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A Critique of the Corporate Governance Approaches from a Deontological Perspective: Can the Corporate Objective Embrace the Interests of Employees?

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Abstract

What should the corporate objective be? How should the interests of employees feature in said objective? Do employees have intrinsic value other than instrumental value? There are, of course, a number of different arguments that have been advanced in response to these questions; the majority of which have been built upon a range of different theoretical positions. In order to answer such questions, this study critically analyses the most prominent corporate governance approaches, which mostly see employees as only means in the corporation's and/or shareholders' ends. The study argues that employees should not merely be treated as instruments to the ends of the corporation or corporate shareholders. It argues that a normative approach to realise the corporate objective can be found within a non-consequential stakeholder theory. Thus according to this paper, employees can be respected genuinely only if the objective of the corporation is redefined from an intrinsic perspective.

Keywords: *Corporate Governance, Business Ethics, Stakeholder Theory, Deontological*

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Kurumsal Yönetişim Teorilerine Deontolojik Bir Eleştiri: Şirketlerin Amacı Çalışanların Çıkarlarıyla Bütünleşebilir mi?

Öz

Bir işletmenin amacı ne olmalı? Bu amacın içinde işletmenin çalışanlarının çıkarları ne ölçüde rol oynamalı? Çalışanlar işletmeye sağladıkları faydanın ötesinde bir değere sahip mi? Elbette bu sorulara şimdiye kadar bir çok teori farklı açılardan yanıtlar aradı. Aşağıda okuyacağınız çalışma bu sorulara cevap ararken işletme çalışanlarını kar maksimizasyonu doğrultusunda araç olarak gören kurumsal yönetişim teorilerinin eleştirel bir analizini sunuyor ve bu teorileri görev ahlakı açısından yeniden değerlendiriyor. Bu değerlendirme işletmenin amacını ve işletme çalışanlarının çıkarlarını araçsal/sonuçsal olmayan normatif bir teori üzerinde yeniden tanımlıyor. Kant'ın görev ahlakını temel alan bu teori, işletme çalışanlarını, yarattığı ekonomik faydanın ötesinde değerlendiriyor. Bu çalışma aynı zamanda çalışanları sadece araçsal değeri üzerinden değerlendiren kurumsal yönetişim modellerinin de bir eleştirisini sunuyor. Yapılan eleştiride yaygın kurumsal yönetişim modellerinin, çalışanlara sadece işletmeye ve hissedarlara sağladıkları fayda üzerinden yaklaştığı üzerinde duruluyor. Bu nitel ve normatif eleştirinin ardından çalışanların içsel değerlerine saygı gösterebilmenin ancak deontolojik bir paydaş teorisi ile mümkün olabileceği savını öne sürüyor.

Anahtar Kelimeler: *Kurumsal Yönetişim, İş Etiği, Paydaş Teorisi, Deontolojik Etik*

Introduction

This paper asserts that most corporate governance theories subordinate the interests of employees to the economic interests of shareholders. The paper begins its examination with the shareholder value theory (SVT)[1]. Shareholders are the investors who hold stocks or shares that are issued or sold by the corporation (Blair, 1996). Shareholder value theory (SVT) states that the objective of the corporate governance should be the maximisation of shareholder-wealth (Bainbridge, 2003; Eisenberg, 1999). Indeed, by following this theory, directors may also consider the interests of non-shareholder stakeholders (Keay, 2011). But as the following paragraphs clarify the crucial point under the notion of SVT is that directors consider the interests of other stakeholders merely as a means to maximising shareholder value. Stakeholders are not intrinsically given weight, at least not as something to be pursued in their own right. Rather, their input is only given weight instrumentally - that is in order to realise the true, higher goal, of maximising shareholder value (Rossouw, 2009). Thus the SVT may be regarded as functionalist or consequentialist towards employees since most justifications of SVT are predominantly based upon the concept of economic efficiency.

On the other hand, stakeholder theory constitutes the most important competitor to the SVT. The theory's chief claim is that corporations should give weight to the interests of non-shareholder stakeholders, as well as those of shareholders. Stakeholder theory (ST) has various strands, and can be categorised under a number of different headings. As this paper shall note, some of these arguments in favour of the stakeholder theory are themselves economic, especially those based upon the importance of fostering productive relationships with valuable employees. However, as critiqued in the following paragraphs, these theories are mostly instrumentalist towards non-shareholding stakeholders, and consequently, are instrumentalist towards employees as SVT. Similarly, other theories, presented as alternative to the SVT, approach stakehold-

[1] *The theory is also called as 'shareholder primacy' or 'shareholder value principle,' or 'shareholder wealth maximisation norm'. (Crane and Matten, 2010, p. 665)*

ers from an instrumentalist perspective too. These theories will be examined in detail below.

However, this paper argues that employees should not merely be treated as instruments to the ends of the corporation. Yet, do today's corporate governance approaches pay attention to intrinsic value of employees? To answer this question, the paper shall critique the main corporate governance approaches from a non-consequential perspective. Before this critique, the paper briefly examines the theory of Kantian deontological ethics. Afterwards, it analyses and criticises the main justifications of the shareholder value theory. In the course of the analysis, enlightened shareholder value theory (ESV) is critiqued as a variation of the SVT. In the following section, the stakeholder theory (ST) is investigated from both economic and non-economic perspectives. The paper then concludes its analysis with non-consequentialist stakeholder theory by highlighting the potential of non-consequentialism in improving the intrinsic interests of employees.

