



# The Purpose of the Corporation Conference:

European Parliament 11 February 2014



The popular conception that corporations exist principally for the purpose of maximizing shareholder value has become so enmeshed with the narrative of business that the issue is rarely given serious consideration. This popular conception is problematic because it is based on a model of the corporation which bears very little relationship to the reality of 21st century corporate activity and because it is implicated in a range of unintended consequences including an inappropriate focus on the short-term, potentially (and paradoxically) sub-optimal returns to shareholders, excessive executive pay and a range of negative social and environmental externalities. There is also significant evidence that it is fundamentally inconsistent with sustainability.

The global financial crisis was clearly linked to the drive to maximize shareholder value yet many of the current responses to that crisis serve only to further entrench shareholder value thinking. A serious consideration of these issues is long overdue. In the wake of the crisis there has been widespread interest in these issues and the potential has arisen for a new view on corporate governance.

In its first major event the **Purpose of the Corporation Project** brought together in excess of 120 thought leaders, drawn from a diverse range of stakeholders including academia, business, civil society and policy makers, in the European Parliament. The event, hosted by **Richard Howitt MEP**, was a collaboration between **Frank Bold**, a purpose driven law firm, and the Modern Corporation Project at Cardiff Business School. [See the videos of the event.](#)

### Speakers included

**Professor Yuri Biondi**, ESCP Europe in Paris, tenured research fellow of the CNRS, **Professor Gerald (Jerry) Davis**, Wilbur K. Pierpont Collegiate Professor of Management, Ross School of Business and Professor of Sociology, The University of Michigan, **Mark Drewell**, CEO, Globally Responsible Leadership Initiative, **Bennett Freeman**, Senior Vice President Sustainability Research and Policy, Calvert Investments, Inc., **Pierre Hubbard**, Senior Policy Advisor, Trade Union Advisory Committee to the OECD, **Susannah Haan**, Secretary General, EuropeanIssues, **Professor Paddy Ireland**, University of Bristol Law School, **Professor Andrew Johnston**, Professor of Company Law and Corporate Governance, University of Sheffield School of Law, **Professor William Lazonick**, Professor of Economics at University of Massachusetts Lowell and Director of the UMASS Lowell Center for Industrial Competitiveness, **Simon Pickard**, Director General, The Academy of Business in Society, **Robert Madelin**, Director-General, European Commission, Directorate-General for Communications Networks, Content and Technology, **John Montgomery**, Silicon Valley based corporate attorney, entrepreneur, executive coach and author, **Klaus Niederlander**, Director, Cooperatives Europe, **Marcello Palazzi**, Co-founder, B-Lab Europe, **Dr Dieter Plehwe**, Research Fellow, WZB., **Jean-Philippe Robé**, Ecole de Droit de Sciences Po, **Professor Beate Sjøfjell**, University of Oslo, Faculty of Law, Department of Private Law and Project Leader for the research project 'Sustainable Companies', **Professor Andre Spicer**, Professor of Organisational Behaviour, Cass Business School, **Susanne Stormer**, Vice President, Corporate Sustainability, Global Stakeholder Engagement, Novo Nordisk, **Professor Lynn Stout**, Distinguished Professor of Corporate & Business Law, Cornell University Law School and **Professor Hugh Willmott**, Research Professor in Organisational Studies, Cardiff Business School



**Corporate governance** organizes internal structures, allocates resources and defines the division of value to various stakeholders. Corporate governance is about who has a say in how corporations and therefore, in many cases, businesses in general are organized and how the value they produce is divided among different constituencies. The way that we think about corporate governance has been influenced by various academic disciplines including law, economics, accounting, politics and business management. **Modern corporate governance is heavily reliant upon a number of taken for granted assumptions which include:**

- Shareholders own corporations.
- Company directors and senior executives are the agents of the shareholders.
- Shareholders are the sole residual claimants in corporations.
- Company directors are legally obliged to maximize shareholder value.
- Shareholders provide capital to corporations.
- Maximizing shareholder value provides better returns to shareholders, is better for the corporation and is in the best interests of the economy.
- It is also often assumed that firms or businesses are legal entities.

**Participants in the event heard that, in fact:**

- It is simply legally incorrect to say that shareholders own companies, rather they own shares in companies which is a very different thing.
- It is a legal fact that shareholders are not principals and directors and executives are not their agents.
- Shareholders are not the sole residual claimants in corporations nor are they the only participants in the economy who bear risk, for example the tax payer also bears risk.
- It is not the law that directors of companies are obliged to maximise shareholder value. The notion that they have such an obligation, though now widespread, is of relatively recent origin.
- This misunderstanding arises, in part because, generally speaking, company law across jurisdictions simply does not explicitly say why we have companies or what the purpose of companies is from society's perspective.
- Firms or businesses are not legal entities. Corporations, or some other legal entity, conduct business.
- Even as the concept of maximising shareholder value (MSV) started to develop in certain academic circles in the 1970s and 80s many within academia could see that it was problematic.
- The empirical evidence against MSV now seems to be overwhelming.
- In the great majority of cases shareholders do not provide capital to companies as they are, generally, purchasing the shares on the secondary market and thus providing nothing to the company itself.
- MSV has led to a massive extraction of value from the economy through the phenomenon of stock buy backs, where companies buy back their own shares from shareholders. This



practice is linked to the situation in the USA where CEO pay in 2012 was 354 times that of an average worker.

