely, what some scholars have understood as the effects of an "abuse of authority" (Sacconi, 1999; Gibbons, 2010). Social justice theory can be used to define and distribute entitlements in the firm, thereby mitigating such abuse.

### 3.2. The problem of a firm's unaccountable hierarchy

The second reason to apply the theory of justice to CG is that the firm's hierarchy is not accountable: the boss is neither elected nor removable by *all* subordinates. The hierarchy represents, in the terminology of Elizabeth Anderson (2017), a *private government*—as opposed to a *public* government (that generally has democratic channels). Rephrasing in the political philosophy language of Philip Pettit (1997), the firm features an absence of *republican freedoms*: as such, the stakeholders are subject to boss's arbitrary and unaccountable will. CG should instead create or increase such republican freedoms, which coincide with Sen's capabilities (Pettit, 2001). Therefore, the theory of justice, and the CA in particular, should be translated into a theory of justice *within* the firm.

### 3.3. The significance of work as an end

A third reason to apply the CA to the theory of the firm is that the firm's hierarchy "violates the moral requirement to respect the autonomy of those who contract into the firm" (Lee, 2018:154). Autonomy reflects a person's freedom to exercise her rationality to determine her own ends. Because of residual control rights, however, the boss has the power to set subordinates' activities within the firm; thus, the boss may fail to respect the autonomy of those involved in the firm. Social justice concerns emerge from this problem to address the morally unacceptable abdication of subordinates' autonomy to set their own ends.

In addition, using a Kantian perspective, the labor is not only a means (namely a productive factor) that the boss can allocate to one or another activity, but an end in itself for workers (Pagano, 1985; Bowie, 2017). Employees have preferences about their own work, but the boss being the ultimate decider may fail to respect workers' autonomy. To solve this problem, the boss's authority should be accepted by the workers in so far as it pursues the workers' goals—and thereby morally legitimized by the workers themselves (Raz, 1985; McMahon, 1989; Sacconi, 2000). Following the language of the CA, the delegation of authority should reflect, safeguard, or promote the distribution of capabilities-as-entitlements in the firm. CA can be used to define such entitlements that ensure workers' (and subordinates') autonomy.

### 3.4. The Penelope canvas paradox

Although functionings and their related capabilities stem from public institutions (e.g., Pogge, 2002), private institutions (like firms) still house many functionings. This is the final reason to apply the CA to the firm. Our point is consistent with Sen's purpose of extending the idea of justice beyond the domain of social institutions (cf. Fia & Sacconi, 2019).

However, capabilities developed by a State may be impoverished in a firm. Fia and Sacconi (2019) explained this issue in terms of the "Penelope canvas paradox": The work accomplished *during the day* by public welfare institutions in forming capabilities is unravelled *during the night* by private institutions (such as the firm). Consider: The public education system seeks to guarantee employability by fostering students' skills development. Developed skills offer a set of achievable functionings (such as "being a good pharmaceutical researcher") that allow one to work according to her own standard of excellence. However, once students enter the firm, the set of achievable functionings can be limited or denied by the boss. For example, the boss can ask the researcher to omit certain controversial aspects in her report or to apply an inferior standard rule in the research project. Our notion of capabilities-as-entitlements and their role in limiting the boss's control rights is fundamental to avoiding the Penelope canvas paradox.

## 4. JURAL RELATIONS AND CAPABILITIES-AS-ENTITLEMENTS

Having an ability (e.g., generated by appropriate education and training) does not make a capability, since the ability may be in vain and frustrated by the absence of freedoms, such as the legal liberty of accessing the means or procedures to exercise such ability. Therefore, a capability, as an effective freedom, needs an entitlement. This section explains and extends Sen's notion of entitlement by relaying on the classical Hohfeld's classification of jural relations (Hohfeld, 1917). In particular, we make sense of the idea of an entitlement supporting an agent's capability by departing from the notion of *legal liberty* in Hohfeld sense. A legal liberty reflects the absence of an opposing *duty*: In Sen's Bengal famine example (mentioned in Section 1), the liberty to enter the food shop is equivalent to the absence of a duty to stay out of the shop. However, capabilities may be completed by further legal entitlements (positive rights and negative rights). Indeed, capabilities and legal liberties are not synonymous since a capability encompasses not only legal liberty but also *full* liberty or freedom of choice. Hence this section concludes by analyzing the necessary and sufficient (legal) conditions for supporting capabilities as full liberty.

#### 4.1. Analyzing entitlements in the firm through Hohfeldian liberties

Hohfeld complained that the notion of a right, as conceived in judicial reasoning, is “multiply ambiguous and that these ambiguities encouraged legal arguments to equivocate as they slid effortlessly from one sense of the notion to another” (Sumner, 1987, p. 18). Hohfeld’s remedy for this conceptual muddle was to map the logical relations among ‘fundamental conceptions.’ Hohfeld’s analysis of legal relations comprises two main components: (i) the action (or abstention), which we will call A, and (ii) the individuals, say X and Y, involved in the action A. Consider the example of the Bengal famine: the owner (X) of a food shop, a starving person (Y), and the act of entry or stay out of the food shop (A). The (first-order<sup>7</sup>) jural relations are presented in Table 1 (readapted by us on Sumner 1987:27).

Table 1. Hohfeld’s fundamental legal conceptions

		Correlatives	
Opposites	<b>Y’s liberty (or privilege, permission)</b>	<b>X’s no-claim</b>	
	Y has a liberty with respect to X to A	X has no-claim against Y that Y not A	
	<i>Y is free to enter X’s shop.</i>	<i>X has no-claim that Y does not enter the shop.</i>	
	<b>Y’s duty (or obligation)</b>	<b>X’s claim/right</b>	
Y has a duty to X not A	X has a claim against Y that Y not A		
<i>Y has the duty toward X not to enter the shop.</i>	<i>X has a claim that Y does not enter the shop.</i>		

In the Hohfeldian scheme, Y’s *liberty* (or privilege, permission) correlates with X’s *no-claim*, just as X’s *claim/right* correlates with Y’s *duty*. Hohfeldian *correlatives* are logical equivalents with switch of persons: For instance, a liberty of the individual Y (e.g., a starving person) toward X (e.g., the owner of the shop) concerning doing action A (e.g., entering the shop) means that X has no-claim that Y does not A. Similarly, a claim/right of the individual X (e.g., the owner of the food shop) toward the subject Y (a starving person) not to perform an action A (not enter the shop) means that the subject Y has a duty toward X not to do A. In addition, Hohfeld identified *opposites*: the same subject with a *negated* action. In other words, an individual’s liberty implies the *negation* of a duty,

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<sup>7</sup> Hohfeld (1917) also defined second order jural relations: While first-order jural relations are exogenous for individuals, second-order jural relations can be modified by individuals (see also Fiorito & Vatiero, 2011; Pagano and Vatiero, 2019).

e.g., the negation of ‘Y has a duty toward X to perform an action A’ entails ‘Y has a liberty (*no-duty*) toward X not to perform an action A’.

