

**Governing the void between stakeholder management and sustainability**

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### **ABSTRACT**

In this paper, we explain why firms selectively responding to the most powerful, legitimate, and urgent demands of their stakeholders will not bring about sustainability and offer suggestions on what we should do in light of this shortcoming. Sustainability issues tend to be wicked problems that require cooperation across parties and over time to define and resolve. Stakeholder pressures can bring sustainability to the fore, but government intervention is necessary to drive meaningful action to resolve such issues. Without government intervention, self-interested stakeholders can pressure firms to move away from the complex, long-term challenges of wicked problems. Yet, stakeholder pressure is also necessary, as without it, industries may self-regulate in self-serving ways. Our analysis thus suggests that collaboration between business, government, and stakeholders is necessary to resolve the wicked problems of sustainability. We therefore urge the stakeholder literature to move beyond its libertarian underpinnings by (re)incorporating government into models of effective corporate governance.

**Keywords:** *stakeholder management, sustainability, government intervention, wicked problems, corporate governance*

*“What is being asked and expected of corporations today is increasing even as the economic contractarian model of the firm itself has revealed clear practical limitations (Gordon, 2002). The free market may not produce the inexorable march toward worldwide prosperity and well-being that is so often anticipated (Stiglitz, 2002). Even as business organizations may be imperfect instruments for advancing a narrowly construed wealth-maximizing objective, ironically, they may also be the entities of last resort for achieving social objectives of all stripes” (Margolis & Walsh, 2003: 296).*

## **INTRODUCTION**

Many of the world’s critical natural resources are limited. Firms often overexploit these limited resources. Such overexploitation threatens the sustainability of both business and society. Their collapse is, well, a highly undesirable outcome. What can we do about this? Stephen Hawking famously declared that we must move to another planet within a century (Zorthian, 2017).

Lacking ample rocketry, we instead focus herein on a nearer-term terrestrial solution.

Specifically we ask, can stakeholders drive firms away from overexploitation of natural resources and toward sustainable practices?

Firms are dependent upon the resources that stakeholders choose to provide or withhold, so firms attend to the demands of their stakeholders (Freeman, 1984). Accordingly, whether the natural environment is considered to be a stakeholder (Driscoll & Starik, 2004) or its interests are represented by other stakeholders, firms are responsive to stakeholder demands to increase the sustainability of their business practices (Murillo-Luna, Garces-Ayerbe & Rivera-Torres, 2008). Stakeholder management thus has been used as a lens to address sustainability issues; in fact, the term sustainability has been used interchangeably with that of stakeholder management

(Schwartz & Carroll, 2008).

In this paper, we argue that though (and because) firms are indeed responsive to stakeholder demands, stakeholder management is *not* an effective way to end overexploitation of natural resources and bring about sustainability. Stakeholder management drives firms to consider the interests of a broader set of stakeholders than does the long-established dictum of shareholder management, but the many stakeholders to which firms attend have many differing interests, many of which are not in sustainability. As they selectively respond to the most powerful, legitimate, and urgent demands of their stakeholders (Mitchell, Agle & Wood, 1997), firms are unlikely to traverse a path to sustainability. Moreover, sustainability issues tend to be wicked problems that require cooperation across parties and over time to resolve, or even just to define (Rittel & Webber, 1973). Managing by prioritizing the demands of some stakeholders over those of others retards necessary cross-stakeholder cooperation. Counter to stakeholder theory's libertarian underpinnings (Freeman & Phillips, 2002) but consonant with the results of decades of stakeholder management in practice (Walsh, 2005), we therefore conclude that government regulation is necessary to put business on a path to sustainability; the strategic management of stakeholder interests alone is not sufficient to motivate or enable firms to do so.

We begin by addressing who "counts" as a stakeholder and how firms manage their relationships with those they deem to be stakeholders. We focus on the stakeholder status of the natural environment and that of the government, which has been the traditional caretaker of the natural environment. We then turn our attention to the wicked problems of sustainability. We define sustainability and then show how its characteristics render many sustainability issues to be wicked problems that require different responses than do tame problems. Having clarified what it means to manage for stakeholders and what it means to be sustainable, we then discuss the ways

in which stakeholder management proves unable to meet the conditions necessary to drive firms toward sustainability. Thereafter, we deviate from the libertarian underpinnings of stakeholder theory to argue that government intervention is essential to achieving sustainability, whereas stakeholder pressures alone fall short. We conclude with a summary and future research implications.

## **MANAGING FOR STAKEHOLDERS**

Firms that manage for stakeholders take into account the interests of a broader set of constituents than do firms operating under the long-dominant shareholder management approach. However, precisely whose interests a firm prioritizes remains the subject of considerable debate. Two approaches to the definition of a stakeholder have emerged in the literature: the broad view and the narrow view (Clarkson, Starik, Cochran & Jones, 1994; Mitchell, Agle & Woods, 1997).

The broad view is derived from Freeman's (1984: 46) original work that defines a stakeholder as "any group or individual who can affect or is affected by the achievement of the organization's objectives." Among other groups identified by Freeman are owners, customers, governments, consumer advocates, environmentalists, employees, media, and suppliers. In this broad view, the list of potential stakeholders can grow quite quickly as the only criteria for determining stakeholder status is influence, without any notion of the "materiality" of that influence. Hence in this view, it makes sense to speak of "fringe" stakeholders (Hart & Sharma, 2004). In contrast, given the cognitive limits of managers and the need to ration their attention, the narrow view limits who is granted stakeholder status (Mitchell et al., 1997). Clarkson (1995: 106) restricts stakeholders to "persons or groups that have, or claim, ownership, rights, or interests in a corporation and its activities, past, present, or future." Orts and Strudler (2002)

emphasize risk as the key attribute of the stakeholder relationship because stakeholders place “some property or other asset ‘at risk’ in a business firm” (2002: 218). Using this risk-based approach, Orts and Strudler (2002) include shareholders, creditors, employees, customers, and suppliers as stakeholders, but exclude governments, third parties harmed by the firm, and the natural environment.