Non-Consequentialism as a Theoretical Approach: A Brief Look at Deontological (Kantian) Ethics

Deontology is a concept grounded in moral duties (Gibson, 2000). According to deontological ethics, 'some actions are right or wrong for reasons other than their consequences'(Beauchamp and Bowie, 1997, p. 33). Therefore, deontological ethics differs from consequentialist ethical theories such as utilitarianism which evaluates an ethical act depending on a favourable outcome.[2]

Immanuel Kant is one of the most important philosophers of modern deontological ethics. Kant argues that the act of a person should not be guided by self-interest, but it should be from his duty (Beauchamp and Bowie, 1997). According to Kant, there are two types of duties or, in his own words – 'imperatives'. The first type of duty is called, hypothetical imperative; referring to the action, which 'is good for some possible or actual purpose'(Kant, 2011, p.57). For instance, if one wishes to develop

[2] *Utilitarianism can be one of the most significant consequentialist ethical theory. According to a Utilitarian, for example, happiness is the only desirable end. (Mill, 1991, p. 168)*

her career, she must study and work for this. Thus, hypothetical imperatives are dependent on persons and their goals. Secondly, the categorical imperative refer to 'the action to be of itself objectively necessary without reference to any purpose'(Kant, 2011, p.59). In other words, the categorical imperative does not depend on any good or unpleasant consequences. It does not vary person to person. It refers to universal duties that every rational human being can have, such as truth telling, or keeping promises.

In spite of the above categorisations, Kantian ethics per se has been predominantly shaped by the elements of the categorical imperative e alone. The categorical imperative can be grounded in three main formulations. The first is based upon the notion of universality. To illustrate this, Kant implores the reader to 'act only according to that maxim through which you can at the same time will that it become a universal law'(Kant, 2011, p.71). Kant articulated this further by saying that 'so act as if the maxim of your action were to become by your will a universal law of nature'(Kant, 2011, p.71). From this perspective, the maxim of an act or rule should be universalizable in order to be ethical. This universality formulation requires consistency (Rowan, 2000). It should be applicable to everyone, without exception to be deemed a valid moral rule. Therefore, it can be seen as a test for an ethical act from the Kantian perspective.

The maxim of some actions definitely exists which cannot be universalized. However, these actions – called immoral actions – are viewed as self-defeating from the viewpoint of Kantian ethics. For example, if a maxim that permitted an immoral action such as theft by employees, managers, or customers were universalized, it would be self-defeating (Bowie, 1999). As Bowie posited, if one universalized a maxim that permits the breach of a contract, no contract would exist, since people would not enter into a contract which they believe that the other party would have no intention of honouring (Bowie, 1999). Therefore, for an ethical act to be deemed as such, the universalization of maxims requires it to be logically coherent.

One may claim that consequentialist ethical theories can also be universalised and be consistent. In this case, utilitarianism, which differs from Kantian ethics by focusing upon the good consequences of an ethical act, may be one example. However, in terms of utilitarianism, the measure of utility can change, for example, the assessment of 'consequences as pleasure or pain might depend heavily on the subjective perspective of the person'(Crane and Matten, 2010, p.99). In other words, utilitarian ethics may be seen as more subjective compared to deontological ethics. Nevertheless, moral duties under Kantian ethics are absolute, and apply to everyone. Thus, in order to make corporations respect the interests of employees globally, Kantian ethics may give us a more extensive prescription.

The second formulation of the CI is based upon the intrinsic value of human beings or, put differently, respect for persons – a central feature of this work. The notion of respect for persons refers to the idea advanced by Kant that the person has the right to be treated as an end in itself. Indeed, one must be treated with respect and moral dignity as the dignity that human beings possess stems from their capability as autonomous and self-governing beings (Bowie, 1999). Kant posits that people as responsible beings can distinguish the right from wrong by themselves. Human beings differ from objects, which have instrumental value, and should not be treated as things. Human beings also differ from animals since they are capable of making rational choices (Bowen, 2006). To this end, the ethos of Kantian ethics advances the view that people need to be free to develop their 'rational and moral capacities'(Arnold and Bowie, 2003, p.223). In summary, persons should be treated as ends in themselves, and not as means to others' ends.

The second formulation of the categorical imperative, in particular, can also be applied to corporate activities. For example, utilising a Kantian perspective, Arnold and Bowie define the ethical obligations of employers as to 'refrain coercion, meet minimum safety standards, and provide a living wage for employees' (Arnold and Bowie, 2003, p.222). From this perspective, it can be argued that employees should not merely be treated as instruments to the ends of the corporation (Rowan, 2000). Hence, corporate governance approaches that see stakeholders as means in the ends of a limited number of people, such as in the ends of shareholders, can be rejected from this angle.

The third formulation of the categorical imperative is called the kingdom of ends. This formulation may be seen as the combination of the first and second. Accordingly, the interactions among the community of human beings should be shaped by laws based on the notion of universalizability and respect for persons as outlined above (Bowie, 1999). Here, every person in the community has equal interests as they possess human dignity.

Autonomy, which enables rational human beings to take ethical decisions, is the main element in the third formulation of CI, to which 'members of the kingdom' are at the same time seen as subject and sovereign legislators of (Bowie, 1999, p.87). From this perspective, to be autonomous 'is to have the mode of self-control that takes account of others' like moral status'(Brummer, 1986, p.179). This constitutes the fundamental root of Kantian ethics since the ethical act is based upon the reason. For example, the corporation can be seen as a moral community made up of human beings. Consequently, corporations need to respect the autonomy of stakeholders, such as employees (Bowie, 1999).