It is important to underline therefore that a claim implies a duty of others (“I cannot have a claim *to do*, only claims *that others do*”; Sumner, 1987:25, italics in original), while a liberty implies *not* having a duty to others (“I cannot have liberties *that others do*, only liberties *to do*”; Sumner, 1987:26, italics in original). Our thesis is that in order to account for the idea of an entitlement making possible an agent’s, say Y’s, capabilities, we basically have to refer to Y’s legal liberty as the negation (or limitation) of another agent’s, say X’s, claim/right.

This is evident in the case of CG and in its key notion of residual control rights à la Hart (Hart, 1995) meant as the authority to command a subordinate to perform an action by means of a residual decision, initially not specified in an incomplete contract and supported by the threat of excluding the subordinate from the firm’s physical assets in case she does not comply with the command. Thus, the crux of the boss’s residual control right is the claim to exclude the subordinate from accessing the firm’s physical assets in case she does not conform to some boss’s order or request. If X (the boss) has residual control rights, then X has a claim that Y (the subordinate) be excluded or does not access the firm’s physical assets in case Y does not comply with some further orders put forward by X. Its correlative is that Y has the duty to stay out or not to access the physical assets of the firm.

Now, let the subordinate’s (Y’s) capability enter the picture. Provisionally accept that a subordinate’s capability is the effective liberty to access some characteristics of the firm in order to transform them into the achievement of some valuable subordinate’s functionings: the satisfaction of a professional ideal, a good income, a decent state of job security, a significant grade of self-determination on the job, etc. This liberty of the subordinate (Y) is the negation of the boss (X)’s claim inherent in the residual control rights, namely the opposite or negation of the claim (namely the no-claim) of the boss (X) that the subordinate (Y) is excluded from the firm’s physical assets; or, equivalently, it is the opposite or negation of duty (namely, the liberty) of the subordinate (Y). Also, in this case it is clear that the subordinate’s (Y’s) liberty entails that she cannot be authoritatively excluded but does not amount necessarily to a replacement in the allocation of the residual control rights (e.g., from the boss X to the subordinate Y). It amounts to a limitation of the boss’s rights, i.e., a limit to the power of excluding the subordinate.

#### 4.2.From Hohfeldian liberties to full liberties and capabilities

So far so good, but we have now to consider the peculiar nature of Hohfeldian liberties. They are *half-liberties*, i.e., privileges to do an act A, which are the opposite of the duties of not doing the act A. However, Hohfeldian liberties are compatible with the duty of doing the act A. In other words,

“having the liberty to do something is compatible with lacking the liberty not to do it” (Sumner, 1987:26). To see the point, let resort to deontic logic notions - *obligation and permission* - to define the above concepts. The *opposite* of ‘Y has an obligation (or duty) to X not to do A’ is ‘Y has a permission (or Hohfeld’s liberty) with respect to X to do A’. The deontic permission of doing A excludes that Y may have an obligation to X of *not* doing A, but it is silent about the case that Y may have the obligation with respect to X to do A. For example, ‘Y has the permission to enter the shop’ is compatible with ‘Y has the obligation to enter the shop’.<sup>8</sup> Thus, a liberty in Hohfeld’s sense is not necessarily a *full* liberty, which would be the possibility of both “doing A” and “not doing A”, what we consider an effective freedom of choice. A full liberty is the sum of two “half-liberties”: first, a liberty to access the food store; second, a liberty to not access it. “Unlike half-liberties, full liberties ensure a normatively unencumbered choice between options” (Sumner, 1987:27).

What about capabilities as liberties? Capabilities may be compatible with (Hohfeld’s) half-liberties and full liberties. This follows from Sen’s discussion on the *instrumental* and *intrinsic* value of capabilities. In fact, capability has an instrumental value when it represents a freedom or opportunity to achieve a valuable functioning (e.g., being well fed). More precisely, a capability is a transformation function that an individual may willingly use to transform some characteristic(s) of goods or resources into a functioning (i.e., the capability of having access to food permits to achieve the functioning of being well-fed). Accordingly, a capability has an *instrumental* value, which magnitude depends on the functioning value itself. Call this instrumental value as the *minimal necessary value* any capability needs to have: at least, it must serve as an effective tool to achieve a valuable functioning. However, having capabilities—understood as freedoms of choice—also has an intrinsic value: we are better off if we have more available significantly diverse options, independent of whether we will choose any of them—call this intrinsic value as the *sufficient value*: The opportunity to select a particular capability among many alternatives brings value to any capability

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<sup>8</sup> To see even better the point, let us turn to the logical modalities *necessary/possible*. An Hohfeld’s legal liberty is the *normative possibility* to do an act, e.g., ‘Y has the normative possibility (a permission) to enter the shop’. However, whatever is ‘necessary’ must be also ‘possible’ (if ‘necessary’, it cannot be ‘impossible’), thus whatever is ‘possible’ can be ‘necessary’. Consequently, a normative possibility to do an act is compatible with the *lack of normative* possibility of *not doing* the act, e.g., ‘Y does *not* have the permission of *not* entering the shop’. To be sure, saying that a person has a liberty, or normative possibility, to do A, and at the same time is under the obligation, or normative necessity, of doing A does not mean that this person lost her agency as she is not under a *physical necessity* of doing A (the physical impossibility of doing other than A). In fact, an individual acting in accordance with an obligation always is a subject endowed with agency—someone who is simply following the reason for acting provided by the obligation; and alternatively, could diverge from the obligation by willingly violating a norm.