Both views present challenges for managers. Given that managerial attention is limited, managers have to determine which stakeholders to pay attention to. In the narrow view, this problem is solved a bit more easily because risk is mutual for this narrow or “primary” (Clarkson, 1995) group of stakeholders. These stakeholders merit the attention of managers because they are groups “without whose continuing participation the corporation cannot survive as a going concern” (Clarkson, 1995: 106). However, in the broad view, the problem is more complicated, requiring managers to take into account the salience of the stakeholder group. Mitchell et al. (1997) claim that managers judge salience based on three attributes: power, legitimacy, and urgency. Managers will pay increasing attention to stakeholders to the degree that they possess more of these attributes. But power is probably the most important of these three attributes (Frooman, 1999). For example, in the arena of environmental problems, Kassinis and Vafeas (2006) find that given the important resources controlled by local communities and the risk they face from toxic environmental emissions, community stakeholders can mobilize to become powerful enough to influence highly polluting firms to reduce plant emissions.

Different stakeholder groups have different interests and within each group, there is often great variation. Community stakeholders are especially characterized by highly heterogeneous interests (Kassinis and Vafeas, 2006). As a result, it can be difficult to determine what stakeholders want, yet these heterogeneous interests, combined with a significant potential to

influence the achievement of firm objectives, necessitates firm responsiveness. Financial theorists postulate that managers should always respond in ways that maximize shareholder value (Jensen, 2002), but stakeholder theorists argue that managers need to “manage for stakeholders,” which can be a more effective way to achieve competitive advantage for the firm. By managing for stakeholders, firms can tap information from friendly stakeholders that can enable the firm to innovate and adapt to a changing environment (Harrison, Bosse & Phillips, 2010).

The key issue then for invoking a stakeholder management approach is to determine whether a particular entity is a stakeholder. Of special interest to our discussion here is how stakeholder theorists have viewed the natural environment and governments as stakeholders. Therefore, we next review arguments surrounding both of these controversial candidates for stakeholder status.

### **Is the Natural Environment a Stakeholder?**

Scholars have taken at least three approaches to the relationship of the natural environment to stakeholder theory: the natural environment is a stakeholder; the natural environment is not a stakeholder, but is accommodated through human stakeholders; and stakeholder theory cannot accommodate the natural environment. Let us examine each of these three approaches.

Starik and his colleagues have contended that the natural environment should be considered a stakeholder and thus subject to the methods of stakeholder management. They claim that the bias against the environment as a stakeholder goes back to Freeman’s definition, which refers to individuals or groups – human actors (Starik, 1995: 208). However, Starik (1995) argues that non-human nature qualifies as a stakeholder because it constitutes a business

environment and is a political-economic entity that has both power and a voice. Building on Mitchell et al. (1999), Driscoll and Starik (2004) argue that non-human nature also has bases for being considered a salient stakeholder because it possesses power, legitimacy, and urgency. Furthermore, they argue for including spatial proximity as an additional attribute of stakeholder saliency, which helps determine which aspects of non-human nature affect the firm.

The second approach to the status of the natural environment is to argue that although the natural environment cannot be considered a stakeholder itself, stakeholder theory can accommodate its needs. Phillips and Reichart (2000) hold that stakeholder status can only be conferred on human individuals or groups because only they can develop obligations to which they freely consent upon receiving the benefits of these obligations. Nevertheless, stakeholder management is able to take into account the natural environment. They explain that the natural environment must necessarily be represented to the firm through human interlocutors. Many of these interlocutors are stakeholders, such as environmental activists, employees, or consumers, who have specific interests in the well-being of the natural environment. However, there may be occasions in which no stakeholder has an interest in the natural environment and managers would need to look outside the stakeholder framework to find moral reasons to be concerned about the natural environment.

Finally, building on the narrow view of stakeholders, Orts and Strudler (2002) find that the natural environment cannot be considered a stakeholder because it does not have an economic stake at risk in the performance of the firm. They conclude that both of the prior approaches to fit the natural environment into the stakeholder framework amount to nothing more than a Procrustean bed. Rather, they recommend abandoning this attempt as there are good legal and moral reasons for managers to care for the environmental impacts of their firms.



## **Is Government a Stakeholder?**

Although less controversial than the natural environment, government has also had a very equivocal relationship with stakeholder theory. On the one hand, according to Freeman's (1984) original "broad" view, government is a stakeholder. According to this view, government clearly can affect and is affected by the firm. On the other hand, in keeping with their "narrow" view of stakeholder status, Orts and Strudler (2002) argue that governments have no economic stake at risk in the firm and therefore cannot be considered a stakeholder without the term losing all meaning. Nevertheless, firms have a moral duty to obey the law and pay their taxes. Balancing stakeholder interests makes no sense in terms of the government when in fact firms may not trade off their duties to obey the law with other stakeholder interests.

A second difficulty with the role of government from the perspective of stakeholder theory is revealed by the strong libertarian streak that runs through much of stakeholder thought. Here we make two points. First, to the extent that government is included as a stakeholder within the stakeholder framework, it seems to become simply one among many stakeholders that managers need to engage. Second, setting aside Tony Blair's invocation of the "stakeholder economy" with slightly socialist overtones, the concept of voluntarism, at least in the US context, was highlighted in Freeman's (1984: 74) initial work: "Voluntarism means that an organization must on its own will undertake to satisfy its key stakeholders. A situation where a solution to a stakeholder problem is imposed by a government agency or the courts must be seen as a managerial failure." Later Freeman and Phillips (2002) defend stakeholder theory from a libertarian perspective. In that essay, they lay the groundwork for understanding how stakeholder theory is compatible with libertarian principles, especially concepts such as consent,

voluntariness, and negotiation. They explain: “Business is founded (and businesses are created) on this idea of making agreements with each other. And we are free to make these agreements because others are not permitted to interfere (so long as they are not substantially affected)” (Freeman & Phillips, 2002: 341). Hence stakeholder theory fits well with the minimal “night watchman” state (Nozick, 1979).