However, the application of Kantian ethics to corporate governance can also attract some criticism. The most important critique may be related to how directors should treat different stakeholders with different ends. For instance, 'a company's shareholders may want profits, while some of the workers within a firm may be striving for higher wages, increased leisure, or perhaps the pursuit of a religious life' (Freeman and Evan, 1990, p.511). Should directors favour shareholders to other stakeholders in this situation? One answer to this question is that even in a situation in which stakeholders are treated as means in others' ends they 'should have the choice between sacrificing their own personal goals in favour of the company's collective ones, or else leaving the firm'(Freeman and Evan, 1990, p.511). In light of this view the remainder of the paper examines the notion, positing the suggestion, that treating individuals, or employees, as a means to an end should not be the objective of the corporation. For this purpose, the following sections examine how prominent corporate governance approaches address the question of the corporate objective. After having investigated this, the paper turns once again to consider the concept of respect for persons, concluding its analysis of non-consequentialist stakeholder theory.

Shareholder Value Theory

In order to see how the SVT addresses the question of the corporate objective, the following sections will examine the main justifications behind and in favour of the theory.

Property Rights

The notion in which companies are viewed as property, conceptualises the company as a fictional instrument through which the company effectively becomes the property of its shareholders (Friedman, 1970) It is claimed that property rights 'give the owner full and absolute disposition rights over the object of ownership'(Engelen, 2002, p. 395). And so, the corporation is seen as legally obliged to serve the interest of its shareholders. It may then be argued that one justification in favour of SVT derives from property rights of shareholders.

A defender of the view that the company is property (while justifying the SVT) may argue that in fact, respecting the rights of shareholders to have their interests given primacy is also likely to promote greater overall social wealth (Parkinson, 2003). This consequentialist notion, as an idea of moral philosophy, can be traced back to the ideology of Adam Smith, who argued that the individual acts of economic self-interest through the invisible hand of market forces serve the best interests of society at large (Ho, 2009). Accordingly, a free competitive market, in which individuals pursue their own private goals, functions better for the public interests (Parkinson, 2003). However, for proponents of the company as property justification for the SVT, the fact that the SVT may also happen to maximise overall social wealth is a mere fortunate by-product of respecting shareholders' private property rights. For the property rights advocate, the SVT is a necessity, as property rights must be respected, and only the SVT achieves that (Parkinson, 2003).

Following the above notions, individual freedom has been regarded as having high moral value. In this respect, traditional inherent property rights continue to allow corporate property to be treated as a private association (Parkinson, 2003; O'Neill, 1991). Assigning control rights to shareholders in the manner described has been associated, by moral philosophy, with generating the greatest good for all. In other words, maximising share value is regarded as the maximisation of the social value and welfare too (Hansmann and Kraakman, 2001). Indeed, this perception creates a theory under which the corporation is regarded not only as a profit-oriented entity, but one that is also beneficial to society as a whole (see McSweeney, 2008). However, it is important to note that the property argument is distinct from, and ultimately not dependent on, such a positive consequentialist outcome since property rights are grounded in deontological ethics. (Staveren, 2007)

Nonetheless, even though the property rights argument may be used as a justification in favour of the shareholder value theory (SVT), it is evident this possesses some weaknesses. First, one may opt to argue that shareholders, technically, cannot be said to be the owners of the corporation, since the property of the corporation belongs to the company itself as a separate entity, and shareholders do not have direct proprietary rights to it (Davies and Worthington, 2012). Rather than shareholders themselves, it is the board of directors within a corporation that has the right to control the corporate assets (Stout, 2012).

Second, SVT states that shareholders, as owners of the company, are entitled to determine in whose interests the company should be run. Typically, this will be in the interest of themselves. However, it does not insist that the company must be run for the interests of shareholders alone. Shareholders may, for example, decide that the company is to be run in the interests of employees. Yet, this result would even depend on shareholders choosing to sacrifice their own interests in favour of other stakeholders instead; that is to say, this is not an outcome that could be imposed upon shareholders, in contravention of their moral, equitable or legal rights as property owners. However, for proponents of the shareholder value theory, who rely on the company as property argument, it is generally assumed that shareholders do not want to incur such a voluntary sacrifice of their own interests, so shareholder value does indeed flow seamlessly from the assumption that the company itself is the property of shareholders.

Third, even where shareholders are named as owners, the property rights they possess are not unlimited. To this end, it is crucial to define the limits of the concept of ownership. One can, for instance, use

Honoré's (1999) example in order to demarcate the limits of ownership rights. According to him, there is 'a substantial similarity in the position of one who 'owns' an umbrella in England, France, Russia, China'(Honoré, 1999, p. 558). Yet, he underlines the significant limits of ownership rights by pointing out nowhere does one have the right 'to poke his neighbour in the ribs or knock over his vase'(Honoré, 1999, p. 558). Furthermore, Donaldson and Preston emphasise that 'property rights are embedded in human rights' and they are restricted against harmful uses (Pejovich, 1990, cited in Donaldson and Preston, 1995, p. 83). Donaldson and Preston also cite Pejovich who states that ''it is wrong to separate human rights from property rights'' in order to depict the arguments that bring stakeholder interests into the conception of the property (Pejovich, 1990 cited in Donaldson and Preston, 1995, p. 83). In addition to specific rights, property ownership creates some duties for owners (Greenfield, 1997). For instance, 'a property owner cannot burn noxious trash in her backyard' (Greenfield, 1997, p. 293). Property rights cannot be seen as justifying harmful activities. Thus it can be argued that the concept of the corporation as property 'does not support the popular claim that the responsibility of managers is to act solely as agents for [and in the interests of] the shareowners' alone'(Donaldson and Preston, 1995, p.84).

Nevertheless, in addition to property rights, there are also contractual theories/economic arguments that can be in favour of the SVT which are addressed in the following section.

