SHAREHOLDERS PROFIT MAXIMIZATION AND STAKEHOLDERS INTERESTS IN CORPORATE GOVERNANCE

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Abstract

Shareholders profit maximization is seen as the traditional role of corporations as directors appointed by the shareholders feel obliged to pursue the greatest benefit of their principals even at the expense of other stakeholders. But that view is gradually conceding ground to the enlightened shareholder value approach to corporate governance arising from over-whelming public pressure on the corporations to expand their scope of interests to reflect societal dynamics. The paper argues that this minimal concession is inadequate to afford the stakeholders a fair protection in the hazardous operations of some multinational corporations in the modern world. A case is made for a shift to the pluralist approach that gives equal consideration to the shareholders and other stakeholders interests in realization of the fact that the stakeholders contribute immensely to the success of the company and suffer enormously from neglect in the course of the company's operations.

Keywords: Shareholders, Stakeholders, Corporate Governance

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Introduction

The corporate bodies whose operations impact significantly on the society do not seem to be ploughing back significant part of their enormous profits for the development of the communities in which their operations are centered. Part of the reasons for this corporate attitude is founded on the old fashioned theory that the primary purpose of the corporation is to maximise profits. The profit maximization objective is seen as the traditional role of the company and its managers.[1] The strengthening of emphasis on this traditional role of corporation is justified by its proponents as the only way of confining the directors within their duties to the company and minimizing the abuse of corporate powers.[2] It is argued by those proponents that the responsibility for providing the legal framework that would regulate company's behavior in relation to the rest of the community is that of the state and must be outside the scope of companies' legislation.[3]

This view of the traditional role of the company is in modern times increasingly coming under a barrage of attack from those who believe that the impacts of the company's operation on the people and the environment are of such significant proportion that it should be accountable, if not responsible, to the societal interests over and above those of the owners and beyond the limits of the law.[4] Motlanthe, recently emphasized that the high prevalence rate of tuberculosis in South Africa is attributed to the mining industries whose mining operations expose the mineworkers to silica dust contained in mine shafts which gives rise to silicosis. This condition is exacerbated by the failure of the corporations to provide accessible and suitable health facilities and accommodation for the workers who are compelled to reside in overcrowded hostels after travelling long distances to keep up with the demands of their engagements, thus are exposed to occupational hazards and high levels of HIV infection.[5]

Any argument that emphasizes a preference for profit maximization against the genuine societal concerns on corporate operations is rather myopic. It overlooks the long-term benefit which the recognition of other stakeholders' interests would confer on the company. Caring for the stakeholders would in the long run build goodwill and create more conducive environment for the company's operations which would translate into greater profits for the company. Such long-term benefit informed the approval by a United States court of corporate donation to a

[1] E Merrick Dodd Jr, 'For Whom are Corporate Managers Trustees' (1932) 45 *Harvard Law Review* 1145, 1146-1147.
[2] A A Berle, 'Corporate Powers as Powers in Trust' (1931) 44 *Harvard Law Review* 1049.
[3] Bob Tricker, *Corporate Governance Principles, Policies and Practices* (New York: Oxford University Press Inc, 2009) p 350.
[4] Ibid.
[5] See South African Vice President, Kgalema Motlanthe 'TB deaths down: Motlanthe' available at *http://www.timeslive.co.za/politics/ 2014/03/24/tb-deaths-down-motlanthe* accessed on 25/03/2014.

University in *AP Smith Manufacturing Company v Ruth F Barlow*[6] where Stein JSC said:

Nothing that aids or promotes the growth and service of the…university or college…can possibly be anything short of direct benefit to every corporation in the land. The college-trained men and women are a ready reservoir from which industry may draw to satisfy its need for scientific or executive talent. It is no answer to say that a company is not so benefited unless such need is immediate. A long-range view must be taken of the matter. A small company today might be under no imperative requirement to engage the services of a research chemist or other scientist, but its growth in a few years may be such that it must have available an ample pool from which it may obtain the needed service. It must also be remembered that industry cannot function efficiently or enjoy development and expansion unless it have at all times the advantage of enlightened leadership and direction. The value of that kind of service depends in great measure upon the training, ideologies and character of the personnel available.