Whether government is classified as a stakeholder – one of many – or as a night watchman that protects citizens from fraud, theft, and violence, stakeholder theory is consonant with a reduced role for the state. After next defining sustainability, we then turn to determining the extent to which a stakeholder approach, with its reduced role for government, can foster sustainability.

### **THE WICKED PROBLEMS OF SUSTAINABILITY**

Before we discuss how an organization can become sustainable, we first need to explain what we mean by sustainability. Sustainable development is defined as the ability to "meet the needs of the present without compromising the ability of future generations to meet their needs." (WCED, 1987: 8). The main principles of sustainable development are environmental integrity, social equity, and economic prosperity (Elkington, 1998). A sustainable enterprise is “one that contributes to sustainable development by delivering simultaneously economic, social, and environmental benefits—the so-called triple bottom line” (Hart & Milstein, 2003: 56). Thus, to be sustainable, a firm must grapple with much more than just maximizing its bottom-line economic returns.

The sustainability management literature (Etzion, 2007) has tended to lump the environmental issues an organization faces into a single problem, such as pollution, waste,

deforestation, or climate change. Such an approach ignores the complexity of sustainability and impedes a systematic understanding of how the problem relates to organizational goals and the stakeholders with whom an organization must partner to achieve said goals. Drawing on Rittel and Webber's (1973) seminal article on the search for scientific bases for confronting problems, we note that particular environmental problems can sometimes be “tame” but often are “wicked” problems. By analyzing the scientific and social characteristics that distinguish tame from wicked problems, we can develop a better sense of how a firm might successfully navigate such problems and with whom to partner when seeking to do so.

Recent research has begun to examine how the complexity associated with climate change can affect an organization’s ability to achieve its sustainability goals (Hahn, Preuss, Pinkse, & Figge, 2014; Neugebauer, Figge, & Hahn, 2016). Our focus herein, however, is on examining how stakeholder management affects sustainability, particularly absent the involvement of governmental agencies as active, legitimate, urgent and powerful stakeholders. The discourse on managing for sustainability at the firm level favors such market-based approaches (Banerjee & Bonnefous, 2011). However, in the face of wicked problems, governmental involvement may prove essential to addressing sustainability goals.

### **Tame versus Wicked Environmental Problems**

Environmental issues are not all alike. Some, like certain types of waste and water pollution, originate from a specific source and can be reduced by the emitter choosing to reduce the activities that cause the polluting activities. Such environmental problems are mostly “tame” in that scientists and engineers can use their knowledge to solve the problem. On the other hand, issues such as climate change originate from multiple sources and cannot be reduced unless all

sources agree to reduce their emissions. These issues are wicked problems.

Wicked problems occur within what Rittel and Webber (1973: 160) call an open societal system where problems are ill-defined, dynamically complex, and “rely on elusive political judgment for resolution.” Their wicked nature “stems not only from their biophysical complexity but also from multiple stakeholders’ perceptions of them and of potential trade-offs associated with problem solving” (Batie, 2008: 1176). Table 1 provides a synopsis of the characteristics that distinguish a tame from a wicked environmental problem. We next discuss how these characteristics affect a firm’s decision-making processes.

INSERT TABLE 1 ABOUT HERE

**Definition and nature of the problem.** Albert Einstein once said: “If I were given one hour to save the planet, I would spend 59 minutes defining the problem and one minute resolving it.” Though often difficult, problem definition is manageable if the environmental problem is tame. A clear definition of the problem elicits the solution and the outcome is determined by whether the solution is successful or not. A tame environmental problem possesses scientific protocols that can guide solutions, is associated with low uncertainty as to the complex system components and outcomes, tends to be confined to one area, and does not change very much across time. Moreover, the actors involved in seeking a solution to the problem agree that the outcome is desirable. Examples include energy conservation, end-of-pipe pollution where the source is known, and waste disposal.

Such is not the case with wicked environmental problems. Here there is no agreement as to the definition of the problem and each possible solution changes the problem. Moreover, there

is no single outcome. Instead, there are assessments as to whether matters have improved or not, as the problem changes across time and spreads over many regions. Thus outcomes are highly uncertain, but so too are the potential causes and effects underlying wicked problems (Batie, 2008; Conklin, 2005).

Consider climate change. Defining the problem requires knowledge of the existing condition, the desired condition, and the complex causal networks within which the problem really lies (Rittel & Webber, 1973). These networks include both the biophysical and societal systems. A problem definition that states that burning fossil fuels causes climate change would inevitably result in a solution that stipulates we stop burning fossil fuels. Negotiating such a solution, however, would be extremely difficult as energy is a critical human need affecting a host of stakeholders and self-interested parties worldwide. A different solution would entail investment in clean technologies, but such a solution begs the question of who will undertake such an investment if fossil fuels continue to dominate. Another solution would suggest that countries with the greatest emissions should be obliged to reduce their emissions accordingly. The social context and the type of knowledge needed to address the problem make the decision process messy despite scientific evidence that climate change has moved firmly into the present and is affecting health, water, energy, and agriculture (Hoffman, 2015), thereby generating other wicked problems. In other words, there are no shared values with respect to the societal goals despite the scientific consensus that the global climate is changing and that humans are partly responsible. Truly wicked stuff.

**Social context and type of knowledge.** A rational scientific approach leading to a negotiated solution may be possible for a tame environmental problem with a limited number of stakeholders, including those who created the problem. But a wicked problem is a public

problem that is dispersed amongst a host of actors that cannot be resolved by a single actor alone. A socially efficient outcome in this case is simply not possible unless property rights are well-defined, enforceable and transferable, and interested parties are keen on getting together to negotiate the associated environmental property rights (Coase, 1960). In other words, wicked problems are not amenable to decentralized policies such as moral suasion, stakeholder negotiation, and liability laws. It is necessary to develop different programs to appeal to many people's sense of moral values or civic duty, but the number of stakeholders is too large for a settlement to be achieved. Relying on liability laws would simply make polluters liable for the damages which, based on the standards of proof required by courts, may be more than the probabilistic proof science can provide.