Contractual Theories

The Theory of Transaction Cost and Incomplete Contracts

According to Coase (1937), firms can perform better than the market since it is the market that minimizes transaction costs. This minimization occurs due to the authority within the firm to affect such costs (Coase, 1937). Even though the price mechanism determines the allocation of factors in the market, in the firm, if an employee 'moves from department y to department x, he does not go because of a change in relative prices, but because he is ordered to do so' (Coase, 1937, p. 387). Therefore, from the perspective of Coase, the authority in the firm reduces the costs which may be possible in the market.

However, according to Alchian and Demsetz (1972), the essence of the firm is based upon contracts, rather than authority. Yet, it is also argued that contracting creates transaction costs within the firm (Riley, 1995). Indeed, following this argument, it may be impossible to write a complete contract since 'a contract that anticipates all the events that may occur and the various actions that are appropriate in these events' cannot be written (Hart, 1988, p.123). Thus, 'any contract written within a firm or between independent firms will be incomplete'(Hart, 1996, p. 372). Because of this contractual incompleteness, 'governance structure can be seen as a mechanism for making decisions that have not been specified in the initial contract'(Hart, 1995, p. 680).

In turn, the firm may be seen as a governance structure (Mallin, 2010). One solution in terms of incomplete contracts can be that 'assigning property rights to one of the parties to the contract' (Blair and Stout, 1999, p. 260). Yet, which party should be assigned these rights? The SVT answers this question by addressing justifications made under the agency theory and the concept of the nexus of contracts. Next section examines these theories.

Agency Theory and the Concept of the Nexus of Contracts

Agency theory constitutes a strong justification in favour of the SVT. According to the agency theory, corporate managers are called to act as the agents of the shareholders, and shareholders are the principals of the managers (Jensen and Meckling, 1976). According to this theory, the agency relationship also creates an 'agency cost' where there exists a risk of agents evading transactions, or acting in their self-interest (Jensen and Meckling, 1976, p. 308). Indeed, anything that reduces shareholder value, arising from the agency relationship, constitutes agency cost. For example, agents may create additional costs if they consider the interests of other stakeholders instead of the interests of shareholders. Agency cost includes direct transfer of value to the agent such as excessive salaries. It also includes monitoring costs incurred by shareholders trying to prevent such transfers of value. As a consequence, the objective of the corporate board needs to be 'reducing agency costs and maximising shareholder wealth' (Stiles and Taylor 2001, p.14).

The agency relationship between principals and agents constitutes a contract (Jensen and Meckling, 1978). Agency theory, therefore, views the corporations as a nexus of contracts (Mallin, 2010, p. 18-19). From this perspective, the corporation is not real, but rather defined as a complex set of contracts among managers, workers, and the contributors of its capital (Easterbrook and Fischel, 1985). For instance, Easterbrook and Fischel (1989) argue that the corporation is made up of a web of contracts in which people who voluntarily agreed to participate. In this context, shareholders are seen as the sole residual claimants and risk bearers because it is they that differ from other stakeholders such as employees who contract for a fixed return (Easterbrook and Fischel, 1989). For instance, a contract specifies how much an employee will be paid or how much a creditor will be repaid. Yet shareholders, who possess no such contracts, are seen as less protected than other corporate constituencies (Bainbridge, 2008). As such, shareholders are regarded as risk bearers in comparison with other stakeholders, such as employees, who enjoy protection under their contracts and various laws (Easterbrook and Fischel, 1989). Williamson further contends that shareholders cannot renegotiate the terms of their contracts (Williamson, 1984). In this vein, shareholders are seen as constituents, who do not have the 'guarantee of any return'(Keay, 2010, p.398).

In light of the above, shareholder value theory sees shareholders as the most vulnerable participants in terms of risk taking. For example, one can ask whether it is possible to give shareholders a fixed dividend, for instance, 5% of the value of their investment each year and assume employees get all the surplus. However, the answer to this question is based on the fact that shareholders can diversify their investments, but employees are risk averse. As a result, shareholders accept more risk and employees want the security of a guaranteed salary. Accordingly, shareholders become residual claimants and risk bearers by purchasing stocks. Hence, the concept of the nexus of contracts, based upon 'the existence of divisible residual claims on the assets and cash flows of the organisation,' can be seen as an important justification for shareholder value maximisation (Jensen and Meckling, 1976, p. 311).

Lastly, it may be argued that there are other supposedly economic benefits guaranteeing that shareholders alone retain the right to have their interests considered above all others, rather than requiring a balancing of the shareholder and non-shareholder claims to profit and corporate assets. For instance, Jensen (2001) argues that the corporation should not maximise both shareholder value and any other stakeholder value at the same time, since this method cannot be efficient. This perspective is grounded in that shareholder value is more certain than other theories in decision-making, since corporate managers do not need to balance different and complicated interests of other stakeholders in decision making (Jensen, 2001). Jensen (2001) points out that corporations should have a single-valued objective for efficiency since multiple objectives may confuse the managers.

However, agency theory and the nexus of contracts arguments in favour of shareholder value theory (SVT) can be critiqued from a number of different perspectives. First, the notion that shareholders are the only residual claimants to corporate profits has a crucial flaw. For example, the corporation can be depicted as mutual assets of the team members who make firm-specific investments; thus these firm-specific investments can hardly be protected by a contract and they are of 'little or no value outside the firm' (Osterloh and Frey, 2006, p. 328). Not only shareholders, but also other stakeholders, such as employees, bear residual risk-specific investments (Blair and Stout, 1999). By making firm-specific investment in the firm, employees become a valid and legitimate risk bearer for residual claims (Brink, 2010). Employees may then suffer losses or receive dividends along with shareholders, depending on the performance of the firm (Stout, 2001).