This judicial recognition of stakeholders interests as having long-term positive impact on the company and the shareholders invariably throws up the question as to whether the director's traditional duty to the company should now be statutorily extended to the stakeholders. Seeking answers to this question requires the consideration of the relevant corporate governance theories and their implications on the companies operations and the society.

Shareholder Value Approach to Director's Duty

Shareholder value is a business term, sometimes referred to as shareholder value maximization or as the shareholder value model, which implies that the ultimate measure of a company's success is the extent to which it enriches shareholders.[7] It is the value delivered to shareholders as a result of management's ability to grow earnings, dividends and share price. In other words, shareholder value is the sum of all strategic decisions that affect the company's ability to efficiently increase the amount of free cash flow over time to the benefit of the shareholders.[8] The concept of shareholder value in corporate law stems from the traditional view of the company as an association of shareholders formed for their private gain and to be managed by its board of directors solely with that end in view.[9] The function of the company is thus seen as being to make profit for the benefit of the shareholders, and which must be the goal of the directors. As the directors are appointed by the shareholders who are the owners of the company, the function of the directors as agents of the owners, is faithfully to advance the financial interests of the owners.[10] There is no distinction in that context between the interests of the company and that of the shareholders as the company, being a statutory creation, cannot have any interests outside those of its shareholders.[11]

The initial judicial pronouncements on the duties of directors were construed in such a manner that views the company as inseparable from the shareholders. In *Re Smith and Fawcett Ltd*[12] Lord Greene MR stated the fiduciary duty of the company directors as being to act 'bona fide in what they consider – not what a court may consider – *is in the interests of the company*, and not for any collateral purpose.' In *Greenhalgh v Arderne Cinemas Ltd*[13] Evershed MR stated that the phrase 'the company as a whole' does not mean the company as a commercial entity as distinct from the corporators, it means the corporators as a general body. Similarly, in *Gaiman v National Association for Mental Health*[14] Megarry J observed that the company being an artificial entity, it

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6 26 N.J. Super. 106; 97 A.2d 186 (1953) at 112-113 (Superior Court of New Jersey, Chancery Division).

7 See 'Shareholder Value' available at http://en.wikipedia.org/wiki/Shareholder_value accessed on 10/12/13.

8 'Definition of 'Shareholder Value'' available at *http://www.investopedia.com/terms/s/shareholder-value.asp#ixzz1nlsJg7qR* accessed on 10/12/13.

9 Dodd op cit note 1 p 1146-1147

10 Lainie Rutkuow, 'Should Corporations Serve Shareholders or Society?: The Origins of the Debate' available at *http://www.corporationsandhealth.org/news/140/15/Should-Corporations-Serve-Shareholders-or-Society-The-Origins-of-the-Debate* accessed on 10/12/13. See also Paul L Davies 'Enlightened Shareholder Value and the New Responsibilities of Directors' (Lecture delivered at the University of Melbourne Law School 4 October 2005) at 2 available at *http://cclsr.law.unimelb.edu.au/files/Enlightened_Shareholder_Value_and_the_New_Responsibilities_of_Directors.pdf* accessed on 10/12/13 where he stated that the underlying theory of English and Australian company law is that directors' managerial powers are the result of a delegation from the shareholders, even if such delegation now is regarded as having a constitutional and not just an agency character to it. Consequently, the role of directors' duties is naturally seen as being focused on the promotion of the interests of the shareholders. William Lazonick and Mary O'Sullivan, 'Maximizing Shareholder Value: a New Ideology for Corporate Governace' available at *http://www.uml.edu/centers/cic/Research/Lazonick_Research/Older_Research/Business_Institutions/maximizing%20shareholder%20value.pdf* accessed on 10/12/13.

11 Compare Derek French, Stephen Mayson, & Christopher Ryan *Mayson, French & Ryan on Company Law* 28th ed (New York: Oxford University Press Inc, 2011) p.489 where the authors stated that a company has dual aspects; as an association of its members and, as a person separate from its members.

