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Beyond shareholders versus stakeholders: Towards a Rawlsian concept of the firm

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ABSTRACT

This paper critiques the principle of shareholder value and offers an alternative paradigm. We consider different theories describing the corporation and its relationship with shareholders, concluding that much of the modern academic discourse on corporate governance centres around the notion of the firm as a contractual arrangement. We provide a full critique of shareholder primacy from an economic as well as a moral perspective, which includes a focus on Rawls. An alternative contractarian paradigm is offered, one that is based on the concept of the corporation as a 'social union.' This characterisation justifies participation of a wider group of stakeholders in the governance of a corporation, and we make a distinction between electoral and moral constituents. A role for the application of the principles of deliberative democracy is also discussed.

1. Corporations and ownership

The essential problem of corporate governance is that of the accountability of management. The essential question is accountability to whom. The two principal standpoints on this problem view corporate accountability as the legitimate concern either exclusively of equity shareholders or, alternatively, of a wider group of stakeholders. Despite this divide there is some degree of overlap between

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these two views of corporate governance, with both sides frequently arguing that the long-term interests of a corporation's shareholders are best served by addressing the needs of multiple stakeholders and of wider society. The responsibility of a corporation, together with its shareholders, as responsible owners, towards wider society is a recurrent theme in the literature on corporate governance, corporate social responsibility and socially responsible investment. This aspect of the discourse on governance is grounded in a view of a corporation as the property of its shareholders, and appeals to the duties of ownership.

1.1. *Ownership as metaphor*

The term 'ownership' is regularly used in the literature on corporate governance, especially in introductory academic texts. It might be useful to think of 'ownership' in the context of an intangible entity such as a business enterprise as a metaphor. This metaphor provides an anchor for conceptualising the relationship between the investor and the business.

In recent decades there has been considerable scholarship in the fields of linguistics and cognitive science on the role of metaphor in structuring concepts. In particular Lakoff and Johnson (1980) have explained how, far from being a purely literary device, metaphor plays a crucial role in our conceptual system, particularly in structuring more abstract ideas. In the light of the research of Lakoff and others, analysis of linguistic devices, especially metaphors, used in communicating ideas should be seen as an essential part of examining the way that concepts are formed and opinion is shaped.

Ownership in the context of a business entity may be best characterised, following Kövecses (2010) as an ontological metaphor, whose role is to 'assign a basic status in terms of objects, substances, and the like to many of our experiences (p. 38).' The concept of ownership most obviously applies to physical objects of varying sizes, such as pens, bags, books, cars and real estate. To apply the same term to characterise the more abstract relationship between a person and a business is metaphorical in character, serving to conceive the enterprise as an object – one that is in the possession of an owner.

Indeed a richer use of the metaphor of ownership is to be found in older texts. For example in a 1911 ruling the US Supreme Court Justice Louis D. Brandeis refers to the widely distributed shareholding as 'absentee landlordism of the worst kind' (Monks and Minnow, pp. 129–130). This conceptual framework is further developed by Thorstein Veblen in *Absentee Ownership: Business Enterprise in Recent Times: The Case of America*, originally published in 1923. Veblen characterises what he terms 'absentee ownership' as a 'remnant of feudalism,' distinct from ownership arising from 'handicraft' and 'natural right' (1997, p. 51). In this characterisation he draws heavily on Locke's view of property ownership as a natural right derived from human labour (Second Treatise of Government). Monks uses a more contemporary metaphor to evoke this same notion of absent and uninvolved owners in his reference to ownerless 'drone corporations' (Absence of Ownership, 2013).

We now turn to the appropriateness of this metaphor in providing a cognitive structure for understanding the relationship between the equity investor and the business enterprise. Our focus is the publicly held corporation.

Monks and Minnow (2008) (p. 95) have outlined four elements of the ownership of property: (1) the right to dispose of the property as one wishes; (2) the right to regulate others' use of the property; (3) the right to transfer ownership; and (4) responsibility for potential damage to others caused by use of the property. Monks & Minnow explain that in the context of the modern limited liability company only one of these elements clearly applies to shareholders, i.e. the right of transfer. In the case of the first two rights, ownership rights can only be exercised in the collective sense, and under numerous legal restrictions.

The relevance of the fourth element is questioned by Berle and Means, in their seminal work on corporate governance in the 1930s. They emphasise a broader conception of responsibility as a feature of ownership, and conclude that the modern context of highly liquid markets renders this little more than irrelevant:

> "...property is immobilized by the necessity that it should have an attentive owner whose activity is indispensable to its continued usefulness... Consequently, to translate property into liquid form the first requisite is that it demand as little as possible of its owner ... Thus if