MAKING CG RESEARCH FIT FOR THE 21ST CENTURY: TIME FOR COURAGE: A NOTE

Gerhard Schnyder[1]

The job of a corporate governance scholar was comparatively simple back in the 1990s. It essentially consisted in figuring out what corporate governance mechanisms maximise shareholder returns. Since then, the world has changed and with it corporate governance scholarship. Not only have never ending news of corporate scandals and major financial crises – most importantly the Global Financial Crisis of 2007 and following – cast serious doubt on the desirability and effectiveness of corporate governance policies of the 1990s; but also have bigger issues – so-called 'Grand Challenges' (Ferraro et al., 2015) – changed policy makers' and the public's the demands on stock corporations.

The alarming degradation of our natural environment – including biodiversity and the climate emergency – has cast a spotlight on global issues with potentially disastrous consequences for humanity at large, making the narrow focus on firm performance – and especially shareholder value – increasingly questionable. Management scholarship has reacted with calls for research that contributes to addressing these 'Grand Challenges,' such as the environmental disasters or the increasingly unsustainable levels of economic inequality in many societies (George et al., 2016; Howard-Grenville, 2020).

Corporate governance scholarship is at the heart of these trends in at least two respects. For one, corporate governance – as the system that allocates rights and responsibilities amongst the stakeholders of the firm and thus confers more power to some and less to others (Aguilera & Jackson, 2003) – arguably has played a role in the increasing economic inequalities in advanced economies since the 1970s (Clarke & Gholamshahi, 2016). For the other, corporate governance reforms can be a key tool in the struggle towards a more sustainable economy, as the French government has recently recognised (Segrestin et al., 2021).

[1] Professor in International Management, The Institute for International Management, Loughborough University, London, U.K., Formerly at the King's College, London.

However, while the move away from the initial narrow focus of CG scholarship on shareholder value towards understanding the role of the modern corporation in society and the natural environment at large is important and long overdue, the transition is not without perils.

1.The reinvention of the wheel

One pitfall corporate governance scholars have to be wary of is to reinvent the proverbial wheel. After decades of a narrow disciplinary focus, developing the tools to tackle the big issues facing humanity in the 21st century is not an easy task for CG scholars. There is a distinct risk that corporate governance scholars rather than standing on the shoulders of the giants in other areas of the social and natural sciences will reinvent the wheel. A recent example of this phenomenon with relevance to CG research, comes from the launch of a new journal *Government & Economics*. In the introductory essay, two of the editors in chief write "we hold out great hope for the emerging field of research called government and economics, which aims to study the government's role, behavior, and incentives in a modern market economy, as well as how government action shapes the economy's performance" (Li & Maskin, 2021: 1). Needless to say, that the launch and the introductory essay drew a great deal of ridicule on social media from scholars pointing out that the discipline of Political Economy has addressed precisely these questions for a very long time (to mention but one seminal contribution: Evans et al., 1985).

'Grand Challenges' are characterised by high levels of complexity and interconnectedness of issues, which span areas of expertise that belong to different academic specialisations. This requires corporate governance scholars to look beyond their 'native' disciplines – which are dominated by economics, accounting, and finance – and seek more exchange with social scientists and natural scientists.

Joining other management scholars in addressing Grand Challenges of societal importance also requires an enhanced methodological openness. Incremental contributions based on quantitative studies that add one new variable to well-established models will certainly continue to be published in and even encouraged by certain journals, but for CG research to remain relevant in the 21st century, scholars need to embrace pluralism and start taking other disciplines more seriously.

2. Stemming or surfing the changing tide? The battle over sustainability and shareholder primacy

A second pitfall for corporate governance scholars is getting stuck in old ideological debates that see the field losing touch with the changing political and economic reality.

A striking example of this phenomenon was the fierce reaction of leading corporate governance scholars to the recent Sustainable Corporate Governance initiative and especially the EY report commissioned by the European Union.[2] The report[3] sparked a series of high-profile US-based academics from law, finance, and accounting into action and led to a frontal attack on the report's methodology, interpretations of existing literature, and conclusions.[4] This was followed by European scholars associated with the European Corporate Governance Institute (ECGI) joining forces with their American colleagues and calling for reflection on the EU proposals.[5] The backlash was also supported by some business people who castigated the reform proposal in the press.[6]

Several of the criticisms made of the EY report are certainly justified. Thus, the feedback by Mark Roe and colleagues (2000) rightly points out that the reports focus on short-termism as the main culprit for unsustainable governance would need more careful investigation and a more systematic review of the literature. Moreover, the issues of time horizon, redistributional outcomes, and externalities of different corporate governance systems that the report confounds according to its critics, would indeed need to be treated as analytically distinct.