12 [1942] Ch 304 at 306 (CA) [1942] 1 All ER 542 emphasis supplied. And more recently in *JJ Harrison (Properties) Ltd v Harrison* [2001] EWCA Civ 1467, [2002] 1 BCLC 162 para 25 Chadwick LJ stated that the powers to dispose of company's property conferred upon the directors by the articles of association, must be exercised by the directors for the purposes, and in the interests, of the company.

13 [1951] Ch 286 at 291, [1950] 2 All ER 1120 at 1126 (CA).

14 [1971] Ch 317 at 330, [1970] 2 All ER 362 (ChD). See also *Brady v Brady* [1988] BCLC 20 at 40 (CA) where Nourse LJ held that 'the interests of a company, as an artificial person, cannot be distinguished from the interests of persons who are interested in it.'

is not easy to determine what is in its best interests without paying due regard to its present and future members as a whole. The interests of the company would be meaningless unless it is aligned with the interests of some identifiable individuals.[15] The word 'company' in this context is synonymous with the shareholders of the company.[16]

The promotion of shareholder value is seen as a way of keeping in check the excesses of the directors who could have inherent incentives to optimize activities and resources for themselves rather than for the shareholders.[17] Dodd,[18] in his criticism of Berle,[19] articulated the background to this narrowly conceived role of the directors as being that the directors and managers of modern large corporations are granted all sorts of novel powers by present day corporation statutes and charters, and are free from any supervision by stockholders by reason of the difficulty which the modern stockholder has in discovering what is going on and taking effective measures even if he has discovered it. The fact that managers so empowered not infrequently act as though maximum stockholder profit was not the sole object of managerial activities has led to the emphasis on the doctrine that managerial powers are held in trust for stockholders as sole beneficiaries of the corporate enterprise. Dodd believes that though the position adopted by Berle which emphasizes the pursuit of shareholder value in corporate management could have given the stockholders the much needed protection against self-seeking managers, that reason is simply inadequate in modern times to justify the concept that corporations exist for the sole purpose of making profits for the stockholders.[20]

Some of the earlier judicial decisions have given impetus to this misconceived role of directors as being to maximize shareholder value. This features prominently in those cases where the court seeks to ascertain the purpose for which the directors have exercised their powers. The court holds the view that the directors' powers must be exercised for the purpose of promoting the interests of the company and not for any collateral purpose. In *Re Lee Behrens & Co Ltd*[21] the directors had voted an annuity to the widow of the company's former managing director in the exercise of power provided in the company's constitution. Eve J struck down the payment as being not reasonably incidental to the carrying on of the company's business, and not for the benefit of, or to promote the prosperity of the company. Similarly, in *Re W & M Roith Ltd*[22] the director wished to make provision for his widow for which he procured the alteration of the company's constitution and entered into a service contract with the company to the effect that on his death his widow would be entitled to pension for life. Plowman J, following *Lee Behrens'case*, held that the transaction, though made in good faith, was not for the benefit of the company and as such not binding on the company. In *Re Cameron's Coalbrook Steam Coal and Swansea and Laugher Railway Co, Bennett's case*[23] Turner LJ said:

In the exercise of the powers given to them…[directors] must, as I conceive them, keep within the proper limits. Powers given to them for one purpose cannot, in my opinion, be used by them for another and different purpose. To permit such proceedings on the part of directors of companies would be to sanction not the use but the abuse of their powers. It would be to give effect to an illegal exercise of legal power.

