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A Critical Look at Four Varieties

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Corporate Leaders Say They Are For Stakeholder Capitalism— But Which Version Exactly?[*]

A Critical Look at Four Varieties

By Lynn S. Paine[†]

Abstract: The past few years have seen an outpouring of articles and statements heralding the arrival of a new and more inclusive form of capitalism often called stakeholder capitalism. The new capitalism promises to strengthen companies, improve outcomes for their constituencies, produce better returns for long-term shareholders, and ultimately strengthen the economy and society as a whole. In line with the new ideology, corporate boards and business leaders are being urged to replace the shareholder-centered approach to governance that has guided their work for the past several decades and, instead, to adopt a multi-stakeholder approach. In speaking with hundreds of corporate directors, executives, investors, governance professionals, and academics over the years, I've found wide differences in how stakeholder capitalism is understood and what it is thought to require of companies and their leaders. Failure to recognize these differences has been a source of much confusion and controversy inside companies and in the public debate. In this paper, I describe four varieties of stakeholder capitalism (also called stakeholderism): *instrumental, classic, beneficial*, and *structural.* The four types reflect significantly different levels of commitment to the interests of stakeholders and rest on very different rationales. Each has very different implications for how companies and their boards function. As more companies embrace stakeholder capitalism, it is important for boards and business leaders to have a shared understanding of what, exactly, they are embracing, and to prepare themselves and their organizations to deliver on their espoused commitment. This paper is intended as a guide to help corporate leaders do just that. It discusses each type of stakeholderism in turn and concludes with some observations on the challenges presented by each.

Key words: corporate governance, boards of directors, stakeholder capitalism, stakeholder theory, stakeholder governance, shareholder primacy

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[*] An abridged version of this paper appears as "What Does 'Stakeholder Capitalism' Mean to You?," *Harvard Business Review*, September-October 2023.

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owed to the many scholars, journalists, and practitioners whose work is cited in this paper. All errors, of course, are mine.

Introduction

The past few years have seen an outpouring of articles and statements heralding the arrival of a new and more inclusive form of capitalism often called stakeholder capitalism. The new capitalism promises to strengthen companies, improve outcomes for their constituencies, produce better returns for long-term shareholders, and ultimately strengthen the economy and society as a whole. In line with the new ideology, corporate boards and business leaders are being urged to replace the shareholder-centered approach to governance that has guided their work for the past several decades and, instead, to adopt a multi-stakeholder approach. Perhaps the best-known public pronouncement on this topic is the Business Roundtable's August 2019 statement on corporate purpose. Signed by 181 CEOs of leading US companies, the statement rejected the BRT's 1997 endorsement of shareholder primacy and declared its signers' commitment to "lead their companies for the benefit of all stakeholders," naming customers, employees, suppliers, communities, and shareholders in particular.[1]

What should corporate boards and business leaders make of this development? On the surface, stakeholder capitalism sounds reasonable enough. In the wake of the pandemic, few would deny that companies are dependent on their stakeholders for their ability to function at all, let alone thrive and prosper over time. Indeed, this statement is something of a truism. When the term "stakeholder" first appeared in the management literature in 1963, it was defined as "those groups without whose support the organization would cease to exist."[2] Still, the fact that companies depend on their stakeholders says nothing about what companies owe their stakeholders—and that is where the debate lies.

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[1] Business Roundtable, *Statement on the Purpose of a Corporation* (August 19, 2019), https://s3.amazonaws.com/brt.org/BRT-StatementonthePurposeofaCorporationJuly2021.pdf The accompanying press release noted that the statement's 181 CEO signers "commit to lead their companies for the benefit of all stakeholders." For comparison with the BRT's prior position, see Business Roundtable, *Statement on Corporate Governance* (September 1997) (stating that "the paramount duty" of managers and boards is to the corporation's stockholders; and that "the principal objective of a business…is to generate economic returns to its owners") at http://www.ralphgomory.com/wp-content/uploads/2018/05/Business-Roundtable-1997.pdf.

[2] R. Edward Freeman, *Strategic Management: A Stakeholder Approach*, Pitman (1984), p. 31. Freeman traces the term "stakeholder" to an internal memorandum developed at Stanford Research Institute, now SRI International, Inc., in 1963. The underlying concept, if not the term, however, goes back further. The earliest known appeal to a multi-constituency view of corporate responsibility is found in a statement made in January 1929 by General Electric Company's President and Chairman Owen D. Young and quoted in E. Merrick Dodd, Jr., "For Whom Are Corporate Managers Trustees?" *Harvard Law Review*, Vol. 45, No. 7 (May, 1932), pp. 1145-1163, at 1154 ("There are three groups of people who have an interest in [the General Electric Company]…people who have put their capital in the company…people who are putting their labor and their lives into the business of the company…The third group is of customers and the general public.")

In speaking with hundreds of corporate directors, executives, investors, governance professionals, and academics over the years, I've found wide differences in how stakeholder capitalism is understood and what it is thought to require of companies and their leaders. Failure to recognize these differences has been a source of much confusion and controversy inside companies and in the public debate. The controversy over so-called ESG (environmental, social, and governance) investing is a case in point.

In this paper, I describe four varieties of stakeholder capitalism (also called "stakeholderism," "stakeholder governance," and "stakeholder theory.") As the discussion will show, these different conceptions of stakeholderism reflect significantly different levels of commitment to the interests of stakeholders, particularly stakeholders other than shareholders, and rest on very different rationales. On a spectrum from weakest to strongest, they range from a commitment that is contingent on its contribution to shareholder value to, at the other end, more emphatic and durable commitments based on adherence to basic ethical norms, advancing stakeholders' welfare, and giving stakeholders more power in the governance process.[3] In this article, I refer to these versions of stakeholderism, respectively, as *instrumental, classic, beneficial*, and *structural*.[4]

As more companies embrace stakeholder capitalism it is important for boards and business leaders—collectively "corporate leaders"—to have a shared understanding of what, exactly, they are embracing. Espousing a commitment to all stakeholders without having reasonable clarity about what it entails in practice is risky business. For one thing, it puts corporate leaders on a collision course with each other when decisions requiring difficult trade-offs among stakeholders' interests arise—as they inevitably do. For another, it creates expectations among stakeholders that if unfulfilled will only fuel cynicism, alienation, and distrust – the opposite of what most proponents of stakeholder governance intend. Meanwhile, shareholders are left wondering what this new ideology means for them.

When corporate leaders say they are committed to serving all their stakeholders and then fail—or are perceived to fail—to deliver on that commitment, they deepen society's distrust in business and invite accusations of hypocrisy or worse. To reduce the risk of such misunderstanding, corporate leaders need to recognize that stakeholder capitalism means different things to different people and be clear on what version of stakeholder capitalism they

[3] Other academics have divided stakeholderism into two types—"instrumental" and "pluralistic." See Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106:91 (2020), pp. 91-178 at 108-115. This two-part typology, however, obscures important distinctions among different pluralistic versions. In this article, I use the term "instrumental" interchangeably with "contingent" and "conditional."
[4] The varieties might also be called, respectively, "conditional/contingent," "categorical/ethical," "positive/ aspirational," and "procedural."

are embracing. Above all, they should prepare themselves and their organizations to act on their espoused commitment. This article is intended as a guide to help corporate leaders do just that. It proceeds by discussing each of the four varieties of stakeholderism in turn and concludes with some observations on the challenges presented by each. Key terms are defined in **Appendix A**.

1. Instrumental Stakeholderism: A means for maximizing long-term shareholder value

One version of stakeholder capitalism takes shareholder value as its touchstone.[5] This version holds that considering the interests of all stakeholders is important for helping corporate leaders maximize returns to shareholders. Notably, shareholder value is to be assessed over the long term though the precise time period and methodology for making this calculation are typically left unspecified.[6] The underlying insight, however, is this: how a company treats its non-shareholder stakeholders today can affect shareholder value in the future.[7] In particular, investments in other stakeholders that reduce shareholder value today may pay off for shareholders in the future. Conversely, shortchanging other stakeholders may benefit shareholders for a time but be detrimental to shareholders if a longer time period is considered. Thus, according to this view, even if their only objective is maximizing value for shareholders, boards and business leaders should consider the interests of other stakeholders.

This appears to be the dominant understanding of stakeholder capitalism in much of the investment community today. Certainly recent statements by heads of the "big three" asset managers in the U.S.—Blackrock, Vanguard, and State Street Global Advisors—seem to reflect this view. In his 2021 letter to CEO's, BlackRock Chairman and CEO Larry Fink stated explicitly: "The more your company can show its purpose in delivering value to its customers, its employees, and its communities, the better able you will be to compete and deliver long-term, durable profits for shareholders."[8] His 2022 letter states succinctly: "Stakeholder capitalism is

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[5] For a more negative view of this version of stakeholder capitalism, see Bebchuk, Lucian A. and Tallarita, Roberto, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Volume 106, 2020, pp. 91-178, at pp. 108-110. Harvard Law School John M. Olin Center Discussion Paper No.1052, Harvard Law School Program on Corporate Governance Working Paper 2020-1, Available at SSRN: https://ssrn.com/abstract=3544978 or http://dx.doi.org/10.2139/ssrn.3544978.

[6] It's often unclear, for instance, whether "long-term shareholder value" refers to the share price at some defined point in the future, accumulated returns to shareholders over some period of time, or something else altogether. An exception is the Total Value Framework developed by hedge fund Engine No. 1, which focuses on cumulative shareholder returns over a specified period of time.
https://engine1.com/files/Engine_No._1_Total_Value_Framework.pdf

[7] A good example in the Total Value Framework developed by hedge fund Engine No. 1.
https://engine1.com/files/Engine_No._1_Total_Value_Framework.pdf

[8] "Larry Fink 2021 Letter to CEOs," January 2021, https://www.blackrock.com/corporate/investor-relations/2021-larry-fink-ceo-letter For similar views linking stakeholder concerns with shareholder value, see "Vanguard

all about delivering long-term, durable returns for shareholders.[9] Similarly, Engine No. 1, the hedge fund known for its successful proxy fight to put directors with a climate focus on the board at Exxon in 2021, states in materials explaining its investment framework: "[We believe] a company will create higher long-term shareholder value when it makes rewarded, material investments in its employees, customers, communities, and the environment."[10]

This view has intuitive appeal and, to some business leaders, is little more than common sense. It recognizes that actions taken today have consequences for tomorrow and that the interests of all stakeholders, shareholders included, are often interdependent. Consider the simple example of investing in employees' development. Giving your salesforce time away from their jobs to learn new skills may hurt this quarter's sales, disappointing some shareholders and possibly causing them to sell their shares to the detriment of the stock price. But it will likely help sales and fuel growth to the benefit of shareholder value in the future, especially in an industry undergoing disruptive change. By the same logic, foregoing such investment may improve the bottom line and benefit shareholders today but lead to declining sales, operational inefficiencies, and ultimately losses in shareholder value that exceed any prior gains if the sales team's skills become outdated.

Numerous high-profile examples show that a single-minded focus on shareholder value at the expense of other stakeholders can generate shareholder value for a time but backfire badly over the long term. Consider the well-known case of Wells Fargo. From 2011 to 2016, its community banking division ran roughshod over customers' interests, opening more than 3.5 million accounts in customers' names without their authorization and then charging them for unwanted and unneeded products, often without their knowledge or consent. These practices helped employees meet their sales goals and the bank grow its revenues. During this period the bank had a total shareholder return of more than 100%,[11] and the CEO's compensation

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Investment Stewardship Insights, Shareholder proposals: Diversity, equity, and inclusion," (May 2021), https://corporate.vanguard.com/content/dam/corp/advocate/investment-stewardship/pdf/perspectives-and-commentary/INVDEIS_052021.pdf ("Risks to shareholder value associated with diversity, equity, and inclusion (DEI) remain a top engagement priority for Vanguard with our funds' portfolio companies.") See also State Street Global Advisors, "Proxy Voting and Engagement Guidelines, North America (United States and Canada)," May 2022, https://www.ssga.com/library-content/pdfs/ic/proxy-voting-and-engagement-guidelines-us-canada.pdf ("We also conduct proactive engagements to address significant shareholder concerns and environmental, social, and governance ("ESG") issues in a manner consistent with maximizing shareholder value.")

[9] "Larry Fink's Letter to CEOs: The Power of Capitalism," January 2022, https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter

[10] Engine No. 1 website, https://engine1.com/total-value-framework, accessed June 3, 2022; see also https://web.archive.org/web/20220322083234/https:/engine1.com/total-value-framework, as captured by Internet Archive Wayback Machine between January 22, 2022 and March 6, 2023, accessed July 5 2023.

[11] Wells Fargo & Company (NYSE:WFC) total shareholder return January 3, 2011 to December 30, 2016, Capital IQ, Inc., a division of Standard & Poor's, accessed June 2022. During the period from 2011 to 2016, the company's market value soared by $111 billion. Wells Fargo & Company (NYSE:WFC) market capitalization data January 3, 2011 to December 30, 2016, Capital IQ, Inc., a division of Standard & Poor's, accessed June 2022.

averaged over $20 million per year.[12] Eventually, however, the practices came to light, triggering a barrage of lawsuits, brand-damaging publicity, and regulatory actions—as well as further investigations that uncovered other types of customer abuse in other divisions. The Federal Reserve Board took the unprecedented step of putting a cap on the bank's asset growth. The total costs to the bank and its shareholders are not known, but fines alone are said to have amounted to more than $4.5 billion.[13] Shareholders suing the bank alleged that the debacle and its aftermath destroyed more than $54 billion in shareholder value.[14]

Had Wells Fargo's board and management been more attentive to the interests of customers—and not just to how profitable they were for the bank—things might have played out differently. The board might have chosen a different CEO, put in place a different executive compensation plan, set different performance goals, or sought out different information. The management team might have adopted a different approach to growing revenues, developed different training programs, or created a different scorecard for employees. Of course, we can never know for sure. Even if more attention had been paid to customers' interests, Wells Fargo's leaders might not have recognized or properly estimated the financial consequences of infringing those interests. In the end, shareholders suffered not just because customers were abused but because the abuse came to light, was widely publicized, and prompted regulators and law enforcement officials across the U.S. to take action to penalize the bank and rectify at least some of the damage done. Still, if customers' interests had been given a more prominent place – in strategy development, goal setting, incentive design, performance evaluation, and decision making—the Wells Fargo debacle might have been averted to the benefit of customers and shareholders alike.[15]

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[12] Wells Fargo & Company, Form DEF 14A (filed March 18, 2014), via SEC.gov, https://www.sec.gov/Archives/edgar/data/72971/000119312514104276/d663896ddef14a.htm#tx663896_31 and Wells Fargo & Company, Form DEF 14A (filed March 15, 2017), via SEC.gov, https://www.sec.gov/Archives/edgar/data/72971/000119312517083591/d305364ddef14a.htm#toc305364_50.

[13] Emily Flitter, "Federal Prosecutors Open Criminal Inquiry of Wells Fargo's Hiring Practices," *The New York Times*, June 9, 2022, https://www.nytimes.com/2022/06/09/business/wells-fargo-fake-interviews-investigation.html, accessed June 2022. See also Jonathan Stempel, "Wells Fargo must face shareholder fraud claims over its recovery from scandals," Reuters, October 1, 2021. https://www.reuters.com/business/finance/wells-fargo-must-face-shareholder-lawsuit-over-compliance-with-consent-orders-2021-09-30/ accessed January 3, 2022.

[14] In re Wells Fargo & Co Securities Litigation, U.S. District Court, Southern District of New York, No. 20-04494, Consolidated Amended Class Action Complaint for Violations of Securities Laws, p. 7 ("All told, investors lost over $54 billion in market capitalization, including a drop in Wells Fargo's share price of over 22.5% after the conclusion of the congressional hearings.") In May 2023, Wells Fargo agreed to pay $1 billion to settle the suit. Robert Burnson, "Wells Fargo to pay $1 billion in class-action suit," *Los Angeles Times*, May 16, 2023, https://www.latimes.com/business/story/2023-05-16/wells-fargo-to-pay-1-billion-in-class-action-lawsuit

[15] For more detail on the Wells Fargo case, see Tayan, Brian, The Wells Fargo Cross-Selling Scandal (January 8, 2019). Rock Center for Corporate Governance at Stanford University Closer Look Series: Topics, Issues and Controversies in Corporate Governance No. CGRP-62 Version 2, Stanford University Graduate School of Business Research Paper No. 17-1, Available at SSRN: https://ssrn.com/abstract=2879102

This view—that considering other stakeholders is a means to enhancing shareholder value—has been called "instrumental stakeholderism" and stakeholder capitalism "lite" because it retains shareholder value maximization as the corporate objective and attaches no intrinsic value to the interests of other stakeholders.[16] It might also be called "contingent" or "conditional" stakeholderism since the weight given to other stakeholders' interests in any particular situation is contingent on their contribution to shareholder value. Take the example of investing in employee development mentioned earlier. In some situations, generous pay and development programs for employees may be beneficial for shareholders because these policies help attract and retain scarce talent. In other cases, the very same policies may put the company at a cost disadvantage, hampering its ability to compete in product markets and ultimately diminishing long-term shareholder value. This view does not require that stakeholders' interests be served or respected, only that they be "considered" or "taken into account."[17] They can be taken into account and dismissed if respecting them would be damaging to shareholder value or unlikely to enhance it.[18]

Instrumental stakeholderism compared to the traditional shareholder view

In holding to shareholder value maximization as the corporate objective, this view should arguably not be categorized as a version of stakeholder capitalism at all. Indeed, some commentators have termed it "enlightened *shareholder* capitalism" or "enlightened *shareholder* value" for just that reason.[19] Some of these same commentators have argued further that an instrumental approach to stakeholders is conceptually and operationally no different from traditional shareholder value maximization and that explicitly calling out stakeholder interests

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[16] Bebchuk, Lucian A. and Kastiel, Kobi and Tallarita, Roberto, "For Whom Corporate Leaders Bargain," *Southern California Law Review*, Volume 94, No. 6, 2021, pp. 1467-1560. Available at SSRN: https://ssrn.com/abstract=3677155 or http://dx.doi.org/10.2139/ssrn.3677155; See also Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106: 9 (2020), pp. 91-178, at 110 ("Whenever treating stakeholders well in a given way would be useful for long-term shareholder value, such treatment would be called for…. And whenever treating stakeholders well would not be useful for long-term shareholder value, such treatment would not be called for.")

[17] In its 1997 Statement on Corporate Governance, the Business Roundtable adopted this view explicitly, stating: "[t]he interests of other stakeholders are relevant as a derivative of the duty to stockholders. The notion that the board must somehow balance the interests of stockholders against the interests of other stakeholders fundamentally misconstrues the role of directors. It is, moreover, an unworkable notion because it would leave the board with no criterion for resolving conflicts between interests of stockholders and of other stakeholders or among different groups of stakeholders." http://www.ralphgomory.com/wp-content/uploads/2018/05/Business-Roundtable-1997.pdf.

[18] See Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106: 9 (2020), pp. 91-177, at 110 (Describing instrumental stakeholderism: "Whenever treating stakeholders well in a given way would be useful for long-term shareholder value, such treatment would be called for…. And whenever treating stakeholders well would not be useful for long-term shareholder value, such treatment would not be called for.")

[19] See Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106: 9 (2020), pp. 91-178, 108-114. See also, Michael C. Jensen "Value Maximization, Stakeholder Theory, and the Corporate Objective Function," *Business Ethics Quarterly*, Vol. 12, No.1, April 2002, pp. 235-256; also published in the *Journal of Applied Corporate Finance*, Vol. 14, No. 3 (Fall 2001), pp. 8-21.

is unnecessary as a practical matter.[20] According to this line of reasoning, a corporate leader focused on maximizing shareholder value will automatically take relevant stakeholder interests into account just as they do a variety of other factors.

At a conceptual level, these commentators have a point. An instrumental approach to stakeholders in no way challenges shareholder primacy and is fully consistent with all of its four main tenets: namely, treating shareholder value maximization as the corporate objective, prioritizing accountability to shareholders over accountability to other stakeholders, subordinating the preferences of other stakeholders to those of shareholders, and giving shareholders the exclusive right to vote on directors and other governance matters.

Basically, an instrumental or contingent approach to stakeholders differs from traditional shareholder capitalism in just two main ways. One is in giving explicit consideration to other stakeholders' interests. The other is assessing shareholder value over a longer time period. However, there is reason to believe that, in practice, these two features can have significant effects on corporate leaders' behavior and decision making—in particular on what possibilities are envisioned, what information is considered, what types of analysis are conducted, how deliberations are structured, and what decisions are ultimately taken. In other words, the case for instrumental stakeholderism has more to do with its operating and behavioral implications than with its conceptual novelty.