[2] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance_en

[3] EY. 2020. "Study on directors' duties and sustainable corporate governance. Final report," https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en

[4] See Roe et al. 2020. "Feedback from: Holger Spamann" https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12548-Sustainable-corporate-governance/F594640_en

[5] https://www.law.ox.ac.uk/business-law-blog/blog/2021/04/ec-corporate-governance-initiative-series-call-reflection-sustainable

[6]https://www.ft.com/content/a2ab26b3-c9fc-4f33-a4bf-96a6e136f890

Yet, the strong rejection of the report's findings and recommendations does not seem warranted based on the critics own evidence. Thus, Roe et al (2000: 7) castigate the report's selection of literature on short-termism and suggest that important studies have been neglected. "There are dozens of empirical studies on short-termism published in economics and finance journals—we count at least 75 in economics and finance journals since 2008, with about half not finding evidence of shorttermism." The implication – that the other half of these studies does find evidence for short-termism – is not acknowledged. Short-termism as a potential problem of current corporate governance systems can therefore not as easily be dismissed as the critics imply and clearly requires further, careful research.

More fundamentally, the attack on the sustainable corporate governance initiative does smack of a staunch defence of shareholder primacy that does not fully grasp the changes in the real world. Thus, it is interesting to note that the authors almost exclusively talk about what CG reforms *should not be undertaken*, but provide precious little by way of what corporate governance reforms *can be undertaken* to address the new priorities of policy makers and societies. It is doubtful whether such a cautious and conservative approach will allow us to make corporate governance fit for the 21st century.

3. Cautious reforms with limited success

Cautious reforms of corporate governance within the shareholder paradigm have of course been undertaken for a long time – with uncertain success.

For instance, a great deal of reform efforts have focussed not on rejecting shareholder primacy, but rather on turning shareholders into a force for good. Shareholder stewardship has become both a promising area of study (e.g. Katelouzou, 2019) and a policy programme. Shareholder stewardship does not reject shareholder primacy but seeks to replace it with an enlightened shareholder approach, where shareholders do not only enjoy rights, but have duties towards companies. Using investor pressure to hold managers and directors accountable not so much for short-term shareholder value creation, but for the pursuit of socially desirable goals may be a promising approach. However, some scholars have voiced doubts about the potential of this approach without more fundamental reform of the economic system investors are embedded in (Talbot, 2011).

Similarly, reform efforts to increase diversity on company boards, notably in terms of gender but also ethnicity, are widely supported by scholars, activists, and policy makers and are expected to contribute to making corporations more socially responsible and sustainable. Yet, here too, recent studies provide evidence that there is a risk for such timid reforms to amount to little more than tokenism (e.g. for the case of India Kanojia and Khanna, 2019).

4. Courageous CG scholarship and its real-world impact

Such timid reforms do not convince scholars who see shareholder primacy as the root cause of the problem or at least an insurmountable obstacle to more sustainable corporate governance. Consequently, they advocate for a more profound set of reforms.

Thus, various research programmes and activist-led initiatives have started questioning the very fundamental of the current corporate governance paradigm, namely the purpose of the corporation. Starting in the USA with the 'Benefit corporation' movement,[7] academics in the UK and other European countries for instance have launched research programmes investigating ways to reform corporate governance laws to encourage or legally oblige corporations to pursue a purpose that goes beyond shareholder value maximisation.[8]

These various initiatives have proven remarkably influential. Most notably perhaps, the French parliament has adopted in 2019 a new law introducing a completely new type of corporate form called '*société à mission*' (mission corporation). This legal form allows companies to write social or environmental goals into the company's by-laws and to set up an ad hoc committee to monitor them, thus moving beyond the singular focus on shareholder value creation (Segrestin et al., 2021).