In the more recent cases the courts have struck down transactions in which the directors conferred benefits on themselves or other persons other than the shareholders as a whole as not being in the interests of the company. One of such is *Neptune (Vehicle Washing Equipment) Ltd v Fitzgerald (No 2)*[24] where the court held that a sole director was not acting in the interests of the company, but in his personal interests, when he procured an ex gratia payment to himself by the company of the sum of £100,000 on termination of his service contract with the company. Similarly, in *Simtel Communications Ltd v Rebak*[25] Forbes J held that a director who released a significant quantity of stock to a customer (who already owes the company money in circumstances where there is no real prospect of recouping it) without prepayment was not acting in the best interests of the company. The purpose of the director's action was found by the court to be 'to maintain good relations with Kenny [the debtor] so as to pave the way for securing investment in the company that was to be set up on the ashes of Simtel.'[26] The courts emphasis in all the above cases

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[15] See Paul L. Davies QC, Sarah Worthington and Eva Micheler, *Gower and Davies Principles of Modern Company Law 8th ed* (London: Sweet and Maxwell, 2008) p 507.

[16] See Farouk HI Cassim 'The Duties and the Liability of Directors' in Farouk HI Cassim, Maleka Femida Cassim, Rehana Cassim, Richard Jooste, Joanne Shev and Jacqueline Yeats (eds), *Contemporary Company Law* (Cape Town: JUTA & Co Ltd, 2011) p 468.

[17] Lazonick and O'Sullivan op cit note 10.

[18] Dodd op cit note 9 p 1147.

[19] See Berle op cit note 2 p 1049 where he stated that 'all powers granted to a corporation or to the management of a corporation, or to any group within the corporation, whether derived from statute or charter or both, are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears.' And at 1074 he stated further that 'Whenever a corporate power is exercised, its existence must be ascertained and the technical correctness of its use must be checked; but its use must also be judged in relation to the existing facts with a view toward discovering whether under all the circumstances the result fairly protects the interests of the shareholders.'

[20] Dodd op cit note 18 p 1148.

[21] [1932] 2 Ch 46 (ChD).

[22] [1967] 1 WLR 432, [1967] 1 All ER 427 (ChD).

[23] (1854) 5 De GM&G 284 at 298 (Ch).

[24] [1995] BCC 1000, [1995] 3 All ER 811, [1995] 1 BCLC 352 (ChD).

[25] [2006] 2 BCLC 571, [2006] EWHC 527 (QB).

[26] Ibid para 102. At para 104 Forbes J came to the following conclusion; 'Accordingly I am satisfied that in the foregoing respects, Mr Rebak acted in breach of his duty to act in bona

is that the exercise of the directors powers and the performance of their duties must be geared at the promotion of the interests of the company, a synonym for shareholder value, any exercise of power outside the pursuit of this goal is seen as a breach of duty.[27]

Companies' legislation in some jurisdictions has codified this primary duty of directors as expounded by the common law courts. In Nigeria, for instance, section 279(1) of the Companies and Allied Matters Act of 1990 declares the relationship between the company and the director as fiduciary, and as such the director shall observe utmost good faith towards the company in any transactions with the company or on its behalf. Subsection 3 of section 279 expresses the duty of the director as being to act at all times in what he believes to be in the best interests of the company as a whole so as to preserve its assets, further its business, and promote the purpose for which the company is formed.

The South African Companies Act of 2008[28] embodies a modified version of the common law expression of the director's fiduciary duty. Section 76(2) of the Act provides that a director of a company must not use the position of a director, or any information obtained while acting in that capacity; to gain an advantage for the director, or for another person other than the company or a wholly-owned subsidiary of the company. As though this were not sufficient to guide the director in the right direction in the exercise of his duty, section 76(3) of the Act stretched this common law principle beyond equivocation by providing that the director of a company, when acting in that capacity, must exercise the powers and perform the functions of director in good faith and for a proper purpose, and in the best interests of the company.

In Lesotho the Companies Act of 2011 introduced some level of objectivity in the pursuit of shareholder value by the director. Section 63(1) of the Act provides that a director shall, when exercising powers or performing duties, act in good faith and on 'reasonable grounds' in the interests of the company. The phrase 'reasonable grounds' introduced an objective standard to the subjective duty of a director. It creates room for the court not to rely solely on the opinion of the director but to objectively assess the entire transaction to ascertain whether it indeed satisfies the requirement of the promotion of the interests of the company. This accords with the statement of Pennycuick J in *Charterbridge Corporations Ltd v Lloyds Bank Ltd*[29] that 'the proper test, I think, in the absence of any separate consideration, must be whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company.' That provision will be revisited later to discover the extent to which it permits a director to consider other interests in the performance of his duty to the company.