in the choice set.<sup>9</sup> Therefore, well-being in the CA depends on two conditions. The minimal necessary condition: which functionings the capability serves and what value the functioning represents (instrumental value); and, the sufficient condition: how many alternatives there are that allow a more or less wide selection of the capability to function (intrinsic value). The minimal necessary condition relates to the instrumental value of having at least one capability to function, and requires then the correspondent Hohfeldian half-liberty, or permission to access the characteristics used to achieve a relevant functioning. Meanwhile, the sufficient condition requires at least two Hohfeldian half-liberties, jointly defining a full liberty, hence getting both the instrumental and intrinsic value of capabilities.<sup>10</sup>

Thus, coming to deal with entitlements within a firm, in order to grant *both* instrumental *and* intrinsic value, at least two half-liberties are needed. That is, Y, the subordinate, is free from the obligation of being excluded from a firm's physical assets' that are conducive to achieving her

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<sup>9</sup> As an example, consider a young woman whose father is a farmer. Both the legal and familial context provide her with the means to be a good farmer—a functioning she values. At the same time, the context is unfavorable for developing other professions; there are no law or medical schools, for instance, simply accessible. While she doesn't lack the capability to function as a successful farmer, the value of this capability is only instrumental; it does not include the intrinsic value deriving from having a choice among different functionings. The wider the agent's set of capabilities, the higher the intrinsic value of any capability selected. When the choice set shrinks to a singlet, the intrinsic value vanishes, even though the remaining capability keeps its minimal value: the instrumental value.

<sup>10</sup> Does the legal ordering needed in order to properly support capabilities require *both* the minimal necessary condition *and* the sufficient condition? Pandemics example may offer an answer: A way the legal ordering may grant everybody the permission to access vaccines, enhancing the capability of preventing a severe contagion, is to require a waiver of patent protection or imposing a moratorium. Thus, individuals are not under the obligation to respect the pharmaceuticals' claim of exclusion from the free use and reproduction of vaccines—which is the essence of the patent regime as exclusionary right to exploit an innovation (many scholars have argued in favor of such a waiver during the Covid19 pandemic). As a result, people have both the half-liberty to vaccinate them and the half-liberty to not vaccinate them. This represents a full liberty. However, the legal system may also oblige some categories (e.g., elderly people, medical personnel, schoolteachers) to access the vaccine (i.e., vaccinate them) in order to mitigate contagion. For these categories, the half-liberty to vaccinate them is combined with the *lack* of a half-liberty to not vaccinate them. Our aim here is not to enter into moral considerations about the freedom of vaccination; we only want to show how the promotion of the simple health capability may sometimes be constrained not to achieve the sufficiency condition (namely full liberties), and to require just to satisfy the minimal necessary condition. Rephrasing in an externality logic: individuals' capability of avoiding contagion and maintaining good health may strongly depend on whether some categories (e.g., elderly people, medical personnel, schoolteachers) decide to not access the vaccine. Then, according to an externality logic, the full liberty to act or not act of these categories may be detrimental to other individuals' capability of avoiding contagion and functioning properly. By no means the duty of vaccination does not realize a full system of capabilities based on the freedom of choice. Nevertheless, it helps to satisfy the minimal necessary condition for granting the capability of functioning well in pandemic prevention.

relevant functionings; *and* she is also not obligated to use them to achieve such functionings, without that it implies a replacement in the allocation of the residual control rights (e.g., from the boss X to the subordinate Y).

The Hohfeldian half-liberty is the opposite of a duty and the basis of an entitlement that supports a capability in the minimal case—where only the capability’s instrumental value is granted (i.e., the necessary condition). In order to make sense of a full system of capabilities, both half-liberties should be granted. Together, the two half-liberties create a full liberty: a freedom of choice. This condition does not contradict the role of Hohfeldian liberties in defining the entitlement that supports any capability (i.e., that any capability at least comprises the liberty of not being excluded from goods and resources that are functional to achieving a relevant functioning). Simply, it requires that the legal liberty should be specified in terms of half-liberties, namely in line with the abovementioned Ostrom’s idea, in terms of *bundle* of rights.

Furthermore, Hohfeld’s jural analysis confirms entitlements are not rights tout court, but the denial of another individual’s property right leading to the definition of bundles of rights. A world full of capabilities is one in which there would be a plenty of liberties (i.e., both half and full liberties) working as entitlements protecting the freedom of functioning in different domains of human flourishing insomuch as they are based on the preemption of inaccessibility claims and exclusion-duties. On the contrary, in a world in which everything was privately owned (but many important goods could not be equally divisible or non-divisible at all<sup>11</sup>) very few capabilities would take place, since access characteristics of many goods needed in order to transform them into achieved functioning would be prohibited. This is the basic idea of the essential connection between the capability approach and the analysis of jural relations. It does not say that Hohfeldian liberties are the only concept needed to characterize entitlements supporting a system of capabilities—also claims do matter. But we emphasize that it is the first basic step and any additional claims, composing a bundle of rights, must be devoted to protecting as much as possible these liberties (capabilities).

## 5. A FORMALIZATION

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<sup>11</sup> A good may be physically, but not economically divisible if the division entails the loss of its value. Team production in a firm has exactly this characteristic (cf. Blair & Stout 1999): splitting the team into individual producers is possible, but it would sharply reduce the value resulting from summing up the individuals’ contributions with respect to the value obtained by their joint production as a team (the production function, in this case, is superadditive).