The knowledge required to address a tame environmental problem is based on the solution chosen (Batie, 2008). For example, if an effluent from a company is emitted into a body of water and the company wishes to reduce the environmental impact of such emissions, the information required would involve either adopting an end-of-pipe solution or a circular system whereby the effluent no longer flows into the body of water. The knowledge required would tend to be confined to a small group of primary stakeholders. In the case of a wicked problem where the problem is not well defined or accepted, tensions between the long-term versus short-term impacts (Slawinski & Bansal, 2015) and the economic versus environmental versus social consequences require that stakeholders to the problem co-create the knowledge necessary to bridge the social, environmental, and economic tensions that such wicked problems entail.

The advent of the motor car was viewed as a solution to the environmental issues associated with horse drawn carriages - that is, dung. According to Geels (2005:456), "the emerging hygiene movement and new health professionals thought that the abundance of

decaying organic filth filled the air with poisonous vapours, miasmas, which caused epidemic diseases.” As cities came to be seen as filthy, unhealthy, and dangerous, solutions emerged including the building of parks to function as the lungs of the city, and the substitution of the horse for other means of transportation such as the electric tram, the bicycle, and the horseless carriage – the predecessor for the car (Geels, 2005). Today, fossil fuel burning cars are viewed as being partly responsible for climate change – another wicked problem. According to Batie (2008: 1183), the “co-creation process, by allowing participants to critically reflect on each other’s views, enables participants to reflect not only on their own preferences and viewpoints but also how they might be changed.” Such co-creation is emerging in the automobile sector where entrepreneurial firms “found creative ways to circumvent the drawbacks of electric vehicles (e.g., cost, range, charging time)” (Bohnsack, Pinkse, & Kolk, 2014: 298), forcing the incumbents to critically reflect on the future of the motor engine and invest in electric vehicles as a possible alternative to the motor vehicle given a carbon-constrained future. Thus, creative solutions do sometimes emerge to address wicked problems. But can stakeholder management be relied upon to address the wicked problems of sustainability? We next address this.

### **SUSTAINABILITY VIA STAKEHOLDERS: CAN WE GET THERE FROM HERE?**

Though certainly not without its backers even today, the view that a firm should be managed solely to maximize shareholder value has come under intense scrutiny in recent years and even been dismissed as “the dumbest idea in the world” by the most revered of management practitioners (Denning, 2015). In its stead, stakeholder management has now “infiltrated the academic dialogue in management” (Harrison & Wicks, 2013: 97). In managing for stakeholders, firms seek not merely to contract with stakeholders but rather, to build and

strengthen mutually beneficial relations with them: “A firm that manages for stakeholders allocates more resources to satisfy the needs and demands of its legitimate stakeholders than would be necessary to simply retain their willful participation in the firm’s productive activities” (Harrison, Bosse & Phillips, 2010: 58). But as they satisfy the needs and demands of their legitimate stakeholders, do firms also manage to foster sustainability?

Consonant with managing for stakeholders, a sustainable firm also must do more than merely optimize returns to its shareholders; it must pursue a triple bottom line that focuses on social and environmental returns alongside economic returns (Hart & Milstein, 2003). In recent years, many stakeholders have taken much greater interest in firms’ social and environmental practices. For example, as Dawkins and Lewis (2003: 185) found: “Traditionally, the factors that mattered most to consumers when forming an opinion of a company were product quality, value for money and financial performance. Now, across a world-wide sample of the public, the most commonly mentioned factors relate to corporate responsibility (e.g. treatment of employees, community involvement, ethical and environmental issues).” Thus, it certainly seems feasible that in the process of satisfying stakeholder demands, firms will become sustainable.

Yet, if we look out across the planet, even absent ample rocketry we can see that despite the deep embeddedness of stakeholder management in theory and practice, firms continue to overexploit natural resources and sustainability remains an elusive goal. Water is critical and finite, yet bottlers overdraw it from aquifers while denying locals access to clean water (Lenzer, 2009), 63 percent of global fish stocks are now considered overfished (Greenpeace, 2017), and polluters have created dead zones in waterways that cover thousands of square miles (GRN, 2017). As the World Wildlife Fund notes, forests “produce vital oxygen and provide homes for people and wildlife. Many of the world’s most threatened and endangered animals live in forests,



and 1.6 billion people rely on benefits forests offer,” yet every minute, we lose the “equivalent to 48 football fields” of forest (WWF, 2017). Even sand – “the essential ingredient that makes modern life possible” – is in finite supply and dwindling (Beiser, 2016). As they overexploit sand stocks, firms are “disrupting ecosystems, killing countless fish and birds” in India, have “damaged coral reefs in Kenya and undermined bridges in Liberia and Nigeria. . . People are getting hurt, too” (Beiser, 2016).

What gives? For stakeholder management to foster sustainability, a firm’s legitimate stakeholders must demand sustainability and, moreover, firms must be able to meet these demands. As we discuss next, these conditions often are not met.

**Stakeholder demand for sustainability.** Though stakeholders now voice greater concern for social and environmental performance (Dawkins and Lewis, 2003), their bark often proves worse than their bite. Consider consumers. Consumers widely report strong preferences for firms to engage in sustainable business practices, but the vast majority will not follow through on their preferences if it requires any significant cost for them to do so (Vogel, 2005). Whelan and Fink (2016) estimate that consumers are only willing to pay up to a 20% price premium for sustainable products. The void between consumer claims and actions is so large that some scholars dismiss consumer action to promote corporate social and environmental responsibility as mythical (Devinney, Auger & Eckhardt, 2010). More generally, Harrison and Wicks (2013: 111) argue: “While stakeholders through their cooperation in firms will want to improve society and not harm the environment, it isn’t clear the extent to which they will do so in their capacity as stakeholders.” For example, although new recruits may be more attracted to and accept lower pay from a company with a good reputation for CSR (Turban & Greening, 1997), there is no hard evidence as to the percentage of the labor pool that is willing to do this.