The United Kingdom (UK) Companies Act of 2006, which serves as model to most of the Commonwealth jurisdictions, unfortunately follows a similar pattern in section 172(1) which provides that a director of a company must act in the way he considers in good faith would be most likely to promote the success of the company for the 'benefit of its members as a whole'. The phrase 'benefit of its members as a whole' is a vindication of the common law courts decisions that the phrase 'interests of the company' is an expression of the interests of the shareholders as a whole, as the company, being a juristic person, cannot have any interests outside those of its shareholders.[30] It is evident from this analysis that the primary duty of the director as reflected in the provision is the pursuit of the shareholder value as the mandate which a director has is to promote the success of the company for the interests of the members as a whole and not for the interests of any individual shareholder or indeed the majority shareholder or shareholders[31] or other stakeholders.

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fide in the interests of Simtel. An intelligent and honest man in the position of Mr Rebak could not, in the whole of the circumstances, have reasonably believed that these transactions were for the benefit of Simtel.' See also *Primlake Ltd v Matthews Associates & Others* [2007] 1 BCLC 666, [2006] EWHC 1227 (Ch) where a de facto director was held liable as constructive trustee of funds which he procured in breach of his fiduciary duty, or by virtue of his dishonest assistance and knowing receipt of fund. At para 334 Lawrence Collins J held: 'If, as I have found, Mr Matthews was a de facto director, it follows that he was in breach of duty by enriching himself at its expense in paying large sums to himself to which he was not, and knew he was not, entitled.' And see *Colin Gwyer & Associates v London Wharf (Limehouse) Ltd* [2002] EWHC 2748 (Ch), [2003] 2 BCLC 153 the court held that where the directors had failed to separate their own interests from that of the company, their assertion that they acted in the interests of the company should be examined with care.

[27] See Brenda Hannigan *Company Law 2nd ed* (New York: Oxford University Press Inc, 2009) p 205 where the author stated that at common law, the directors were under a fiduciary duty to act bona fide in what they considered to be in the interests of the company, interpreted as meaning in the interests of the shareholders as a general body.

[28] Act 71 of 2008.

[29] [1970] Ch 62 at 70. Cf *Regentcrest plc v Cohen* [2001] 2 BCLC 80 at 105 (ChD) where Jonathan Parker J said: 'The question is not whether, viewed objectively by the court, the particular act or omission which is challenged was in fact in the interests of the company; still less is the question whether the court, had it been in the position of the director at the relevant time, might have acted differently. Rather, the question is whether the director honestly believed that his act or omission was in the interests of the company. The issue is as to the director's state of mind.' This principle is certainly inapplicable under the present provision of the Lesotho Companies Act.

[30] See *Greenhalgh v Arderne Cinemas Ltd* [1951] Ch 286 at 291, [1950] 2 All ER 1120 at 1126 (CA), *Gaiman v National Association for Mental Health* [1971] Ch 317 at 330, [1970] 2 All ER 362 (ChD). See also *Brady v Brady* [1988] BCLC 20 at 40 (CA).

[31] See Mark Arnold and Marcus Haywood, 'Duty to Promote the Success of the Company' in Simon Mortimore QC (ed)