A stakeholder approach implies a richer, more inclusive process for a range of tasks from corporate planning and strategy development to organizational design and risk management. When the stakeholder idea was first introduced into the management literature, it was presented as an aid to corporate planning, useful for ensuring that companies were responsive to the various groups on which they depended for their existence.[21] Later, R. Edward Freeman put forth "stakeholder theory" as a framework for helping executives understand changes in the external environment and develop a corporate strategy aligned with those changes.[22] Notably, Freeman's early work did not put forth stakeholder welfare as the purpose of the firm. Rather, it took the position that attending to stakeholders could be useful for advancing the

[20] See, e.g., Clifford Asness, Glenn Hubbard, Martin Lipton, Michael R. Strain, "American Enterprise Institute Roundtable: Was Milton Friedman Right about Shareholder Capitalism?" *Journal of Applied Corporate Finance*, Vol. 33, No. 1., Winter 2021, pp. 36-47, at 45. (Glenn Hubbard commenting, "To the extent that stakeholder capitalism amounts to long-run positive-NPV corporate investments in their stakeholders, then there's no debate.") See also Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106: 91 (2020), pp. 91-178, 97, 110. ("[A]n instrumental version of stakeholderism…is not conceptually or operationally different from the traditional shareholder value principle, and there seem to be no good reasons for restating this principle in the language of enlightened shareholder value.") ("Enlightened shareholder value is thus no different from shareholder value tout court.")
[21] R. Edward Freeman, *Strategic Management: A Stakeholder Approach*, Pitman (1984), pp. 31-32
[22] R. Edward Freeman, *Strategic Management: A Stakeholder Approach*, Pitman (1984), p. 44 ff.

firm's purpose, whatever it might be. Other scholars wrote about the implications of the stakeholder concept for organizational design.[23]

Rationales for instrumental stakeholderism

One benefit of paying explicit attention to stakeholders' interests is to broaden and extend corporate leaders' field of vision. The discipline of considering stakeholders' interests, assessing how a proposed course of action would likely affect them and, further, how those stakeholders would likely react—an exercise sometimes called "stakeholder analysis"—can bring to light risks to shareholder value that decision makers often do not recognize when they are focused narrowly on shareholder returns. Consider again what happened at Wells Fargo or at other companies such as Bridgestone Firestone (unsafe tires), Siemens (corrupt payments), Volkswagen (diesel emissions), and Boeing (737 Max airliner crashes)—to name just a few examples from recent decades. Had leaders of these companies paid more attention to the interests of their non-shareholder stakeholders, they would perhaps have pursed different practices or strategies, and avoided these costly disasters.

Paying attention to stakeholder interests and taking a longer view can also reveal an enlarged set of strategic opportunities. It is doubtful that corporate leaders narrowly focused on near-term returns to shareholders would choose to build a new plant in their distressed home region rather than in a lower-cost overseas location. But that's what Indiana-based diesel engine maker Cummins Engine did in 2010 when it decided to manufacture its new line of high-speed, low-emissions engines in Seymour, Indiana. The decision meant that the company would have to make significant investments in the community and its schools, but it also meant the possibility of raising educational attainment and income levels of the region's residents and creating a global hub for advanced manufacturing in Southeast Indiana. In 2015, Cummins opened its new technical center and began producing its new line of engines at the Seymour plant. Thanks in part to a major collaboration among Cummins, other companies, and the region's civic and educational leaders, the region also saw notable improvement in residents' educational attainment, incomes, and wage rates.[24] Cummins, whose CEO signed the BRT's 2019 statement, has a 100-year history and a long tradition of civic engagement which, no doubt, made the interests of the community a salient factor in its leaders' decision-making process and enabled them to take a longer-term view.[25]

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[23] E.g., Eric Rhenman, *Organization Theory for Long-Range Planning*, 1973.
[24] For more details, Joseph L. Bower, Herman B. Leonard, and Lynn S. Paine, *Capitalism at Risk: How Business Can Lead* (Boston: Harvard Business Review Press, 2020), pp. 258-264. See also Joseph L. Bower and Michael Norris, "Cummins, Inc.: Building a Home Community for a Global Company," Case 9-313-024 (Boston: Harvard Business School, March 21, 2014).
[25] Cummins's home state of Indiana is one of some 31 U.S. states to have adopted what is known as a "constituency statute" giving corporate directors the authority to consider the interests of various stakeholders. Indiana Code Title 23. Business and Other Associations § 23-1-35-1 (as of June 8, 2021)

Research suggests, moreover, that how decision makers define their role—as shareholder-focused or stakeholder-focused—and what information they take into account about the effects of actions they are considering can affect the decisions that result.[26] In role-playing research conducted in the 1970s, Wharton professor Scott Armstrong found that mock "boards of directors" who were told that their role was to maximize returns to stockholders were less likely to withdraw a harmful drug from the market and more likely to fight a regulatory ban on the drug than boards who were told that their duty was to recognize the interests of all the company's stakeholders. Importantly, the "stakeholder boards" were provided with information quantifying the likely effects of the possible actions under consideration on the relevant stakeholders. Three-quarters of the 41 "stockholder boards" in the study favored action to prevent a regulatory ban, compared to just over a fifth of the 57 "stakeholder boards."[27]

Armstrong's research does not speak directly to the comparison between traditional stockholder boards and instrumentalist stakeholder boards as his study compared traditional stockholder boards with boards that were duty-bound to respect stakeholders' interests. Nonetheless, his work underscores the practical importance of how decision makers conceive of their role and of access to information that reinforces and supports that conception.

In contrast to the rational agents of economic theory, real corporate leaders are subject to a wide range of decision-making biases such as the tendency to rely on information that is readily available (the "availability" bias) or more perceptually prominent (the "salience" bias). Given these and other well-known behavioral biases, it is reasonable to think that an "instrumentalist stakeholder board" presented with information about the likely consequences of its decisions for each of the company's stakeholders would in some situations make different and better decisions (from a shareholder value point of view) than a "traditional shareholder board." Some of the board's decisions would also be better for the affected stakeholders. Directors would have greater clarity about their role and a more complete picture of the potential consequences of the alternative choices before them and, therefore, of the potential repercussions both negative and positive for shareholder value.

Some challenges for instrumental stakeholderism

From a shareholder value point of view, instrumental stakeholderism appears to be an improvement over traditional shareholder capitalism. Leading and governing with stakeholder

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[26] J. Scott Armstrong, "Social Irresponsibility in Management," *J. of Business Research*, 5 (September 1977); pp. 185-213. Armstrong differentiates between a stakeholder orientation and a public interest orientation, arguing that seeking to act in the best interests of society could lead managers to take arbitrary actions. According to Armstrong, under a stakeholder orientation, management "should try to ensure that the marginal rate of return on contributions is equal for each of the primary interest groups," at 193.

[27] J. Scott Armstrong, "Social Irresponsibility in Management," *J. of Business Research*, 5 (September 1977); pp. 185-213, at 204.

interests in mind also promises real benefits for stakeholders and society. Importantly, however, those benefits go only so far. Recall that instrumental stakeholderism requires corporate leaders to take stakeholders' interests into account, but it does not require them to respect those interests unless doing so would be financially beneficial for shareholders. According to this view, an investment in the company's stakeholders, like any other investment, should be pursued only if it is NPV (net present value)-maximizing.[28] Conversely, investments in stakeholders that reduce long-term shareholder value should be avoided. While proponents of instrumental stakeholderism tend to focus on examples like the Cummins Engine case mentioned above—so-called *win-win* situations—in which investing in stakeholders benefits society and translates into longer-term shareholder value, corporate leaders frequently face pressures and opportunities to generate shareholder value in ways that do not benefit all stakeholders.

Consider AT&T's recent decision to cut life insurance and death benefits for some 220,000 retired employees.[29] Since the early 1990s the company's life insurance plan documents have included language reserving the company's right to change benefits at any time, but many retirees said they had been promised certain benefits and never anticipated that AT&T would make such changes. One employee quoted by the *Wall Street Journal* said the company had agreed to pay at least $63,000 at his death as an incentive for his retirement but, under the changes, would pay $15,000 at most. The cuts allowed AT&T to book a $2.7 billion accounting benefit and reduce ongoing stress on the fund set aside for making post-employment payments to retirees. Over the previous decade, the fund's value had fallen from some $13 billion to $4 billion as payouts exceeded the fund's investment returns and the company's contribution. In explaining decision, a spokesperson for the company noted the need to cut costs in order to "remain competitive and attract capital."[30]

This decision might appear to conflict with the commitment made by AT&T's former CEO when he signed the BRT's statement vowing to lead AT&T for the benefit of all its stakeholders

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[28] Clifford Asness, Glenn Hubbard, Martin Lipton, Michael R. Strain, "American Enterprise Institute Roundtable: Was Milton Friedman Right about Shareholder Capitalism?" *Journal of Applied Corporate Finance*, Vol. 33, No. 1., Winter 2021, pp. 36-47, at 45, 46. Asness and Hubbard argue that investments in stakeholders and charitable giving are appropriate only if they are "NPV-maximizing" or "long-run positive NPV." Says Asness, "Take all positive-NPV projects—and reject the rest."
https://onlinelibrary.wiley.com/doi/10.1111/jacf.12443 (accessed December 31, 2021).

[29] Unless otherwise indicated, the facts of the AT&T example are taken from Theo Francis and Drew Fitzgerald, "AT&T Slashed Promised Life Insurance for Former Workers—and Time Runs Out at Year-End," *Wall Street Journal*, December 26, 2021, https://www.wsj.com/articles/at-t-slashed-promised-life-insurance-for-former-workersand-time-runs-out-at-year-end-11640544022, accessed December 26, 2021. See also, Erik Sherman, "AT&T Changes Life Insurance Promises To Retired Employees," *Forbes*, December 29, 2021,
https://www.forbes.com/sites/eriksherman/2021/12/29/att-changes-life-insurance-promises-to-retired-employees/, accessed June 25, 2022.

[30] Erik Sherman, "AT&T Changes Life Insurance Promises To Retired Employees," *Forbes*, December 29, 2021
https://www.forbes.com/sites/eriksherman/2021/12/29/att-changes-life-insurance-promises-to-retired-employees/, accessed June 25, 2022.

and not just its shareholders.[31] To be sure, retired employees were not on the list of stakeholders mentioned in that statement, but if we count them as stakeholders (which seems fair), the decision certainly did not benefit them and, arguably, frustrated legitimate expectations they had based on AT&T's long-standing practice if not on promises it had made to the retirees when they were still employed. Nonetheless, from an instrumental stakeholderism point of view, the decision was perfectly correct. Cutting the payments to retirees created value for shareholders by reducing the company's ongoing financial obligations and carried little risk of significant negative repercussions given that the affected retirees had no legal recourse against the company, little or no market power as workers or consumers, and no regulator or other third party to act on their behalf.

Proponents of instrumental stakeholderism tend to downplay the possibility that it can justify indifference or even serious harm to non-shareholder stakeholders.[32] Companies that mistreat their stakeholders, it is said, will suffer reputational damage, stakeholder defections, or legal sanctions sufficient to outweigh the financial benefits of such behavior—at least over the long term. According to the Business Roundtable, for example, "While… different stakeholders may have competing interests in the short term… the interests of all stakeholders are inseparable in the long term."[33] However, the AT&T example shows that this statement is at best an overgeneralization. The relationship between stakeholder welfare and shareholder value is highly contingent on the specific facts and circumstances of the situation. As noted earlier, investing in employee development or improved customer service or any other initiative that benefits an important stakeholder group will in some situations contribute to shareholder value and in others, diminish it, even when taking a long-term perspective. In situations like the Wells Fargo case, where stakeholders may not even know that they are being harmed, companies can be shielded from any negative repercussions at all for quite some time.

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[31] It is unclear whether the signers of the BRT statement had the authority to sign on behalf of their companies or to bind their successors in any way.

[32] See, e.g., Michael C. Jensen, "Value Maximization and Stakeholder Theory," *HBS Working Knowledge*, July 24, 2000 ("Indeed, it is obvious that we cannot maximize the long-term market value of an organization if we ignore or mistreat any important constituency.") See also Clifford Asness, Glenn Hubbard, Martin Lipton, Michael R. Strain, "American Enterprise Institute Roundtable: Was Milton Friedman Right about Shareholder Capitalism?" *Journal of Applied Corporate Finance*, Vol. 33, No. 1., Winter 2021, pp. 36-47, at 42. (In response to concerns about shareholder value coming from failures to meet the claims of non-investor stakeholders, Hubbard replies "that's not really the optimal thing for a firm to do if its aim is to maximize long term value.") Asness and Hubbard argue that investments in stakeholders and charitable giving are appropriate only if they are "NPV-maximizing" or "long-run positive NPV." https://onlinelibrary.wiley.com/doi/10.1111/jacf.12443 (accessed December 31, 2021). See also, Michael C. Jensen "Value Maximization, Stakeholder Theory, and the Corporate Objective Function," *Business Ethics Quarterly*, Vol. 12, No.1, April 2002, pp. 235-256; also published in the *Journal of Applied Corporate Finance*, Vol. 14, No. 3 (Fall 2001), pp. 8-21.

[33] Business Roundtable, "Redefined Purpose of a Corporation: Welcoming the Debate," *Medium*, August 25, 2019, https://bizroundtable.medium.com/redefined-purpose-of-a-corporation-welcoming-the-debate-8f03176f7ad8, accessed June 2022.

Economists Roy Shapira and Luigi Zingales have shown that polluting the environment, even when it is against the law and results in serious harm to public health, can in some circumstances be long-term value-maximizing for shareholders.[34] Using information in company documents disclosed in numerous trials including multi-district litigation settled in 2017 for $670 million,[35] Shapira and Zingales examined the decision DuPont executives made in 1984 regarding toxic emissions of perfluorooctanoic acid (PFOA), a chemical used in making Teflon that was seeping into the drinking water supply of the community where it was manufactured. The documents showed that executives knew PFOA is toxic to humans and does not break down in the environment. As reported in the study, three options were considered: ending production of PFOA, continuing production but with measures to abate the harmful emissions, continuing production without abatement measures. Shapira and Zingales then modeled the decision from the perspective of a rational, shareholder-value-maximizing manager using the present value of the long-term costs and benefits to the company associated with each option. Their analysis found that, in retrospect, the executives' decision—to continue producing PFOA without abatement — was shareholder-value-maximizing, even after taking into account the legal liabilities, regulatory sanctions, reputational effects, and other costs to the company over the ensuing thirty years.

The happy coincidence between shareholder gains and stakeholder welfare envisioned by instrumental stakeholderism presupposes a demanding set of real-world conditions not found in the DuPont case. Besides a sufficiently long timeframe and a high degree of transparency, convergence also depends on the presence of a timely accountability mechanism to translate any benefits bestowed (or harms visited) on other stakeholders into commensurate financial benefits (or costs) to the company and its shareholders. That mechanism might be robust competition that gives stakeholders options to take their business or talents elsewhere. It might be a legal system that affords injured stakeholders timely recourse against the company and compensation for harm they've suffered. It might be a regulatory agency that takes action against the company on behalf of injured stakeholders. It might be an NGO that mobilizes the public to support new laws or regulations to limit the offending conduct. In the absence of some such mechanism to translate harms to other stakeholders into costs for shareholders, however, those harms do not even enter the calculation of shareholder value and cannot be financially material for shareholders. Put differently, if stakeholders have no alternative to dealing with the company and no recourse against it, and if there is no third party with market or legal power to act on their behalf to reward or punish the company, stakeholders' interests will necessarily be subordinated to those of shareholders. And, as the DuPont case illustrates, even if such mechanisms exist, the optimal choice from the perspective of long-term shareholder value may

[34] Roy Shapira and Luigi Zingales, "Is Pollution Value-Maximizing? The DuPont Case," NBER Working Paper 23866, September 2017. http://www.nber.org/papers/w23866
[35] Kris Maher and Cameron McWhirter, "DuPont Settlement of Chemical Exposure Case Seen as a 'Shot in the Arm' for Other Suits," *Wall Street Journa*l, February 13, 2017, https://www.wsj.com/articles/dupont-chemours-settle-teflon-chemical-exposure-case-for-671-million-1486987602, accessed January 15, 2022.

be to ignore other stakeholders' interests and take the risk of stakeholder defections, litigation, regulatory action, or reputational damage.

Proponents of instrumental stakeholderism sometimes cite the clarity of its decision rule as one of its principal virtues. The rule's clarity, it is said, facilitates decision making and makes it easier to hold corporate leaders accountable. In principle, the rule does seem to be clear: respect other stakeholders' interests whenever doing so will maximize shareholder value. In practice, however, predicting which course of action will most likely maximize long-term shareholder value is an exercise fraught with difficulty, especially when it requires putting a value on goods such as health, clean air, or justice for which there is no market price, or predicting how laws, policies, or public sentiment will evolve over the long term. The longer the time frame, the more speculative the exercise.

When diesel engine manufacturers in the U.S. were caught using "defeat devices" in the 1990s to disguise their environmental emissions during on-road driving, they were fined a relatively modest $83.4 million by U.S. regulators and largely ignored by the general public.[36] When regulators and the public learned fifteen years later that Volkswagen had done the same thing with diesel-powered cars, enforcement priorities and public attitudes had changed dramatically. Even if Volkswagen executives had tried to quantify the long-term impact on shareholder value at the time the defeat device program was initially considered in 2006, it is doubtful they could have anticipated the nearly $35 billion the company would have to pay in fines and settlements alone by 2020[37] or the 46 percent drop in the company's share price in the two months after the scandal came to light, a loss of some $42.5 billion in the company's market cap.[38] The decision rule may be clear, but that does not mean it is easy to apply or free of difficult judgments. These judgments are just hidden from view, buried in the process of making assumptions, identifying options, forecasting future possible outcomes, assessing probabilities, setting discount rates, choosing analytical methods, and the like.[39]

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[36] Jo Warrick and Michael Grunwald, "Diesel Makers Settle Case, Agree to Cut Air Pollution," *The Washington Post*, October 23, 1998, https://www.washingtonpost.com/archive/politics/1998/10/23/diesel-makers-settle-case-agree-to-cut-air-pollution/34b4520c-3bc7-4d74-b046-5331b1053196/, accessed June 2022.

[37] For date of the original decision, see Jack Ewing, "Engineering Deception: What Led to Volkswagen's Diesel Scandal," *New York Times*, March 16, 2007, https://www.nytimes.com/interactive/2017/business/volkswagen-diesel-emissions-timeline.html
"Volkswagen says diesel scandal has cost it $34.69B," *Business Insurance*, March 17, 2020. https://www.businessinsurance.com/article/20200317/NEWS06/912333571/Volkswagen-says-diesel-emissions-scandal-has-cost-it-$3469B-Frank-Witter

[38] Geoff Colvin, "5 years in, damages from the VW emissions cheating scandal are still rolling in," *Fortune*, October 6, 2020, https://fortune.com/2020/10/06/volkswagen-vw-emissions-scandal-damages/, accessed June 2022.

[39] See, e.g., Stephen A. Ross, "Uses, Abuses, and Alternatives to the Net-Present-Value Rule, Financial Management; Fall 1995, Vol. 24, No. 3; pp. 96-102.

Critics of the Business Roundtable's statement on corporate purpose have said that it has no 'teeth" unless it causes decision makers to subordinate shareholder welfare to stakeholder welfare.[40] But that is a somewhat arbitrary definition of "teeth." If having "teeth" means helping corporate leaders adapt to the changing environment, see new opportunities, recognize previously unseen risks, and develop multi-purpose strategies that serve the interests of shareholders, stakeholders, and society alike, then a contingent stakeholder lens is surely preferable to a traditional shareholder value lens. Still, contingent stakeholderism is not without its own difficulties. Most notably, as discussed, it can sometimes justify serious harm to stakeholders and to society at large. And it glosses over the discrepancy between the actual time frames used by analysts, investors, and boards to evaluate executive and corporate performance and the much longer periods often needed for the interests of different stakeholders to converge. Moreover, while it is an improvement over traditional shareholder capitalism, it seems unlikely to win the hearts, minds, and trust of stakeholders—one of the stakeholder movement's core aims. For that, a more robust commitment to stakeholders is needed.

2. Classic Stakeholderism: Respecting stakeholders' legitimate claims

A different conception of stakeholder capitalism values stakeholder well-being in its own right. This version holds that stakeholders' interests must not only be considered, but that at least some of them must also be respected. Importantly, this view differentiates among types of interests, giving priority to those protected by ethical or legal norms as compared to those based on wishes, wants, or desires. The core idea is that the former, more fundamental interests, give rise to claims whose validity is not contingent on their contribution to shareholder value. In this sense, they are unconditional or categorical claims. They create ethical obligations to stakeholders that sit alongside the financial and strategic imperatives that corporate leaders must manage. This view, which I call "classic" stakeholderism for its similarity to early expressions of stakeholder theory, might also be termed "categorical" stakeholderism for its insistence that companies observe certain ethical norms in their dealings with their stakeholders.[41] This version of stakeholderism recognizes that serving stakeholder interests can often contribute to shareholder value but, in contrast to instrumental stakeholderism, it also holds that some stakeholder interests should be respected whether or not doing so will maximize value for shareholders.[42]

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[40] See, e.g., Clifford Asness, Glenn Hubbard, Martin Lipton, Michael R. Strain, "American Enterprise Institute Roundtable: Was Milton Friedman Right about Shareholder Capitalism?" *Journal of Applied Corporate Finance*, Vol. 33, No. 1., Winter 2021, pp. 36-47, at 44.