- On a macro level shareholders take more money out of companies [through dividends and stock buy backs] than they put in.
- Other than senior executives the only other group that benefits from buy backs are shareholders, such as activist hedge funds, who elect to sell their shares back to the company thus undermining long term shareholding.
- In 1960 the average holding period of stock in the S&P 500 was eight years. Today it is four Months.
- MSV is bad for shareholders. It has resulted in an almost 10% decline in returns to public shareholders in the S&P 500 (over the last 20 years).
- MSV contributes to a hollowing out of companies, through practices such as off shoring.
- Managing a firm in order to maximize shareholder value is not only a tragedy for the economy but is simply bad management, in fact it can be thought of as “junk” management, where CEOs can spend about half their time talking to share analysts instead of running their companies.
- In the 1950s the average life expectancy of a Fortune 500 company was 50-60 years, now it is 15 years.
- Policies that encourage MSV are not likely to address pressing economic concerns such as creating employment, indeed one popular strategy for maximizing shareholder value is to reduce employment or shift it to a lower cost country.
- An orientation toward MSV leads to companies doing what the markets like such as domain shopping for tax havens and not doing what the markets do not like. It also introduces tendencies towards bubbles and crises.
- The legacy of inadequate corporate governance has led to the greatest destruction of economic value in modern history.
- MSV, often more as a social rather than a legal norm, is the main barrier to many things that we want as a society including environmental sustainability, quality employment, quality products, corporate financial stability and perhaps even macro-economic stability as it results in a massive polarisation of wealth.
- We cannot just look at company law in isolation. We need to look at the whole corporate governance ‘ecosystem’ which includes regulation across the board as well as the impact of financial markets which are a major source of pressure on companies

### Participants were also told that:

- There are already other ways of conducting large and successful businesses that do not seek to maximize shareholder value for example there are approximately 160,000 cooperatives in Europe, indeed about one in five Europeans is a member of a cooperative.
- Nineteen states in the USA now allow the incorporation of “Benefit Corporations” or “B Corps” which in addition to a profit making goal are required to make a material positive impact on society and the environment. This effectively puts a planetary triple bottom line into the corporate conscience.



- The B Corp movement has spread to 32 countries and came to Europe in 2013 in the form of B Labs Europe. This movement has been largely driven by entrepreneurs and investors. <https://www.bcorporation.net/community/global-partners>
- Companies such as Novo Nordisk, which is, by market capitalisation, the largest company in Scandinavia are able to stay aligned to their values and purpose by having a dual class share structure with a foundation owning shares which allows for effective voting control.
- The time has indeed come to reassess—and in some ways redefine—the purpose of the corporation. This is exemplified by Investors such as Calvert Investments who have embraced and advanced a broader view of that purpose.
- The Association of Chartered Certified Accountants (ACCA) has launched a discussion paper “Creating value through governance-towards a new accountability”. Submissions are open until 31 August 2014. It contains question 9.6 “*Is there a need to review the purpose of the corporation in society?*” <http://www.accaglobal.com/content/dam/accaglobal/PDF-technical/corporate-governance/tech-tp-cvtg.pdf>
- The OECD Principles of Corporate Governance, which have significant influence both at the EU level and in nations that are not OECD members, the latter due to the fact that the World Bank and IMF use them as benchmarks, are up for review this year and this is an opportunity to advocate for a move away from MSV. <http://www.oecd.org/daf/ca/2014-review-oecd-corporate-governance-principles.htm>
- In order to create a new generation of globally responsible leaders it is necessary to re-visit the purpose of the corporation. One outcome of that process is the 50+20 Agenda which has produced a vision of the future of management education. <http://50plus20.org/>
- The aim of the Sustainable Companies Project has been to find out how to integrate environmental concerns better into the decision-making in companies. The goal is through that to contribute to sustainable development. The Project prepared a paper for the conference, below and will be working on EU level reform proposals to be presented in Brussels later this year. <http://www.jus.uio.no/ifp/english/research/projects/sustainable-companies/news/sustainablecompanies2pagesummarycompanylaw.pdf>  
<http://www.jus.uio.no/ifp/english/research/projects/sustainable-companies/>
- Through the coordination of Jeroen Veldman of the Modern Corporation Project at Cardiff Business School academics from a variety of disciplines have graciously written succinct memos dealing with MSV. Disciplines include accounting, law, politics and business management are freely available and a Green Paper is being prepared. <http://themoderncorporation.wordpress.com/>

The event ended with participants offering their own thoughts, developed in groups, on four themes:

1. The most interesting thing from the conference.
2. The thing that their group agreed on.
3. What the Purpose of the Corporation Project should do next.
4. What we, as a society, could do.

The results are available upon request.