The pursuit of shareholder value by the company has come under a barrage of criticisms. Martin quoted Jack Welch as referring to the concept as the 'dumbest idea in the world' stating that shareholder value should be seen as a result, not a strategy, as the company's main constituencies are the employees, the customers and its products.[32] The concept has also been described in some quarters as a short-term approach to company's business, which lays emphasis on immediate profits in preference to long-term growth, and which is bad for the economy.[33] Short-term business maximization, it is observed, does not necessarily increase shareholder value. If a business sells sub-standard products to reduce cost and make a quick profit, it damages its reputation and therefore destroys competitive advantage in the future.[34] While a focus on shareholder value can benefit the owners of a corporation financially, it does not provide a clear measure of social issues like employment, environmental issues or ethical business practices. A management decision can maximize shareholder value while lowering the welfare of third parties. It can also disadvantage other stakeholders such as customers, for a company could in the pursuit of shareholder value cease to provide support for old, or even relatively new products.[35] Lazonick observed that corporations pursuing shareholder value are invariably devoting increasing amounts of the considerable and growing financial resources to redistribution rather than innovation with the effect that corporate profits are increasingly going to share buybacks and dividend distribution, but very little is going into research and development efforts, capital reinvestments and employment.[36] Dodd contends that the role of business in the community is not limited to profit-making, it also has social function which is why it is permitted by law. 'Accordingly, where it appears that unlimited private profit is incompatible with adequate service, the claim of those engaged therein that the business belongs to them in an unqualified sense and can be pursued in such manner as they choose need not be accepted by the legislation.'[37] Booth observed, from an economic perspective, that there is no theoretical justification in economics to support creating shareholder value, when it is simply a transfer of wealth from other claimants on the firm to the shareholders.[38]

Some earlier judicial pronouncements significantly articulated the dynamics of corporate practices and societal change which justify a shift from the rigid and primordial concept of shareholder value as the only corporate purpose. In *Steinway v Steinway & Sons*[39] the New York Supreme Court observed that 'as industrial conditions change, business methods must change with them, and acts become permissible which at an earlier period would not have been considered to be within corporate power.' In *A P Smith Manufacturing Co. v Ruth F. Barlow*[40]Stein JSC stated that the 'emancipation from earlier constricting attitudes and holdings is part of the judicial growth and public service.' This buttresses the court's positive disposition to imbibing new approach in defining corporate purpose. In *Hutton v West Cork Rly Co*[41] Bowen LJ expressed the judicial willingness to accommodate other stakeholders interests in the exercise of the directors duties so long, but only so long, as it promotes the interests of the company. His Lordship conveyed this massage in captivating words which have continued to serve as reference points in discussions on this concept. He said:

The law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company…. It is not charity sitting at the board of directors, because as it seems to me charity has no business to sit at boards of directors qua charity. There is, however, a kind of charitable dealing which is for the interest of those who practice it, and to that extent and in that garb (I admit not a philanthropic garb) charity may sit at the board, but for no other purpose.

In a more recent decision of the Canadian Supreme Court in *Peoples Department Stores Inc. (Trustee of) v Wise*[42] the court was more direct in

Company Directors Duties, Liabilities, and Remedies (New York: Oxford University Press Inc 2009) p 254-255.

[32] Roger L. Martin, 'Fixing the Game: Bubbles, Crashes, and What Capitalism Can Learn from the NFL' *Harvard Business Review Press* 2011 referred to at *http://www.forbes.com/sites/stevedenning/ 2011/11/28/maximizing-shareholder-value-the-dumbest-idea-in-the-world/4/* accessed on 13/12/13.

[33] See French, Mayson, & Ryan, op cit note 11 p 490 referring to the observations made by the Commission of Public Policy and British Business, 'Promoting Property: a Business Agenda for Britain' (London: Vintage, 1997).

[34] See 'Shareholder value' available at *http://en.wikipedia.org/ wiki/Shareholder_value* accessed on 13/12/13.

[35] Ibid.

[36] Marshall Auerback William Lazonick, 'The Myth of Maximizing Shareholder Value' available at *http://ineteconomics.org/ institute-blog/myth-maximizing-shareholder-value* accessed on 01/05/2014.

[37] Dodd op cit note 20 p 1149.

[38] Laurence Booth, 'What Drives Shareholder Value?' (A paper presented at the Federated Press 'Creating Shareholder Value' conference, October 28, 1998) available at *http://www.exinfm.com/pdffiles/value.pdf* accessed on 13/12/13.

[39] 17 Misc. 43, 40 NYS 718, 720 (1896).