[41] The term also evokes the notion of a "categorical imperative" as a moral requirement put forth by the eighteenth-century German philosopher Immanuel Kant in his *Groundwork of the Metaphysics of Morals* (1785).

[42] See, e.g., Robert Phillips, R. Edward Freeman and Andrew C. Wicks, "What Stakeholder Theory Is Not," *Business Ethics Quarterly*, October 2003, Vol. 13, No. 4, pp. 479-502, at 481. Freeman and his co-authors state that "for

The DuPont case discussed earlier provides an example. In that case, allowing toxic chemicals to pollute the local water supply and endanger community health was shown to be shareholder-value-maximizing over the long term, and thus justified from an instrumental stakeholderism point of view. However, it would not be justified from a classic or categorical stakeholderism perspective. On this view, the company would acknowledge that members of the community have a fundamental interest in health that must be respected whether or not doing so would maximize shareholder value. This interest is protected by a basic ethical norm that proscribes knowingly causing injury to innocent parties. Classic stakeholderism would thus favor a decision to invest in abatement measures, even though the decision would not be shareholder-value maximizing compared to allowing the contamination to continue.

As this example shows, a commitment to ethics and classic stakeholderism are essentially two sides of the same coin. [43] That is because ethical norms are generally relational. [44] They define how individuals and companies should treat others—be they stakeholders or other parties—how others can expect to be treated. The reciprocal relationship between ethical norms and stakeholder claims can be seen in several of the cases discussed above. For instance, when AT&T cut certain life insurance and death benefits for its retirees, many of those affected appealed to norms such as promise-keeping or honoring agreements as a basis for their claim against the company. One *Forbes* article was even titled "AT&T Changes Life Insurance Promises To Retired Employees."[45]

Rationales for classic stakeholderism

As noted, classic stakeholderism recognizes that serving stakeholders can often contribute to shareholder value, but the view is rooted in other ideas. Basic decency, the need for stakeholders' trust, the requirements of corporate citizenship, preserving society's support for capitalism—all have been offered as rationales for adopting a form of categorical stakeholderism.[46] Proponents have argued, for example, that companies and their managers, no

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stakeholder theory, attention to the interests and well-being of some non-shareholders is obligatory for more than the prudential and instrumental purposes of wealth maximization of equity shareholders."

[43] Indeed, some scholars have called stakeholder theory "a theory of organizational management and ethics." See Robert Phillips, R. Edward Freeman and Andrew C. Wicks, "What Stakeholder Theory Is Not," *Business Ethics Quarterly*, October 2003, Vol. 13, No. 4, pp. 479-502, at 480.

[44] Ethics also speaks to individuals' aspirations and obligations to themselves.

[45] Erik Sherman, "AT&T Changes Life Insurance Promises To Retired Employees," *Forbes*, December 29, 2021 https://www.forbes.com/sites/eriksherman/2021/12/29/att-changes-life-insurance-promises-to-retired-employees/, accessed June 25, 2022.

[46] For a list of various rationales offered by academics, see Robert Phillips, R. Edward Freeman and Andrew C. Wicks, "What Stakeholder Theory Is Not," *Business Ethics Quarterly*, October 2003, Vol. 13, No. 4, pp. 479-502, Table 1 at 481.

less than other individuals, are obliged to respect society's basic ethical norms.[47] According to the this perspective, corporate leaders' responsibilities to shareholders are subordinate to their responsibilities as citizens and members of the community.[48] Research has shown that business practitioners generally agree with this point and its implied corollary that companies have certain obligations to each of their stakeholder groups.[49] Reflecting this insight, many companies organize their codes of conduct around responsibilities to their stakeholders. A well-known example is the Johnson & Johnson credo. As early as 1943, the credo laid out the company's responsibilities by its core constituencies—users of its products, its employees and managers, the communities in which it operated, and its stockholders.[50] Many contemporary codes of corporate conduct have a similar structure.[51]

Other commentators have emphasized that honoring basic ethical norms in dealing with stakeholders is crucial for establishing and maintaining their trust in the company and in the broader market system.[52] Indeed, most people are more likely to trust a company that is categorically committed to honesty and fair dealing than one that says "we treat you fairly only when it will maximize shareholder value to do so."[53] In other words, companies are more apt to enjoy their stakeholders' trust—and reap the benefits that flow from it—if they take a categorical rather than an instrumental approach to stakeholder interests. In fact, acting ethically toward stakeholders when it is *not* obviously in the company's financial interest to do

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[47] See, e.g., Lynn Sharp Paine, *Value Shift: Why Companies Must Merge Social and Financial Imperatives to Achieve Superior Performance*, New York: McGraw-Hill, 2003, esp. pp. 154-160.
[48] Some of these arguments depend on attributing entity status and agency to companies, while others rely only on the moral obligations of managers as individuals. For the latter, see e.g., Nien-hê Hsieh, "The Responsibilities and Role of Business in Relation to Society: Back to Basics?," *Business Ethics Quarterly,* Vol. 27, No. 2 (April 2017), pp. 293-314,
https://www.hbs.edu/ris/Publication%20Files/The%20Responsibilities%20and%20Role%20of%20Business%20in%20Relation%20to%20Society%20Back%20to%20Basics_4e10dd36-bf51-48d6-8491-5e8f981fd433.pdf.
[49] See Lynn S. Paine, Rohit Deshpandé, and Joshua D. Margolis, "A Global Leader's Guide to Managing Business Conduct," Harvard Business Review online, September 2011, https://hbr.org/2011/09/a-global-leaders-guide-to-managing-business-conduct; see also Lynn S. Paine, Rohit Deshpandé, Joshua D. Margolis, and Kim Eric Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?" *Harvard Business Review* 83, no. 12 (December 2005): 122–133, https://hbr.org/2005/12/up-to-code-does-your-companys-conduct-meet-world-class-standards. The article describes the Global Business Standards Codex, a compilation of widely accepted standards of conduct to govern companies' relationships with their various stakeholders.
[50] For the Credo as originally written, see Richard S. Tedlow and Wendy K. Smith, "James Burke: A Career in American Business (A), Harvard Business School Case, 9-389-177 (1989), Exhibit 3, p. 21.
[51] See Lynn S. Paine, Rohit Deshpandé, Joshua D. Margolis, and Kim Eric Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?" *Harvard Business Review* 83, no. 12 (Dec 2005): 122–133, https://hbr.org/2005/12/up-to-code-does-your-companys-conduct-meet-world-class-standards.
[52] On the dynamics of trust in individual companies, see, e.g., Sandra J. Sucher and Shalene Gupta, *The Power of Trust*, New York: PublicAffairs, 2021, especially pp. 22-25. On the role of trust in sustaining social and political support for market capitalism, see, e.g., Joseph L. Bower, Herman B. Leonard, and Lynn S. Paine, *Capitalism at Risk: How Business Can Lead*, Harvard Business Review Press, 2020, especially pp. 245-248.
[53] On the relationship between ethics and trust, see e.g., Brenkert, G., "Trust, Business and Business Ethics: An Introduction. *Business Ethics Quarterly,* 8 (2), 195-203.

so may be one of the most effective ways to generate trust.[54] By the same token, corporate activities that injure stakeholders or harm society only destroy trust—and not just in the offending company. When companies inflict harm on their stakeholders or other third parties, they contribute to the perception that business as a whole is corrupt and cannot be trusted.

The idea that corporate leaders are permitted, let alone required, to act in ways that do not necessarily maximize shareholder value may sound like heresy. But that is far from the case. Even the best-known proponent of shareholder primacy, Milton Friedman, acknowledged that shareholder value must be pursued within the rules of society as embodied in law and "ethical custom."[55] In his well-known *New York Times* article of 1970, he defined ethical custom quite narrowly as requiring only that companies compete "without deception or fraud," but presumably he would have condemned deception of *any* stakeholder – customers, employees, suppliers, shareholders, and communities alike—and would not have condoned deception even if it could be shown to create long-term value for shareholders. He would not, for example, have condoned Wells Fargo's deception of customers even in a context where it was unlikely to be exposed and penalized. (There are many such contexts across the world.) Insofar as Friedman regarded corporate leaders as bound to respect stakeholders' interest in not being deceived, he might even be classified as a supporter of categorical stakeholderism—albeit of a very delimited sort.

A more robust form of categorical stakeholderism is found in the Business Roundtable's 1981 statement on corporate responsibility. In that statement, the BRT declared that "the shareholder must receive a good return but the legitimate concerns of other constituencies also must have the appropriate attention."[56] Although the statement does not say what claims are "legitimate," or how legitimacy is to be assessed, the implicit message is that some claims deserve to be recognized in their own right, independently of their contribution to corporate profit or shareholder gain. This doesn't mean that honoring these claims will necessarily hurt shareholders. Indeed, the document states that "some leading managers" believe that attending to the legitimate claims of all constituencies will best serve the interests of shareholders.[57]

[54] A classic example is Johnson & Johnson's handling of the Tylenol crisis in 1982. At the time of the company's nationwide recall of Tylenol following seven unexplained deaths, it was not at all obvious that the decision would be long-term beneficial for the company. Commentators at the time predicted that the recall would be the death of the Tylenol brand. See Richard S. Tedlow and Wendy K. Smith, "James Burke: A Career in American Business (B)," Harvard Business School Case, 9-390-030 (1989), p.3 (quoting an advertising executive predicting that the company would be unable to sell another product under the Tylenol name).
[55] Milton Friedman, "The Social Responsibility Of Business Is to Increase Its Profits," *New York Times Magazine,* September 13, 1970. Friedman does not provide a rationale for urging managers to adhere to ethical custom and forgo fraud, but some economists have argued that adherence to ethical norms such as forbearance from fraud contributes to market efficiency. See, e.g., Daniel M. Hausman and Michael S. McPherson, "Taking Ethics Seriously: Economics and Contemporary Moral Philosophy," *Journal of Economic Literature*, Vol. 31, No. 2 (June 1993), pp. 671-731. There is, of course, a vast philosophical literature going back to ancient Greece on why adherence to ethical norms is important for individuals, groups, and society.
[56] The Business Roundtable, *Statement on Corporate Responsibility* (October 1981), p. 9.
[57] The Business Roundtable, *Statement on Corporate Responsibility* (October 1981), p. 9.

However, in contrast to instrumental version stakeholderism, the legitimacy of these claims does not depend on their contribution to shareholder value.

A version of categorical stakeholderism can also be found in the American Law Institute's 1992 *Principles of Corporate Governance*, which explicitly acknowledge that corporate decision makers may take ethical considerations into account "even if corporate profit and shareholder gain are not thereby enhanced."[58] The accompanying commentary names various constituencies, in addition to shareholders, with which corporations are legitimately concerned, specifically calling out "employees, customers, suppliers, and members of the communities in which the corporation operates."[59] While noting that actions taken on the basis of ethical considerations are often consistent with long-term increases in value, the text observes that such actions may be not only appropriate but desirable at times even if they do not enhance corporate profit or shareholder gain.[60] The text goes on to say, "Corporate officials are not less morally obliged than any other citizens to take ethical considerations into account, and it would be unwise social policy to preclude them from doing so." In effect, the ALI's 1992 principles say that categorical stakeholderism is both legally permissible and socially desirable.[61]

Recent court cases in Delaware go further, suggesting that categorical stakeholderism may also be legally desirable if not required as a matter of fiduciary duty in certain situations.[62] The recent case against the board of directors of Boeing, maker of the MAX 737 narrow-body airliner, speaks to this point.[63] After two fatal crashes killing 346 passengers and crew, shareholders filed a derivative suit on behalf of the company alleging that the board had

[58] The American Law Institute's *Principles of Corporate Governance* were adopted in 1992 and published in 1994. See American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations* (St Paul, MN: American Law Institute Publishers, 1994), §2.01(a) and (b), p. 53 ((a) "[A] corporation…should have as its objective the conduct of business activities with a view to enhancing corporate profit and shareholder gain. (b) Even if corporate profit and shareholder gain are not thereby enhanced, the corporation…(1) Is obliged… to act within the boundaries set by law; (2) "May take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business; and (3) May devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes.")

[59] American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations*, 1994, p. 55.

[60] American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations*, 1994, pp. 60-61 ("Corporate officials are not less morally obliged than any other citizens to take ethical considerations into account, and it would be unwise social policy to preclude them from doing so.")

[61] For a similar interpretation, see Thomas Donaldson and Lee E. Preston, "The Stakeholder Theory of the Corporation," *Academy of Management Review,* Vol. 20, No. 1 (1995), pp. 65-91, at p. 82.

[62] See Jill E. Fisch and Steven Davidoff Solomon, "Should Corporations Have a Purpose?" *Texas Law Review*, Vol.99, Issue 7, 2021, p. 1309, at 1325-1326. https://texaslawreview.org/wp-content/uploads/2021/07/Fisch.Printer.pdf (arguing that failure to given sufficient attention to certain stakeholder interests may put corporate leaders at risk of legal action for breach of fiduciary duty).

[63] Another recent case in this line of cases on what is known as "*Caremark* duties," is the Blue Bell Creameries case: *Marchand v. Barnhill*, 212 A.3d 805 (Del. 2019). In this case against the board of ice cream maker Blue Bell Creameries USA, the shareholder plaintiffs alleged that the board had failed in its duty to oversee food safety, a "mission-critical" issue for the company. In allowing the case to proceed beyond the pleading phase, the court emphasized the importance of consumer confidence in the health and safety of the company's products.

breached its duty of oversight by failing to oversee and monitor airplane safety. [64] As evidence, plaintiffs cited several factors: the absence of board or board-level committee discussions of safety, the absence of a committee charged with monitoring safety, the absence of safety in Boeing's enterprise risk management system, and the lack of a safety reporting system to the board. In allowing the case to proceed beyond the pleading phase, the court noted that while certain board and management communications mentioned safety "in name," they were not "safety-centric." That is, they focused on the financial, operational, public relations, or legal implications of safety rather than on safety itself.[65]

To be sure, establishing a board's liability for a failure of oversight is extremely difficult, and the case against Boeing's board was ultimately settled before trial with insurance companies paying shareholders some $237 million.[66] For directors and officers, however, the case suggests that due regard for stakeholders' fundamental interests—and not just their impact on shareholder value—is increasingly seen as part of being a good fiduciary. From a categorical stakeholderism point of view, the MAX 737 debacle's estimated $68 billion cost to the company and its shareholders is certainly noteworthy but it is not the principal reason for protecting passenger safety or preventing deadly airplane crashes.[67]

Some challenges for classic stakeholderism

Compared to instrumental stakeholderism, classic stakeholderism posits much stronger protection for stakeholder and societal interests. As discussed earlier, classic stakeholderism holds that stakeholder claims derived from basic ethical and legal norms deserve to be respected in their own right, independent of their implications for shareholder value. This view rules out behavior that deceives, wrongs, disregards, or otherwise injures fundamental stakeholder interests even if the behavior would create shareholder value. As critics of stakeholderism have noted, however, determining which interests must be respected is not always easy.[68]

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[64] *In re The Boeing Company Deriv. Litig., 2021 WL 4059934,* at *1 (Del. Ch. Sept. 7, 2021). The court denied the company's and board's motion to dismiss the case at the pleading stage, noting that the pleadings had established that the board faced a substantial likelihood of liability. ("[Director liability] may be based on the directors' complete failure to establish a reporting system for airplane safety, or on their turning a blind eye to a red flag representing airplane safety problems.") https://courts.delaware.gov/Opinions/Download.aspx?id=324120
[65] *In re The Boeing Company Deriv. Litig.*, 2021 WL 4059934, at *1 (Del. Ch. Sept. 7, 2021), at 77, 80-81.
[66] Andrew Tangel, "Boeing Board to Add Safety Expert, Make Other Changes in 737 MAX Settlement," *Wall Street Journal,* November 5, 2021, https://www.wsj.com/articles/boeing-board-to-add-safety-expert-make-other-changes-in-737-max-settlement-11636150675
[67] See Chris Isadore, "Boeing's 737 Max debacle could be the most expensive corporate blunder ever," CNN Business, November 17, 2020, https://www.cnn.com/2020/11/17/business/boeing-737-max-grounding-cost. As of November 2020, Boeing had estimated its direct costs from the crashes at some $20 billion. Taking into account other costs, Bank of America put the estimate closer to $25 billion. Some commentators say that if lost sales are taken into account the cost could exceed $68 billion (the cost of BP's Deepwater Horizon explosion).
[68] See, e.g., Elaine Sternberg, "The Stakeholder Concept: A Mistaken Doctrine," Foundation for Business Responsibilities, Issue Paper No. 4, November 1999.

For practical purposes, a useful starting point is the basic norms of corporate conduct that research has shown to be widely accepted by leading companies and business practitioners around the world.[69] These norms speak to basic precepts such as obeying the law, respecting human rights, truth and honesty, honoring promises, protecting health and safety, and so on. Attending to these norms would have surely given pause to the decision makers at Wells Fargo, DuPont, Boeing, Volkswagen, and AT&T discussed above. Rather than trying to reduce the costs and benefits of each and every decision to a financial calculus, it may be easier, more prudent, and more efficient simply to follow time-tested principles of ethics. Decision makers at Volkswagen, for example, would likely have had an easier task and made better decisions from the perspective of all involved had they simply given top priority to their customers' and the public's interest in having accurate information about emissions.

Still, there is no question that corporate leaders can face difficult judgments about which interests must be protected. Consider a corporate restructuring that involves mass layoffs. The company can save millions of dollars by eliminating its customary (but legally optional) practice of giving advance notice and severance packages to departing employees. Assume further that eliminating notice and severance packages will help management meet the guidance on margins previously announced to shareholders. Some managers will see the proposal as perfectly valid, arguing that employees have no legitimate claim to advance notice or severance payments in this situation, while other managers will find the proposal profoundly unfair to employees and thus inconsistent with the requirements of classic stakeholderism.

An equally, if not more, vexing challenge for classic stakeholderism is resolving conflicts among competing stakeholder claims. Even if the universe of claims is limited to those based on basic legal and ethical principles, corporate leaders can still face gut-wrenching trade-offs. The world does not necessarily arrange itself so that every legitimate claim can be satisfied at every moment. During the early days of the COVID-19 pandemic, for instance, some companies in the food sector faced conflicts between ensuring the safety of employees working in plants plagued by Covid outbreaks and meeting their responsibilities to get food to distributors and consumers confined to their homes.[70] Unlike contingent stakeholderism, which offers "maximize shareholder value" as a single all-purpose decision rule for resolving such dilemmas, classic stakeholderism holds that they can only be resolved through a process of

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[69] See Lynn Paine, Rohit Deshpandé, Joshua Margolis, and Kim Eric Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?"*Harvard Business Review* 83, no. 12 (December 2005): 122–133, https://hbr.org/2005/12/up-to-code-does-your-companys-conduct-meet-world-class-standards The article describes the Global Business Standards Codex, a compilation of widely accepted standards of conduct to govern companies' relationships with their various stakeholders.

[70] See, e.g., Tom Polansek, "Smithfield Foods shuts U.S. bacon, ham plants as coronavirus hits meat sector," Reuters, April 15, 2020, https://www.reuters.com/article/us-health-coronavirus-usa-smithfield-foo/smithfield-foods-shuts-u-s-bacon-ham-plants-as-coronavirus-hits-meat-sector-idUSKCN21X3DM

deliberation that weighs and compares the particular interests at stake, and seeks to minimize harm and maximize human well-being in those circumstances.

Critics of stakeholder theory often point to the lack of a single decision rule for resolving trade-offs as a major shortcoming.[71] Its proponents, however, see the demand for a single decision rule as based on a misguided and overly narrow conception of rationality, and divorced from the messy realities of corporate leadership.[72] They have a point. By its very nature, the corporate leaders' job entails multiple obligations. In such a world, it is not possible to say in advance how real-world conflicts among obligations should be resolved or whose interests should take priority. Both depend on the facts and circumstances of the situation and the nature of the particular interests at stake. Imaginative leaders can sometimes find creative strategies that reconcile such conflicts, but there are also times when tradeoffs cannot be avoided. In those situations, there will be times when employees' interests must come first, times when customers' interests take priority, times when public need is paramount, and times when shareholders' interests should prevail.[73]

Moreover, as discussed earlier, applying the logic of shareholder value maximization to decisions that involve factors such as human health, rule of law, climate control, or public trust for which there is no market price is perilous.[74] The rule to "maximize shareholder value" does not have much purchase when the issue is deciding how much to invest in personal protection equipment for employees—a decision many leaders faced in the early days of the Covid pandemic. Or take the example of deciding whether to invest scarce resources in reducing toxic emissions in the supply chain or, alternatively, in curbing greenhouse gas emissions. For these

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[71] This is a long-standing critique of stakeholder theory from both economists and business practitioners. See, e.g., the Business Roundtable's 1997 Statement on Corporate Governance, stating: "The notion that the board must somehow balance the interests of stockholders against the interests of other stakeholders…is, moreover, an unworkable notion because it would leave the board with no criterion for resolving conflicts between interests of stockholders and of other stakeholders or among different groups of stakeholders." http://www.ralphgomory.com/wp-content/uploads/2018/05/Business-Roundtable-1997.pdf. See also, Elaine Sternberg, "The Stakeholder Concept: A Mistaken Doctrine," Foundation for Business Responsibilities, Issue Paper No. 4, November 1999; Michael C. Jensen "Value Maximization, Stakeholder Theory, and the Corporate Objective Function," *Business Ethics Quarterly*, Vol. 12, No.1, April 2002, pp. 235-256 (also published in the *Journal of Applied Corporate Finance*, Vol. 14, No. 3 (Fall 2001), pp. 8-21.