Limited liability protects only the assets of the shareholders from large losses, regardless of their cause (Kraakman et al., 2009). Under such protection, shareholders are not liable for more than the nominal amount they invest. Furthermore, shareholders can renegotiate their contracts in the stock market, and can sell their shares whenever they wish to (Freeman and Evan, 1991). However, other stakeholders may not have such an exit option. For example, employees bear risks as much as shareholders bear (Ghosal, 2005). They cannot change their job easily (Blair, 2003). Employees can be seen as residual claimants since their income depends upon a hazardous quasi rent (Brink, 2010). This notion will be analysed further below. Hence, it is problematic to say that shareholders are the 'only risk bearers' (Sharplin and Phelps, 1989, p. 50).[3]

Second, whereas the SVT sees shareholders as corporate constituents who always share identical interests, this assumption may not be true in some circumstances. Although some shareholders may possess short-term profit driven interests, others may be interested in the long-term success and sustainability of the firm.[4] For instance, they may 'prefer their companies not earn profits by harming third parties or breaking the law' (Stout, 2012, p.9).

Third, even if some claim that shareholder value is efficient, shareholder value maximization may not always necessarily be efficient (Lee, 2006). When it comes to the costs created by corporate externalities for stakeholders other than shareholders, the SVT may not be justified by the efficiency argument (Keay, 2012). The SVT, through share price maximisation, often leads directors to externalise the costs on to other stakeholder groups (Deakin, 2005). Therefore, the SVT may be one of the contributory factors leading to plant closures, unsafe products, and polluted environments (Mitchell, 2002). Hence, in order to justify the SVT from an efficiency perspective, the cost created to other stakeholders must also be considered (Keay, 2012).

Fourth, share prices as performance indicators in favour of the SVT can and have been criticised. Share prices may not represent accurate indicators, these may increase or decrease without any change in the corporation's fundamental values (Letza et al., 2004). Thus, share prices may not evaluate corporate performance holistically or accurately. For instance, in some circumstances, whereas the company performs poorly, executive compensation may continue increasing (Dent, 2005).

Lastly, the SVT and one of its justifications, namely the notion of nexus of contracts, draws most of its support from economic efficiency. However, this consequentialist approach subordinates non-shareholder

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[3] According to Sharplin and Phelps (1989), the corporation may be conceptualised as a nexus for contracts among stakeholders and the management can act as an agent for each stakeholder group, who can all be treated as residual claimants (p. 50).

[4] Some investors specifically abstain from investing in particular companies citing ethical justifications. (See Lewis, 2001, p. 332)

stakeholder interests. It is essential to note that the SVT, which relies upon some of the arguments examined above, could not be deemed acceptable according to deontological ethics since all the arguments advanced fail to treat the other stakeholders as their ends in themselves. Indeed, even if it is claimed that maximising shareholder value results in efficiency of corporations and leads to the indirect improvement of other stakeholders' interests, this does not change the instrumentalist characteristics of the SVT (Rossouw, 2009). In other words, from this viewpoint, the interests of stakeholders can only enjoy instrumental value. Thus, the interests of non-shareholder stakeholders, such as the interests of the employees, in the SVT are constrained, and limited by the functionalist perspective. This behaviour cannot be regarded as ethically right from a deontological perspective.

Dismissing Enlightened Shareholder Value

In this section, the paper shall briefly consider – although only to dismiss – the enlightened shareholder value (ESV).[5] ESV may be thought of as another version of the corporate objective, and a variation on Shareholder Value Theory (SVT). However, as the following paragraphs shall try to illustrate, as an approach, it does not really provide an alternative, and rather should be understood as a clearer and explicit depiction of what is already implicit in any clear understanding of SVT.

ESV was put forward by the Companies Act (CA) 2006 in the UK. Some commentators conceptualised the ESV as a third way, and considered it a move towards a more stakeholder-driven corporate governance model (Williams and Conley 2005; Millon, 2011). The ESV essentially refers to long-term shareholder wealth maximization (Millon, 2011). Accordingly, stakeholder interests are seen as material in maximising financial performance and the creation of long-term value. Consequently, ESV requires directors to promote the success of the company in the interests of all stakeholders (Companies Act 2006, s. 172).

[5] The concept of the ESV was first used by the Company Law Review Steering Group in the UK. (Department of Trade and Industry 1999, para 5.1.11).

With ESV, shareholder value maintains its primary role as the objective of the corporation. However, a subtle difference can be outlined between SVT and ESV (Ho, 2010). ESV may be seen as a way of complying with shareholder interests, without neglecting legitimate stakeholder claims. Whereas SVT claims that maximizing 'the wealth of shareholders' improves the value of the firm, according to ESV, maximizing the long-term value of the firm improves 'the wealth of shareholders'(Ho, 2010, p. 99).

As with SVT, ESV may also be critiqued from a number of similar perspectives. Firstly, the market driven nature of this theory can be criticised for making it insufficient with respect to long-term sustainability (Millon, 2011). As Millon (2011) highlights in his research, even if requirements upon companies to avoid wrongdoing towards its stakeholders result in some improvements, the market driven nature of ESV – where shareholders create pressure to achieve short-term results – constitutes a significant weakness to the approach. Secondly, whilst ESV touches upon issues such as long-termism, and the consideration of stakeholders' interests, ultimately it fails to provide a direction such as 'to what degree management should or may deviate from shareholder wealth maximization'(Henderson, 2009, p.27). Thus the management of the corporation may fail to balance the interests of all stakeholders, since even though the theory requires the consideration of all stakeholders in terms of corporate governance, it does not propose 'how and when that is to be done' (Keay, 2012, p. 290). Lastly and most importantly, much like SVT, ESV considers stakeholder interests as merely instrumental. It focuses on how the interests of employees can be used to improve efficiency and profitability. ESV, by highlighting long-term shareholder value, can even be interpreted as if to provide 'guidance on how to discriminate between the interests of different stakeholders' in order to maximize shareholder value (Kiarie, 2006, p.340). Therefore, one conclusion can be that employees, along with other stakeholders, are expected to be treated instrumentally, rather than being given intrinsic weight or value in ESV.

