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THE DRAMATIC SHIFT IN EMPHASIS FROM A SHAREHOLDER-DOMINATED APPROACH TO A STAKEHOLDER-ORIENTED CORPORATE GOVERNANCE MODEL

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Abstract: Corporate governance (CG) has emerged as one of the most recognized areas for researchers, academics, practitioner, and regulators over the last few decades. This paper will initially present an epigrammatic overview on key developments in corporate governance along with the intellectual foundations of the 'shareholder versus stakeholder' argument. Additionally, this study tries to analyze the contemporary shift in the perception of corporations from the shareholders wealth maximization to stakeholder's valuation. It has been noticed that investigating cross country and firm based variances in wealth distribution between diverse interest groups is likely to continue as major focus for CG study. It has been experienced that the nature of the corporation is changing around the globe, Big multinationals have been splitting into smaller liberated corporation, access to capital market is become easier and physical resources are easily replaceable and less exclusive to business strategy therefore the human resources turn into significantly important means to a corporation's existence and growth. In addition to that firm's relationships with community and goodwill are becoming equally crucial. In line with that, the implementation of corporate governance principle in every country can be vary because of their different cultural, existing legal system, environmental condition, social and historical values. In addition to the principle differences regarding the interests of the parties served, the two orientations of corporate governance also differ in terms of purpose. This means that the corporate governance evolution will be progressive and different according to individual countries. Furthermore, from a systems-based viewpoint, recent progresses are often viewed as a "mixture" of domestic CG framework. Fundamental features from stakeholder leaned system are reframed with latest aspects of equity-holder leaned models, such as comprehensibility and precision. Shareholder and stakeholder focused CG, might help to create an equilibrium or complement each other such as happening in Germany and Japan. Global standards are also playing a major role in the recent convergence of CG.

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Introduction

Corporate governance is a system designed to improve corporate performance through supervision of management performance to ensure accountability to stakeholders based on regulatory framework. The concept of corporate governance developed into a very interesting issue since the occurrence of important events in the business world (Taylor, 2010). An attention to the importance of corporate governance increased after the big scandals that occurred in the U.K and the U.S companies, in the 1980s. This is inseparable from the conflict of interests between personal freedom and responsibility to the common interest of the organization, which makes it a trigger of the need for 'good' corporate governance (Boyd (1996); Keasey et al., (1997)).

The last decade has seen a rapid development in corporate governance systems around the world (Shleifer & Vishny (1997); Aguilera & Jackson (2010)). However, the theoretical discussion of corporate governance system is still dominated by a debate between shareholder approach and stakeholder approach (Bottenberg et al.,2017). Each of these adherents of the approach seeks to convince with rationality, argument, and reason that are equally strong.

For decades, maximizing shareholder wealth has become a dominant corporate focus and goal (Lazonick & O'Sullivan, 2000). In recent time, this view has been challenged by the growing of stakeholder theory, assert that the company interacts not only with shareholders, but also other stakeholders, such as employees, consumers, creditors, and surrounding communities, where they have own respective roles in corporate governance systems (Smith (2003); Pfarrer (2010)). Furthermore, many parties questioned the corporate governance convergence around the world ((Shleifer & Vishny (1997); Monks & Minow (2011)).

This paper will primarily criticize the suggestion mentioned by Forbes, et al.,(2013) that there is a dramatic shift in emphasis in Corporate Governance from a shareholder-dominated approach to

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corporate governance to a stakeholder-oriented corporate governance model, both in practice and in academic literature. This essay begins by reviewing the corporate governance concept. Further discussion will lay down some major points regarding the two noteworthy approaches, especially the various matters relating to the characteristics underlying each perspective by presenting academic view related to the global convergence of corporate governance systems.