[72] See, e.g., Robert Phillips, R. Edward Freeman and Andrew C. Wicks, "What Stakeholder Theory Is Not," *Business Ethics Quarterly*, October 2003, Vol. 13, No. 4, pp. 479-502, at 485-488 (arguing that it is impossible to say *a priori* how stakeholder interests should be accounted for). See Nien-hê Hsieh, "Maximization, Incomparability, and Managerial Choice," *Business Ethics Quarterly*, Vol. 17, Issue 3, July 2007, pp. 497-513 (arguing that rationality does not require managers to have a single measure to compare alternatives). See also Colin Meyer, "Shareholderism versus Stakeholderism—A Misconceived Contradiction. A Comment on 'The Illusory Promise of Stakeholder Governance' by Lucian Bebchuk and Roberto Tallarita," EGCI (European Corporate Governance Institute) Law Working Paper No. 522/2020, June 2020), http://ssrn.com/abstract_id=3617847 (arguing that judgment and trade-offs are inherent in a board's job whether the firm is a shareholder or stakeholder oriented).

[73] Lynn S. Paine, "Covid-19 Is Rewriting the Rules of Corporate Governance," *Harvard Business Review* (online edition), October 6, 2020, https://hbr.org/2020/10/covid-19-is-rewriting-the-rules-of-corporate-governance

[74] For a classic critique of cost-benefit analysis along these lines, see Steven Kelman, "Cost-Benefit Analysis: An Ethical Critique," *AEI Journal on Government and Society*, January-February 1981, pp. 33-40.

types of decisions, corporate leaders need a richer set of criteria. Ultimately, they must make an all-things-considered judgment, taking into account their responsibilities to the company, its stakeholders, and society at large.

In recent discussions, stakeholderism has sometimes been framed as a new conception of corporate purpose. The Business Roundtable, for example, called its 2019 statement on its signers' commitment to their companies' various stakeholders "Statement on the Purpose of a Corporation." But classic stakeholderism is not so much a theory of corporate purpose as a theory of corporate responsibility. As discussed in the previous section, early formulations of stakeholder theory were agnostic on the question of corporate purpose. Recall that in his seminal book on stakeholder theory Freeman defined "stakeholder" as "[a]ny group or individual who can affect or is affected by the achievement of the firm's objectives."[75] As this definition makes clear, a company's objectives or purpose and the interests of its stakeholders are two separate things. Conceptually, at least, classic stakeholderism is consistent with almost any overarching corporate purpose—be it maximizing returns to shareholders, increasing company value, promoting employee welfare, delivering a particular product or service, or providing a public benefit. It just holds that other stakeholders' legitimate interests must be respected in achieving that purpose, whatever it may be. How precisely to do that is left to the judgment of corporate leaders.

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Critics of stakeholderism have sometimes argued that it diminishes corporate leaders' accountability to shareholders.[76] In the case of classic stakeholderism, the validity of this critique is questionable. In no way does it reduce managers' responsibility to answer to shareholders. On the contrary, it appears to expand corporate leaders' accountability by making them accountable to shareholders for respecting the legitimate claims of other stakeholders. This expanded accountability can be seen in shareholders' increasing demands for disclosure and reporting on how companies are handling certain social and environmental issues.[77] In holding that certain stakeholder interests must be respected in their own right, regardless of the impact on shareholder value, classic stakeholderism challenges one aspect of shareholder primacy but it leaves fully intact its other main pillars—accountability to shareholders and shareholders' exclusive right to vote on directors and other corporate matters.

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[75] R. Edward Freeman, *Strategic Management: A stakeholder approach* (Boston: Pitman, 1984), Exhibit 1.5, p. 25.
[76] See, e.g., Council of Institutional Investors Press Release, "Council of Institutional Investors Responds to Business Roundtable Statement on Corporate Purpose," August 19, 2019. https://www.cii.org/aug19_brt_response
[77] See, e.g., Lydia Beyoud, "Shareholders Up Demands for Workplace Diversity Data Seen by Few," Bloomberg Law, June 7, 2021, https://news.bloomberglaw.com/esg/shareholders-up-demands-for-workplace-diversity-data-seen-by-few, ("Shareholders are increasingly asking corporations to reveal gender and diversity data about their workforces…") and Caroline Flammer, Michael W. Toffel, and Kala Viswanathan, "Shareholders Are Pressing for Climate Risk Disclosures. That's Good for Everyone," *Harvard Business Review Digital Articles*, April 22, 2021, https://hbr.org/2021/04/shareholders-are-pressing-for-climate-risk-disclosures-thats-good-for-everyone ("Shareholders are becoming more vocal in demanding companies disclose the risks of climate change.")

As noted, classic stakeholderism provides stronger protection for stakeholders than does instrumental stakeholderism. However, some proponents of stakeholderism envision an even more robust commitment to stakeholders—one that delivers substantive improvements to non-shareholder stakeholders' welfare and calls for rethinking boards' fiduciary duties as traditionally understood under the law of Delaware, legal home to more than 66 percent of Fortune 500 companies.[78]

3. Beneficial Stakeholderism: Improving outcomes for stakeholders

Yet another version of stakeholder capitalism takes stakeholder betterment as its touchstone. This version seeks not just to meet stakeholders' basic claims but also measurably to improve their well-being. This view is motivated in part by a belief that optimizing for shareholder returns over the past four decades has led many companies to underinvest in their non-shareholder constituencies and, in the aggregate, resulted in a disproportionate share of capitalism's gains going to the owners of capital as compared to workers, consumers, the environment, local communities, and society-at-large. It is also driven by a belief that running companies to improve the lives of all stakeholders will help address some of the large-scale problems and inequities facing society today and thereby help protect the long-term health of the economy and quell growing discontent with capitalism.

I call this view "beneficial stakeholderism" for its similarity to the view of stakeholders associated with the benefit corporation movement—by which I mean both the spread of the new legal structure known as the benefit corporation and the effort to certify traditional corporations as so-called B Corps. Since 2010 some 40 U.S. states and 8 countries or provinces have adopted legislation permitting businesses to organize themselves as a "benefit corporation" or "public benefit corporation."[79] Although these statutes vary from jurisdiction to jurisdiction, they have certain common features. One is a requirement that the company's directors "balance" or "consider" the interests of its various stakeholders when setting policies

[78] Delaware Division of Corporations, About the Division of Corporations, https://corp.delaware.gov/aboutagency/, accessed August 2022.

[79] For the number of U.S. states with benefit corporation legislation, see Grunin Center for Law and Social Entrepreneurship, NYU Law School, "The State of Social Enterprise and the Law 2021-2022," p. 5, https://socentlawtracker.org/wp-content/uploads/2022/08/2021-2022_Grunin_Tepper_Report.pdf. The term "benefit corporation" is the more common term used in these state statutes, although Delaware and Colorado use the term "public benefit corporation" according to Mark J. Loewenstein, "Benefit Corporation Law," *University of Cincinnati Law Review*, Vol. 85, 2017, p.382. The B Lab Company website lists the following additional countries or provinces as having benefit corporation legislation: British Columbia, Canada, Colombia, Ecuador, France, Italy, Peru, Rwanda, Uruguay. See "Stakeholder Governance. Making business accountable to people and planet," https://www.bcorporation.net/en-us/movement/stakeholder-governance (accessed April 16, 2023).

and making decisions.[80] Another is periodic reporting on the company's progress in advancing its stakeholders' well-being.[81] This legislation was enacted, in part, to create a legal structure that unambiguously gives corporate boards discretion to protect the interests of non-shareholder stakeholders.[82] Similarly, B Corp certification — which is granted by a non-profit known as B Lab and, unlike incorporating as a benefit corporation, carries no legal significance—requires directors to consider the interests of all stakeholders. To earn and maintain B Corp certification, companies must undergo periodic assessments that identify and track outcomes for defined stakeholders, including the environment, communities, customers, employees, and shareholders.[83]

Beneficial stakeholderism has certain affinities with the benefit corporation approach to stakeholders, but it is not necessary to be a benefit corporation or a certified B Corp to adopt its tenets. Unilever's approach to stakeholders under the leadership of Paul Polman is an example. In Polman's 2021 book with Andrew Winston, *Net Positive: How Courageous Companies Thrive By Giving More Than They Take,* he writes that "creating positive returns for all stakeholders" is a core principle of his approach to business leadership.[84] During Polman's tenure as Unilever's CEO from 2009 to 2019, the company pursued a multi-stakeholder agenda that delivered gains for many of its stakeholders. As detailed in Unilever's ten-year progress report on its Sustainable Living Plan, the company improved employees' health and well-being, made its pay system more equitable, paid all employees a living wage, and improved the livelihoods of more than 800,000 smallholder farmers. It also advanced human rights in the supply chain, improved the nutritional value of its products, improved the health and hygiene of more than a

[80] Delaware's law on public benefit corporations is often cited as a model. The law states that the board of directors "shall manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation." Delaware Code, Title 8, §365(a) (https://delcode.delaware.gov/title8/c001/sc15/ accessed September 21, 2022). By comparison, § 301 (a) of the model legislation for benefit corporations developed by B Lab states that corporate directors "shall consider the effects of any action or inaction" on various parties including shareholders, employees, suppliers, subsidiaries, customers, the community, the local and global environment, as well as the ability of the corporation to accomplish its general and specific public benefits (as reported in J. Colombo, "Taking Stock of the Benefit Corporation," 7 *Texas A&M Law Review*, Vol. 7 (2019), 73-124, at p. 85.)

[81] For Delaware's reporting requirements for public benefit corporations, see Delaware Code, Title 8, §366(b) (https://delcode.delaware.gov/title8/c001/sc15/ accessed September 26, 2022).

[82] See Edward B. Rock, "For Whom Is the Corporation Managed in 2020? The Debate over Corporate Purpose," *The Business Lawyer*, Vol. 76, Spring 2021, pp. 363-395, at p. 392, https://www.americanbar.org/content/dam/aba/publications/business_lawyer/2021/76_2/essay-corp-purpose-202104.pdf
Leo E. Strine, Jr., "Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy—A Reply to Professor Rock," *The Business Lawyer*, Vol. 76, Spring 2021, pp. 397-435, at pp. 429-430, https://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.27526.21.pdf

[83] See B Lab Company website, https://www.bcorporation.net/en-us/programs-and-tools/b-impact-assessment?_ga=2.89192027.1359832834.1663596610-1726797052.1663596610 (accessed September 19, 2022).

[84] Paul Polman and Andrew Winston, *Net Positive: How Courageous Companies Thrive By Giving More Than They Take* (Boston, MA: Harvard Business Review Press, 2021), pp. 34-36.

billion people, and made progress toward cutting its environmental impact in half by 2030.[85] During roughly the same period, Unilever also delivered a total shareholder return of 290 percent, well above the median of 165 percent for eighteen consumer goods companies in its peer group.[86]

The Coalition for Inclusive Capitalism is another group whose approach to stakeholders could be categorized as beneficial stakeholderism. Founded in 2014 by investor Lynn Forester de Rothschild, the Coalition is a non-profit that works with leaders from the private, public, and civic sectors "to make capitalism inclusive and its benefits more widely and equitably shared." [87] According to the Coalition's website, "Inclusive capitalism is fundamentally about creating long-term value that benefits all stakeholders—businesses, investors, employees, customers, governments, communities, members of society, and the planet."[88] The Coalition has called on companies to broaden the set of stakeholders to whom they are responsible and proposed that the U.S. Securities and Exchange Commission develop mandatory corporate disclosures encompassing the full range of stakeholders.[89] The Coalition has also offered a number of targeted proposals aimed at improving the lives of workers in particular. Among these, a "living wage" for the lowest paid, more profit- and gain-sharing programs, more opportunities for promotion to higher-paying jobs, and expanded access to retirement programs.[90]

The spirit of beneficial stakeholderism can also be seen in various company initiatives. One example is the Cummins Engine case discussed earlier. As noted, Cummins helped create a global hub for advanced manufacturing in southeast Indiana through a major collaborative effort involving other companies and the region's civic and educational leaders. Employees benefited from new, higher-skill jobs; the region's residents benefited from higher levels of educational attainment, higher incomes, and higher wage rates; and the company was able to manufacture a new line of high-speed, low-emissions diesel engines in its home region.

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[85] "Unilever Sustainable Living Plan 2010 to 2020: Summary of 10 years' progress," Unilever, March 2021, https://www.unilever.com/files/92ui5egz/production/16cb778e4d31b81509dc5937001559f1f5c863ab.pdf, accessed September 26, 2022.
[86] The total shareholder return figure for Unilever covers the period from 2009 to the end of 2018 and comes from Unilever's press release announcing Polman's plan to retire: https://www.unilever.com/news/press-and-media/press-releases/2018/unilever-ceo-announcement/. Total shareholder return calculations for peer group companies are based on financial and share price data as converted to U.S. dollars at the spot price as of August 20, 2019, where applicable, from Capital IQ, Inc, a division of Standard & Poor's.
[87] See Coalition for Inclusive Capitalism website, https://www.coalitionforinclusivecapitalism.com/ (accessed September 19, 2022).
[88] See Coalition for Inclusive Capitalism website, https://www.coalitionforinclusivecapitalism.com/what-is-inclusive-capitalism/ (accessed September 18, 2022).
[89] Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government & American Workers,* February 2021, https://www.coalitionforinclusivecapitalism.com/wp-content/uploads/2021/10/The_Framework_for_Inclusive_Capitalism.pdf, accessed September 26, 2022.
[90] Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government & American Workers*, February 2021, p. 6. (The framework starts with the principle that workers are "deserving [of] certain basic rights, including the right to be paid a fair share of the value they create.")

JPMorgan Chase's efforts to help revitalize Detroit is another example. Working with the mayor's office, community development financial institutions, and other city leaders, the bank invested funds and talent in bringing economic opportunity back to Detroit and its residents after the city's fiscal crisis and bankruptcy in 2013. The $200 million effort included funding for housing and neighborhood development, workforce development, and small businesses growth—all aimed at fostering racial equity and inclusive growth. During this period, the city's unemployment rate declined, companies began moving to Detroit, and mortgage markets started to rebound. Based on its experience in Detroit, the bank launched similar efforts in other distressed cities, including parts of Chicago, Washington, D.C., and areas of greater Paris with high levels of poverty.[91]

Beneficial stakeholderism compared to other versions

As these examples suggest, beneficial stakeholderism is similar to classic stakeholderism in attributing intrinsic (not just instrumental) value to certain interests of non-shareholder stakeholders. However, it goes beyond classic stakeholderism in its more expansive commitment to stakeholders' well-being. Consider employees. Classic stakeholderism is concerned with employee safety, equal opportunity, equal pay for equal work, and other interests protected by basic legal and ethical norms. Beneficial stakeholderism would expand this list to include dignity, inclusion, meaningful work, and economic equity in the broad sense—whether employees earn a decent livelihood, receive a fair share of the value they help create, and have sufficient opportunities for advancement. Or consider customers. Classic stakeholderism focuses on issues like truth in advertising, product safety, and fair pricing, whereas beneficial stakeholderism calls on companies to do more – to create products and services that improve customers' lives, that are meaningful or serve a social purpose, and that are widely accessible and affordable, especially for low-income consumers.

Beneficial stakeholderism is more demanding than classic stakeholderism in other ways as well. It is more dynamic. It envisions ongoing improvement in the outcomes delivered to stakeholders. It thus implies defined goals for each stakeholder group and methods for tracking, measuring, and reporting on those outcomes, as well as appropriate incentive and compensation systems. It requires an imaginative approach to strategy that incorporates stakeholder interests as essential building blocks rather than as side-constraints. And it requires a holistic approach to decision making and resource allocation. Rather than making each decision in isolation on its own terms, corporate leaders must view each decision as part of an

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[91] For details, see Joseph L. Bower, Herman B. Leonard, and Lynn S. Paine, *Capitalism at Risk: How Business Can Lead* (Boston: Harvard Business Review Press, 2020), pp. 250-264. See also Joseph L. Bower and Michael Norris, "JPMorgan Chase: Invested in Detroit (A)," Case 9-918-406 (Boston: Harvard Business School Publishing, March 2018).

overall portfolio of decisions that taken together over the specified time period achieve the desired outcomes for all stakeholders.

As noted earlier, beneficial stakeholderism is motivated in part by concerns about economic justice and the potential social and political consequences of ignoring the plight of those who feel left behind.[92] Proponents point out that over the past several decades, under the sway of shareholder primacy, U.S. workers' productivity increased markedly and their corporate employers enjoyed higher profits.[93] Shareholders, too, enjoyed higher returns.[94] Yet, workers' hourly wages barely budged.[95] Low-income workers, in particular, saw reduced access to jobs that pay a living wage and, equally important, to jobs that provide opportunities to move up the income ladder.[96] Middle-skilled workers also saw declining employment and stagnating wages.[97] At the same time, consumers have had to pay more for essentials such housing, education, and healthcare, further burdening low- and middle-income families.[98] Advocates of beneficial stakeholderism see it as helping narrow an otherwise growing and politically dangerous divide between the few who benefit from shareholder primacy and the many who are struggling or left out entirely.

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[92] Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government, & American Workers*, February 2021, pp. 2-5. See also Leo E. Strine, Jr., "Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy—A Reply to Professor Rock," *The Business Lawyer,* Vol. 76 (Spring 2021), pp. 397-435, at 418-421. Strine, at p. 419, n. 69, points out that these trends have disfavored Black Americans in particular since they are much more likely to be in low- and lower-middle income households.
[93] See, e.g., Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government, & American Workers*, February 2021, pp. 2-3 and research cited therein. The Coalition cites figures for the period between 1979 and 2018.
[94] See Economic Policy Institute (EPI), "The Productivity–Pay Gap," https://www.epi.org/productivity-pay-gap/, as updated October 2022.
[95] E.g., Zohar Goshen and Doron Levit, "Agents of Inequality: Common Ownership and The Decline of the American Worker," *Duke Law Journal,* Vol. 72, No. 1 (October 2022), https://ssrn.com/abstract=3832069. Recent research suggests that tight markets for low-wage workers following the Covid-19 pandemic counteracted about a quarter of the previous four-decade increase in wage inequality. See David Autor, Arindrajit Dube, and Annie McGrew, "The Unexpected Compression: Competition at Work in the Low Wage Labor Market," NBER Working Paper No. 31010, March 2023, http://www.nber.org/papers/w31010
[96] See e.g., Jared Bernstein, "The Living Wage Movement—Viewpoints," Economic Policy Institute (EPI), March 4, 2002, https://www.epi.org/publication/webfeatures_viewpoints_lw_movement/ and Michael D. Carr and Emily E. Wiemers, "The decline in long-term earnings mobility in the U.S.: Evidence from survey-linked administrative data," *Labour Economics*, Vol. 78 (October 2022), https://www-sciencedirect-com.ezp-prod1.hul.harvard.edu/science/article/pii/S0927537122000616. According to McKinsey Global Institute, job growth in OECD countries from 2000 to 2018 was driven largely by growth in part-time jobs. McKinsey Global Institute, *The Social Contract in the 21st Century,* February 2020 (Executive Summary), p. 6, https://www.mckinsey.com/~/media/mckinsey/industries/public%20and%20social%20sector/our%20insights/the%20social%20contract%20in%20the%2021st%20century/mgi-the-social-contract-in-the-21st-century-executive-summary-final.pdf accessed November 1, 2021.
[97] McKinsey Global Institute, *The Social Contract in the 21st Century,* February 2020 (Executive Summary), pp. 5-9.
[98] By contrast, consumers have seen lower costs and increased accessibility for many discretionary goods and services. McKinsey Global Institute, *The Social Contract in the 21st Century,* February 2020 (Executive Summary), pp. 10-11.