Stakeholder Theory

Stakeholder theory constitutes the most important competitor to SVT. Stakeholder theory's chief claim is that corporations should give weight to the interests of non-shareholder stakeholders, as well as those of shareholders (Reynolds, Schultz & Hekman 2006). Thus, stakeholder theory can be depicted as a more comprehensive approach to that of SVT, encompassing all relevant parties to the corporation (Fontrodona and Sison, 2006).

Before analysing the main concepts of stakeholder theory, exactly who stakeholders in the present context are require identification. Scholars have advanced suggestions in this regard. According to Dodd (1932), three groups of people have interests in the corporation as stakeholders. The first are its stockholders, with their capital, the second are its employees, who provide labour and invest their lives into the operation and business of the company, and the third group is its customers, and the general public (Dodd, 1932). By contrast, Freeman (1984) defines stakeholders from a much broader perspective. In his definition, stakeholders refer to 'any group or individual who can affect or is affected by the achievement of the organization's objectives' (p. 46). According to Clarkson (1995), 'stakeholders are [those] persons or groups that have, or claim, ownership rights, or interests in a corporation and its activities, past, present, or future' (p. 106). Similarly, according to Donaldson and Preston (1995), 'stakeholders [can be] identified by their interests in the corporation, whether the corporation has any corresponding functional interest in them' (p. 67). Donaldson and Preston's definition of stakeholders reflects the approach of this paper towards stakeholders.

Having defined who stakeholders are, it is noteworthy that one of the key concepts advanced within stakeholder theory is that corporate managers ought to balance the interests of stakeholders in terms of decision making (Smith, 2003). As such, the corporate objective, as previously highlighted in this paper, is part based upon a measure of satisfaction for all corporate stakeholders, rather than just shareholders. In SVT, although non-shareholder stakeholders can create value, value distribution tends only to favour shareholders (Ghoshal, 2005). Unlike SVT, stakeholder theory contends that the philosophy of the corporate governance should be based upon creating 'as much value as possible for stakeholders'(Freeman et al., 2010, p. 28)

Stakeholder theory may specifically be examined from a descriptive, instrumental or normative perspective (Donaldson and Preston, 1995). From a descriptive perspective, stakeholder theory can 'be used to describe, and sometimes explain, specific corporate characteristics and behaviours' (Donaldson and Preston, 1995, p. 70). Alternatively, stakeholder theory may be justified by employing instrumentalist arguments, such as highlighting the role of stakeholder management in the profitability of the corporation (Donaldson and Preston, 1995). Lastly, a stakeholder theory may be grounded in normative arguments that focus upon intrinsic value of stakeholders (Evan and Freeman, 1998). In this respect, one may ask 'why corporations ought to consider stakeholder interests, even in the absence of any apparent benefit'(Gibson, 2000, p.245).

The remainder of this paper examines stakeholder theories in two sections: strategic/instrumental stakeholder theories and non-consequentialist theories.

Strategic/Instrumental Stakeholder Theories

As outlined above, the major arguments in favour of the SVT are the supposed economic benefits it engenders by producing ever greater social wealth. Indeed, some instrumentalist proponents of stakeholder theory have also sought to use economic justifications to defend stakeholding (See Smith, 2003). Accordingly, the major justification of instrumental stakeholder theories is that companies practising stakeholder management will maximize their financial performance (Egels-Zandén and Sandberg, 2010). Moreover, if the corporation considers the interests of its stakeholders, then profit maximisation may be more stable, long-lasting and effective than in the SVT.

For example, changes in the relative importance of capital, and (at least in part) labour in generating value for companies, constitute a strong argument in favour of strategic/instrumental stakeholder theories. Indeed, the accelerated change from a physical to a knowledge-based economy in recent decades - making human intelligence a crucial factor in today's corporate world, may be seen as a factor improving the position of stakeholders in relation to the capital supplier shareholders. As Drucker (1994) had observed, technological devices (purchased with shareholders' capital) are not productive tools without qualified employee users. Thus, in addition to shareholders who ensure financial investment in the firm, other stakeholders, such as employees, gain importance by making firm-specific investments (Egels-Zandén and Sandberg, 2010). Therefore, the concept of ownership based upon financial investment would appear to, in part, be losing significance. Indeed, in addition to the 'buildings and machinery', it is 'the skills and experience of workforce' that play a vital role in the value of the company (Handy, 2002, pp. 51-52). Thus, in this environment, 'when workers leave, their information and skills-the corporation's permanent capital-do go with them'(Mitchell, 1998, p. 873).

The instrumental stakeholder theory (IST) finds some of its economic justifications in strategic management (Freeman et al., 2010). One such justification in favour of the IST can be related to competitive advantage (Jones, 1995). For instance, the IST may specifically depict the role of trust and cooperation as improving the competitive advantage of the firm (Jones, 1995). According to Jones (1995), for example, the firms pay attention to trust and cooperation 'will experience reduced agency costs, transaction costs, and costs associated with team production' (p. 422).