Corporate Governance Concept

The concept of corporate governance has existed and evolved since the concept of corporation was introduced in the UK in the mid-nineteenth century (Ireland, 2010).This concept then derives various definition, theories, & models as follows:

Corporate Governance Definition

There is no single definition of corporate governance (Solomon, 2013). Shleifer & Vishny (1997) explain that 'corporate governance' is concerned with how 'financial suppliers' of the companies make sure they get a return on their investment. Furthermore, in Cadbury report, corporate governance is defined as a system that directs and controls the company, to ensure its sustainability and accountability (Cadbury, 1992). This definition is close to the Organization of Economic Co-operation and Development (OECD)'s understanding that corporate governance structure determines the distribution of rights and responsibilities among various participants, such as boards, managers, shareholders, and other stakeholders, and explains the procedures for making decisions regarding company affairs that determine the company's direction (OECD, OECD Principles of Corporate Governance, 1999).

Corporate Governance Theories

The two main theories associated are Stewardship Theory and Agency Theory. Stewardship theory views management as trustworthy to act as best as possible for the public interest in general as well as shareholders (Donaldson & Davis (1991); Mallin (2016)). Meanwhile, Jensen & Meckling (1976) through Agency Theory explain how contractual relationships between the owners (principals) delegate certain decision-making to improve their welfare and the management who receives the delegation. Contrary to Stewardship Theory, Agency Theory considers that management cannot be trusted to act the best for the principals' interest (Solomon (2013); Mallin (2016)).

Moreover, there are two other common theories related to corporate governance. One of them is Shareholder Theory that is framed in its current form by Milton Friedman, who argues that the main task of management is to maximize shareholder returns (Stout, 2013). This is also links to the Agency Theory since they are conferred with the principals' power to generate profits and the management's responsibility to increase the investors' wealth. The proponent of Shareholder Theory believes that when the company is run to maximize shareholder value, the performance of the whole economic system can be improved (Smith (2003); Stout (2013)). Secondly, in 1984, Freeman presented Stakeholder Theory that begins with the assumption that values are explicit and undeniably part of business activities (Freeman et al., 2010). Unlike Agency Theory that focuses exclusively on shareholder interests, Stakeholder Theory concentrate on all party's interests, such as customers, suppliers, and neighbouring communities since they can be affected by the success or failure of a corporation. Furthermore, an effective implementation of corporate governance cannot be explained by one theory, but it is best to combine theoretical variations (Abdullah & Valentine (2009); Solomon (2013)).

Corporate Governance Models

As mentioned before, there are two main different corporate models, shareholders-oriented model and stakeholders-oriented model (Maher & Andersson, 1999), as follows:

Shareholders-Oriented Model

The Concept

The concept of the shareholders-oriented model is concerned with the principal-agent relationship between shareholders and management (Jeffers, 2005). Shareholders-oriented approach refers to a system, which gives the shareholders' interest the highest priority and will therefore first and foremost the management will try to create maximum value for them (Smith (2003); Brandt & Georgiou (2016)). This fundamental idea is manifested in the legal framework of Anglo-Saxon countries, such as the U.S. and the U.K.

Shareholder-oriented model is characterized by very much dispersed ownership: shareholders control the managers' activities through their right to vote, in accordance with their shareholdings. When the owners are dissatisfied, they can sell their shares as a sign of mistrust, thereby opening the possibility of a takeover, followed by changes in the board's composition. In this context, corporate governance system tends to support profit maximization: indeed, it allows companies to meet shareholder expectations for short-term remuneration and the market forces become influential in the resource allocation process, where companies adapt their strategy based on capital market demand ((Smith (2003); Salvioni, et al.,(2016)).

The Issue

The academic support brings shareholder-oriented model to achieving dominance by the end of millennium. However, the application of the shareholder-value principle reap some criticism. This model, which is only emphasizes the interest of shareholders, is considered ineffective in supporting the implementation of good corporate governance (Brandt & Georgiou, 2016). Many people believe that shareholders are not the only ones investing in the company. The ultimate success of a company is the result of teamwork that embodies the contributions of different resource providers including investors, employees, creditors, suppliers, and customers (Maher & Andersson (1999); Smith (2003)). Moreover, after the scandal and global crisis, such as Enron and Worldcom, the premise of a shareholder-oriented perspective has risen in question (Smith, 2003).