The call for beneficial stakeholderism is also driven by a belief that continuing to focus on short-term shareholder value maximization will exacerbate other major problems facing society such as climate change, resource scarcity, biodiversity loss, and accumulating non-recyclable waste. Without a change in priorities, companies will continue to produce externalities that, in the aggregate, threaten to disrupt the entire economic system.[99] Moreover, few companies will be in a position to make the long-term, and in some cases moonshot, investments necessary to find solutions to slow or head off these forces. Such investments are by definition uncertain. If they do pay off, it may take years if not decades. Companies focused on improving this quarter's earnings have neither the time nor the inclination to take such risks. According to proponents of beneficial stakeholderism, a shift in the corporate objective—from shareholder value to stakeholder well-being—is necessary to enable companies to play a role in helping combat these societal challenges and forging a more sustainable economic system.[100]

Like instrumental stakeholderism, beneficial stakeholderism rejects the short-termism of traditional shareholder value maximization and insists on a longer-term perspective. The two views diverge, however, in how they approach investment decisions. Instead of allocating resources based solely on the likely return to shareholders, beneficial stakeholderism prioritizes projects with the potential to improve outcomes for all the stakeholders affected. Although proponents have not, to my knowledge, spelled out precisely how such decisions should be made, the process presumably involves analyzing the expected impact on each affected stakeholder group and choosing either the project with the greatest total benefit in aggregate or the project that by some methodology optimizes across the groups. Consider two hypothetical projects whose total benefits are the same. One promises outstanding returns to shareholders but does little for customers or employees; the other promises good but lower returns to shareholders and also benefits customers and employees. Presumably, instrumental stakeholderism would favor the first project, while beneficial stakeholderism would favor the second.

This hypothetical is structurally similar to the decision that Professor Scott Armstrong gave to mock "boards of directors" in the role-playing research discussed earlier.[101] As noted, this research compared the decisions taken by boards who were told that their role was to maximize returns to stockholders with those taken by boards told that their duty was to recognize the interests of all the company's stakeholders. The "stakeholder boards" were given information

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[99] See Joseph L. Bower, Herman B. Leonard, and Lynn S. Paine, *Capitalism at Risk: How Business Can Lead*, (Boston, MA: Harvard Business Review Press, 2020).
[100] See, e.g., Paul Polman and Andrew Winston, *Net Positive: How Courageous Companies Thrive By Giving More Than They Take* (Boston, MA: Harvard Business Review Press, 2021).
[101] See above at pp. XXX. J. Scott Armstrong, "Social Irresponsibility in Management," *J. of Business Research*, Vol. 5, No. 3 (September 1977), pp. 185-213. According to Armstrong, under a stakeholder orientation, management "should try to ensure that the marginal rate of return on contributions is equal for each of the primary interest groups," at p. 193.

quantifying the likely effects of five possible actions the board could take on each of three relevant stakeholder groups—stockholders, customers, and employees—and in total. While the "stockholder boards" tended to choose the action that was best for shareholders but very bad for the others, the "stakeholder boards" favored the actions that distributed the benefits across the various stakeholders and that were better in aggregate.[102]

Proponents of beneficial stakeholderism also envision a change, relative to traditional shareholder value maximization, in how companies distribute the value they create, with a larger share going to non-shareholder stakeholders. In *Net Positive*, for instance, Polman and Winston urge corporate leaders to consider investing in the company and its stakeholders rather than returning capital to shareholders.[103] Instead of buying back shares or paying special dividends, they suggest ramping up R&D to develop more sustainable products and services, accelerating the shift to renewable energy and zero-carbon operations, investing in employee training and development, or fixing human rights issues and paying workers in the supply chain a living wage. As mentioned, other proponents of beneficial stakeholderism have called on corporate leaders to pay workers a living wage, offer employees more opportunities to advance to higher-paying jobs, expand access to retirement benefits, introduce more profit- and other gain-sharing programs, and offer more broad-based equity awards.[104] Shifting to a more stakeholder-oriented allocation of resources, say proponents of such measures, would ultimately lead to a more productive workforce, higher employee earnings, a stronger consumer base, increased GDP, and improved corporate profits, as well as a stronger social and political fabric.[105]

Some challenges for beneficial stakeholderism

Beneficial stakeholderism holds out the prospect of positive and ever improving outcomes for all stakeholders. Indeed, we have seen numerous examples of how investing in other stakeholders can at the same time advance the interests of companies and their shareholders. Many more examples can be found in the steady stream of publications by proponents of

[102] J. Scott Armstrong, "Social Irresponsibility in Management," *J. of Business Research*, Vol. 5, No. 3 (September 1977), pp. 185-213, at 202-204.
[103] Paul Polman and Andrew Winston, *Net Positive: How Courageous Companies Thrive By Giving More Than They Take*, Boston: Harvard Business Review Press (2021), p. 203
[104] Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government & American Workers*, February 2021, p. 6. (The framework starts with the principle that workers are "deserving [of] certain basic rights, including the right to be paid a fair share of the value they create.")
[105] E.g., Coalition for Inclusive Capitalism, *Framework for Inclusive Capitalism: A New Compact Among Business, Government, & American Workers*, February 2021, p. 4 (and studies cited there).

stakeholderism.[106] These examples of so-called "*win-win*" strategies are important to dispel the once-prevalent notion that investing in other stakeholders is necessarily detrimental to corporate and shareholder interests and to inspire others to pursue multi-stakeholder strategies. These stories show what imaginative business leaders can do when they take the needs of their stakeholders seriously, and think creatively about how to address them.

However, critics of stakeholderism are right to caution against expecting too much.[107] Like classic stakeholderism, beneficial stakeholderism at times entails trade-offs among the interests of different stakeholders, but its concern for a broader set of interests can make those trade-offs even more challenging. Moreover, there is a real question as to how much corporate leaders can invest in their non-shareholder stakeholders without running afoul of their legal duties as fiduciaries for the companies they serve or losing shareholders' support. To be sure, the law gives boards broad discretion to determine the company's strategy and time horizon, and to consider the interests of other stakeholders.[108] The one notable exception is when the board has decided to sell the company—a point to which I return below.[109] Otherwise, outside the context of a sale, the proper exercise of fiduciary duty arguably *requires* corporate leaders to consider the interests of other stakeholders even in a traditional corporation. [110] The Boeing example

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[106] See, e.g., Rebecca Henderson, *Reimagining Capitalism in a World on Fire* (New York: PublicAffairs, 2020); Alex Edmans, *Grow the Pie: How Great Companies Deliver Both Purpose and Profit* (Cambridge: Cambridge University Press, 2020); Sandra J. Sucher and Shalene Gupta, *The Power of Trust* (New York: PublicAffairs, 2021); Hubert Joly with Caroline Lambert, *The Heart of Business: Leadership Principles for the Next Era of Capitalism* (Boston: Harvard Business Review Press, 2021); Paul Polman and Andrew Winston, *Net Positive: How Courageous Companies Thrive By Giving More Than They Take* (Boston: Harvard Business Review Press 2021); Ranjay Gulati, *Deep Purpose: The Heart and Soul of High-Performance Companies* (New York: Harper Business 2022); Alan Murray with Catherine Whitney, *Tomorrow's Capitalist: My Search for the Soul of Business* (New York: PublicAffairs, 2022).

[107] See, e.g., Lucian A. Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance," *Cornell Law Review*, Vol. 106: 9 (2020), pp. 91-177, at p. 96.

[108] See, e.g., Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?* 99 *Texas L. Rev.* (2021), p. 1309, at p. 1325 ("[e]ven if the Delaware case law is properly understood as conveying a strong commitment to shareholder primacy in the takeover context, we question its relevance to the day-to-day operational decisions…"); Edward B. Rock, *For Whom Is the Corporation Managed in 2020? The Debate over Corporate Purpose*, 76 *Bus. Law.* 363, 368 (2021) at 375–76 ("outside the "end-game" or conflict situations . . . disinterested directors seeking in good faith to promote the value of the corporation have the discretion to the make the decisions that they believe are best for the corporation and its stakeholders").

[109] Under Delaware law, directors selling a company are obliged to seek the best price reasonably available to shareholders. See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d, 173, 184 (Del. 1986) (once a board decides to sell the company, its duty changes from preserving the company as a corporate entity ("defend[ing] the corporate bastion") to maximizing the company's value at a sale for the stockholders' benefit). See also *In re Lukens, Inc. S'holders Litig.*, 757 A.2d 720, 731 (Del. Ch. 1999). Aff'd sub nom, *Walker v. Lukens*, 757 A.2d 1278 (Del. 2000), citing *Paramount Communications, Inc. v. QVC Network, Inc.,* Del. Supr., 637 A.2d 34, 48 (1994) (in conducting a sale of the company, a director's duty is to seek out "the best value reasonably available to the stockholders.")

[110] Martin Lipton, "The New Paradigm," response to Lenore Palladino, "The American Corporation is in Crisis—Let's Rethink It," *Boston Review* (Oct. 1, 2019),), https://www.bostonreview.net/forum_response/martin-lipton-new-paradigm/, ("The fiduciary duty of the board is to promote the value of the corporation. In fulfilling that duty, directors must exercise their business judgment in considering and reconciling the interests of various stakeholders—including shareholders, employees, customers, suppliers, the environment and communities—and the attendant risks and opportunities for the corporation. The board's ability to consider other stakeholder interests is not only

discussed earlier illustrates the point. The challenge for beneficial stakeholderism is not whether the law permits corporate leaders to consider the interests of other stakeholders—it does—but how much corporate leaders can actually invest in addressing those interests given the legal, economic, competitive, and financial markets context in which they operate.

Under the law of Delaware, considered the "gold standard" for corporate law in the United States, investments in other stakeholders must, first of all, have a rational relationship to advancing the interests of the corporation and its shareholders.[111] Commentators often ignore or brush off this limitation, noting that courts are reluctant to second-guess business decisions taken by boards.[112] For conscientious corporate leaders, however, the requirement of a rational relationship to the corporation's interests is an important benchmark. If a proposed investment in other stakeholders does not advance the interests of the corporation, then it must be justified on some other basis. As discussed earlier, one possibility is that it is required or allowed as a matter of law or ethics.[113] Another possibility is that it is permitted as a charitable contribution.[114] If the investment in other stakeholders cannot be justified in one of these ways, then it is (legally) a waste of corporate assets and grounds for legal action against the company's directors.[115] In other words, corporate leaders' discretion to invest in other

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uncontroversial, it is a matter of basic common sense and a fundamental component of both risk management and strategic planning.")

[111] See, e.g., Leo E. Strine, Jr., *The Dangers of Denial: The Need for a Clear-Eyed Understanding of the Power and Accountability Structure Established by the Delaware General Corporation Law*, 50 *Wake Forest L. Rev*. 761, 768 (2015). Brea Hinricks, "Does (and Should) Delaware Law Allow 'Long-Term Stakeholder Governance'?" Colum. L. Sch.: Millstein Center Blog (June 26, 2019), https://blogs.cuit.columbia.edu/millsteincenter/2019/06/26/does-and-should-delaware-law-allow-long-term-stakeholder-governance/

[112] Under the business judgment rule, a court will not second-guess a board's business decisions so long as (1) the directors had no conflicting interests and (2) the decision was made in good faith, on an informed basis, and in the honest belief that the action taken was in the best interests of the company. See, e.g., *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34 (Del. Ch. 2010) (quoting *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1373 (Del. 1995) (quoting *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984)). Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?* 99 TEXAS L. REV. 1309, 1325 (2021) ("[e]ven if the Delaware case law is properly understood as conveying a strong commitment to shareholder primacy in the takeover context, we question its relevance to the day-to-day operational decisions.

[113] See above at page XX and note YY. American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations* (St Paul, MN: American Law Institute Publishers, 1994), §2.01(a) and (b), p. 53 ((a) "[A] corporation…should have as its objective the conduct of business activities with a view to enhancing corporate profit and shareholder gain. (b) Even if corporate profit and shareholder gain are not thereby enhanced, the corporation…(1) Is obliged… to act within the boundaries set by law; (2) May take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business; and (3) May devote a reasonable amount of resources to public welfare, humanitarian, educational, and philanthropic purposes.") On the scope of corporate leaders' discretion to sacrifice profits for the public interest, see Einer Elhauge, "Sacrificing Corporate Profits in the Public Interest," Vol. 80, No. 3, *N.Y.U. Law Rev*. 733 (2005).

[114] In most U.S. states, companies are permitted to make charitable contributions, even if they are unlikely to benefit the company, so long as the amount is reasonable—often determined by reference to industry norms or tax deductibility. John A. Pearce II, "The Rights of Shareholders in Authorizing Corporate Philanthropy," Vol. 60, No. 2, *Vill. L. Rev*. 251 (2015). Available at: https://digitalcommons.law.villanova.edu/vlr/vol60/iss2/1

[115] The law has defined corporate waste as a transaction 'for consideration so disproportionately small as to lie beyond the range at which any reasonable person might be willing to trade…an act equivalent to [a] 'gift' or 'spoliation' of corporate assets." For a history of how the doctrine of corporate waste has been understood, including

stakeholders is not unlimited. In the eyes of the law, there is such a thing as excessive corporate generosity. As responsible stewards of the corporation's assets, corporate leaders will want to stay within the bounds of legal acceptability even if the risk of liability for exceeding them is minimal.

The more pressing issue for most corporate leaders is not what the law allows but what is realistic given the company's economic and competitive situation. As a practical matter, even stakeholder interests that are directly related to the business can be satisfied only up to a point. Customers, for instance, almost always want better quality, better service, and lower prices, but companies' ability to satisfy those interests is not infinite. Investing more in customers typically means investing less in something else. And, whether organized as a traditional corporation or a benefit corporation, a company can undermine its own viability as a going concern if its generosity to customers (or any other stakeholder) results in too many loss-making transactions. How much corporate leaders can invest in any one stakeholder depends on many factors—the company's strategy, the expectations of other stakeholders, what resources are available, what competitors are doing, how the industry is changing, and so on. Even for fast-growing companies in high-growth industries, delivering on a multi-stakeholder strategy can be difficult. For distressed companies and those in low-growth or declining industries, it is even more so.

The so-called *Revlon* rule poses a particular challenge for traditional Delaware corporations wishing to pursue a multi-stakeholder strategy. This rule concerns the legal duties of directors when selling the company. It says, roughly, that if the board decides to sell, it is obliged to seek the best value reasonably available to shareholders.[116] The rule's significance for other stakeholders can be seen by considering the hypothetical case of a board contemplating offers from two potential buyers.[117] One plans to keep the company's existing facilities operational, retain its workforce, and maintain its strong environmental record. This buyer's offer represents a 35 percent premium to the company's highest stock price over the previous three years. The other buyer plans to close multiple facilities and move production to low-cost countries with

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recent cases where it has been used to challenge excessive executive compensation, see Harwell Wells, "The Life (and Death?) of Corporate Waste," 74 *Wash. & Lee L. Rev.* 1239 (2017). Available at: https://scholarlycommons.law.wlu.edu/wlulr/vol74/iss2/23

[116] The rule is named for the case in which it was first announced. See *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d, 173, 184 (Del. 1986) (once a board decides to sell the company, its duty changes from preserving the company as a corporate entity ("defend[ing] the corporate bastion") to maximizing the company's value at a sale for the stockholders' benefit.) See also *In re Lukens, Inc. S'holders Litig*., 757 A.2d 720, 731 (Del. Ch. 1999). Aff'd sub nom, *Walker v. Lukens*, 757 A.2d 1278 (Del. 2000), citing *Paramount Communications, Inc. v. QVC Network, Inc.*, Del. Supr., 637 A.2d 34, 48 (1994) (in conducting a sale of the company, a director's duty is to seek out "the best value reasonably available to the stockholders.")

[117] This case is based on a hypothetical developed by former Chief Justice of the Delaware Supreme Court Leo E. Strine, Jr. See Leo E. Strine, Jr., "The Social Responsibility of Boards of Directors and Stockholders in Change of Control Transactions: Is there any 'There' There?" *So. California Law Review*, Vol. 75, 1169, at 1177-1187 (2002), https://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.27005.02.pdf.

weak environmental and labor laws. This buyer is offering a price that represents a 40 percent premium over the previous three-year high. On the face of it, *Revlon* would require the board to choose the offer with the highest pay-off for shareholders regardless of its impact on other stakeholders.[118]

Technically, *Revlon* applies only when a company is being sold, but its effects flow back to decision- making long before a sale is even contemplated. Even if the law gives directors broad discretion to consider other stakeholders and take the long-term view outside the context of a sale, that discretion is tempered by directors' knowledge that their decisions are scrutinized and evaluated by watchful shareholders on a daily basis. Directors are well aware that the market value of the company is determined by the views of shareholders who buy and sell its shares every day and who have ultimate say over the company's direction through their power to elect directors. If shareholders disagree with how resources are being allocated or have a short-term focus, they may sell their shares. If a sufficient number of them do so, the company's stock price will fall. If the drop is severe or prolonged, the company may become the target of a proxy fight to replace directors or a takeover bid by an acquirer seeking to buy the company at a premium to its depressed stock price and put in place a board that will run the company in a way that is more to shareholders' liking. While the board may have good reasons to believe that its multi-stakeholder strategy is best for the company over the long term, shareholders may disagree or be concerned more with the short term. Pressure to sell the company may become overwhelming. At that point, if the board decides to sell, it becomes subject to *Revlon*. If the board decides not to sell, it may be voted out of office. Even if corporate leaders believe that investing more in other stakeholders is warranted, the prospect of such an outcome provides a strong disincentive to doing so if it would reduce short-term returns or otherwise fuel shareholder unrest.

As this scenario suggests, corporate leaders' ability to invest in other stakeholders depends ultimately on shareholders' willingness to support those investments. It is extremely difficult to pursue a robust multi-stakeholder strategy if shareholders are unhappy with the strategy or dissatisfied with the returns they are receiving. Whatever decision-making discretion the legal system gives corporate leaders, their decisions are constrained by the preferences of shareholders who, as noted, have ultimate power over the company's direction through their

[118] Some states have so-called "constituency statutes" that either allow or require the board to take into account the interests of other constituencies in considering a takeover bid, but recent research has shown that deals with protections for other stakeholders are rare. See Lucian A. Bebchuk, Kobi Kastiel & Roberto Tallarita, "For Whom Corporate Leaders Bargain," *So. California Law Review*, 2021, Vol. 94, No. 6, pp. 1467-1560. See also Julian Velasco, "The Fundamental Rights of the Shareholder," 40 *U.C. Davis Law Rev*. 407, 463–64 (attributing these statutes' ineffectiveness to their permissive nature—i.e., they permit but do not require boards to consider the interests of other stakeholders—and to the absence of any enforcement mechanism).

rights to buy and sell shares, elect directors, vote on major transactions, and challenge directors in court.

Large sample research is lacking, but the experience of companies that have tried to pursue multi-stakeholder strategies suggests that shareholders are supportive so long as investments in other stakeholders do not reduce or compromise shareholders' own returns. There is little, if any, evidence that significant numbers of public market shareholders are willing to forgo meaningful returns for the sake of other stakeholders' well-being.[119] In 2015, when Walmart announced the expected hit to profits it would take for its decision to increase the floor for hourly wages to $9, from the federal minimum of $7.25 that some workers were then earning, the stock price dropped by 10 percent.[120] And when PwC surveyed global investors in 2021, 49 percent said they would be hesitant to forgo any returns for the sake of environmental, social, or governance goals, and only 19 percent expressed willingness to forgo more than one percentage point.[121] This reality perhaps explains why PwC's 2021 survey of U.S. corporate directors found that only 21 percent very much agreed that boards should prioritize a broader group of stakeholders (other than just shareholders).[122] Another recent PwC survey found that only 13 percent of directors strongly agreed that climate change should be a priority even if it affected short-term financial performance.[123]

[119] For recent research related to this topic, see e.g., Malcolm Baker, Mark L. Egan, and Suproteem K. Sarkar, "How Do Investors Value ESG?,"NBER Working Paper No. 30708, December 2022, http://www.nber.org/papers/w30708 ("Investors, on average, have been willing to pay an additional 20 basis points to invest in funds with an ESG mandate." (p. 1); also noting that the study captures the actual trade-offs ESG investors are making, and "not the tradeoffs they necessarily intended to make." (p. 15)). See also Harrison G. Hong and Edward P. Shore, "Corporate Social Responsibility," (November 12, 2022). *Annual Review of Financial Economics*, Forthcoming, https://ssrn.com/abstract=4267476 (as revised June 29, 2023) (analyzing finance studies suggesting that some shareholders may be willing to trade off returns for non-pecuniary concerns). For research on investors in "impact funds," a subset of venture capital and equity growth funds that explicitly seek the dual objective of generating a positive social or environmental impact alongside of financial returns, see Brad M. Barber, Adair Morse, and Ayako Yasuda, "Impact investing," *Journal of Financial Economics* 139 (2021) 162–185 (finding that investors in impact funds may be willing to accept internal rates of returns that are 2.5 to 3.7 percentage points lower than investors in traditional VC funds).

[120] Andrew Edgecliffe-Johnson, "How Walmart convinced critics it can sell more stuff and save the world," *Financial Times,* October 13, 2022, https://www.ft.com/content/0975d1e3-d95f-4b77-8d58-5d95a751f31a.