[40] 26 NJ Super 106 (1953) 97 A 2d 186 (Superior Court of New Jersey, Chancery Division).

[41] (1883) 23 Ch D 654 at 673 (CA). Bowen LJ cited an example of the decision in *Hampson v Price's Patent Candle Co* (1876) 45 LJ Ch 437 (CA) where it was held that the company might lawfully expend a week's wages as gratuities for its servants because that sort of liberal dealings with servants eases friction between masters and servants, and is, in the end, a benefit to the company.

[42] [2004] 3 S.C.R. 461, 2004 SCC (Canlii) at para 42. Interestingly, the court was interpreting the provisions of section 122(1) of the Canadian Business Corporations Act of 1985 bearing a provision reminiscent of the promotion of shareholders value in the strict sense. The provision is as

expressing its willingness to accommodate stakeholders interests in the exercise of directors duty. Major and Deschamp JJ said:

We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.

In *BCE Inc v 1979 Debentureholders*[43] the court emphasized that the fiduciary duty of the directors to the corporation is a broad, contextual concept. It is not confined to short term profit or share value, and as such the corporation as a going concern must look to its long term interests. This minimal concession by the courts to the consideration of stakeholders interests by the directors in the discharge of their responsibilities to the company is now encapsulated by writers as the concept of enlightened shareholder value approach to corporate governance.

Enlightened Shareholder Value Approach

Enlightened shareholder value approach to a director's duty entails an obligation on the director to pursue the interests of the company for the benefit of the shareholders by taking due cognizance of all relevant factors including a proper balanced view of the short and long term benefits to the company; the need to sustain effective ongoing relationships with employees, customers, suppliers and others; the need to maintain the company's reputation, and to consider the impacts of its operations in the community and the environment.[44] The concept is propelled by the understanding that company's operations have very wide reach and as such all the stakeholders' interests, not just the shareholders, should be considered in the discharge of the responsibilities of directors. There is a symbiotic relationship between the company and the society as the long-term viability of the corporation depends upon its responsibility to the society of which it is part, and the well-being of society depends upon profitable and responsible business enterprise.[45] This relationship evolves into what is described as the triple-bottom line (social, economic and environmental concerns) approach to corporate governance. The economic aspect concerns financial and non-financial demands of the company, environmental aspect relates to considerations of the impacts of corporate operations on the environment, and the social concerns addresses the relationships of the corporation and the stakeholders other than shareholders.[46] These other interests, however, remain subordinate to the shareholders interests[47] and could be pursued by the directors only to the extent that the protection of those other interests promotes the over-riding interests of the shareholders.[48] Accordingly, the consideration of ethical, charitable or environmental concerns are important only in the realization that there disregard could, at least in the long-term, lead to losses for the shareholders.[49] It is in that regard that enlightened shareholder value has been described as involving the requirement of paying attention to typical stakeholder interests as a means of fostering shareholder long-term wealth.[50] Such long-term benefit could be inferred from the reflections on this concept by Carrillo who observed that increasingly consumers prefer to buy products from companies they trust, suppliers are interested in business partnerships with companies they can rely on, large investment funds favour socially responsible firms, and that most respected NGOs prefer to cooperate with companies conciliating their investment interests with community goals.[51]

follows: '122(1) Every director and officer of a corporation in exercising their powers and discharging their duties shall (a) act honestly and in good faith with a view to the best interests of the corporation.' See also *BCE Inc v 1976 Debentureholders* 2008 SCC 69 (CanLII), [2008] 3 SCR 560 paras 39 and 40.

[43] 2008 SCC 69 (CanLII), [2008] 3 SCR 560.

[44] Simon Deakin and Ajit 'Shareholder Value Reconsidered' available at *Sing hhttp://www.cbr.cam.ac.uk/pdf/Anniv_Conf_Deakin _Singh_Presentation.pdf* accessed on 13/12/13. Taken from UK Company Law Review Steering Group, 2000. This understanding of the concept was reiterated by Davies where he stated that the directors must take into account 'any need of the company' to have regard to the interests of its employees; business relationships with suppliers, customers and others; the impact of its operations on the community and the environment; and to maintain a reputation for high standards of business conduct. As far as directors' duties are concerned, this is the heart of the ESV approach. See Davies op cit note 10 p 5.