A central distinction in the CA is between functionings (i.e., states of being and doing that a person has reason to value) and capabilities (i.e., the functionings that a person can potentially achieve through her choice). For a formal description of our conception of capabilities-as-entitlements, we introduce some notations that extend Sen (1985) and Kuklys and Robeyns (2005):

$$Q_i(X_i) = \{\mathbf{b}_i = f_i(c(\mathbf{x}_i) | \mathbf{z}_P, \mathbf{z}_C, \mathbf{q}_S, \mathbf{q}_L) \mid \forall f_i \in F_i \text{ and } \forall \mathbf{x}_i \in X_i\}$$

$Q_i(\cdot)$  is the set of achievable functionings, representing the capability set comprising all functionings  $\mathbf{b}_i$  that an individual can choose to achieve;  $\mathbf{b}_i$  is an agent's vector of functionings;  $f_i(\cdot)$  (a subset of all possible conversion function  $F_i$ ) is an individual  $i$ 's conversion function that maps characteristics of commodities onto the space of functionings;  $c(\mathbf{x}_i)$  is a vector of characteristics of an individual  $i$ 's commodities,  $\mathbf{x}_i$ , belonging to a set  $X_i$  of all possible commodity vectors; finally,  $f_i(\cdot)$  works conditionally on the elements  $\mathbf{z}_P, \mathbf{z}_C, \mathbf{q}_S, \mathbf{q}_L$ , where:

- $\mathbf{z}_P$  are conversion factors at the *personal* or individual level,
- $\mathbf{z}_C$  are *non-personal* conversion factors at the social and environmental level,
- $\mathbf{q}_S$  defines a *psychological/cognitive* conversion factor (skills),
- $\mathbf{q}_L$  defines a *legal* conversion factor (entitlements).

The achieved functioning depends on the employed commodities  $x_i$  (or, more precisely, on the employed commodities' characteristics  $c(x_i)$ ), the conversion factors  $\mathbf{z}_P$  and  $\mathbf{z}_C$  (which are *constraints* on individuals' choices), and the conversion factors  $\mathbf{q}_S$  and  $\mathbf{q}_L$  (which are *constitutive elements* of individuals' freedom to choose and act, i.e., agency).

We can envision a vector of commodity  $x_i$  as a bundle of goods: foods, bicycles, car, etc. Functioning depends on the characteristics of good  $c(x_i)$ : for bicycles, it may be fast transport, but also health or leisure; for foods, it may be good taste, but also nutritional qualities. In the corporate domain, the vector of commodity can be tangible goods (e.g., offices, machineries, etc.) or intangibles (e.g., information, data, know-how, etc.), while the characteristics of an office (and in general, facilities) can be performing a task of a team member  $i$  in a production process.

Conversion functions are not infinite, but limited by personal, social or environmental factors. Hence, the conversion factors  $\mathbf{z}$ , which constrain individuals' choice (capability set), can be distinguished in personal factors (i.e., objective individual factors  $\mathbf{z}_P$ ) and non-personal factors at the social and environmental level  $\mathbf{z}_C$  (i.e., the context). Objective individual factors ( $\mathbf{z}_P$ ) are *basic* characteristics such as physical disabilities, intelligence, and metabolic rate (none of which can be changed by individuals' agency). For instance, a child needs more protein than an adult to achieve a similar level of healthy functioning. Social and environmental (contextual) factors ( $\mathbf{z}_C$ ) are factors

such as population density, climate, the proximity of rivers, levels of environmental pollution, the state of roads. The conversion factor  $z_C$  also includes socio-cultural factors, such as social norms and specific cultures (e.g., whether women are allowed to ride a cycle).

Granted, we want to highlight the precondition for agency rather than limit our analysis to a deterministic approach. Thus, we added two further conversion factors  $q_S$  and  $q_L$  that are preconditions of individuals' capabilities understood as the ability to be active, or to act purposively and intentionally: *skills*, which represent the psychological/cognitive factors ( $q_S$ ) and *entitlements*, which represent legal factors ( $q_L$ ) (Fia & Sacconi, 2019). Skills ( $q_S$ ) include psychological abilities, i.e., cognitive or practical skills that can be natural or learned (e.g., in school), such as the ability to eat, drive, read, etc., but also higher-level abilities like as to reason or to establish an order of preference or importance amongst alternatives. These skills may compensate for personal factors ( $z_P$ ) that are *objective* and constrain our capabilities: For example, having a walking disability may constrain an individual from attending classes at school and achieving some functioning in education, but an individual can counterbalance this handicap by developing a skill to ride a hand bicycle to reach school. Skills are a subjective (vs. objective) transformation factor.

Of course, these skills may be ineffective in the absence of non-personal context conditions ( $z_C$ ) that sustain them. If an individual has the skill to ride, but the state of the road ( $z_C$ ) does not allow her to do so, then the capability may be undermined. Further, skills can be ineffective in the absence of an entitlement, i.e., legal factors ( $q_L$ ). In the Bengal famine example, food was available in the shops ( $z_C$ ) and people could prospectively eat ( $z_P$ ), but individuals lacked the legal entitlement to access the food ( $q_L$ ).

To sum up our theoretical setting consider the case of a bicycle (cf. Sen, 1985). Bicycles are a commodity ( $x_i$ ) that provides transport ( $c(x_i)$ ), and the functioning ( $b_i$ ) is represented by moving about freely. The conversion of the commodity into functionings depends on conversion factors such as a person's ("objective") ability to cycle ( $z_P$ ). It also depends on non-personal factors, such as the conditions of roads ( $z_C$ ), and entitlements ( $q_L$ ) (guaranteed by the law), such as the liberty to access the urban traffic by bicycle. This liberty is supported by a *bundle* of entitlements: first, the bikers' claim to move that correlates with car drivers' duty not to obstruct bikers from using the city streets; and second the public policy that protects access to the urban traffic by bicycle by providing bike lanes and affordable bike rentals within the city limits ( $q_L$ ). These entitlements increase the set of capabilities  $Q$ : the person has the freedom to freely move and cycle.

## 6. DEFINING STAKEHOLDERS' CAPABILITIES IN TERMS OF DEMOCRATIC CORPORATE CITIZENSHIP

Creating capabilities requires creating entitlements (for a similar view, see Pogge, 2002). In her work “Capabilities as fundamental entitlement”, Nussbaum (2003) pointed out that capabilities encompass many of the entitlements being stressed in the human rights movement: political liberties, the freedom of association, the free choice of occupation, and a variety of economic and social rights.<sup>12</sup>

However, we do not want to cover all juridical notions of entitlements; rather, we want to use the concept of capabilities-as-entitlements to operationalize capabilities in the CG domain. CG can be seen as a bundle of liberties and rights—such as stakeholders’ liberty to participate, the right to be informed, etc.—which delimit the domain of a boss’s legitimate authority. The legal conversion factor ( $q_L$ ) represents a bundle of entitlements where the boss’s residual control rights are counterbalanced by limitations that provide stakeholders with substantive freedoms to access resources. The notion of capability-as-entitlement captures the bundle of entitlements protecting from excludability from accessing resources that are relevant, for instance, for realizing a worker’s valued functioning in work. This implies limits imposed on the excludability claim of others (which requires the half-liberty to access resources), as well as by additional positive and negative claims (rights).