[121] As reported in James Chalmers, Emma Cox, and Nadja Picard, "The economic realities of ESG," *strategy+business* (PwC), October 28, 2021, https://www.pwc.com/gx/en/services/audit-assurance/corporate-reporting/esg-investor-survey.html (citing PwC's 2021 Global Investor Survey of 325 global investors, the majority of whom described themselves as active asset managers investing for the long term and 80 percent of whom said ESG was an important factor in their investment decision-making).

[122] PwC, 2021 Annual Corporate Directors Survey, October 2021. Survey responses came from 851 directors of U.S. public companies, 76 percent of which had revenues greater than $1 billion. The survey found that another 38 percent of respondents somewhat agreed that companies should prioritize a broader group of stakeholders.

[123] PwC, 2022 Annual Corporate Directors Survey, October 2022. Survey responses came from 704 directors of U.S. public companies, 72 percent of which had revenues greater than $1 billion. The survey found that another 37 percent of respondents somewhat agreed that climate change should be a priority even if it affected short-term financial performance.

Commentators sometimes point to the rise in ESG (environmental, social, and governance) investing as evidence of shareholder support for beneficial stakeholderism. In the U.S., so-called "sustainable assets" stood at $8.4 trillion in 2022, up from $639 billion in 1995.[124] Globally, the figure was said to be $35.3 trillion in 2020, nearly double what it was in 2014.[125] The increase is noteworthy but it says little, if anything, about investors' willingness to trade off returns for social and environmental benefits. Indeed, research suggests that investors in ESG funds on average expect them to outperform the market.[126] The popularity of ESG investing tells us that many investors do care about social and environmental impacts – if taking those into account increases or, at least, does not compromise financial returns.

The limits of benefit corporation status

Compared to traditional corporations, benefit corporations in theory have more leeway to invest in other stakeholders since by design they are not subject to the *Revlon* rule. As noted earlier, directors of benefit corporations are required by law to consider (or balance) the interests of all stakeholders when making decisions even when selling the company. Returning to the hypothetical case about selling the company discussed above, the board of a benefit corporation could presumably accept either offer—the one that is better for shareholders or the one that spreads the benefit among multiple stakeholders—without fear of legal repercussions from shareholders. Despite this legal difference at the time of sale, it is far from clear that shareholders are willing to accept lower returns from publicly-traded benefit corporations under normal operating circumstances. On the contrary, it appears from the few available examples that publicly-traded benefit corporations are subject to the same capital markets

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[124] US SIF Foundation, "2022 Report on US Sustainable Investing Trends," (Executive Summary). The 2022 figures reflect a change in SIF's methodology for measuring ESG investment dollars compared to its 2020 report which gave the figure as $17.1 trillion. See the US SIF Foundation's 2020 "Report on US Sustainable and Impact Investing Trends," (Executive Summary). For the 1995 figure of $639 billion in total, see its 2010 "Report on Socially Responsible Investing Trends in the United States" (Executive Summary). SIF, formerly known as the Social Investment Forum," defines "sustainable assets" as assets held by investors who incorporate ESG criteria, promote ESG advocacy through, for example, shareholder proposals, or do both. According to SIF, US sustainable assets grew at a compound annual rate of 19 percent between 2010 and 2020 based on the figures reported in those years.
[125] Global Sustainable Investment Alliance, *Global Sustainable Investment Review*, 2016 and 2020 editions. The review defines "sustainable investment" as investment approaches that consider environmental, social, and governance (ESG) factors in portfolio selection and management, and regards the term "sustainable investment" to be interchangeable with "responsible investment" and "socially responsible investment." The review does not differentiate between funds that consider ESG factors for purposes choosing investments that will maximize returns to shareholders and those that use ESG factors for purposes of choosing investments that meet certain social or ethical criteria.
[126] See Stefano Giglio, Matteo Maggiori, Johannes Stroebel, Zhenhao Tan, Stephen Utkus, and Xiao XuGiglio, "Four Facts About ESG Beliefs and Investor Portfolios," NBER Working Paper No. 31114, April 2023, p. 5. https://www.nber.org/papers/w31114) (Analyzing ten waves of a survey administered by Vanguard to a random sample of U.S.-based brokerage and retirement fund clients between June 2021 and December 2022, the authors found that "Among the small fraction of individuals actually investing in ESG funds, the expected excess returns of those investments are positive.")

pressures as traditional corporations.[127] This should not be surprising considering that the benefit corporation structure does not alter shareholders' traditional powers to buy and sell their shares freely, elect directors, vote on major transactions, and bring suit against directors.

Consider the experience of French food and beverage company Danone. Another company with a long-standing commitment to a stakeholder approach, Danone became France's first publicly-traded "*société à mission*" [purpose-driven company] in June 2020 when 99 percent of its shareholders voted in favor of changing the company's articles of association to adopt the new legal status. The French equivalent of the benefit corporation, the "*société à mission*" was introduced as a new legal option for corporations under France's 2019 PACTE law.[128] At the time of the shareholder vote, more than thirty Danone entities had earned or were in the process of earning B Corp certifications attesting to their social and environmental performance and their stakeholder *bona fides*. In arguing for the proposed change in legal form, Danone's board expressed its members' conviction that the company's commitment to all its stakeholders would create more value for all, including shareholders.[129]

Within a few months of the vote, shareholders' dissatisfaction with Danone's financial performance, which had been simmering for some time, bubbled to the surface. Disappointed by the company's sluggish revenue growth, unimpressive margins, and stock price underperformance relative to peers, shareholders began calling for the board to replace chairman and CEO Emmanuel Faber. The head of activist fund Bluebell Capital Partners expressed support for the company's new legal status but argued that, under Faber's leadership, Danone had not managed "to strike the right balance between shareholder value creation and sustainability."[130] Investor pressure continued to mount and within another few months, the board had split the roles of chairman and CEO, and Faber had stepped down.

Whether the Danone story points to the inherent difficulty of pursuing a multi-stakeholder agenda, to a flaw in Danone's particular multi-stakeholder strategy, or simply to a failure to execute is hard to say. The company's critics blamed its poor operational record and questionable resource allocations, citing underinvestment in innovation, product development,

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[127] As of May 2023, the United States had an estimated 13 publicly-traded public benefit corporations (out of some 4,572 publicly-traded corporations in total). (List on file with the author.)
[128] *Plan d'Action pour la Croissance et la Transformation des Entreprises* (Action Plan for Business Growth and Transformation). https://www.gouvernement.fr/en/pacte-the-action-plan-for-business-growth-and-transformation, accessed November 8, 2021. The requirements to become a "société à mission" are found in Article L. 210-10 of the French Commercial Code.
[129] Danone, "Danone to pioneer French 'Entreprise à Mission model to progress stakeholder value creation," May 20, 2020. https://www.globenewswire.com/news-release/2020/05/20/2036111/0/en/Danone-to-pioneer-French-Entreprise-%C3%A0-Mission-model-to-progress-stakeholder-value-creation.html
[130] Leila Abboud,"Activist fund Bluebell Capital takes aim at Danone," *Financial Times*, January 18, 2021, https://www.ft.com/content/2df158fb-357a-499a-b51c-025b4f1d5c97

and product support, in particular.[131] Whatever the final diagnosis, Danone's experience shows that a company's legal status as a benefit corporation (or *société à mission*) does not shield it from capital markets pressures.[132] Indeed, some investors in publicly traded benefit corporations have stated their belief that an investment in the stock of a benefit corporation is no different from an investment in the stock of a non-benefit corporation.[133] Benefit corporation or traditional corporation, the evidence suggests that shareholders are willing to support a robust multi-stakeholder strategy only if they are receiving what they regard as an acceptable return, by whatever measure and time frame they choose to apply. In this context, it is extremely difficult for corporate leaders to adopt any multi-stakeholder strategy that would shift value from shareholders to other constituencies as many proponents of beneficial stakeholderism would advocate.

To be sure, some shareholders say they are sympathetic to strategies that invest heavily in other stakeholders, and may be willing to share more of the company's surplus for any number of reasons. Perhaps they think it will generate more value over the long run, lead to a better political environment for business, make for a less divided society, or is simply a more equitable way to run a company. But shareholder solicitude for other stakeholders cannot be presumed. Shareholders have widely varying goals, time frames, and preferences. So long as shares are freely traded and so long as shareholders have their other traditional rights and powers—to buy and sell their shares, elect directors, vote on major transactions, and bring suit against the board—the company's strategy and direction will be heavily influenced by what the majority or most powerful shareholders want. Judging by today's markets, most shareholders want companies to invest in other stakeholders so long as it does not compromise the returns they would otherwise receive.

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[131] Leila Abboud,"Activist fund Bluebell Capital takes aim at Danone," *Financial Times*, January 18, 2021, https://www.ft.com/content/2df158fb-357a-499a-b51c-025b4f1d5c97. See also Letter from Artisan Global Value Strategy and Artisan International Value Strategy to Gilles Schnepp, Lead Independent Board Member Elect at Danone, Inc. (February 11, 2021), https://www.prnewswire.com/news-releases/letter-from-artisan-global-value-strategy-and-artisan-international-value-strategy-to-gilles-schnepp-lead-independent-board-member-elect-at-danone-inc-301226405.html

[132] Etsy, the online seller of vintage and hand-crafted items, is another frequently cited example. Etsy went public as a certified B Corp, but after weak results for several quarters was targeted by activists calling for the company's sale. Under pressure from the activist group and other investors who had begun buying shares, the board replaced the CEO and the company made its first big lay-offs. The team overseeing the company's social and environmental programs was subsequently disbanded, and the company gave up its B Corp certification. These facts are taken from David Gelles, "Inside the Revolution at Etsy," *New York Times*, November 25, 2017, https://nyti.ms/2i4GjKE

[133] See, e.g., Novus Capital Corporation, Form S-4/A (filed December 1, 2020), https://www.sec.gov/Archives/edgar/data/1807707/000110465920131168/tm2032410-7_s4a.htm in which special purpose acquisition company (SPAC) Novus Capital Corporation discusses its business combination with AppHarvest, a benefit corporation: "Novus does not believe that an investment in the stock of a public benefit corporation differs materially from an investment in a corporation that is not designated as a public benefit corporation. Novus believes that AppHarvest's ongoing efforts to achieve its public benefit goals will not materially affect the financial interests of the Combined Company's stockholders."

In summary, beneficial stakeholderism is promising in principle, but corporate leaders embracing it face a challenging path. By comparison with instrumental and classic stakeholderism, beneficial stakeholderism envisions a more significant shift (away from traditional shareholder value maximization) in how companies deploy resources and distribute the value they create, with a greater share of both going to non-shareholder stakeholders. Yet, as we have seen, there are real constraints on how generous companies can be to their non-shareholder stakeholders. Given the structures and norms that shape how capital markets function, it is quite difficult for corporate leaders to invest in advancing the well-being of other stakeholders unless the company is meeting or exceeding the expectations of shareholders. It is more difficult still if investing in other stakeholders would mean reducing shareholder returns. Recall that only 13 percent of corporate directors responding to a recent survey by PwC agreed strongly that climate goals should be a priority even if it affected short-term financial performance.[134] While there are no doubt some prosocial shareholders who would gladly trade off a measure of return for a more equitable society or a greener planet, they appear to be few in number.

In view of this reality, there is reason to be skeptical that beneficial stakeholderism can deliver the societal benefits its proponents seek. Certainly some headway can be made. The successful examples of beneficial stakeholderism discussed earlier show what companies can accomplish—and how they can benefit—when they take the needs of stakeholders seriously and apply their talents and resources to addressing them. As these examples indicate, and as discussed earlier in connection with instrumental stakeholderism, investing in other stakeholders can be good for shareholders as well. But it is doubtful that a collective corporate turn to beneficial stakeholderism alone can adequately address large-scale problems such as economic inequality, climate change, or the disintegrating social and political fabric so long as most shareholders are unwilling to invest in other stakeholders beyond what is needed to maximize their own returns and so long as shareholders have ultimate say over how companies are run.

This limitation perhaps explains why some stakeholder advocates have proposed an even more robust form of stakeholderism—one that gives non-shareholder stakeholders formal powers in the governance process.

[134] See above at note XX. PwC, 2022 Annual Corporate Directors Survey, October 2022. Survey responses came from 704 directors of U.S. public companies, 72 percent of which had revenues greater than $1 billion.

4. Structural Stakeholderism: Increasing stakeholder power

The three versions of stakeholderism discussed above all focus on the first pillar of shareholder primacy—the idea that maximizing value for shareholders is (or should be) a corporation's principal objective. They all call for refinements or changes in how that objective is understood and implemented, and they are similar in leaving the traditional governance structures and processes that define the balance of power between shareholders and other stakeholders largely intact. That is to say, they all accept the second pillar of shareholder primacy: the idea that shareholders are (or should be) the only constituency with a formal voice in corporate governance. A fourth version of stakeholder capitalism challenges that pillar. This fourth version, which I term "structural stakeholderism," calls for giving non-shareholder stakeholders formal voting or other powers in the governance process. In essence, advocates of this view seek to hardwire the interests of other stakeholder groups into the process rather than relying on the good offices of corporate directors and business leaders to take them into account. In particular, many in this camp say that non-shareholder stakeholders should have a legally defined role in electing corporate directors or be formally represented on corporate boards.

Where this idea has been widely implemented, most notably in Europe, employees are the stakeholder group (other than shareholders) most typically given board representation. Germany's two-tiered board system is a well-known example. By law and tradition dating to the country's post-World War II co-determination movement—encouraged incidentally by the U.S. government—one-third to one-half of the directors on the supervisory boards of German companies are elected by employees and the rest, by shareholders.[135] In a different arrangement, since 2014, French law has mandated that the boards of French companies have one or two directors elected by employees, the number depending on the size of the board.[136] Other approaches to employee participation can be found in other European countries. Although it has been rare in the U.S., employee representation on boards is not unheard of. A 1919 Massachusetts law (still in effect) permitted manufacturing companies to adopt bylaws empowering employees to nominate and elect one or more directors,[137] and unions have on

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[135] On co-determination in Germany, see Grant M. Hayden and Matthew T. Bodie, "Codetermination in Theory and Practice," *Florida Law Review*, Vol. 73, 2021, p. 321 at p 332. Discussing the U.S., Hayden and Bodie note (p. 325) that a 1919 Massachusetts law expressly permits corporations to have employee representatives on their board.

[136] France's law requires companies to write employee representation into their articles of association. In July 2022, the French government issued a report on the economic and managerial effects of adding employee directors to the boards of French companies. See "Rapport remis par le gouvernement au parlement: Evaluant les effets economiques et manageriaux de la presence d'administrateurs representant les salaries au sein des conseils d'administration ou de surveillance des societes" ("*Report submitted by the government in parliament: Assessing the economic and managerial effects of the presence of directors representing the employees on boards of directors or supervision of companies*"), July 18, 2022, https://www.tresor.economie.gouv.fr/Articles/5511a03e-3897-4dd8-b795-a2c1926617ef/files/115f4181-c769-4640-bcf5-633336d7229b

[137] See Ewan McGaughey, "Democracy in America at Work: The History of Labor's Vote in Corporate Governance," *Seattle University Law Review*, Vol. 42 (2019), 697-753, at 718. See Massachusetts General Laws, Part 1, Title XXII, Ch. 156, §23 (Manufacturing corporations; election of directors by employees)). See also, Grant M. Hayden and Matthew

occasion secured a seat on the company's board.[138] In an unusual arrangement for a U.S. company today, the board of Delta Air Lines includes a pilot nominated by the governing body of its pilot association.[139]

The appointment of directors to represent the public interest has also been proposed from time to time. The idea gained currency among law and business academics in the U.S. in the 1970s, following a spate of corporate failures and scandals.[140] It was actually tried on the boards of Irish banks that received government bailouts during the global financial crisis of 2008.[141] The Irish government mandated that each of Ireland's six leading domestic banks appoint at least one, but no more than two, non-executive public interest directors from a panel approved by the country's Minister for Finance.[142] Other commentators have proposed that customers, communities, and taxpayers or other stakeholders should have board representation.[143] For

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T. Bodie, "Codetermination in Theory and Practice," *Florida Law Review*, Vol. 73 (2021), at 325; Phillip I. Blumberg, "Reflections on Proposals for Corporate Reform through Change in the Composition of the Board of Directors: Special Interest Or Public Directors," 53 *B.U. L. REV*. 547 (1973), at 553.

[138] See Grant M. Hayden and Matthew T. Bodie, "Codetermination in Theory and Practice," *Florida Law Review*, Vol. 73, 2021, p. 325-328 (giving the example of a United Auto Workers representative on Chrysler's board in 1980, and a union member on Pan American Airways' board in 1982; also citing instances of employee board representation as a result of stock ownership, for example, through an Employee Stock Ownership Plan (ESOP)).

[139] According to the Delta Airlines, Inc., 2022 proxy statement: "Delta, the Air Line Pilots Association, International (ALPA), the collective bargaining representative for Delta pilots, and the Delta Master Executive Council, the governing body of the Delta unit of ALPA (Delta MEC), have an agreement whereby Delta agrees (1) to cause the election to the Board of Directors of a Delta pilot designated by the Delta MEC who is not a member or officer of the Delta MEC or an officer of ALPA (Pilot Nominee)…"
https://www.sec.gov/Archives/edgar/data/27904/000130817922000308/ldal2022_def14a.htm

[140] See, e.g., Phillip I. Blumberg, "Reflections on Proposals for Corporate Reform through Change in the Composition of the Board of Directors: Special Interest Or Public Directors," 53 *B.U. L. REV*. 547 (1973); Christopher D. Stone, *Where the Law Ends: The Social Control of Corporate Behavior* (New York, Harper & Row, 1975); Alfred F. Conard, "Reflections on Public Interest Directors," *Michigan Law Review*, Vol. 75, No. 5/6, Faculty Essays in Honor of the 75th Anniversary of the *Michigan Law Review* (April-May, 1977), pp. 941-961; Thomas M. Jones and Leonard D. Goldberg, "Governing the Large Corporation: More Arguments for Public Directors," *The Academy of Management Review*, Vol. 7, No. 4 (Oct. 1982), pp. 603-611.

[141] Blanaid J. Clarke and Gail Elizabeth Henderson, "Are Public Interest Directors a Good Idea? Lessons from the Irish Banking Crisis," UCD Working Papers in Law, Criminology & Socio-Legal Studies, Research Paper No. 11/2015.

[142] The public interest directors were not required to stand for election at the respective banks' annual shareholder meetings. See Blanaid J. Clarke and Gail Elizabeth Henderson, "Are Public Interest Directors a Good Idea? Lessons from the Irish Banking Crisis," UCD Working Papers in Law, Criminology & Socio-Legal Studies, Research Paper No. 11/2015, pp. 18-19.

[143] See, e.g., William Lazonick, "Investing in Innovation: Confronting Predatory Value Extraction in the U.S. Corporation," theAIRnet (The Academic-Industry Research Network) Working Paper #22-09/01, September 26, 2022, pp. 41-44 (arguing that workers and taxpayers should be represented on boards); Lenore Palladino, "Economic Democracy at Work: Why (and How) Workers Should be Represented on US Corporate Boards," *Journal of Law and Political Economy*, 1(3), (2021); Lenore Palladino, "The Economic Argument for Stakeholder Corporations," Roosevelt Institute Working Paper, June 2019, at p. 18 (suggesting that different stakeholders need not have equal roles in governance and that "[f]urther research must be devoted to analyzing the specific role of customers and community in stakeholder corporations.") https://rooseveltinstitute.org/wp-content/uploads/2020/07/RI_Economic-Argument-for-Stakeholder-Corporations_Working-Paper_201906.pdf; See also, Abram Chayes, "The Modern Corporation and the Rule of Law," Ch. 2 in E. Mason (ed.), *The Corporation in Modern Society* (1959), pp. 25-45 at 40-41 (discussing a regularized role in corporate governance for all those "having a relation of sufficient intimacy with the

some, the term "stakeholder capitalism" itself implies that corporate boards should comprise representatives of different stakeholder groups.[144]

As noted, employee or other stakeholder representation on boards has been extremely rare in the U.S., but the idea has recently gained attention as a result of several proposed bills in the U.S. Senate. Put forth by former presidential candidates Senators Elizabeth Warren and Bernie Sanders, as well as by Senator Tammy Baldwin, these bills would all give employees the right to elect a certain portion of the company's directors. Warren's proposal would require companies with more than $1 billion in annual revenues to obtain a federal charter obligating directors to consider the interests of all stakeholders and giving employees the right to select at least 40 percent of the board.[145] Baldwin's bill would require all listed companies to allow employees to elect one third of their company's board.[146] Sanders's proposal would cover all publicly-traded companies as well as privately-held companies with at least $100 million in revenues. Like Warren's proposal, Sanders's bill would require covered companies to obtain a federal charter committing them to take the interests of all stakeholders into account, but his proposal would give employees the right to elect at least 45 percent of the board.[147]

The past few years have also seen the emergence of shareholder proposals on adding non-management employees to the board at several large U.S. companies. Between 2020 and 2023, 15 such proposals were voted on at 13 different companies including Alphabet, AT&T, FedEx, GE, Microsoft, Starbucks, Walmart, and others.[148] These proposals vary, with about half asking that non-management employees be included on the list of candidates from which director nominees are chosen, and others asking the board to nominate an employee representative director or to prepare a report to shareholders on the opportunities for employee representation on the board. Most of the proposals to add an employee representative envision the individual as being nominated by the board's nominating and governance committee and elected by shareholders, even if initially recommended by employees. However, a few suggest that direct nomination by employees could be written into the company's proxy access policy.[149]

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corporation or subject to its powers in a sufficiently specialized way"); Robert Dahl, *After the Revolution: Authority in a Good Society Revised Edition* (New Haven: Yale University Press, 1990) at p. 102 (suggesting a role in governance for those who make vital contributions to the corporation).