Employees may indicate a preference to work for clean firms, but their employers are more likely to keep them satisfied by increasing employee pay and benefits than by reducing polluting emissions. Thus, in many cases, sustainability issues “are not clearly or directly tied to value creation for stakeholders and the utility they seek in the firm” (Harrison & Wicks, 2013: 111).

Stakeholders may even fail to make sustainability demands or choose to support unsustainable options. Industries that produce products higher up the value chain could avoid stakeholder pressures if their detrimental activities are not visible to the end-consumer. Doonan and Laplante (2005: 82), in their study of the Canadian pulp and paper industry, found that “capital markets and consumer markets did not appear as statistically significant sources of pressure” insofar as environmental performance was concerned and that the most important source of pressure was government. Moreover, industry resistance to calls to improve environmental practices can be bolstered by union and employee fears that environmental efforts may negatively impact competitiveness and thereby threaten their jobs (Räthzel & Uzzell, 2011).

Nonetheless, sustainability is an actionable concern to at least some stakeholders, including those whose demands may be powerful, legitimate, and urgent. But even for these stakeholders, cognitive constraints forge a gap between the occurrence of sustainability problems and their demands for firms to act. As Barnett (2014: 695) notes, “Whether primary or secondary, legitimate or illegitimate, powerful or weak, a stakeholder is constrained by limited attention” and this binding constraint means that stakeholders, no matter how concerned with sustainability issues, will overlook a significant portion of the socially and environmentally destructive behaviors of firms. Gao and Bansal’s (2013: 51) claim that “in most issue domains, stakeholders are unaware of relatively small improvements in a firm’s social and environmental management, partly because the firm’s operations are not completely transparent and partly

because such small improvements are difficult to measure” further widens this gap. Firms’ sustainability programs can be slow to produce substantial change. If the small changes along the way are unlikely to be noticed and rewarded by stakeholders, firms may be less likely to undertake the costly and lengthy burden. As are many managers and their firms (Lavery, 1996), many stakeholders are myopic, favoring near-term gains over distant potential (March, 1991).

**Firm’s ability to meet sustainability demands.** Because stakeholders are self-interested, myopic, and heterogeneous, firms typically face a rather limited set of demands to engage in sustainable business practices, relative to the totality of demands that stakeholders place upon them. But in those cases where legitimate stakeholders do place powerful and urgent demands upon them to become sustainable, firms may still be unable to comply. Many sustainability problems are wicked, involving uncertainty and disagreement over scale, scope and timeframe to resolve. Although a manager may be able to define, say, corporate carbon emission targets for the firm, the outcome of such efforts may not be apparent or visible to stakeholders, given the complex nature of climate change, which requires the participation of all emitters for there to be improvements in the damaged ecosystem (Pogutz, Micale & Winn, 2011). Given their tendency toward risk avoidance (Cyert & March, 1963), managers may thus not prioritize such problems, reasoning that the inability to demonstrate direct and immediate improvements will fail to appease stakeholder demands.

Regardless of the actions that firms undertake to appease stakeholder demands for sustainability, they may prove inadequate to abate such wicked problems. Again consider climate change. There is no direct link between what stakeholders may individually or jointly demand and the total amount of climate change mitigation that individual firms need to provide in order to abate climate change. Moreover, stakeholder management does not provide a mechanism for

coordinating action across unrelated firms. For example, the Mexican beverage company FEMSA and Oneida Silver, a manufacturing company in the US, may not have any stakeholder relations. Yet if both firms need to reduce greenhouse gas emissions, how do they coordinate their reductions? When has each one done enough? The bargaining problem among firms quickly becomes unmanageable.

Where firms compete, there is an incentive to do less and in this way gain a competitive advantage with respect to firms that do more. Heterogeneous stakeholders have little interest in or ability to punish unrelated and distant climate change laggards. The ability of the firm to reason when faced with self-interested, myopic and heterogeneous demands is further distorted by media where “the economic and ideological interests of those who stand to lose in the face of climate change solutions have tremendous power to sway public debate that is marked by low scientific literacy, expanding sources of information, and a fractured and conflicted world of 24-hour news cycles” (Hoffman, 2015: 47).

Further, time is not on sustainability’s side. Sustainability is an intergenerational dilemma. Intergenerational dilemmas are defined as “decisions that entail a tradeoff between one’s own self-interest in the present and the interests of other people in the future” (Wade-Benzoni & Tost, 2009: 365). Decisions to ignore climate change, for example, affect other people in the future. An intergenerational perspective broadens the definition of economic interests to include multiple parties across time (Wade-Benzoni, 1999). Wade-Benzoni and Tost (2009) argue that intergenerational reciprocity, uncertainty, and legacy creation can help reduce both the intertemporal and interpersonal distances that tend to increase intertemporal and social discounting of the future. More specifically, where prior generations have passed on benefits to future generations based on how well they were treated by past generations, when the outcome

uncertainty suggests that future generations may receive nothing, and where the legacy of the generation is one of great burdens for future generations, there will be greater intergenerational beneficence or generosity (Wade-Benzoni, Sondak & Galinsky, 2010). The question remains as to who has the hindsight and foresight to take on this intergenerational analysis. Given that stakeholders tend to be self-interested, myopic, and heterogeneous, it is unlikely that an intergenerational dilemma like climate change can be addressed by firms, customers, employees, investors, communities or suppliers.

Overall, when managing for stakeholders, firms are likely to face low demand for sustainability relative to the many other demands that stakeholders place upon them, and firms are likely to provide even less, given limited ability to meet the demands for sustainability that do arise. Given the resulting undersupply, we next explore the role of government in bringing about sustainability.

### **THE ROLE OF GOVERNMENT IN SUSTAINABILITY**

Though it has become synonymous with corporate social and environmental responsibility, stakeholder management was put forth as a strategy to benefit the firm. As Harrison et al (2013: 59) clarify, when firms profit by gaining and maintaining stakeholder favor, any benefit beyond the firm is incidental:

*“From its early development, the stakeholder concept has emphasized effective management of a broad group of stakeholders rather than social responsibility [emphasis in original] (Freeman, 1984; Walsh, 2005). Overemphasis on society (broadly defined) as a stakeholder seems to have led some strategic management scholars to believe that stakeholder theory is about managing social interests*

responsibly rather than managing a firm effectively.”