### 6.1. Identifying capabilities: some criteria

Sen evaluated institutions comparatively based on how good they are at advancing everyone’s capabilities, rather than on whether they are perfect according to an ideal of justice. Sen suggests that the identification of “fundamental” capabilities should rest on *public reasoning* or discussion, which is defined as an impartial democratic procedure to incorporate different argumentations in a shared evaluation (Sen, 1999, 2009). The idea is that public reasoning might broaden the perspectives of those participating in it, allowing people from disadvantaged positions to express their needs to higher-status individuals (e.g., the boss in the corporate domain). A public criterion of social justice should not be dictated by one person, but should be adopted democratically after broad and vigorous debate. Even if it’s not possible to resolve all conflicting positions through public reasoning, this approach can help solve the problems of both social justice and the conflicted distribution of

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<sup>12</sup> Nussbaum’s perspective introduces an interesting bridge between capabilities and human rights. It is worth noting that the CSDD also refers to human rights. The link between human rights and capabilities is beyond scopes of this work. In any case, there are excellent works developing that link, e.g. by Nussbaum (2003).

capabilities within institutions (Sen, 2009). We can extend this concept to the business domain: A form of democracy is required to identify which capabilities should be guaranteed to stakeholders and to what extent. In this sense, participation is an essential (corporate) entitlement that can guarantee the trade-off solutions through public discussion.

Martha Nussbaum (2011) advanced another solution to the problem of identifying capabilities. Unlike Sen, Nussbaum developed a list of basic capabilities that enable individuals to achieve minimum levels of education, protect them from harm, give them access to health care, and foster different forms of affiliations, among others. Nussbaum justified the list on the grounds of human dignity. The list constitutes a basic normative threshold for societies to be deemed just without limiting them to a single form of institutional realization. In principle, only societies that give all members the opportunity to realize these capabilities can be called just.

Elizabeth Anderson (1999, 2010) offered a sufficientarian criterion that approximates our approach to democratic governance within corporations. According to Anderson, the principle of distributive justice for distributing CA entails creating or increasing capabilities in order to reach a sufficient level that permits the exercise of an *equal* democratic citizenship. Namely, she argued that “[n]egatively, people are entitled to whatever capabilities are necessary to enable them to avoid or escape entanglement in oppressive social relationships. Positively, they are entitled to the capabilities necessary for functioning as an equal citizen in a democratic state” (Anderson, 1999: 316). The sufficientarian view assesses any institution based on how well it allows its participants to exist above the sufficientarian threshold. Adopting the Andersonian perspective, we extend the notion of an equal democratic *political* citizenship to a comparable *corporate* citizenship. This entails that large corporations (serving as private governments) should be reformed to provide an equal democratic citizenship to their stakeholders.

By combining Nussbaum’s basic capabilities with those of participation (referring to Sen’s public reasoning and Anderson’s sufficientarian criterion), we can address incomplete contract issues that influence stakeholders’ further capabilities to achieve functionings in different domains. This may also involve (non-zero sum) conflicts among different stakeholders concerning the possibility of achieving some level of functioning.

## 6.2. Democratic corporate citizenship in the social contract theory

In what follows, we explain how the sufficientarian criterion of equal *political* citizenship (Anderson, 1999, 2010) may be adapted to equal *corporate* citizenship. Specifically, we link the (sufficientarian) principle of equal citizenship to corporations by means of the idea of a social contract of the firm (Sacconi, 2000, 2006, 2007, 2011a, 2011b) seen as a component of the

constitutional and post constitutional contracts model (Buchanan, 1975),<sup>13</sup> and, additionally, by means of the idea of macro and micro social contracts (Donaldson & Dunfee, 1995).<sup>14</sup> Let us split the argument in four steps as follows.

First, as free and equal persons, citizens must be assumed to have capabilities (and the supporting entitlements) to make collective choice on any given constitutional domains. Collective choice on a constitutional agreement entails and allows persons to develop fundamental capabilities, i.e., by giving principles and rules to themselves they activate and develop the capability to live under self-given agreed principles of justice (the “sense justice”) and the capability to settle autonomously their own plans of life. This corresponds to what Rawls called the persons higher-level interests for the development of their moral powers.<sup>15</sup> Moreover, people undertake their constitutional *collective* choice through the exercise of capabilities such as the public use of reason (Rawls, 1993) or the capability to take part in deliberation and impartial debate (Sen, 2009).

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<sup>13</sup> While the distinction between constitutional and post-constitutional contracts is traceable back to Buchanan (1975), the way in which the theory has been developed in cooperative bargaining game theoretical terms, so to include the constitution of the firm, involves principles of justice like ‘relative needs’ and ‘relative contributions’ (Brock 1979; Sacconi, 2000, 2006) that belong to *liberal egalitarian* theories of justice mostly represented by Rawls (1971). Moreover, having taken the state of nature perspective (repeated non-cooperative games) to model the constitutional contract, Binmore (2005) concludes that the only equilibrium selection solution possible under the veil of ignorance is egalitarian, which entails the Rawlsian *maximin* principle (see Sacconi 2001b and Fia and Sacconi 2019 for the implication on the constitution of the firm). Voluntary compliance with the micro social contract has been tested experimentally (Sacconi and Faillo, 2010; Faillo et al., 2015) on the basis of a model of psychological games in which the impartial agreement elicits conformity preferences and reciprocal expectations coherent with the Rawlsian idea of a sense of justice (Sacconi 2007).

