# Can Purpose Deliver Better Corporate Governance?

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Yes

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# Verbiage

**from the French verbiage/ verbier, is: “superabundant or superfluous wording; profusion of words without good cause, or without helping to make the intended meaning clearer or more precise; excessive wordiness or elaborateness of language.” (Oxford English Dictionary)**

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# Twaddle

“senseless, silly, or trifling talk or writing; empty verbosity; dull and trashy statement or discourse; empty commonplace; prosy nonsense.” (Oxford English Dictionary)

# Four Alternatives to the Friedman Doctrine

**Enlightened shareholder value**

**Stakeholder theory**

**Shareholder welfare**

**Corporate purpose**

# 1. Enlightened Shareholder Value

# S.172 UK Companies Act 2006

**A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole**

# S.172 UK Companies Act 2006

**A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole and in doing so have regard (amongst other matters) to: (a) the likely consequences of any decision in the long term, and (b) the interests of and its impact on its other stakeholders – employees, suppliers, customers, communities, the environment, the company's reputation, and its members**

# Implications

**Cross-sectional**

**Time-series**

# Implications

Cross-sectional

Time-series

Companies should take account of interests of stakeholders in so far as this enhances the value of the company over the long-run

# Issues

**Instrumental**

**Enlightened in name but not in spirit**

**No protection against activism or acquisition**

# 2. Stakeholder Theory

# Stakeholder Theory

## Minnesota Constituency Statute

**“[A] director *may*, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as short-term interests of the corporation and its shareholders including the possibility that these interests might be best served by the continued independence of the corporation.”**

# Implications

Companies should take account of all stakeholders

Should do so in an intrinsic sense

Should promote long- and short-term shareholder and other stakeholder interests

# Issues

Verbiage

Impossible management task

Weak corporate governance

Confused incentives

May not must is mush

# 3. Shareholder Welfare

# Shareholder Welfare

**“It is too narrow to identify shareholder welfare with market value. The ultimate shareholders of a company (in the case of institutional investors, those who invest in the institutions) are ordinary people who in their daily lives are concerned about money, but not just about money. They have ethical and social concerns.” (Hart and Zingales (2017))**

# Implications

Retains focus on shareholder interests

Relevance of societal and environmental considerations

Fiduciary duties of companies and institutions to beneficiaries

Inefficient or impractical to rely on philanthropy or regulation

Balancing of interests and role of mutual funds

# Issues

**Boycotts, divestment and engagement**

**Pivotal shareholders**

**Investment chains**

**Activism and takeovers**

**Intrinsic and extrinsic interests**

# 4. Corporate Purpose

# Corporate Purpose

**Why business exists, is created, reason for being**

**Profitable solutions, not profiting from problems**

**Clarity and credibility**

**Enacting purpose**

# S.172 UK Companies Act 2006 – Para 2

A director of a company must act in the way he considers, in good faith, would be most likely to promote the purpose of the company and in doing so have regard (amongst other matters) to: (a) the likely consequences of any decision in the long term, and (b) the interests of and its impact on its other stakeholders – employees, suppliers, customers, communities, the environment, the company's reputation, its members, and its creditors when it nears insolvency

# Policy and Practice

Law – duties of directors
Regulation – rules, enforcement

Ownership – rights, responsibilities
Governance – appointment, alignment, accountability

Measurement – metrics, accounting, valuation
Performance – profits and incentives

Finance – funding, stewardship
Investment – resource allocation

# Current Arrangements

**Law - duties of directors to shareholders;**
**Regulation - “rules of the game” and their enforcement.**

**Ownership - rights of shareholders;**
**Governance - resolution of “agency problem”.**

**Measurement - financial/material assets;**
**Performance - profits.**

**Finance – responsibilities to investors;**
**Investment - maximizing shareholder value.**

# Proposed Arrangements

**Law – duties to deliver purpose;**
**Regulation - align purpose with social licenses.**

**Ownership - of purpose;**
**Governance - accountability for delivering purpose.**

**Measurement – metrics, accounting, valuation of purpose;**
**Performance - profits in relation to purpose.**

**Finance - funding and stewardship of purpose;**
**Investment - partnerships to deliver purpose.**

# Implications

Validity of purpose

Plurality of purpose

Clarity of purpose

Innovation in delivery

Accepted standards in measurement

Financial and operational resilience

# Issues

**Understanding of purpose**

**Precision of metrics**

**Accountability and governance**

**Investor interests**

# 5. Relationship Between Concepts

# Enlightened Shareholder Welfare

A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the welfare of its shareholders and in doing so have regard to the likely consequences of any decision in the long term, and the welfare of its stakeholders