Furthermore, another substantial argument against a shareholder approach is that it is said to support the "short-term" decision because shareholders have power in a company and can even get managers fired, then management has a very strong incentive to meet the demands and interests of shareholders. Threats to support short-term and endanger the wellbeing of the company in the long run are the real thing (Brandt & Georgiou, 2016).

Stakeholders-Oriented Model

The Concept

The basic idea of a stakeholder-oriented model is to consider the interests of various stakeholders. In 1984, Freeman published his landmark book, which point out that the relationship between corporations and stakeholders in the social context is conducted within the framework of a "long-term relationship" in both contribution and risk sharing that will affect the achievement of corporate objectives. Specifically, the "welfare" of all stakeholders should be taken into consideration in making decisions (Freeman et al., 2010). Monks and Minow (2004; 2011) advocate that effective corporate governance should be developed to deal with various stakeholders in determining the company's performance.

Moreover, in most of European Continental and Asian Countries, both laws and policies support the stakeholder-oriented approach, which believe that the company has a purpose to advance the interests of stakeholders, not only shareholders but also employees, suppliers, creditors, or other stakeholders (La Porta, et al.(1998); Jeffers (2005)). Stakeholders-oriented proponents believe that corporate social responsibility (CSR) should go beyond the act of maximizing profits for shareholder, that the welfare created by a company is not necessarily limited to the interests of shareholders but also to the interests of all parties related (Freeman et al.(2010); Salvioni et al.(2017)).

The Issue

Indeed, the Stakeholders Theory, as a basic concept of stakeholders-oriented approach, offers a more holistic approach that includes more parties than the Shareholder Theory. However, it is also detrimental to its critics. According to Jensen (2001), Stakeholder Theory should not be considered as a valid competence theory because it does not provide the full specification of the objective function of the company. Unlike the clarity given by one objective of shareholder theory, stakeholder theory leads managers to multiple goals, creating confusion, conflict, inefficiency, and competitive failure for the organization (Jensen, Value Maximization, Stakeholder Theory, and the Corporate Objective Function, 2001).

Other issue related have been exemplified by scandals such as Parmalat in Italy and Vivendi in France. Additionally, in Germany, the legitimate representation of trade unions on the board of directors sometimes leads to the practice of considering these organs of control to be meaningless (Jeffers, 2005). Moreover, in Germany and Japan, management control is easy and not too expensive, where employee commitment is also high (Bottenberg et al.,2017). Yet at the same time the awards to management are also low. This lack of respect for management leads to a lack of management incentives to work well for the stakeholders' interest. Additionally, the economic difficulties faced by several countries whose systems are based on a stakeholder model have contributed to the questioning of this type of governance (Jeffers, 2005).

Global Convergence of Corporate Governance Model

According to Forbes, et al. (2013), the corporate governance concept has undergone the evolution from its current form. Similarly, Yoshikawa & Rasheed (2009) argue that there is evidence to support the convergence of specific corporate governance practices around the world. However, although empirical evidence and well developed theoretical models exist, the debate about the superiority of either model is ongoing (Bottenberg et al.(2017)). Furthermore, there is subsequent debate related to the corporate governance convergence, towards Stakeholders-Oriented Model or towards Shareholders-Oriented Model.

Change Towards Stakeholders-Oriented Models

Many researchers mentioned that the diversity of corporate governance principles has evolved over the past decade, challenging the dominant status of shareholders and stakeholder principles (Letza et al.,(2004); Witt (2004); Waldkirch (2008)). Some research indicates the development of corporate management concept starting from the concept that gives more attention to the shareholders' interest and then experienced a change towards the stakeholders' interest (Forbes, Hodgkinson, & Solomon, 2013).

Forbes, et.al (2010) suggest that a 'good' corporate governance requires accountability to flow in many directions among various stakeholders. The corporate governance framework should recognize the rights of stakeholders established by law or agreement and encourage active cooperation between the company and stakeholders (OECD, G20/OECD Principles of Corporate Governance, 2015). Moreover, According to Vinten (2001), Stakeholder theory is not a universal idea, but is now increasingly universally present, beyond the Anglo-Saxon world in influential economies such as Japan, France and Germany. They even found that in the U.S., it is calculated that 75 percent of those working in the company recognize the meaning of stakeholder terms.