Nonetheless, much as the “invisible hand” of the market is assumed to metaphorically guide the pursuit of individual self-interest toward the benefit of society (Smith, 1776), the business and society literature commonly assumes that the oft-visible hands of stakeholders guide self-interested firms toward sustainable practices. However, stakeholders may actually use their powerful hands to push firms in the opposite direction, driving out the greater good as they pursue their self-interest: “[I]t is now time to recognize that stakeholder theory may not be effective at managing many of society’s pressing problems and, in fact, could be driving firms away from deeper involvement with society” (Barnett, forth: 20)

Firms must prioritize stakeholder demands. This means serving the interests of their most powerful stakeholders, a group that rarely includes the natural environment. Empirical studies that have parsed types of stakeholders have indeed found that firms advance their financial interests by advancing the interests of their primary stakeholders, but when they devote greater effort to serving secondary stakeholders such as the natural environment, firms may suffer financially. For example, a study by Berman, Wicks, Kotha and Jones (1999) found a positive relationship between return on assets and the degree to which firms concern themselves with serving the needs of their employees and customers, but no relationship between return on assets and efforts to safeguard the natural environment. Hillman and Keim (2001) also found that it pays to serve the needs of primary stakeholders, but *a fortiori*, found a negative relationship between firm financial and broader social performance. Likewise, Van der Laan, Van Ees, and Van Witteloostujin (2008) found that the positive relationship turns negative when firms stray beyond serving their primary stakeholders. Of course, the true relationship for any given firm

varies based on numerous contingencies (Barnett, 2007), and so across the hundreds of published empirical studies, when measured in different ways across different time periods with different firms in differing settings, sometimes it also pays to be green. Nonetheless, as firms become more and more strategic about serving their own interests through stakeholder management, the interests of the natural environment, where returns are more distant and uncertain than when serving primary stakeholders, may rationally be driven out, not incidentally or strategically advanced (Barnett, forth). As stakeholders gain greater voice in firm governance, they may use this voice to secure their own gains at the expense, not benefit, of the greater good.

Despite this, the stakeholder literature often highlights the ability of firms to “do well by doing good.” By arguing that stakeholder pressure suffices to bring about the greater good, the literature retards calls to do so through formal regulation. Yet government intervention is necessary to “own” problems of the scale and scope of sustainability and to provide the authority and ability to bring about solutions. As Coase (1960) argued, for some types of problems where rational actors transact freely, there is no need for government intervention, since the actors can negotiate their own optimal solution. Where the affected parties are few, they can negotiate a solution with the offending firms. Where there are few firms generating external social costs and few affected parties (stakeholders), bargaining makes sense. But in many environmental problems, this condition is not met. In the case of air pollution, polluting firms may be few, but the affected parties may be quite numerous and bargaining becomes impossible (Baumol and Oates, 1975). In addition, sustainability problems often extend over generations (Wade-Benzoni, 1999). For such wicked problems, the affected parties (future generations) may not yet even exist. Moreover, the causal chain for wicked problems is highly ambiguous. Although air pollution may be traceable to a specific source, climate change is complicated by the fact that all

living beings generate carbon emissions. Assigning responsibility among so many sources is almost impossible.

Thus, a gap exists. Self-interested firms serving self-interested stakeholders does not sum to sustainability. Government exists to fill such a gap. Governments have many advantages over self-interested firms and stakeholders. Effective governments can reduce uncertainty (North, 1991), which enables firms to compete on a level playing field. Governments can often assume greater risk than firms in innovation and can undertake pilot projects and experiment with possible solutions that firms could never undertake. Therefore, risk aversion by the private sector on issues that are of importance to society has often been taken up by governments. Mazzucato (2015) debunks the myth that the public sector is not a risk-taker. According to her research, Apple, Google and Amazon would not have been possible without the public investments that gave rise to the internet, microchips, GPS and the touchscreen. In the case of wicked environmental problems, there needs to be an agent who can take risks on possible solutions despite their complexities. Pilot programs are one example where governments can test possible solutions to determine if the solution improves the current context or not (Batie, 2008). Finally, governments are much less likely to go out of business and so can provide continuity to the solution of wicked problems.

Government intervention can take many forms. Three of the most common forms are command-and-control regulation, taxation, and market solutions (Dales, 1968; Montgomery, 1972). Command and control regulation occurs when government prohibits certain kinds of behavior and castigates violators with fines or even incarceration. Taxation is often used to provide incentives to avoid socially undesirable behavior (taxes on emissions) or engage in positive behavior (subsidies for solar energy). Finally, in the environmental arena, governments



have experimented considerably with the creation of environmental markets for SO<sub>x</sub>, NO<sub>2</sub>, and carbon emissions. Whereas taxes provide certainty for firms with respect to the price by letting polluters determine the quantity of emissions, environmental markets provide society with certainty with respect to the total quantity of emissions by letting prices fluctuate. We next describe how such governmental interventions can push firms beyond just managing for stakeholders, to actually manage for sustainability.

### **MANAGING FOR SUSTAINABILITY: MOVING FORWARD**

In his 1981 inaugural address, Ronald Reagan famously declared that “government is not the solution to our problem; government is the problem.” This ushered in a broad and deep shift toward deregulation in the US and beyond, under the assumption that markets achieve the best outcomes when left unburdened by government intervention. The stakeholder view arose during this period (Freeman, 1984). In arguing that firms serve their own interests by serving the interests of their stakeholders, the stakeholder view suggests that burdensome government intervention is not needed to induce firms to serve the greater good. Glad to avoid the heavy hand of government regulation, firms were quick to adopt this view, thereby helping to legitimize and promulgate it across both scholarship and practice (Rowley & Berman, 2000). Today, the notion that firms produce widespread “win-win” outcomes by managing for stakeholders dominates the business and society literature (Harrison et al., 2010). Along the way, the role of government in regulating firm behavior has fallen to the wayside (Barnett, forthcoming).