Nevertheless, instrumental stakeholder theories suffer from some apparent weaknesses. First, much like shareholder value theory, instrumental stakeholder theories apply economic justifications, and address the issue of efficiency. Whilst these justifications may mean profit maximisation, they may not mean value creation for all stakeholders (Phillips, 2003) since instrumental theories can be interpreted as using stakeholder management in maximizing shareholder value (Cooper, 2004).

Second, unlike the main arguments of instrumental stakeholder theories, companies may not be affected financially even if they act badly towards stakeholders. For instance, although corporations can maximise profit by considering the interests of stakeholders, some corporations may still continue externalising some costs placed upon stakeholders. In effect, sometimes corporate misdemeanour may not even affect companies in the long run. The Ford Pinto case may be one example in this regard. Ford, which company used to produce cars called Pinto with unsafe fuel-tank systems, caused many deaths and injuries (Stuart, 1979). Although the company 'acted badly' in this case, it has not been hurt seriously (Gibson, 2000, p. 245).

Thus, in some circumstances, it is possible to say where market actors cannot adequately sanction companies, companies may not be eager to give respect to the interests of stakeholders. For example, consumers may be less effective to influence some companies through purchasing power, if such companies do not produce consumption goods. (Graham and Woods, 2006). Similarly, the same may apply where a company possesses a monopoly within the market. As such, from an instrumental perspective, where there is no business case to consider the interests of stakeholders, then it would seem unlikely to expect companies to offer genuine respect to stakeholders.

Lastly, even where there may be strategic value with respect to stakeholders' interests, one may argue that instrumental approaches may not be as successful as non-instrumental ones (Quinn and Jones, 1995). Conversely, instrumental and strategic thinking may even result in detrimental effects upon ethics (Gibson, 2000). For example, if employees, or other stakeholders, realise that ethical policies are justified, instrumentally, such as in terms of the self-interests of the corporation, or its shareholders, they may act in the same way (Quinn and Jones, 1995). Thus, one can argue that intrinsic approaches, rather than instrumental ones, may result in better outcomes even for the corporation (Quinn and Jones, 1995).

In summary, consequentialist/strategic arguments in favour of stakeholder theory, without substantial empirical evidence, do not seem as robust as normative arguments in order to justify stakeholder theory (Donaldson and Preston, 1995). These theories are also morally problematic from an ethical (deontological) point of view, since the respect offered to stakeholders in these theories is dependent upon good consequences for the company. Even though these theories differ from shareholder value oriented approaches, by considering the interests of other stakeholders, they do not recognise the moral value of treating stakeholders as ends in themselves. When stakeholders are approached instrumentally, their interests are considered 'only if they have strategic value to the firm' (Berman et. al, 1999).

Non-Consequentialist Stakeholder Models

The beneficial outcomes of considering the interests of stakeholders have been the central focus of corporate governance theories (including stakeholder theory) so discussed so far. However, a normative theory can also ask why the corporation should consider the interests of stakeholders even if there are no beneficial outcomes (Gibson, 2000).

For instance, if the corporation is seen as 'a community of persons' by placing emphasis upon 'the nodes of relationships', intrinsic worth and human dignity can be recognized instead of the instrumental value of what an employee does for the firm (Fontrodona and Sison, 2006, p. 39). As Donaldson and Preston (1995) quoted above, stakeholders can be defined 'by their interests in the corporation', rather than their functional outcomes for the corporation (p. 67). Accordingly, Donaldson and Preston (1995) note: '…each group of stakeholders merits consideration for its own sake and not merely because of its ability to further the interests of some other group, such as the shareowners'(p. 67).

Non-consequentialist deontological ethics, as introduced above, can help us to develop such notion of intrinsic value towards stakeholders. Most importantly, from the perspective of deontological ethics, the interests of stakeholders should not be treated as a means in increasing corporate ends (Evan and Freeman, 1988). Among the early scholars applying Kantian arguments to stakeholder theory were Evan and Freeman (1988). According to them, stakeholder rights are seen as a key element that needed to be ensured by the corporation and its managers. Indeed, Evan and Freeman (1988) had contended that the corporation and its managers should not act to 'violate the legitimate rights of others [in order] to determine their own future'(p. 259). 'If the modern corporation insists on treating others as a means to an end, then at minimum they must agree to and participate (or choose not to participate) in the decisions to be used as such'(Evan and Freeman, 1988, p. 258). Evan and Freeman (1988) assert that the objective of the corporation must be redefined in favour of Kant's principle of respect for persons.

Even though the work of Evan and Freeman addresses Kant's respect for persons principle, it is the work of Norman Bowie (1999) that discusses other formulations of categorical imperatives, namely 'universalizability' and 'kingdom of ends' as these relate to business practices. According to him, business practices should be consistent with the three formulations of the categorical imperative. However, as Bowie (1999) himself emphasises, in terms of the relationship between the corporation and its stakeholders, the second formulation of the categorical imperative, namely 'respect for persons', has a more important role (p. 38).

According to Evan and Freeman (1988), stakeholders should have a say in decision making that has a significant impact upon their lives. Evan and Freeman (1988) suggest that some stakeholder groups should participate in decision making through their representatives, on 'the stakeholder board of directors' (p. 263). While Evan and Freeman (1988) categorise stakeholder participation in the corporation as a prerequisite for the Kantian respect for persons principle, this principle can also be interpreted as 'no stakeholder may be forced to deal with the corporation without his or her consent' (Smith and Hasnas, 1999, p. 116). This point of view 'entails not treating [employees] as things, objects, or tools in an effort to achieve one's own goals (as a manager, say) or the goals of the corporation'(Rowan, 2000, p. 357).