<sup>14</sup> We are perfectly aware of being ‘unorthodox’ in suggesting the joint use of the capability approach and the constitutional and post constitutional contracts perspective. In doing so, however, we are in line with the view (Anderson 2010) that the subject matter of ‘what is valuable to us’ - what is at stake in justice - and hence the ‘metric’ of justice need to exploit the informative richness of concepts like ‘capabilities’ and ‘functionings’, even if the principle of their distribution - in what extend they should be distributed equally - may derive from concepts partly independent of them. Concepts like as the idea of ‘equal citizenship’, or that of impartial agreements at the constitutional and post constitutional level. Of course, Anderson cannot be quoted in support to the contractarian method – we are entirely responsible for that (but see also Fia and Sacconi 2019). On the other hand, Nussbaum (2011) herself suggests that her list of capabilities can be derived from an application of the theory of ‘overlapping consensus’ (Rawls 1993), a reformulation of the original Rawlsian view of the social contract (Rawls 1971).

<sup>15</sup> Similarly, Rawls (1980) affirmed that the social contract under the veil of ignorance pursues the higher interest of the parties (i.e., the interest in developing their moral powers). In other words, the capability of having a sense of justice, the capability of being autonomous (i.e., being capable to settle one’s own conception of the good and the following plan of life) and the capability to select the effective means for pursuing that life plan.

Second, we extend the constitutional social contract perspective to cover the *corporate domain*. As far as the constitutional contract is concerned, all the citizens are involved. Admittedly, the constitutional social contract does not define details; rather, it defines general principles, such as the economic principles that govern subsequent business interactions. It needs nevertheless to encompass the corporate domain and the general principle of business governance because corporations, or any other form of economic organization, can vitally support or obstruct capability creation, and specifically the creation of many capabilities that affect stakeholders' well-being. In this sense, individuals exercise equal *corporate* citizenship at the constitutional level by choosing the constraints on corporate actors (and other business agents like associations) that will affect post-constitutional business interactions. Constitutional constraints consist of the entitlements supporting capabilities allocated to any individual in order to affect the way in which she will afterward be capable in the post-constitutional stage to undertake her stakeholder position in regard to any corporation or economic organization she will enter or will interact with. The constitutional contract on corporate domain hence implies entering the post-constitutional agreement with equal entitlements. As said, the exercise of equal *corporate* citizenship at the (macro) constitutional contract level does not define all aspects of the firm's orderings. On the contrary, it works at an abstract, hypothetical level by building agreement for the general principles that work as constitutional constraints over the corporations' legal and organizational forms. At the cost of blurring important legal distinctions, we approximately treat general principles of private law, company law, and labor law as outputs of the constitutional (macro) contracts in the relevant domain. At that point, many concrete features are left to the post-constitutional (micro) social contracts among stakeholders, where they exercise the capabilities-as-entitlements (liberties and rights) granted by the constitution in the corporate domain.

Third, we transfer the idea of equal citizenship from the constitutional (macro) level to the post-constitutional (micro) level. For each corporation or economic organization—by means of which economic activity is coordinated and cooperation is made possible—only the relevant stakeholders (see Sacconi, 2006) are parties involved in the micro-social contract. Hence, for any corporate actor or economic organization, stakeholders are the relevant free and equal agents who exercise *corporate citizenship* at the post-constitutional level. Accordingly, stakeholders express their agency via the capabilities they inherited from the constitutional level to choose the post-constitutional (micro) social contract of the firms- by which they will cooperate- and the correspondent corporate governance structure. Citizens as a whole agree on the general setting in the constitutional sphere, while stakeholders agree case by case on the corporate form and corporate governance via the post-constitutional (micro) contracts. Hence, they choose for example whether to cooperate through a capitalist-owned corporation, like as a stock market-listed company, or a small family-owned company, or through a State-owned or State-participated company, a worker or consumer

cooperative, a non-profit organization or social enterprise, etc. But, in order to safeguard their status as equal citizens and the constitutional entitlements allocated to them, each post-constitutional agreement will shape the governance structure functionally to the achievement of all the stakeholders' joint objectives (understood in terms of stakeholders' functionings) and their fair distribution, and in addition, will prevent abuse of authority. Hence, any post-constitutional agreement, for whatever ownership form (see Hansmann 1988), will provide a type of economic democracy, recognizing all the relevant stakeholders' entitlements and capability in corporate governance. For example, in any non-worker-owned company, works councils and substantial board level representation may grant workers participation and co-determination (i.e., the German model).

Fourth, a corporation's day-by-day management coordinates and directs the use of the stakeholders' capabilities (skills, abilities) through the firm operations in order to achieve the stakeholders' joint objectives and ultimately the stakeholders' functionings. At the same time, the managers respect the stakeholders' entitlements by favoring the development of the stakeholders' capabilities functional to the achievement of their functioning in different areas of human well-being.

Capabilities operate at the four levels outlined above. First, they are implicitly developed to be able of making the constitutional social contract. Second, allocated extensively at the constitutional contact stage so to include the business domain. Third, exercised at the post-constitutional level by choosing the corporate form and its governance structure. And, fourth, developed in accordance with the stakeholders' entitlements and collectively used in the day-by-day operations of the firm. This reasoning naturally leads to different forms of economic democracy established by the stakeholders themselves at the post-constitutional level, but each able to comply with the constitutional constraints on the entitlements to be granted to each stakeholder in order to be part in the post constitutional contracts. All these, as a whole, constitute a sufficient level of capability creation in order to satisfy the ideal of equal *corporate* citizenship.

### 6.3. The micro social contract in managing conflicts among entitlements in a firm

Following this reasoning path, we advance a conception of CG where the allocation of rights and duties within corporations is set according to distributive justice criteria based on capabilities. However, we must note that capabilities-as-entitlements have an adversarial nature as jural relations (cf. Pagano & Vatiery, 2019): Clearly, conflicts *may* emerge between persons who are involved in a jural relation. While claims and liberties can be desirable for individuals, duties and no-claims are not. Indeed, the claim-holder is the beneficiary of a protected interest, which rests on a set of duties imposed on the other(s); while the liberty-holder is the beneficiary of permitted choices, which rest

on a set of no-claims by the other(s). Thus, an individual may prefer having claims and rights, but these may conflict with the preferences of others to have liberty and the related capabilities.