Yet in matters of sustainability, as we have argued above, stakeholders may be the problem and government the solution. Though some “tame” problems are amenable to resolution

through stakeholder pressure, the “wicked” problems of sustainability cannot be resolved absent government intervention. Thus, it is time to (re)introduce government into the conversation about how firms can manage for sustainability.

#### INSERT TABLE 2 ABOUT HERE

The four quadrants in Table 2 above show how firms vary in their approaches to sustainability, depending upon the combination of pressures they face from their stakeholders and the government. In quadrant 1, labeled “Carefree”, the threat of formal regulation is low and stakeholders have little power, so firms face few external pressures to become more sustainable. However, this does not mean that such firms will never pursue sustainability. Rather, a firm in this quadrant will undertake more sustainable practices if there is a clear “business case” for doing so. For example, such a firm might switch from incandescent to LED lighting or add solar power capacity if the total savings from such programs are expected to exceed the total costs of implementation. As a result, a firm in this quadrant may exploit the “low-hanging fruit” of sustainability but is unlikely to go beyond this. This approach fits well within Friedman’s (1970) perspective that “the business of business is business,” not social and environmental advancement.

In quadrant 2, labeled “Calculation”, the threat of government intervention remains low, but firms are faced with many pressing demands from stakeholders to become more sustainable. Under these conditions, a firm retains considerable discretion but must make decisions about how to ration its limited resources amongst the myriad demands its stakeholders place on it. Accordingly, the firm is likely to prioritize the most legitimate and urgent issues brought forth by its most powerful stakeholders (Mitchell et al., 1997). This can lead to improved sustainability

practices to resolve tame problems but can also produce perverse outcomes, such as the Brent Spar incident in which Shell was pressured by Greenpeace to alter its practices regarding disposal of a defunct oil platform. This quadrant is consistent with the stakeholder view of the firm (Freeman, 1984).

As we move into the bottom two quadrants, we introduce government back into the mix. In quadrant 3, which we label “Collusion,” firms face low threat of stakeholder action but high threat of government intervention. Perceiving a credible threat of government stepping in to require more sustainable practices, firms in this quadrant may work together to mitigate this threat. Often this takes the form of industry self-regulatory programs. For example, facing stricter formal regulation of their industry in the aftermath of the deadly Bhopal poison gas leak, chemical firms came together through their trade association to create the Responsible Care program, in which member firms agreed to abide by a code of conduct requiring improvements in their operating practices (Barnett & King, 2008). Firms tend to prefer self-regulation over formal regulation, as the latter tends to be heavy handed and blunt. Many governments have welcomed self-regulation, given limited resources to enact formal regulation. However, such programs have been criticized for serving the needs of industry rather than meaningfully addressing sustainability problems; in fact, such programs have been shown to increase pollution (Gamper-Rabindran & Finger, 2012).

Finally, in quadrant 4, which we label “Collaboration,” firms face strong pressures from both stakeholders and the government to improve their sustainability practices. Here, firms are highly constrained and so, given limited resources, will seek to collaborate with both government and powerful stakeholders to achieve a suitable solution. With the involvement of government, it becomes possible and perhaps necessary to bear the risk of collaborative experiments that seek to

bridge the social, environmental and economic tensions inherent in wicked sustainability problems (Rittel & Webber, 1973; Batie, 2008).

Two collaborative agreements between government, business, Indigenous peoples, and environmental non-government organizations (NGOs) in Canada provide excellent examples of parties coming together to deal with wicked problems when facing pressures from government as well as powerful stakeholders to do so. Forest conservation and biodiversity is a wicked problem. The economic, social, and environmental interests are diverse and at times diametrically opposed. The Canadian Boreal Forest Agreement (CBFA, 2017), signed on May 10, 2010, recognizes that although the responsibility for the future of forestry and conservation in Canada's boreal forest rests with government, business, Indigenous peoples, and NGOs have an obligation to help define that future. The agreement seeks to implement world-leading sustainable forest management practices, improve forest conservation, protect boreal forest species, and improve the prosperity of the Canadian forest sector and communities that rely on this sector. With the intervention of government, environmental NGOs agreed to stop boycotting the forestry companies, and the forestry companies, in turn, agreed to suspend logging operations on nearly 29 million hectares of boreal forest that is home to the boreal caribou. Parties to the agreement are co-creating the knowledge necessary to bridge the social, environmental, and economic tensions that exist (Rittel & Webber, 1973).

The second example is the 20-year battle to protect the Great Bear Rainforest, which is the largest coastal temperate rainforest in the world (Hunter, 2016). The British Columbia government announced an agreement with environmentalists, forestry companies, and First Nations that applies to 6.4 million hectares of coast and protects 85 percent of the region's old-growth forests from logging. The agreement "recognizes aboriginal rights to shared decision-

making and improves economic opportunities for the 26 First Nations that reside in the region with a greater share of timber rights” (Hunter, 2016). The common value that aligned all the parties in this rainforest agreement was collaboration around values of protecting the land for future generations - a critical issue for First Nations. Thus, the Indigenous peoples brought and shared the intergenerational hindsight and knowledge needed for the agreement (Wade-Benzoni, Sondak & Galinsky, 2010), but the conditions for such an agreement would not have been possible without government intervention.

## CONCLUSION

Our analysis suggests that collaboration between business, government, and stakeholders is necessary to resolve the wicked problems of sustainability. The management literature has successfully pushed beyond sole shareholder concern as shown in quadrant 1 of Table 2, but we cannot be satisfied with advancing only as far as the next two quadrants. Shifts toward stakeholder management and industry self-regulation have helped to harvest low-hanging fruit, but the wicked problems of sustainability remain beyond our grasp. We must instead advance to quadrant 4, wherein stakeholder pressures are backed, bolstered, augmented, and given teeth by government. Though stakeholder pressures can bring sustainability issues to the fore, government intervention is necessary to set the stage for meaningful action and to ensure follow-through. Without government, self-interested stakeholders can pressure firms to move away from the complex, long-term challenges of wicked problems, and without stakeholder pressures, industries may self-regulate in ways that prove little more than “the fox guarding the hen house.” Said another way, we must move beyond the established “BS” of business and stakeholders, to (bear with us) think “BiGS: business interrelating with government and stakeholders.”