# Enlightened Stakeholder Welfare

**A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the welfare of all its stakeholders, and in doing so have regard to the likely consequences of any decision in the long term**

# Shareholder Welfare Corporate Purpose

**A director of a company must act in the way (s)he considers, in good faith, would be most likely to enhance shareholder welfare by solving problems of people and planet, and not producing problems for either**

# Implications

Makes shareholder welfare derivative of stakeholder welfare

Clarity of who and what

Effective governance and accountability with legal lock-in

Promotes fair competition and diversity of purpose

Lower cost of capital from shareholder welfare

# 6. Conclusion

**Stakeholder theory unworkable and impractical**

**Enlightened shareholder value minimum standard**

**Purpose verbiage fills the void of vagueness**

**Precision in purpose reflected in practice**

**Public policies and corporate laws to support it**

**Shareholder welfare reduces cost of capital of purpose**

# Example

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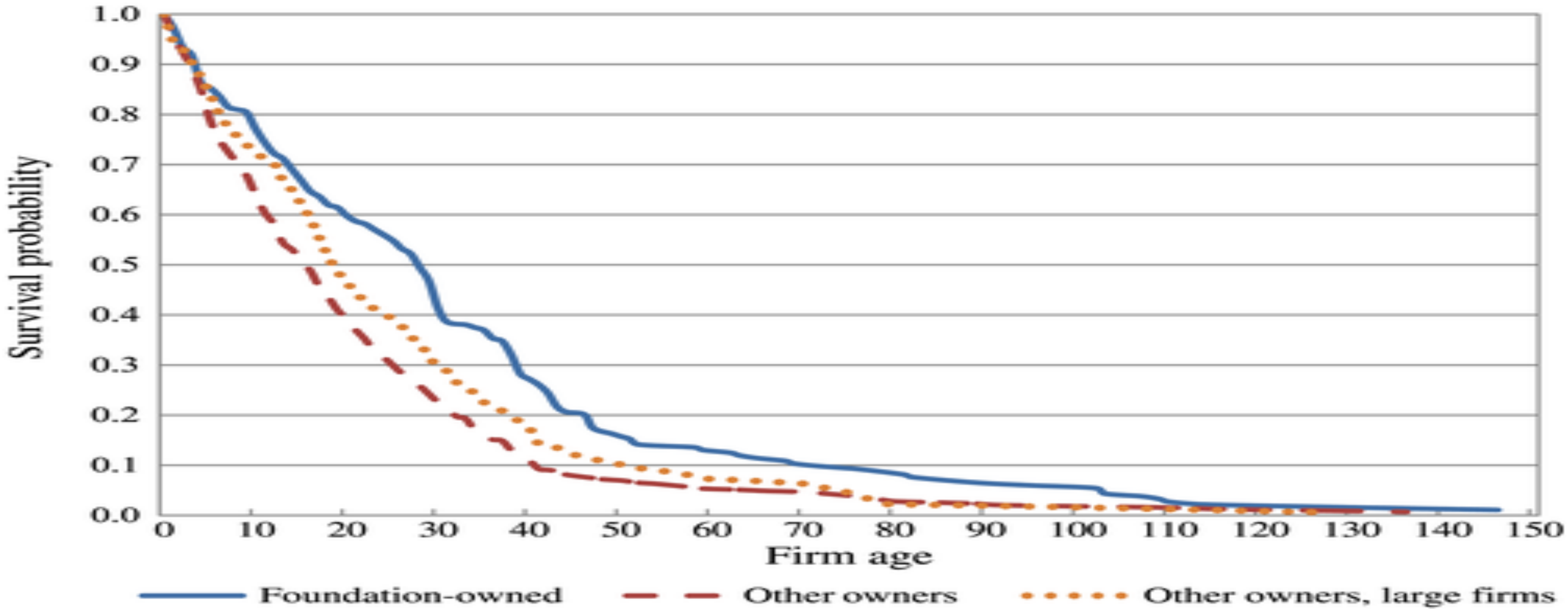


Source: Steen Thomsen, Thomas Poulsen, Christa Borsting, Johan Kuhn (2018)