[144] Silvia Ayuso and Antonio Argandoña, "Responsible Corporate Governance: Towards a Stakeholder Board of Directors?" (February 25, 2009). IESE Business School Working Paper No. 701. https://ssrn.com/abstract=1349090.

[145] S. 3348. Accountable Capitalism Act, 115th Congress (2017-2018).

[146] S. 915. Reward Work Act, 116th Congress (2019-2020).

[147] Friends of Bernie Sanders, "Issues: Corporate Accountability and Democracy." https://berniesanders.com/issues/corporate-accountability-and-democracy/.

[148] The 15 proposals voted on by shareholders at large U.S. companies between 2020 and 2023 also included proposals at Amazon (3 proposals), Automatic Data Processing, DuPont, Gilead Sciences, Procter & Gamble, and The Walt Disney Co. Source: ProxyMonitor.org, database of shareholder proposals at the 250 largest U.S. public cos. ranked by revenue.

[149] An example is the proposal put forth by NorthStar Asset Management at Automatic Data Processing (ADP) in 2020 asking the board to prepare a report on opportunities for including non-management employees on the board. The proposal asks that the board prepare a report addressing, among other things, "procedures through which non-

Rationales for structural stakeholderism

Proponents of stakeholder representation on boards have offered a range of supporting arguments and rationales. Some appeal to the potential benefits for shareholders of bringing stakeholder concerns directly into the boardroom. The shareholder proposal filed at AT&T in 2020 by an undisclosed sponsor, for example, states that having an employee representative on the board would "add knowledge and insight on issues critical to the success of the Company, beyond that currently present on the Board, and may result in more informed decision making."[150] The proposal calls out corporate culture, in particular, as an area for which an employee perspective would be especially useful, noting the substantial culture-related risks facing the company. Similarly, the proposal filed by NorthStar Asset Management at ADP in 2020 highlighted the potential benefit of "a direct line of communication between employees and the board," and expressed NorthStar's belief that employee representation on the board would enhance long-term value creation.[151] Other proponents of employee representation claim other potential benefits for the company and its shareholders—getting employee buy-in for difficult decisions, increased trust between the board and employees, more new ideas, and greater accountability for ethical decision making.[152] Notably, members of this group see employee representation as entirely consistent with a corporate objective of maximizing long-term shareholder value, and apparently do not see employee representation as leading to any significant change in how corporate leaders allocate or distribute resources. The proposal filed at AT&T states explicitly that "employees have a sincere interest in the ongoing viability of the company, aligning their interests with those of long-term shareholders."[153]

Other advocates of stakeholder representation are more concerned about giving employees and other stakeholders a voice in governance as a matter of principle. Many in this group challenge the premises on which shareholders' control of governance has been traditionally based. For example, they question the assumption that shareholders should have a monopoly on control because they are the last to get paid in bankruptcy or because they are the constituency most in

management employees could gain nomination to the board, such as allocation of board slots or special board nomination processes for non-management employees, potential for building upon the company's existing proxy access provision, and any needed changes to corporate governance documents to accomplish such changes." https://www.sec.gov/Archives/edgar/data/8670/000120677420002764/adp3788011-def14a.htm#p85

150 AT&T Inc., 2020 Proxy Statement, Schedule 14A https://www.sec.gov/Archives/edgar/data/732717/000119312520070302/d867502ddef14a.htm#toc867502_6

151 Automatic Data Processing, Inc., 2020 Proxy Statement, Schedule 14A, https://www.sec.gov/Archives/edgar/data/8670/000120677420002764/adp3788011-def14a.htm#p85

152 See, e.g., Jon Mertz, "Why You Should Consider Having Employees on Your Board," *The Startup*, December 9, 2019, https://medium.com/swlh/why-you-should-consider-having-employees-on-your-board-6676d957aedf

153 AT&T Inc., 2020 Proxy Statement, Schedule 14A https://www.sec.gov/Archives/edgar/data/732717/000119312520070302/d867502ddef14a.htm#toc867502_6

need of protection, as some economists have argued.[154] According to these arguments, the nature of their investment and their position as residual risk bearers make shareholders, as compared to other stakeholders, the most deserving of control over governance and the most likely to be effective monitors of the company.[155] Critics, however, contend that employees also take on risk when they go to work for a corporation. Not only are employees more invested in the company than many shareholders—think of traders who know little and care less about the companies whose shares they trade—but it is also generally harder for employees to change jobs than for shareholders to change investments. Indeed, most Americans are dependent on their jobs—not their investments—for their income and wealth.[156] Even for the roughly 50 percent of Americans with investments in the stock market, losing a job is far more consequential than a failed investment.[157] By the traditional logic that shareholders' electoral rights are justified by their position as risk bearers, employees and perhaps others such as long-term suppliers and customers should also be entitled to vote on directors and other significant corporate matters.[158]

Still other proponents of stakeholder representation on boards liken corporations to nation states, and corporate governance to political governance. Members of this group say corporate governance should more closely resemble democratic governance.[159] On this view, the corporate "republic" is said to comprise all parties subject to the corporation's powers or substantially affected by its activities.[160] As citizens of the republic, all of these parties—not just

[154] See, e.g., Oliver Williamson, "Corporate Governance," *Yale Law Journal*, Vol. 93: 1197-1230 (1984) (arguing that shareholders are most deserving of protection through corporate governance since other constituencies are protected in other ways).
[155] See, e.g., Michael C. Jensen & William H. Meckling, "Rights and Production Functions: An Application to Labor-Managed Firms and Codetermination," *Journal of Business*, Vol. 52, No. 4 (1979), pp. 469–506, at pp 485-486. (arguing that employees lack the incentives necessary to make them efficient monitors).
[156] Board of Governors of the Federal Reserve System, "Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances," Federal Reserve Bulletin, Vol. 106, No. 5 (September 2020), https://www.federalreserve.gov/publications/files/scf20.pdf.
[157] Board of Governors of the Federal Reserve System, "Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances," Federal Reserve Bulletin, Vol. 106, No. 5 (September 2020), https://www.federalreserve.gov/publications/files/scf20.pdf.
[158] See, e.g., Lenore Palladino, "Economic Democracy at Work: Why (and How) Workers Should be Represented on US Corporate Boards," *Journal of Law and Political Economy*, 1(3), (2021), pp. 373-396, at 374-378 (arguing that "[a]s workers are a key corporate claimant, they should share governing power within American corporations through meaningful representation on corporate boards of directors").
[159] See, generally, e.g., Ewan McGaughey, "Democracy in America at Work: The History of Labor's Vote in Corporate Governance," *Seattle University Law Review*, Vol. 42, pp. 697-753 (2019).
[160] See, e.g., Abram Chayes, "The Modern Corporation and the Rule of Law," Ch. 2 in E. Mason (ed.), *The Corporation in Modern Society* (1959), pp. 25-45 at 40-41 (discussing a regularized role in corporate governance for all those "having a relation of sufficient intimacy with the corporation or subject to its powers in a sufficiently specialized way"). Other conceptions of the "corporate republic" envision shareholders as its only citizens. See, e.g., the use of the term "corporate republic" in Leo E. Strine, Jr., "Who Bleeds When the Wolves Bite?: A Flesh-and-Blood Perspective on Hedge Fund Activism and our Strange Corporate Governance System," 126 *Yale Law Journal* 1870 (2017), pp. 1871-1872. Those who envision shareholders as the only citizens are apt to speak of "shareholder democracy," while those who also include other constituencies as citizens are more apt to speak of "corporate democracy."

shareholders—should have the right to elect their representatives to the corporation's highest decision-making body as well as the right to vote on significant corporate matters. This way of thinking about corporate governance owes much to political theory and especially to John Locke's proposition that legitimate governing power can only be derived from the consent of the governed.[161] This view could hardly be further from that of financial economists who have traditionally seen the right to govern as arising from the ownership of capital and the goal of corporate governance as ensuring providers of capital a return on their investment.[162]

Most advocates for adding stakeholder representatives to boards or extending voting rights beyond shareholders also claim that the more robust involvement of other constituencies will strengthen companies' ability to create long-term value by boosting productivity, enhancing employee engagement, sparking innovation, or other channels. But, for most, these are secondary consequences. The principal goal is to protect the interests of non-shareholder stakeholders and increase the weight given to them in corporate decision making. These advocates of structural stakeholderism are skeptical of directors' willingness and ability to stand up for any interests other than those of shareholders within the current governance structure. They doubt that a shift in how corporate leaders define their objective will be sufficient on its own to bring about the changes in corporate decision making needed to effect a more equitable distribution of value, reduce the economic insecurity experienced by working families, and protect the interests of other stakeholders such as customers, communities, and the environment.

Some challenges for structural stakeholderism

The call to add representatives of employees or other stakeholders to corporate boards may seem like a modest proposal, but it raises fundamental questions about the nature of corporate boards and the duties of directors, as well as about the basis of directors' authority to govern. Under the prevailing legal model, as discussed earlier, the board is by law the governing body of a corporation and its members are fiduciaries for the corporation and its shareholders. In making decisions and setting policy, directors are expected to exercise independent judgment on behalf of the corporation. That typically means considering a wide array of factors and giving due regard to the interests of the company's various stakeholders, but in the end trying to do what's best for the company as a whole while acting ethically and within the law. Director independence is crucial. It is generally thought to require that directors have no conflicts of interest—conflicts that would force them to choose between their personal interest and that of the corporation—and that they make their own decisions rather than follow the

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[161] See Ralph Nader, Mark Green, and Joel Seligman, *Taming the Giant Corporation: How the Largest Corporations Control Our Lives* (New York: W.W. Norton & Company, Inc., 1976), p. 123.
[162] Financial economists typically define corporate governance as "the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment." See, e.g., Andrei Schleifer and Robert Vishny, "A Survey of Corporate Governance," *Journal of Finance*, Vol. 52, No. 2 (1997): 737-783.

dictates of third parties who may wish to influence them.[163] For this reason, most boards have a recurring process for identifying potential conflicts of interest that might arise from directors' relationships with management and key stakeholders such as customers, suppliers, and business advisors.[164]

Although directors are sometimes referred to as shareholders' "representatives"—and indeed, as discussed earlier, directors are elected by shareholders—their role as traditionally defined in law is more akin to that of trustees for the institution than to delegates representing a particular constituency.[165] That is why other shareholders may protest when a hedge fund negotiates a seat on the board for its own nominee or offers additional compensation to that director for achieving its goals.[166] As fiduciaries, directors owe duties of care and loyalty to the corporation as a whole and are obliged to exercise independent judgment on its behalf—not to promote the interests of the particular shareholders who elected them. Nor are directors obliged to follow current shareholders' preferences, though failure to do so may of course cost them their board seat in a shareholder vote.[167]

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[163] In the U.S., director independence is understood as "independence from management," while in some parts of Europe it is understood more broadly. For instance, under France's corporate governance code, "[A]n independent director is understood to be any non-executive director of the corporation or the group who has no particular bonds of interest (significant shareholder, employee, etc.) with them." Accordingly, under France's code, the independence of a director affiliated with a shareholder holding more than 10 percent of the company's capital or voting rights would have to be determined on a case-by-case basis given the existence of a potential conflict of interest. See Afep-Medef Corporate Governance Code of Listed Corporations (December 2022), §§ 10.2, 10.7, pp. 9-10 (English translation). https://www.lagardere.com/wp-content/uploads/2023/01/code_afep_medef_december_2022_en.pdf

[164] In the U.S., New York Stock Exchange (NYSE) and Nasdaq rules detail independence requirements for listed companies; see, e.g., NYSE Listed Company Manual, Section 3 Corporate Responsibility, 303A.00 Corporate Governance Standards, https://nyseguide.srorules.com/listed-company-manual/09013e2c85c00744 and Nasdaq Stock Market LLC Rules, The Qualification, Listing and Delisting of Companies, 5600. Corporate Governance Requirements, https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/Nasdaq%205600%20Series.

[165] Experts on political representation have traditionally distinguished between "delegate" and "trustee" conceptions of representation. "Delegates" are bound to follow the express preferences of their constituents, whereas "trustees" are expected to exercise their own independent judgment (as informed by their constituents). For a discussion of this long-standing debate, see Hanna Fenichel Pitkin's classic, *The Concept of Representation*, Berkeley: University of California Press, 1967.

[166] For example, other shareholders and the board of Dow Chemical took issue when activist fund Third Point proposed to pay a bonus to its director nominees to Dow's board in 2014. For other examples see, Matteo Tonello (The Conference Board, "Activist Hedge Funds, Golden Leashes, and Advance Notice Bylaws," *Harvard Law School Forum on Corporate Governance* (blog), January 7, 2016. https://corpgov.law.harvard.edu/2016/01/07/activist-hedge-funds-golden-leashes-and-advance-notice-bylaws/; and Rakhi Kumar and Ron O'Hanley (State Street Global Advisors), "Protecting the Interests of Long-Term Shareholders In Activist Engagements," *Harvard Law School Forum on Corporate Governance* (blog), October 17, 2016, https://corpgov.law.harvard.edu/2016/10/17/protecting-the-interests-of-long-term-shareholders-in-activist-engagements/.

[167] See *In re Trados Inc. S'holder Litig*., 73 A.3d 17, 38 (Del. Ch. 2013) ("The duty to act for the ultimate benefit of stockholders does not require that directors fulfill the wishes of a particular subset of the stockholder base."), citing *In re Lear Corp. S'holder Litig*., 967 A.2d 640, 655 (Del. Ch. 2008) ("Directors are not thermometers, existing to register the ever-changing sentiments of stockholders….[D]irectors may take good faith actions that they believe will benefit stockholders, even if they realize that the stockholders do not agree with them."); *Paramount Communications Inc. v. Time Inc*., 1989 WL 79880, at 30 (Del. Ch. July 14, 1989) ("The corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares. In fact, directors, not shareholders, are charged with the duty to manage the firm."); *aff'd in pertinent part*, *Time,* 571 A.2d

Under the traditional model, a corporate board is thus a "fiduciary board" rather than a "constituency board." That is, its individual members are each fiduciaries appointed to serve the interests of the institution on whose board they sit, rather than delegates appointed to serve the interests of the constituency they represent.[168] On a fiduciary board, a director's loyalty runs to the institution being governed; on a constituency board, the director's loyalty is to a specific constituency. In practice, these two orientations—to the interests of the institution and to the interests of the constituency—lead to very different mindsets and very different requirements for director effectiveness. For example, it is important for constituency directors to have ongoing communication with their constituency group. If the group is large, the director needs to have systematic ways of gathering and aggregating information about its members' needs, concerns, and preferences. Conversely, the group's members typically expect their representative to provide them with ongoing information about matters of concern. These two orientations can also lead to very different positions on issues presented to the board, depending on the nature and purpose of the institution and the nature and number of constituencies represented.

Few if any of the proposals to add employees or other stakeholders to corporate boards raise this issue explicitly, but many of them seem to envision corporate boards as being—or becoming—constituency boards made up of representatives of different stakeholder groups. Although constituency boards are very appropriate for some organizations, there are reasons to be wary of a constituency model for business corporations. Perhaps the most worrisome is the potential effect on the speed and coherence of board decision making. If directors' principal duty is to serve the interests of the stakeholder group they represent rather than the interests of the company being governed, the prospect of lengthy negotiations and contentious stand-offs quickly rears its head. Decisions about strategy, investments, leadership, acquisitions, disposals, restructuring, and the like often need to be made quickly. In a rapidly changing business environment, taking time to solicit the views of various stakeholder groups and to negotiate a resolution of the differences among them may not be feasible. Moreover, without a shared duty to the company to anchor and focus the negotiations, the odds of a suboptimal result are high.

at 1150; *TW Servs*., 1989 Del Ch. LEXIS 19, 1989 WL 20290, at 8 n. 14 ("While corporate democracy is a pertinent concept, a corporation is not a New England town meeting; directors, not shareholders, have responsibilities to manage the business and affairs of the corporation, subject however to a fiduciary obligation.")

[168] The boards of International Financial Institutions, for example, are categorized as constituency boards. See Stilpon Nestor, "Board Effectiveness in International Financial Institutions: A Comparative Perspective on the Effectiveness Drivers in Constituency Boards," Ch.1 in *Good Governance and Modern International Financial Institutions (AIIB Yearbook of International Law 2018)*, edited by Peter Quayle and Xuan Gao (Leiden; Boston: Brill | Nijhoff, 2019), pp. 3-24. https://doi.org/10.1163/9789004408326_002; https://brill.com/view/book/9789004408326/BP000002.xml

Dealing with conflicting interests and making trade-offs is likely to be even more challenging for a constituency board than a fiduciary board.[169] Instead of a predominantly analytical and deliberative exercise, requiring each director to form a judgment and discuss with other directors what's best for the company, the process is more likely to resemble a negotiation among parties with differing objectives. Since each director's primary duty runs to a particular constituency, each is bound to advance that constituency's interests to the maximum degree possible. A fair worry is that outcomes will be determined more by directors' skill at advocating their constituency's cause than by reasoned judgment about what's good for the company. Given directors' differing duties, psychological and emotional ties, and sense of accountability to the groups they represent, more decisions will likely be made by vote rather than consensus, raising the prospect of more time spent wrangling over procedural rules.

The effect on board dynamics is another concern. When each board member's loyalty is to a particular constituency, it is more difficult to build trust in the boardroom. Directors may be less willing to share information or to take other directors' stated positions at face value. There is greater risk that the board will devolve into factions or cliques, and that critical decisions will be made behind closed doors by representatives of the most powerful constituencies. Instead of informed, open discussions, directors may resort to trading favors, private agreements with other directors, and various other tactics to secure their group's preferred outcome – in the extreme case to the detriment of the enterprise as a whole. To be sure, factions can be a problem and lead to dysfunctionality on fiduciary boards as well. But the risk is heightened when directors lack a common objective and sense of shared responsibility.

Proponents of employee and other stakeholder representation on boards may consider this an overly pessimistic view of how a stakeholder board is likely to work. Perhaps these dangers can be mitigated if the board's members are seen as having a dual responsibility – to their particular constituency as well as to the company as a whole. A dual responsibility, or hybrid, model helps so long as the interests of the constituency and the interests of the company are aligned or, at least, do not conflict. In the case of conflict, however, the dual responsibility model may exacerbate the director's dilemma. Consider, for example, a company in difficult circumstances considering the possibility of cutting the workforce significantly. Even if directors representing employees agree that the cuts are necessary to preserve the company's viability it may be emotionally and politically difficult for them to give their approval. They may feel they are letting their fellow employees down, and may even become the target of public criticism, or worse, by employee groups who believe their interests are not being adequately protected.

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[169] For an interesting analysis of areas in which various stakeholder interests are likely to converge and those in which they are likely to diverge, see, Alfred F. Conard, "Reflections on Public Interest Directors," *Michigan Law Review*, Vol. 75, No. 5/6, Faculty Essays in Honor of the 75th Anniversary of the *Michigan Law Review* (April-May, 1977, pp. 941-961. https://www.jstor.org/stable/1288020

In the two recent examples of stakeholder representation on boards that have been studied—public interest directors on the boards of Ireland's banks and employee directors on the boards of French companies—the stakeholder directors supposedly had the same legal duty as the other independent directors. All were fiduciaries for the company. Nonetheless their explicit designation as representatives of particular constituencies added complexity and ambiguity to their role, in part by creating heightened expectations on the part of the represented constituency. The public interest directors appointed to the boards of Ireland's banks found themselves in the public's crosshairs in several situations where the interests of the banks and the interests of the public appeared to diverge. Public critics contended, for instance, that the public interest directors should have done more to get the banks to contain credit card interest rates and to pass along the European Central Bank's interest rate reductions to customers with fixed-term mortgages.[170] Employee directors on the boards of French companies apparently felt or anticipated similar pressures from their designated constituency group. A recent study by the French government found that some employee directors refused to participate in the board's compensation committee out of concern that it could put them at odds with other employees or employee groups such as unions and works councils that nominated them.[171]

Some might say that dilemmas such as these experienced by designated stakeholder directors are no different from the dilemmas experienced by independent directors. It is certainly true, as discussed earlier, that independent directors sometimes find themselves torn between their duty to do what they think is best for the company and pressure to do what a group of shareholders with the power to unseat them may want. While the situations are similar in some respects—both present a choice between two mutually exclusive alternatives—the dilemma for designated stakeholder directors is potentially more acute because of their dual responsibility as fiduciary for the company as well as delegate of their constituency group. Regardless of how stakeholder directors are nominated and elected, the fact that they are designated and identified as *employee* directors or *public interest* directors suggests to the world that they are delegates of the named constituency. Anyone who takes on such a named role will understandably feel some sense of responsibility to represent the interests of that constituency. If stakeholder directors are elected or otherwise appointed by their respective constituency, their sense of loyalty and responsibility will likely be even stronger. In the case of employee directors who work shoulder-to-shoulder with other employees on a daily basis, they may also have psychological, social, and emotional ties to other members of their constituency group.