The dilemma with managing for stakeholders is that it tends to focus on who should be listened to rather than on the co-creation of the knowledge necessary to understand and deal with wicked problems. Government has the power and ability to bring actors to the table and to set the collaborative agenda on wicked problems. Nobel laureate Elinor Ostrom argued that a “polycentric approach” with experimental efforts at multiple levels (governments, business, community) is needed to assess and compare the veracity and efficiency of climate change solution strategies across ecosystems and avoid free-riding (Ostrom, 2014). Figueres and colleagues (2017: 593), in a *Nature* article regarding climate change, argued that we are running out of time and called on the G20 leaders of the world’s largest economies to “highlight the importance of the 2020 climate turning point for greenhouse-gas emissions, and to demonstrate what they and others are doing to meet this challenge.” Note that the call is to governments, not stakeholders, because of the urgency and complexity of the matter. More specifically, all levels of governments “must help drive the ambition of national governments on climate change, particularly through smart infrastructure and transport policy” (Figueres et al, 2017: 595). Time is of the essence. The point of no return is in three years, as they note. For other reasons, atomic scientists argue that we are a mere two-and-a-half minutes away from “doomsday.”

Unless we can resolve a myriad of sustainability problems in the very near future, it appears that our choice set will consist of abandoning this planet for another, finding a way to evolve as a species to adapt to the forthcoming drastic changes in this planet’s environment, or extinction. As we have seen after decades of stakeholder management, free market approaches are inadequate to bring firms around to addressing anything but the tamest of our sustainability problems. Voluntary efforts are simply not sufficient to deal with wicked problems. Rather, government intervention is necessary to address the wicked problems that threaten our survival.

If we are to live long, long live Leviathan (Hobbes & Gaskin, 1998)!

Of course, governments also have their limitations. Their inefficiency, failure to represent the interests of the people they were elected to serve, and tendency to be captured by special interests, or worse, subject to corruption, all provide reasons to be skeptical of governments (Besley & Ghatak, 2007). Future research must seek to find ways to use the strengths of government in convening, coordinating, and coercing the many parties that must come together over time to find meaningful, workable solutions to wicked sustainability problems, without succumbing to its dark side and harming economic prosperity and social wellbeing. Indeed, that is a balance that has always been sought implicitly but governments need to become stronger long-term stewards. However, since the rise and now dominance of stakeholder management, government has been given less and less heed, leaving managerial approaches to organizational sustainability out of balance, unable to guide firms toward it. It is well beyond time to reverse this by bringing business and government back into our research and teaching lexicon. Think BiGS!

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**Table 1: Tame versus Wicked Environmental Problems**

<b>Characteristics</b>	<b>Tame Environmental Problem</b>	<b>Wicked Environmental Problem</b>
<i>Definition and nature of the problem</i>	<ul style="list-style-type: none"> <li>❖ Clear definition of the problem elicits the solution</li> <li>❖ Outcome determined by whether solution is successful or not                             <ul style="list-style-type: none"> <li>❖ Scientific based protocols guide solutions</li> </ul> </li> <li>❖ Problem associated with low uncertainty as to system components and outcomes</li> <li>❖ Shared values as to desirability of outcomes</li> <li>❖ Problem largely unchanging across time</li> <li>❖ Problem usually confined to specific area</li> </ul>	<ul style="list-style-type: none"> <li>❖ Disagreement as to definition of the problem as each possible solution changes the problem</li> <li>❖ No single outcome - assessment whether things are better or worse                             <ul style="list-style-type: none"> <li>❖ Solution(s) based on judgement of multiple stakeholders</li> </ul> </li> <li>❖ Problem is associated with high uncertainty as to system components and outcomes</li> <li>❖ No shared values with respect to societal goals</li> <li>❖ Problem changes over time</li> <li>❖ Problem not confined to specific area or region</li> </ul>
<i>Social context and type of knowledge</i>	<ul style="list-style-type: none"> <li>❖ Handled by limited number of stakeholders including those who created the problem – a mostly private problem                             <ul style="list-style-type: none"> <li>❖ Solution dictates the knowledge necessary to proceed</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>❖ Public problem dispersed amongst a host of actors that cannot be resolved by a single actor alone                             <ul style="list-style-type: none"> <li>❖ Requires co-creation of knowledge to bridge social, environmental &amp; economic tensions</li> </ul> </li> </ul>
<i>Problem resolution</i>	<ul style="list-style-type: none"> <li>❖ Few stakeholders, so easier to bargain for solution</li> </ul>	<ul style="list-style-type: none"> <li>❖ No definitive solution; depends on judgements of many key stakeholders</li> </ul>
<i>Examples of problems</i>	<ul style="list-style-type: none"> <li>❖ Point pollution (single source of pollution is known), food contamination, soil erosion, energy efficiency</li> </ul>	<ul style="list-style-type: none"> <li>❖ Climate change, income inequality, biodiversity, deforestation, water, poverty</li> </ul>

Source: Adapted from Batie (2008), Rittel & Webber (1973) and Neugebauer, Figge, & Hahn (2016)

**Table 2: Resolving Sustainability Problems**

		Threat of Stakeholder Action	
		Low	High
Threat of Government Action	Low	<p><i>Carefree</i></p> <p>Managing for shareholders</p> <p>Friedman, 1970</p>	<p><i>Calculation</i></p> <p>Managing for stakeholders</p> <p>Freeman, 1984</p>
	High	<p><i>Collusion</i></p> <p>Managing for industry</p> <p>Barnett &amp; King, 2006</p>	<p><i>Collaboration</i></p> <p>Managing for sustainability</p> <p>Batie, 2008</p>

**1 2**  
**3 4**