Business Associations and Behavioral Research

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Why do various constituencies in business associations behave as they do? Scholarship addressing this question in an empirical or scientific way is relatively thin, with only a few scholars examining closely the true behavioral science arguably relevant to the question of why power-figures within business entities behave the way they do.[1] The paucity of writing in this area is a reflection of the infancy of this area of research, the lack of true behavioral experts writing in this area, and the fact that business associations scholars generally are not trained to do the necessary underlying experimental research.

In this presentation, I will review the existing business associations scholarship that incorporates behavioral research from the social sciences, and I will identify a few nagging weaknesses in this literature.

In short, the existing scholarship in this area has four main weaknesses: First, the business associations scholars who address human behavior within the business entity tend to attempt primarily to explain failings as opposed to propose behavior modification and reform.[2] Second, those who look at the psychology relevant to

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[1] *See* Renee Jones, *Law, Norms, and the Breakdown of the Board: Promoting Accountability in Corporate Governance,* 92 IOWA L. REV. 105, 108-158 (2006); Lisa M. Fairfax, *Spare the Rod, Spoil the Director? Revitalizing Directors' Fiduciary Duty Through Legal Liability*, 42 HOUS. L. REV. 393 (2005-2006); Mechele Dickerson, *A Behavioral Approach to Analyzing Corporate Failures,* 38 WAKE FOREST LAW REV. 1 (2003); Lynn A. Stout, *On the Proper Motives of Corporate Directors (Or, Why You Don't Want to Invite Homo Econimous to Join Your Board,* 28 DEL. J. CORP. L. 1 (2003); Margaret Blair & Lynn Stout, *Director Accountability and the Mediating Role of the Corporate Board,* 79 WASH. U. L. Q. 403 (2001); Margaret Blair & Lynn Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735 (2001); David A. Skeel, Jr., *Shaming in Corporate Law,* 149 U. PA. L. REV. 1811 (2001); Donald C. Langevoort, *Behavioral Theories of Judgment and Decision Making in Legal Scholarship: A Literature Review,* 51 VAND. L. REV. 1499 (1998); Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?,* 44 UCLA L. REV. 1009 (1997).

[2] Professor Donald Langevoort is among the most prolific corporate and securities law scholars examining behavioral science for purposes of explaining business associations' machinations. Donald C. Langevoort, The *Epistemology of Corporate-Securities Lawyering: Beliefs, Biases and Organizational Behavior,* 63 BROOK. L. REV. 629 (1997); Donald C. Langevoort, *Behavioral Theories of Judgment and Decision Making in Legal Scholarship: A Literature Review*, 51 VAND. L. REV. 1499 (1998); Donald C. Langevoort, *The Human Nature of Corporate Boards: Law, Norms, and the Unintended Consequences of Independence and Accountability,* 89 GEO. L.J. 797 (2000-2001);

partner, principal, or director behavior tend to focus on the research of other corporate law or management scholars as opposed to dissecting the organic empirical research done by behaviorists. Third, even those who examine true behavioral studies to answer questions about why business associations constituencies behave the way they do look at a narrow range of research from the social sciences as opposed to the broader body of behavioral literature based on actual experiments in controlled and uncontrolled environments. Fourth, business association scholars often tend to rely on the rational actor theory to explain individual actor's behavior within the firm without assessing (a) the relevance of the rational actor theory in a particular context and (b) whether the theory's basic underlying assumptions hold in a given situation.[3]

Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance With Law,* 2002 COLUM. BUS. L. REV. 71 (2002). Langevoort's writing has elucidated several key behavioral points in the context of business associations (e.g., various cognitive biases hamstring the behavior of corporate gatekeepers, including the tendency to justify prior decisions as opposed to concede mistakes, optimism bias, "motivated inference," the inclination to overrate one's ability to judge the trustworthiness of others (compounded by an underestimation of the influence situational factors as opposed to character have on decision making), and the perils of groupthink and cohesion), but Professor Langevoort does less in terms of proposing reforms based on behavioral research.

Contrariwise, in a recent article, Professor Renee Jones uses accountability research to justify the position that increased director accountability for fiduciary duty violations is critical to counteracting director abdication or inattention. Renee Jones, *Law, Norms, and the Breakdown of the Board: Promoting Accountability in Corporate Governance*, 92 IOWA L. REV. 105, 108158 (2006). Professor Jones argues for at least minimally enhanced legal liability for directors for breaches of their fiduciary duties, pointing to the social sciences literature dealing with accountability versus reliance on norms, and noting that "[s]ocial psychologists have found that requiring accountability can counteract the distorting impact of conformity and consistency." *Id.* at 145. In addition to examining the literature on accountability, Jones thoughtfully critiques reliance on norms as the optimal way to encourage director responsibility, arguing among other things that a director's cognitive biases weigh against his effective utilization of norms as the base-line for his decision-making.

[3] The "rational actor" theory originates in both psychology and neoclassical microeconomics, and it postulates that a person's behavior is designed to maximize her ability to achieve her goals. Edward l. Rubin, *The Legal Implications of Psychology: Human Behavior, Behavioral Economics, and The Law*, 51 VAND. L. REV. 1705, 1706 (1998). The "rational actor theory" is contingent on several basic assumptions, which developed as the neoclassical economic theory underlying the rational actor theory evolved. Roger G. Noll & Barry R. Weingast, *Rational Actor Theory, Social Norms, and Policy Implementation: Applications to Administrative Processes and Bureaucratic Culture,* THE ECONOMIC APPROACH TO POLITICS: A CRITICAL REASSESSMENT OF THE THEORY OF RATIONAL ACTION 237, 243 (1991). The assumptions include the following: Actors pursue goals, and these goals reflect the actors' perceived self-interest. Behavior results from a process that involves conscious choice. Actors have preference orderings that are consistent and stable. Given options, actors chose the option with the highest expected utility. Actors possess extensive information on both the available alternatives and the likely consequences of their choices. Kristen R. Monroe, *Psychology And Rational Actor Theory*, 16 POL. PSYCH. 1, 2 (1995).