Furthermore, according to Aguilera & Jackson (2003), the corporate governance is the result of interaction among many stakeholders. For example, markets for corporate control can serve shareholders by reducing unprofitable investments, but may also face resistance from employees who are afraid of violating the beliefs about their company's specific investments. It is also adjusted the Shareholders-Oriented Model in terms of financing through equity, dispersed ownership, active markets for corporate control; and Stakeholders-Oriented Models in terms of long-term debt financing, by large block holders, weak markets for corporate control, and a rigid labor market.

Over the past few years, issues of sustainable development and corporate global responsibility have emerged as a relevant factor for the effectiveness of corporate governance. Ayuso et al.(2014) suggest that employees, creditors, suppliers, customers and local community are company's key stakeholders. The recent corporate governance code emphasizes stakeholder management practices, often related to social responsibility. An attention is given to concrete mechanisms to engage multiple stakeholders in corporate governance system and to use this mechanism to meet the needs of multiple stakeholders (Ayuso et al.,2014).

Moreover, Salvioni, et al. (2017), suggest that the emergence of the concept of CSR involves modification in a corporate governance approach, in accordance with sustainable development philosophy as an essential element for long-term success in global markets. They argue that in successful corporations, corporate governance is characterized by a wide range of objectives, in which the company should pay attention to the entire network of internal and external relationships, in accordance with approaches based on information exchange and behavioral optimization in relation to the stakeholders' expectation. CSR and sustainability require good corporate governance, based on stakeholder engagement, fairness, transparency and accountability. It is critical to long-term corporate success and to ensuring that markets deliver value across society. The broader concept of sustainability and CSR imply a shift in the spirit of government, leading to de facto convergence between different corporate governance systems throughout the world (UN Global Compact (2015); Salvioni, et al. (2017)).

Change Towards Shareholders-Oriented Models

Although many studies have found a shifting trend towards stakeholders-oriented approach, some researchers also found a changing towards shareholders-oriented model in many countries. According to Clarke (2016), The Anglo-American government system supports a dynamic market orientation with liquid capital that can quickly pursue market opportunities wherever it occurs. Likewise, Schmidt & Spindler (2002) argue that the U.S corporate governance system is the dominant system since it is more efficient in terms of economics and can adapt more quickly to changes in the market environment than the system in most of European Countries.

Furthermore, many scientists have observed that various pressures have increased on the German corporate governance system that raises questions about its sustainability in its current form (O'Sullivan (2000); Vitol (2004); Witt (2004)). Similarly, Lazonick & O'Sullivan (2000) posited that the boom in the U.S stock market encouraged convergence to the shareholder model, as this had impressed European and Japanese corporate executives about the potential of shareholder value as a corporate governance principle. Moreover, the necessity to raise amount of capital towards cross-border takeover has also led many Continental European firms list their security on London or New York Stock Exchange, thereby subjecting to Anglo-Saxon corporate governance constraint even though their main headquarters remain outside of these country (Gugler et al.,2004).

Other research by Coffee (2001) discussed the change of stakeholders oriented in Europe & Japan. He includes four areas where convergence is proven: i) formal legal reform, ii) propagation of ownership, iii) the rise of international markets for corporate control, and iv) growth of European stock markets. The influence of institutional shareholders and their increased firmness on European managers may also be a force for convergence and increasing shareholder rights in Europe (O'Sullivan, 2000).

Moreover, Hansmann & Kraakman (2000) suggest that corporate governance convergence towards the shareholder-oriented model is not only desirable and inevitable, it has already happened. The consensus on a shareholder-oriented model not only extends in the Anglo-Saxon countries, but has also grown worldwide due to the success of contemporary companies operating under this system. They argue that the shareholder model has out-competed the stakeholder model, and that economic and social globalization pressures will transform stakeholders-oriented model into shareholders-oriented model (Hansmann & Kraakman, 2000). However, a number of recent corporate scandals in the U.S have raised doubts about the superiority of the Anglo-American corporate governance model (Aguilera & Jackson, Comparative and International Corporate Governance, 2010).