Similarly, while Harvard professors caution against changing director duties to encompass more than shareholder value creation (Roe et al. 2020), the UK Institute of Directors recently launched the 'Better Business Act' campaign, actively promoting a more extensive definition

---

[7] https://benefitcorp.net/

[8] E.g. Colin Mayer's Future of the Corporation programme supported by the British Academy https://www.thebritishacademy.ac.uk/programmes/future-of-the-corporation/ ; The research programme on 'Mission Companies' in France at Mines ParisTech https://www.te.minesparis.psl.eu/societes-a-mission/ and the trans-European programme The Modern Corporation https://themoderncorporation.wordpress.com/

of director duties by calling for "an amendment to Section 172 of the Companies Act that would empower directors to align the long-term interests of people, planet and profit."[9]

Given this sea change in politics and the economy, there is a risk that CG scholars lose any real-world relevance if the signs of the times are not understood and taken seriously. Warnings about unintended consequences of ill-conceived governance reforms are justified (e.g. based on the experience with the Sarbanes-Oxley Act in the USA). Yet given that "[t]he fundamental principles underlying a grand challenge are the pursuit of bold ideas and the adoption of less conventional approaches to tackling large, unresolved problems" (Colquitt & George, 2011: 432); and given the urgency with which policy makers have started moving forward, simply calling for caution will not allow CG scholars to remain relevant in the new context. Rather than caution, it may be time for courage.

References:

Aguilera, Ruth V and Gregory Jackson. 2003. "The Cross-National Diversity of Corporate Governance: Dimensions and Determinants." *Academy of Management Review* 28(3):447–65.

Clarke, T., & Gholamshahi, S. (2016). Corporate Governance and Inequality: The Impact of Financialization and Shareholder Value. In *Finance and Economy for Society: Integrating Sustainability* (pp. 27–55). https://doi.org/10.1108/S2043-905920160000011001

Colquitt, J. A., & George, G. (2011). Publishing in AMJ—Part 1: Topic choice. Academy of Management Journal, 54, 432–435.

Dmytriyev, Sergiy D., R. Edward Freeman, and Jacob Hörisch. 2021. "The Relationship between Stakeholder Theory and Corporate Social Responsibility: Differences, Similarities, and Implications for Social Issues in Management." *Journal of Management Studies* (September).

Evans, Peter B., Dieter Rueschemeyer, and Theda Skocpol. 1985. *Bringing the State Back In*. Cambridge: Cambridge University Press.

[9] https://www.iod.com/news-campaigns/news/articles/IoD-Directors-join-forces-to-make-the-case-for-a-cleaner-greener-future

Ferraro, Fabrizio, Dror Etzion, and Joel Gehman. 2015. "Tackling Grand Challenges Pragmatically: Robust Action Revisited." *Organization Studies* 36(3):363–90.

Freeman, R. E., & Harrison, J. S. (2010). Stakeholder Theory: The State of the Art. *Academy of Management Annals*, *4*(1), 403–445. https://doi.org/10.1080/19416520.2010.495581

George, Gerard, Jennifer Howard-Grenville, Aparna Joshi, and Laszlo Tihanyi. 2016. "Understanding and Tackling Societal Grand Challenges through Management Research." *Academy of Management Journal* 59(6):1880–95.

Howard-Grenville, Jennifer. 2021. "Grand Challenges, Covid-19 and the Future of Organizational Scholarship." *Journal of Management Studies* 58(1):252–56.

Katelouzou, Dionysia. 2019. "Shareholder Stewardship: A Case of (Re)Embedding Institutional Investors and the Corporation?" in *Cambridge Handbook of Corporate Law, Corporate Governance and Sustainability*, edited by B. Sjåfjell and C. M. Bruner. Cambridge, UK: Cambridge University Press.

Kanojia, Sunaina and Gunjan Khanna. 2019. "Women Directors on Corporate Boards: Evidence for good governance" Corporate Governance Insights, 1(1): 26-52. https://grfcg.in/images/Sunaina_Gunjan.pdf

Li, David Daokui and Eric S. Maskin. 2021. "Government and Economics: An Emerging Field of Study." *Journal of Government and Economics* 1(June):100005.

Roe, Mark J., Holger Spamann, Jesse M. Fried, and Charles C. Y. Wang. 2020. *The EY Sustainable Corporate Governance Report's Major Flaws: Discussion and Analysis*. Harvard University: Cambridge, MA.

Segrestin, B., Hatchuel, A., & Levillain, K. (2021). When the Law Distinguishes Between the Enterprise and the Corporation : The Case of the New French Law on Corporate Purpose. *Journal of Business Ethics*, *171*(1), 1–13. https://doi.org/10.1007/s10551-020-04439-y

Talbot, Lorraine E. 2011. "Polanyi's Embeddedness and Shareholder Stewardship: A Contextual Analysis of Current Anglo-American Perspectives on Corporate Governance." *Northern Ireland Legal Quarterly* 62(4):451–68.