Using micro social contracts to define equal *corporate* citizenship and the related democratic CG structure can help clarify the allocation of capabilities-as-entitlements among corporate stakeholders, as well as solve potential conflicts and trade-offs. The micro social contract provides a test of whether the vector of functionings achievable by one stakeholder could be acceptable in comparison to those achievable by other stakeholders, given the available resources (e.g., the company revenues) and the capabilities effectiveness in improving stakeholders' functionings.

Take the illustrative case of exorbitant CEO pay—like those normally paid to top managers in large corporations in the US and Europe—which is a major contributor to rising inequality. Currently, the high compensation is the result of CEOs' entitlements in terms of decision-making power over resource allocation, while employees' much lower compensation is due to lacking such entitlements. The issue is whether the CEOs' functioning is acceptable in comparison to the functioning achievable by a typical worker (e.g., an employee in the supply chain with a poor remuneration). Is this gap the acceptable output of an exercise of equal citizenship at the level of the micro social contract? That is, could such a compensation arise in a democratized CG structure—resulting from the micro social contract—wherein the supply chain employees would be represented alongside the CEO? Would an *impartial* employee agree to such large gaps in compensation between corporate shareholders, top managers, and average employees? The entire probable “No” answers suggest that the stakeholders' (here, employees') entitlements, allowing them to take part in the social contract of the firm, would legitimately limit the residual control rights of some parties (e.g., in capitalist-owned corporations: shareholders and top managers) and consequently their appropriation of the corporate output.

However, the achievable functioning also depends on factors other than entitlements, such as personal and non-personal/contextual factors and skills. For example, the employees may lack the subjective abilities and skills for immediately achieving those functionings. Additionally, physical, technological, or social limits may obstruct entitlements beyond what employees can affect (e.g., the state of local economies, the social norms about women, etc.). Nevertheless, some arrangements are clearly not compatible with equal citizenship exercised at the corporate level, since they would never be accepted in any democratic form of governance built upon a micro-level social contract among stakeholders. On the contrary, other arrangements are acceptable because they significantly improve stakeholders' capabilities, even if the improvements occur gradually based on internal and external conditions. These latter arrangements extend the “sufficientarian” view to economic equal citizenship.

## 7. ASSESSING CAPABILITIES WITHIN THE FIRM: SOME EXAMPLES

We want to develop some examples that capture some of the fundamental aspects for assessing CG regimes in terms of the CA. As we mentioned in the introduction, the measures that we propose could be useful to give robustness to due diligence, such as that provided for by CSDD that has the aim of ensuring that firms identify and minimize potential or actual adverse human rights and environmental impacts. Indeed adverse *human rights and environmental impacts* represent negative impacts on capabilities such as the capability for functioning “being in good health” (that refers to the entitlement to safety and accident prevention at work as CSDD requires), “being in a healthy and clean environment” (which is the entitlement to work in a healthy place as CSDD requires), “achieving a decent standard of living” (which consists of a fair and decent wage as CSDD requires), “achieving and protecting competences” (which relates to non-discrimination in employment as CSDD requires), etc. Moreover, according to CSDD, to gather information, identify and assess actual and potential adverse impacts as well as to prevent, cease or minimize such adverse impacts, the company shall develop in consultation with affected stakeholders an action plan--stakeholders include workers and other relevant stakeholders such as other individuals, groups, communities or entities whose rights or interests are or could be affected by the products, services and operations of that company, its subsidiaries and its business relationships. Namely, the CSDD gives to stakeholders ample room for information and voice mechanisms in line with the CA (see section 6). Thus, for assessing the CG regime, one should consider if/how such a CG regime creates and supports functionings such as “being informed and express an opinion on the firm’s positive and negative externalities” and “participating in (pivotal) choices of the firm” (which consist of the entitlement of being involved and consulted in decisions as CSDD requires). So our approach allows us to construct measures measures of capabilities within firms that are in line with aims of CSDD.

To this end, we followed a flexible and open methodology that mirrored the one adopted by Burchardt and Vizard (2011) in the context of human rights. Specifically, we used the three main dimensions identified in the UN’s HDI, which Sen himself also worked on (Sen, 2005): (1) health, (2) education, and (3) standard of living.<sup>16</sup> We introduced an additional component, (4) *participation*, which is a key component of a capability in itself and simultaneously connected to the definition of

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<sup>16</sup> This internationally acknowledged index captures key functionings of human development and the related measures: health (people’s life expectancy at birth), education (years of schooling), and a decent standard of living (GNI per capita). While the HDI was developed to facilitate growth and development measures on dimensions that are not solely economic (cf. Hirai, 2017), it is not without flaws (see Klugman et al., 2011).

further entitlements. These dimensions have the advantage of *assessing* capabilities within the firm and the related CG regime.

#### 7.1. Examples for the health domain – workers, consumers, communities

Let's start by considering the dimension of worker health. The capability for the functioning "being in good health" stems from, for example, the entitlement to safety and accident prevention at work. Thus, one can capture the number and types of policies that outline safety procedures and prevent work-related accidents. Another example is workers' entitlement to a holiday, which can be captured by the number of guaranteed paid holidays (see Armour et al. 2016 for an analysis of national legislative efforts to codify and measure the entitlement to holidays). Another example of workers' health capability is the entitlement to access an affordable firm health insurance.

For consumers, the health capability is reflected in the entitlement to consume a good that is consistent with a safe and sustainable production process. To this end, one could measure the number and types of checks performed on the product before and during the production process, as well as the transparency of corporate communication. For communities, the health capability could involve the entitlement to not be negatively impacted by the firm's operations. This could be measured by the firm's adoption and adherence to social responsibility standards with respect to the local community. In addition, there could be a community's entitlement (supported by a positive claim toward the firm operating in its territory) to supplementary local welfare systems, which pursue the well-being of all the company's territorial stakeholders (not only its workers). In this perspective, a good environment is the basis for a community's functionings; in the absence of a community's entitlements, others' priorities prevail. These entitlements regarding health for workers, consumers and communities may provide guidance on evaluating and reshaping governance at the firm level.