Other study conducted by Yoshikawa & Phan (2001) that examined two pairs of comparative case examples to illustrate the differences of two corporate governance systems in Japan. They found that, the changes in ownership structures and institutional expectations will enforce the company to focus on maximizing shareholder value even if stakeholder interests are more emphasized. However, other study conducted by Allen (2000) mentioned that although there is a noticeable tendency of the convergence towards Anglo-American approach, reflecting the strength of the US and the UK economy, but it is difficult for Asian governance to move exactly towards shareholders-oriented system because of their uniqueness of local business culture and legal systems.

Nonetheless, Palmer (2011) mentioned that in the worldwide convergence argument, it cannot be denied that the transformation of corporate governance paradigm against the Anglo-Saxon corporate model is an unfinished portrait, although some countries have recently begun the process of changing their corporate law toward the Anglo-Saxon Shareholder Model.

Future Trend

Schmid & Spindler (2002) suggest that the convergence towards a universally best corporate governance system is not likely to be fast. Aguilera & Jackson (2003) mentioned that some companies in shareholder-oriented countries explicitly tend to follow a stakeholder-oriented approach, and vice versa. Organizations and individuals from every countries inevitably press for the adoption of "best practice" in corporate governance, and it is difficult without significant adaptation (Bottenberg et al.,2017).

Aguilera & Cuervo-Cazurra (2009) shown that there are several transnational bodies that allow the development of codes, such as the World Bank or the OECD. They promoting a similar set of practices regardless to the characteristics of the state, which can indirectly contribute to the achievement of convergence across national governments practice. In other words, they do not move corporate governance to a particular model (eg,Anglo-Saxon or Continental Europe) but lead to a more general global model (Haxhi & Aguilera, 2012).

Furthermore, one of the most challenging tasks in the reform agenda is how to develop a framework that drive a social efficient level of investment by all stakeholders while at the same time maintaining the aspect of performance accountability provided by the shareholders-oriented model (Maher & Andersson, 1999). With this in mind, OECD has articulated a set of corporate governance practices that bind the relationship among shareholders, managements, and stakeholder in connection with the rights and obligation for each party (OECD, OECD Corporate Governance Factbook 2017, 2017).

Essentially, the convergence point between the prominent shareholder model adopted by Americans and the extreme stakeholder model advocated by Europeans, may be in the sense of "socially-responsible corporate governance," a concept that seeks to unite two important themes that have not been incorporated so far: good corporate governance and corporate social responsibility (Bottenberg et al.(2017), and therefore each model tends to converge because corporate governance practices continue to grow.

Conclusion

This paper reviews the research by Forbes et al.(2013) mentioned that there is a shift in emphasis, both theory and practice, from the shareholder-dominated approach to a stakeholder-oriented approach to a corporate governance. Questions that have been raised in shareholders approach versus stakeholder approach's struggle are related to the future development of corporate governance. Many researchers belief that the long-term stakeholder-orientation of some European Continent government systems are under intense pressure to provide shareholder value. However, similar with Forbes et al. (2017), other people belief that the short-run Anglo-Saxon Shareholders-oriented approach itself is challenged by international, national, and community agencies to recognize wider social and environmental responsibilities, therefore need to be adjust. Substantially, the principles of corporate governance continue to grow, each system faces pressure to change, not only Shareholder-Oriented Model, but also Stakeholder-Oriented Model (Gugler et al.(2004); Aguilera & Jackson (2010); Clarke (2016). In line with that, the implementation of corporate governance principle in every country can be vary because of their different cultural, existing legal system, environmental condition, social and historical values. In addition to the principle differences regarding the interests of the parties served, the two orientations of corporate governance also differ in terms of purpose. This means that the corporate governance evolution will be progressive and different according to individual countries (Yoshikawa & Phan (2001); Salvolini et al.(2016)). Furthermore, in this literature review there are still limitations on empirical evidence related to the convergence process. Besides, various studies will continue to emerge regarding to the development of corporate governance in line with the globalization and paradigm shifts. In essence, the debate about convergence still needs to be resolved and should be monitored further (Young et al.,2004).

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