Therefore, corporate managers should respect the autonomy of persons (Jones, Parker and Bos, 2005). In this regard, Bowie (1999) interprets the relationship between the managers and employees at the workplace from a Kantian perspective. Here, he highlights how coercion and deception are important obstacles in treating employees as ends in themselves (Bowie, 1999, p. 48). Hence, one conclusion from a Kantian perspective can be that managers should not coerce or cheat anyone in any form and instead should work 'to develop the humane, rational and moral capacities of people' within the corporation'(Jones, Parker and Bos, 2005, p. 45).

There are certainly many corporate practices that may be considered questionable in relation to the respect for persons principle. For example, can we say child labour is ethical? In fact, one cannot easily say that it is children's 'autonomous decision' to work (Crane and Matten, 2010, p.102). Thus child labour itself can be seen as in contradiction with this principle. One could also ask 'Is it ethical for managers to fire employees in order to maximise profits?' The answer to this question may be somewhat more complicated than the previous one. As Bowie (1999) highlights, if the answer is given from Williamson's point of view, layoffs can be ethical since employees as rational actors accept the risk of being dismissed by agreeing their employment contracts.[6] However, if the managers deceive employees as to the corporation's management policies, without providing the necessary information, they simply violate the principle of respect for persons (Bowie, 1999). Consequently, for this purpose, if no other, employees should not be misled with respect to the nature of their labour contracts.

Nevertheless, even if employees are informed of all the management policies, and agree with the terms of their employment contracts as free persons, in some circumstances these choices may be made with a lack of bargaining power, rather than by free will (Bowie, 1999). As highlighted in the critique of shareholder value theory above, employees cannot renegotiate their contracts as shareholders can.

However, no matter what, the existence of asymmetrical information between the management and employees may result in the deception of 'employees regarding the necessity of certain management policies' (Bowie 1999, p. 53). Thus, even if employees accept the prospect of being made unemployed through a clause in their contracts – if a manager dismisses an employee for profit maximisation purposes, for example – this act may be viewed as being in breach of 'the respect for persons principle'. Even in such circumstances, employees should be informed. For instance, they should be informed on issues such as the financial situation of the firm (Bowie, 1999). With that sort of information, deception and coercion could be avoided, and employees can make more rational decisions.

Key aspect to the Kantian (deontological) understanding is that human beings need to be fully informed in order to make autonomous decisions (Bowie, 1999). Thus, true information may well constitute a fundamental requirement in respect of being autonomous, as a lack of transparency may constrain the freedom of rational actors (Bowie, 1999).

[6] *According to Oliver Williamson, 'the risks of layoff have been incorporated in the salary contract' (Bowie, 1999, p. 49)*

Evidence suggests that a lack of information may reduce the capacity of individuals to choose and make them act 'in a manner that is more inconsistent with their values'(Brummer 1986, p. 159).

For instance, the work of Brummer (1986) has addressed how the lack of information constrains the rational choices of shareholders. According to him, '…the policy of management misstating or omitting material facts in an intentional or knowing manner is that it leads to treating the shareholders as mere instruments of the will of the managers'(Brummer 1986, p. 160). However, the motivation of corporate disclosure that only aims to inform shareholders is problematic since lack of information may also restrain rational decisions taken by other stakeholders, such as employees. The truth cannot be described by only the financial matters useful for shareholder. Other stakeholders, such as employees, are human beings and rational actors as well. Therefore, they should be informed about matters relating to themselves.

In short, the principle of respect for persons offers us a prescription for the normative questions posed at the beginning of this paper, what the corporate objective ought to be. From the perspective of non-instrumental stakeholder theory, the interests of stakeholders should be treated as ends in themselves, and thus shareholders' interests should not be privileged above those of any other constituent group (Gamble, Kelly and Kelly, 1997). Even if treating stakeholders as ends in themselves may result in profit maximisation, the corporate objective should not focus upon instrumental value. As the evidence outlined would appear to suggest, corporate managers should offer genuine respect to employees.

Conclusion

This paper has focused its analysis upon examining what the objective of the corporation ought, in order so it may determine what may be required to improve the interests of employees. Its main focus has also been to outline, and critique the instrumental perspective of the key corporate governance approaches.

The main debate here has been between two corporate governance models, namely the shareholder value theory (SVT) and stakeholder theories. Two main approaches in favour of the SVT, the property ownership theory and contractual theories were discussed above. In this respect, most of the justifications of the SVT (including the enlightened shareholder value theory) were found predominantly economic and instrumental towards stakeholders, and therefore employees also. The paper then sought to rebut those arguments for shareholder value, before turning its attention to stakeholding, and setting out the arguments in its favour.

As the paper has noted, some of the arguments in favour of stakeholder theory are themselves consequentialist, especially those which are based upon instrumental stakeholder theories and the importance of fostering productive relationships with valuable employees. However, other arguments in favour of the ST moved beyond the economic realm to consider the importance of such values as participation within decision-making structures, which significantly affect the life of the employee, the protection of human rights, and so forth.

As it is underlined above, from deontological perspective, treating employees with genuine respect requires treating them as an end in themselves. The interests of employees should not be seen as means to increase shareholders' or corporate ends. For this purpose, within the final area of analysis, the paper argued that the objective of the corporation should be redefined from the perspective of non-consequentialist stakeholder theory. The notion stems from intrinsic value of persons had provided with the fundamental basis upon which we may argue for the elevation of employees' interests. However, it is still important to specify how this elevation of employees' interests is to be achieved, such as what strategies are required or ought to be employed. Although Kant's work merely gives weight better regarding the interests of employees, it leaves open to the reader the best way of achieving this. A future research might look for an answer to this conundrum.

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