#### 7.2. Examples for the education domain – workers, consumers, communities

To better suit the business arena, we renamed education in HDI as "cognitive skills," which relate to stakeholders' freedom to undertake human capital investments in the corporate domain in pursuit of a standard of excellence.

For workers, the capability of acquiring new knowledge to maintain and support the achievement of a professional ideal can be measured in terms of boss's obligation to offer on-the-job training. For consumers, cognitive skills could be proxied by tools that the firm provides (e.g., marketing, informative flyers, web information) to educate consumers about their products' characteristics and uses. For communities, cognitive skills can be measured by the entitlement to be

informed and express an opinion on the firm's positive and negative externalities. This might be reflected in boss's obligation to provide/disclose information and create community engagement opportunities for relevant decisions.

In short, we believe the structure of rights, duties and responsibilities at the firm level (namely, the structure of CG) should include entitlements related to the knowledge domain.

### 7.3. Examples for the standard of living domain – workers, consumers, suppliers

For workers, the entitlement to fair and decent wages is a vital term of employment for achieving a decent standard of living. One measurable proxy in this regard would be the ratio between workers' salary and production's added value, or the wage gap between managers and workers. For consumers, the standard of living may involve fair pricing strategies for goods and services that play prominent roles in people's lives.

A contemporary example is the provision of masks during the COVID-19 pandemic at *fair* prices. Suppliers and subcontractors, especially in the context of global value chain, typically have fewer options and less decision-making flexibility than their buyers. For example, garment industry brands and retailers directly influence supply corporations (even if they do not own them) (see, among others: Gibbon et al., 2008; Schrage & Gilbert, 2021). As pointed out by Oxfam (2014:4), "business models push cost and risk down the supply chain to maximize profit for shareholders". Thus, the entitlement to a fair price of goods is centrally important to standard of living in this group.

### 7.4. Examples for the participation dimension – workers, consumers, communities

With reference to workers, participation may protect them against the boss' authority, and more generally empower them to assert their respectability and autonomy in and outside the workplace. Participation is a capability in itself, but also underlies other capabilities: For example, workers may claim additional entitlements (e.g., an entitlement on company revenues) through a deliberative process.

More precisely, workers' participation dimension may take several forms (cf. Sacconi 2019; Frega, 2021) and determine several entitlements: (i) information, (ii) consultations/involvement, and (iii) co-decision/representations (e.g., in restructuring plans involving firing decisions or salary cuts, decisions concerning corporate welfare policies, etc.). Here, voice is exercised through (i) and (ii), while co-determination (iii) implies that decisions cannot be achieved in the absence of an agreement. For that reason, work councils (such as in the German tradition) are the stronger form of support to capabilities, as they limit the boss's authority. Granted, these forms of participation are not the only

ones that characterize CG regimes. On this point, Armour et al. (2016, 2017) provided indexes and measures on these corporate entitlements for workers operating under different national legislations.

Another aspect related to participation is connected to the right to work, which guarantees that workers cannot be arbitrarily excluded (i.e., fired without just cause). Stricter dismissal rules reduce the *expected* exit costs and increase people's readiness to participate in on-the-job decision processes because retaliations (in the form of dismissals) would be an unlikely scenario. This entitlement is created at the 'constitutional level', as we define it, which affects the governance procedure by which a company may renegotiate and terminate labour contracts with its employees. Here, the functioning stemming from "participating in the decision-making" process could also be measured in terms of the restrictions on and remedies for unfair dismissal. Again, Armour et al. (2016) provided an index and measures on this issue through their analysis of national legislations.

For consumers, participation encompasses the entitlement to be heard. This can be measured by the transparency, efficiency and responsiveness of the process for managing consumers' complaints. For instance, the United Nations Guidelines for Consumer Protection (UNGCP) (cf. resolution 70/186 of 22 December 2015) defines a right to be heard by consumers within the principles of "consumer complaints and disputes".

Finally, participation for communities relates to the entitlement to be informed about decisions that affect them (e.g., about new industry settlements in the area) or, more generally, the entitlement to corporate accountability toward said communities. In fact, corporate accountability is a precondition for stakeholders' voice. Participation can also relate to community engagement in relevant decisions: For example, external stakeholder associations may want information and consultation entitlements on strategic decisions that affect the community (e.g., the adoption of a new technology or a plant closure). Some innovative proposal—looking for a balance amongst different participatory entitlements—suggests the participation of communities' representatives in committee similar to works councils where traditionally workers exercise more effective codetermination at least at the factory level (Sacconi 2019).

## **8. FINAL REMARKS**

Transactions within a firm are marked by a hierarchical nature that differentiates them from market transactions (Coase, 1937). Because a firm's hierarchy can and does affect substantially stakeholders' well-being and the inequalities of well-being distribution amongst them, we adapted

and adopted a theory of social justice (namely the CA) to analyze CG. Traditionally, the CA focuses on *public* or *State* institutions. We extended this framework to the firm—an institution often seen as only belonging to the autonomy sphere of private economic agents, but that according to the CA, integrated with the perspective of constitutional and post-constitutional contracts, can suitably take a place in the theory of distributive justice. In this view CG is a structure of entitlements aimed at supporting and protecting stakeholders' capabilities, primarily by means of their liberty to access the firms' characteristics, and consequently by shaping and constraining property and residual control rights in order to achieve their functionings. Accordingly, this paper provides a new foundation of corporate governance based on Sen's capability approach.

Despite its contribution to theory, our paper features limitations that may inspire future research. The first weakness is that we defined capability at the individual level (because the functioning depends on individuals' capacities and conditions), but we could assume a conversion factor at the class level (e.g., the class of workers, consumers, etc.). Surely, one can make further distinctions—for instance, the class of shareholders includes majority shareholders and minority shareholders who both have different conversion factors—but a measure at the individual level is a step forward. Moreover, our tool does not claim to be a complete map of capabilities-as-entitlements within firms; rather, we provide several examples of how that concept could be practically applied within firms.

Future research should strive to exhaustively populate our framework: for instance, by conducting comparative analyses that assess different CG regimes from different national systems. Such research could produce a normative evaluation of CG regimes, answering whether there are *optimal* governance structures that can be associated with *maximal* capability sets.

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