[170] Blanaid J. Clarke and Gail Elizabeth Henderson, "Are Public Interest Directors a Good Idea? Lessons from the Irish Banking Crisis," UCD Working Papers in Law, Criminology & Socio-Legal Studies, Research Paper No. 11/2015, p. 24.
[171] In July 2022, the French government issued a report on the economic and managerial effects of adding employee directors to the boards of French companies. See, p. 28. https://www.tresor.economie.gouv.fr/Articles/5511a03e-3897-4dd8-b795-a2c1926617ef/files/115f4181-c769-4640-bcf5-633336d7229b

By contrast, an independent director has no responsibility to promote the interests of any particular constituency—and, in fact, doing so at the expense of the interests of the company as a whole would be a breach of the independent director's duty as a fiduciary. Moreover, while independent directors are elected by the company's shareholders, they do not typically have close working relationships or deep social ties with members of the electorate. And shareholders, unlike employees, are likely to have widely dispersed interests in many other companies and be far less inclined to take a personal interest in the ongoing decisions of any particular board. The relationship between independent directors and the shareholders who elect them is thus more impersonal than the relationship between stakeholder directors and the constituency group that elects or appoints them. As a result of these differences, independent directors and constituency directors are likely to experience conflicts between the company's interests and the interests of the group that elected them quite differently. For constituency directors, such conflicts present true moral dilemmas between competing responsibilities. For independent directors, they are dilemmas between responsibility and self-interest. While most independent directors would like to avoid being voted out of office, that does not alter the fact that their single overarching responsibility as a fiduciary is to do what is best for the company.

To date, the discussion of full-fledged stakeholder boards for corporations has been mainly among academics.[172] And the prospect of stakeholder boards being enacted into law or adopted voluntarily in practice seems quite remote given wide acceptance of current practice and the many unanswered questions about how stakeholder boards would function in practice. The lack of clarity around stakeholder directors' role and responsibilities is just the beginning. A serious proposal for stakeholder boards must address at least two other sets of questions for which the answers are not obvious.

One set centers on which stakeholders would be represented, and how board seats would be allocated among them. Much of the discussion of stakeholder boards focuses on employee representatives and tacitly assumes that other stakeholders should also be represented. But the "stakes" held by different constituencies vary dramatically. The case for giving long-term employees board representation does not automatically translate to giving customers board representation, especially in businesses with high customer turnover. Long-term employees have a much bigger stake in the company than occasional customers who can readily take their business elsewhere. And, unlike employees who may have a strong interest in the ongoing health of the enterprise, customers cannot be presumed to have such an interest.

[172] In addition to articles cited above see Silvia Ayuso and Antonio Argandoña, "Responsible Corporate Governance: Towards a Stakeholder Board of Directors?" (February 25, 2009) IESE Business School Working Paper No. 701. https://ssrn.com/abstract=1349090

As these observations suggests, the case of each stakeholder needs to be assessed separately.[173] But even if we assume for the sake of argument that all core stakeholders should be represented, the question of weighting remains. Should each stakeholder group get an equal number of seats or should some, such as shareholders or employees, have a larger presence—and how should that determination be made? And what about other stakeholders such as creditors, partners, governments, or end users of the company's products? Should there also be a designated representative of the environment? If we assume 11 board seats, a size generally thought to be workable and the average for S&P 500 boards in 2022, and five to eight groups with a significant stake in the business, some logic must be devised for how the board should be constituted. [174]

Another cluster of questions centers on how stakeholder directors would be chosen. Must stakeholder directors be a member of the stakeholder group they represent or could employees, for example, choose a non-employee to be their representative? Will stakeholder directors be appointed or elected? And, in either case, by whom? As noted earlier some proponents of employee directors would have them elected by shareholders while others would have them elected by employees. If stakeholder directors are to be elected by other members of their stakeholder group, how is membership in the group and eligibility to vote to be determined? Surely the spot market customer does not have the same voting rights as the customer under a multi-year contract. Should eligibility to vote depend on the duration of the stakeholder relationship? For example, should an hourly worker who has been on the job for a week have the same vote as the long-tenured employee who has risen through the ranks? If an individual shareholder's voting power is determined by the number of shares held, how is the voting power of individual employees, customers, or suppliers to be determined? And, equally important, how are such votes to be conducted? Ensuring the integrity of shareholder voting is already difficult, but ensuring the integrity of such a complex voting system would be daunting.

These are just a few of the practical questions raised by the concept of stakeholder boards. Assuming that these questions can be dealt with—a big assumption—the larger issue is how these boards would ultimately function. As this discussion has indicated, the concept of stakeholder boards runs directly counter to the ideals of director and board independence at the core of good governance today. From a stakeholder board perspective, having a stake (or interest) in the business as an employee, customer, supplier, or other stakeholder is a qualification for service. From an independence point of view, these stakes are sources of potential conflict that can compromise a director's judgment and undermine boards' ability to

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[173] For an analysis of each stakeholder group's claim to board representation, see Oliver Williamson, "Corporate Governance," *Yale Law Journal*, Vol. 93: 1197-1230 (1984) (arguing that shareholders are most deserving of protection through corporate governance since other constituencies are protected in other ways).
[174] See 2022 U.S. Spencer Stuart Board Index, p. 25 (the average for S&P 500 boards is actually 10.8 directors).

make overall value-creating decisions. Proponents of stakeholder boards envision their members as engaged collaborators working toward a common purpose, while skeptics envision them as arm's-length negotiators seeking to advance their own group's interests.

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Proponents of structural stakeholderism have yet to make the case that ideals of director and board independence should be abandoned or that stakeholder boards will be more effective than fiduciary boards at making critical board decisions—about strategic direction, capital allocation, financial risk, executive appointments, executive pay, acquisitions, divestitures, reporting, and so on. Yet these are the decisions that must be made wisely in order for companies to thrive and wealth to be created at all. Judging from the gridlock that has seized many representative legislatures today, there is little reason to believe that transforming boards into mini-legislatures would improve the quality of corporate decision making or produce outcomes that serve the best interests of the company or, indeed, the best interests of the parties that advocates of stakeholder boards are seeking to protect. While the performance of fiduciary boards can certainly be improved, a move to full-fledged stakeholder boards seems unlikely to address the problems they are meant to solve and may even make those problems worse.

It is doubtful that the CEOs who signed the Business Roundtable statement committing to run their companies for the benefit of all stakeholders thought they were signing up for stakeholder boards or stakeholder voting rights, or indeed for any change in the prevailing configuration of governance powers. But it is not surprising that advocates of structural change have appealed to the Business Roundtable's statement. It is a short step from the idea of stakeholder capitalism to the idea of stakeholder boards and stakeholder voting rights, especially since the term "stakeholder capitalism" has long been associated with European models of corporate governance that give workers formal rights and powers in the process. However, implementing structural stakeholderism in the U.S. context raises a host of questions that proponents have yet to acknowledge, let alone address. More important, there is little reason to believe that widespread adoption of stakeholder boards would yield the results its proponent envision, and a good chance that it would result in weaker boards and weaker corporate performance, and ultimately be less beneficial for non-shareholder stakeholders than the status quo.

Conclusion

The stakeholder movement picked up momentum in the wake of the 2008 financial crisis as the shortcomings of the then-dominant shareholder paradigm became more apparent. Critics of the shareholder view pointed to a range of problems from its tendencies toward short-termism and excessive risk-taking to its role in exacerbating inequality, climate change, and other economic and societal problems. While calls for stakeholder capitalism have mounted since then, little attention has been paid to the changes it would imply for how companies and their leaders operate—changes in how boards and business leaders make decisions, allocate resources, share information, design incentives, or measure performance, to mention just a few critical areas. And its proponents have tried to walk a fine line between claiming that it would bring improvements in the welfare of non-shareholder stakeholders while also reassuring shareholders they would lose nothing and, in fact, would also gain from a shift to stakeholder-focused governance. This unsatisfying state of affairs has persisted in part because the concept of stakeholder capitalism has yet to be given precise meaning.

As the analysis above suggests, stakeholderism can be both more or less than meets the eye—and more or less of a challenge to shareholder primacy—depending on what version is assumed. Instrumental stakeholderism, the version that seems to be most widely embraced in the business and investment communities, is no threat to shareholder primacy at all. It simply says that stakeholder interests will be respected if doing so will advance shareholders' interests. As discussed, corporate leaders operating within the traditional shareholder paradigm have typically not given explicit consideration to stakeholders' interests, so adopting instrumental stakeholderism may well require an adjustment to their decision making and other processes. But this adjustment is quite consistent with the idea that companies' ultimate objective is maximizing returns to shareholders. Instrumental stakeholderism also leaves the other pillars of shareholder primacy wholly intact. It does not challenge shareholders' exclusive right to vote on directors and other corporate matters, nor does it lessen corporate leaders' accountability to shareholders. However, instrumental stakeholderism offers no assurance to other stakeholders that even their fundamental interests will be respected. And, in some situations as discussed, it is compatible with serious harm to other stakeholders and to society.

Structural stakeholderism, by contrast, does indeed pose a direct challenge to shareholder primacy in proposing to give other stakeholders formal powers in corporate governance—either by putting their representatives on boards or giving them rights to vote on directors or other corporate matters. This threat, however, seems more theoretical than real. There is little likelihood that today's corporate leaders would propose, or that shareholders would vote, to change their investee companies' bylaws to give other stakeholders board representation or voting rights. It is also highly improbable that proponents could mobilize the political support necessary to enact legislation requiring these measures. More fundamentally, while the inclusion of public directors or employee directors on boards could be beneficial in certain circumstances, full-fledged stakeholder boards seem unlikely to improve outcomes for any stakeholders, given the many problems such boards would likely experience.

This brings us to classic stakeholderism and beneficial stakeholderism, both of which pose, at most, a modest challenge to shareholder primacy in calling on corporate leaders to respect some stakeholders' interests even if doing so would not advance the interests of shareholders. But classic stakeholderism is nothing new. In fact, it is just basic business ethics, and the limits it imposes on shareholder primacy need no special justification. In calling on companies to treat all stakeholders in accordance with basic ethical and legal norms, it is asking only that companies observe the standards of conduct that all members of society are expected to observe. To be sure, as already noted, corporate leaders operating within the traditional shareholder value paradigm have not historically given explicit consideration to other stakeholders' interests. So even classic stakeholderism may require those leaders to alter their companies' decision making and other processes to take stakeholders' interests into account. But, conceptually, classic stakeholderism should not be controversial—unless you hold the position that companies and their leaders are exempt from ordinary ethical norms.[175] In contrast to instrumental stakeholderism, classic stakeholderism offers other stakeholders some measure of assurance that certain of their interests will be respected, and thus goes some way toward facilitating trust in companies and in business more generally. However, classic stakeholderism is unlikely to improve other stakeholders' welfare to the degree that many stakeholder proponents envision or to address the large-scale societal problems and inequities that many stakeholder proponents are seeking to address.

Beneficial stakeholderism is more ambitious in both regards, but it is also much more demanding in terms of the governance and management changes it implies (relative to the traditional shareholder paradigm). A serious commitment to beneficial stakeholderism would require corporate leaders to adopt new and more generous forms of gain-sharing and to set specific, measurable goals for improving the well-being of the company's stakeholders. They would need to establish systems to track and report on progress toward those goals, to align their performance measurement processes with those goals, and to adjust their incentive and compensation systems to take those goals into account. They would also need to alter their information and decision support systems so that critical decisions on strategy, capital allocation, R&D, mergers & acquisitions, and the like would be informed by an understanding of likely stakeholder impacts. And they would need to adapt their sourcing, lobbying, political spending, public communications, and investor relations activities to reflect their stakeholder commitments.

Moreover, even if a company's governance and management systems are fully aligned with a multi-stakeholder agenda, beneficial stakeholderism can go only so far toward the espoused

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[175] For analysis of this position, see Lynn Sharp Paine, *Value Shift: Why Companies Must Merge Social and Financial Imperatives to Achieve Superior Performance*, New York: McGraw-Hill, 2003, pp. 155-159 (arguing that the position is untenable).

goals of stakeholder advocates given the competitive, legal, and capital markets context in which companies operate. As discussed, companies' ability to improve stakeholders' welfare is constrained by many factors—not least their limited resources; the legal requirement that investments in other stakeholders must advance the interests of the corporation; and the need to maintain shareholders' buy-in.

If corporate leaders are serious about stakeholder capitalism, they need to take a hard look at which version they are prepared to practice. Each version involves a distinctive set of commitments and challenges. And each has very different practical implications for how companies and their boards function. Corporate leaders need to have a clear understanding of what those implications are. And they need to be honest about what their version can actually deliver for stakeholders, what it can deliver for society, and what it means for shareholders. We have passed the point at which concerns about conflicting interests can be brushed off with easy appeals to the long-term harmony of interests among shareholders, stakeholders, and society. The time has come to clarify what we mean by "stakeholder capitalism." It sounds like a nice idea but we can't really tell unless we know what we are talking about.

Appendix A: Key Terms

What is a stakeholder? The term "stakeholder"—what it means and to whom it refers—has been a topic of much discussion and debate. One academic review of the literature on stakeholder theory identified some 885 definitions.[176] It was originally defined as "those groups without whose support the organization would cease to exist."[177] It is often used to refer to the groups that most companies regard as their core constituencies: customers, employees, suppliers, shareholders, and communities or the general public.[178] To be sure, a case can be made for other definitions and a more extensive list. Some companies include business partners, creditors, governments, the environment, or even competitors as stakeholders.[179] A leading proponent of stakeholder theory, Darden Professor R. Edward Freeman, has defined "stakeholder" as "any group or individual who can affect, or is affected by, the achievement of a corporation's purpose."[180] Many companies find it useful to start with a broad definition like Freeman's to identify their various stakeholder groups and then to sort them into tiers using criteria such their contribution to the company, their power to influence the company, the strength of their claims, or other dimensions relevant to the purpose at hand. It is important to recognize that the set of relevant stakeholders can vary from situation to situation and change over time. Most companies, however, regard the five or six constituencies noted above as core standing stakeholders. These groups can be thought of as the primary reference groups for purposes of this article. Although shareholders are themselves a core stakeholder group within this framework, the term "stakeholder" is sometimes used to refer collectively to constituency groups other than shareholders.[181]

[176] The study categorized the definitions into four general types: Influencer-type definitions were the most common; followed by recipient and claimant definitions; collaborator-type were the least common (but still widespread). See Samantha Miles, "Stakeholder Theory Classification: A Theoretical and Empirical Evaluation of Definitions," *J. of Business Ethics*, Vol. 142, No. 3 (May 2017), pp. 437-459.

[177] Scholars trace the term "stakeholder" to an internal memorandum developed at Stanford Research Institute, now SRI International, Inc., in 1963. See R. Edward Freeman, *Strategic Management: A stakeholder approach* (Pitman, 1984), pp. 31-32. The underlying concept, if not the term, however, goes back further. The earliest known appeal to a multi-constituency view of corporate responsibility in the academic literature is found in a statement made in January 1929 by General Electric Company's President and Chairman Owen D. Young and quoted in E. Merrick Dodd, Jr., "For Whom Are Corporate Managers Trustees?" *Harvard Law Review*, Vol. 45, No. 7 (May, 1932), pp. 1145-1163, at 1154 ("There are three groups of people who have an interest in [the General Electric Company]…people who have put their capital in the company…people who are putting their labor and their lives into the business of the company…The third group is of customers and the general public.")

[178] Lynn Paine, Rohit Deshpandé, Joshua Margolis, and Kim Eric Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?" *Harvard Business Review* 83, no. 12 (December 2005): 122–133.

[179] Lynn Paine, Rohit Deshpandé, Joshua Margolis, and Kim Eric Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?" *Harvard Business Review* 83, no. 12 (December 2005): 122–133.

[180] R. Edward Freeman, *Strategic Management: A stakeholder approach* (Pitman, 1984), Exh. 1.5, p. 25 (defining stakeholder as "any group or individual who can affect, or is affected by, the achievement of the firm's objectives").

[181] Whether society, in the sense of society-at-large, or the environment should be considered as stakeholders is another matter of contention.

What is shareholder primacy? "Shareholder primacy" is another widely-used term with multiple meanings. It typically refers to one or more of four different, but related, propositions. One is about the corporation's objective or purpose: it is the idea that companies should be run with the sole objective of maximizing returns to shareholders. This seems to be what the signers of the 2019 Business Roundtable (BRT) statement on corporate purpose had in mind when they said they were rejecting shareholder primacy and committing to lead for the benefit of all stakeholders.[182] Another is about accountability for the company's performance. This proposition holds that boards and managers are, or should be, accountable principally to shareholders (rather than to other stakeholders). This was the idea apparently animating the Council of Institutional Investors' (CII) when it criticized the BRT statement for "undercut[ting] notions of managerial accountability to shareholders."[183] The CII objected to the statement's treating shareholders as just one of several stakeholders and failing to recognize management's special responsibility to answer to shareholders. A third idea associated with shareholder primacy concerns governance powers. This proposition holds that shareholders have, or should have, the exclusive right to elect corporate directors and vote on other corporate matters traditionally subject to voting.[184] A fourth proposition, perhaps implicit in the others, is that companies should be run according to the preferences of shareholders – not just their preferences for financial returns but also their preferences on social, political, environmental, and other policy matters.[185] These differences are often overlooked in discussions of shareholder primacy, but they are noted in this article when relevant.

What is shareholder value? The term "shareholder value" is yet another ubiquitous term used in different ways. Perhaps most commonly, it is used to refer to financial returns to shareholders. Although financial experts debate how best to measure shareholder value in this sense, a widely-used metric is "total shareholder return" (TSR), calculated as the sum of dividends, stock price appreciation, and other payments to shareholders over a given period of time. The term is also used to refer to the economic value of the company or to increases in that value—again using various metrics. Note that shareholder value in this sense is not necessarily identical to shareholder value in the first sense. While any increase in the company's value will

[182] Business Roundtable Press Release, "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans,' Updated Statement Moves Away from Shareholder Primacy, Includes Commitment to All Stakeholders," August 19, 2019. https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans
[183]Council of Institutional Investors Press Release, "Council of Institutional Investors Responds to Business Roundtable Statement on Corporate Purpose," August 19, 2019. https://www.cii.org/aug19_brt_response
[184] Shareholders typically elect directors and vote on the liquidation or sale of all the companies' assets, certain mergers and acquisitions, executive pay arrangements, and resolutions put forth by other shareholders. For background on the shareholders' exclusive right to vote, see, e.g., Robert J. Rhee, "A Legal Theory of Shareholder Primacy," 102 *Minnesota Law Review*, 1951, 1994 (2018).
[185] For an example, see Oliver Hart and Luigi Zingales, "The New Corporate Governance," ECGI (European Corporate Governance Institute), Law Working Paper, No. 640/2022 (April 2022), p. 3. ("As a result, we think that the paradigm needs to change. This is true even if one accepts, as we do, the idea of shareholder primacy, that is, that companies should act on behalf of shareholders.") http://ssrn.com/abstract_id=4087738

in theory benefit shareholders through an increase in the stock price, it is also possible to increase returns to shareholders, at least in the short term, by taking actions that reduce the company's longer-term prospects. A third usage treats shareholder value as broader than financial returns or economic value. In this usage, shareholder value encompasses anything that shareholders in fact value—including particular business strategies or management practices, or particular policies on environmental, social, or political issues. As between two companies with identical financial returns to shareholders, one can deliver more "shareholder value" in this sense by pursuing policies and practices preferred by a majority of the company's shareholders.[186] In this article, the term "shareholder value" is used in its most common sense as financial returns to shareholders unless otherwise indicated.

[186] Economists Luigi Zingales and Oliver Hart refer to shareholder value in this third sense as "shareholder welfare." They argue that companies should be run to maximize shareholder welfare rather than to maximize shareholder value in the traditional sense of economic returns to shareholders. See Oliver Hart and Luigi Zingales, "The New Corporate Governance," ECGI (European Corporate Governance Institute), Law Working Paper, No. 640/2022 (April 2022), http://ssrn.com/abstract_id=4087738.