[45] Jia Lynn Yang, 'Maximizing shareholder value' available at *http://www.journalgazette.net/article/20130902/BIZ/3090299 88* accessed on 01/05/2014.

[46] Irene-Marie Esser, 'The Protection of Shareholder Interests in Terms of the South African *King III Report on Corporate Governance:* An Improvement on *King II*?' (2009) 21 *South African Mercantile Law Journal* 188 at 192.

[47] See 'The code of directors' duties' available at *dutieshttp://www.out-law.com/page-8206* accessed on 13/12/13. It does not necessarily imply the elevation of other stakeholders interests above that of the shareholders as suggested by Professor Ian Ramsey, 'Directors duties and stakeholder interests Viewpoint' (Australian Institute of Company Directors) available at *http://www.companydirectors.com.au/Director-Resource-Centre/Publications/Company-Director-magazine/Back-editions-2000-2009/2005/May/Directors-duties-and-stakeholder-interests-Viewpoint* accessed on 13/12/13.

[48] See Davies op cit note 44.

[49] See 'What is Corporate Governance? - A definition' available at *http://www.worker-participation.eu/Company-Law-and-CG/Corporate-Governance/What-is-CG* accessed on 13/12/13.

[50] Andrew Keay, 'Moving Towards Stakeholderism? Constituency Statutes, Enlightened Shareholder Value and All That: Much Ado About Little?' (Working Paper, 4 January 2010) p 19 available at *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=153099 0* accessed on 13/12/13.

[51] Elena F Perez Carrillo, 'Corporate Governance: Shareholders' and other Stakeholders' Interests' (2007) 4(4) *Corporate Ownership & Control* 96 at 99.

Proponents of this concept are convinced that protecting the long-term interests of the shareholders requires the company to properly manage its relationships with all of its stakeholders. A company cannot maximize the shareholder value through a systematic exploitation of its stakeholders. Companies that charge too much for their goods and services would lose customers to the competitors. Companies that charge too little may have happy customers but will be unable to meet their other financial obligations or offer new and improved products and services to the customers.[52] Thus, Martin had observed that 'if you take care of customers, shareholders will be drawn along for a very nice ride. The opposite is simply not true: if you try to take care of shareholders, customers don't benefit and, ironically, shareholders don't get very far either.'[53] A company that fails to care for its customers could enjoy a short-term benefit, but would fizzle out once the customers are provided with alternatives by the competitors. A business that sells sub-standard products to reduce cost and make quick profit would damage its reputation and therefore destroy competitive advantage in the future.[54]

The same is true of the community and the environment in which the company operates. A company that takes care of the community and the environment builds good will and ensures the sustainability of its operations in the long-term. The recurrent communal restiveness witnessed in those regions whose environment is vastly degraded by industrial activities of corporations which consider its immediate profit interests more important than long-term planning and caring for the community and the environment presents a good example. The impact of the degraded environment such as the destruction of farm land, fishing ponds and contaminated water with the resultant health hazards to the inhabitants of the host community have in some cases given rise to armed resistance to the operations of the corporations leading to the destruction of company facilities, kidnapping of the workers and demanding of ransom and sometimes out-right killing of the employees of such corporations. Those regions have become increasingly dangerous for the operations of the corporations which are counting their losses from the stoppage of operations, damaged facilities and loss of personnel; situations which could have been avoided by factoring the stakeholders interests into those companies operations. With the greater awareness of the people of their rights to decent living in a clean and unpolluted environment, the corporations can no longer safely continue to neglect the interests of the community and the environment where they operate. The South African platinum mines present good example. The operations of the mining corporations are in recent years being undermined by incessant strikes by the workers demanding living wage. The strike had in some cases turned violent leading to destructions of lives and property.[55]

The dynamics of business and societal change have been accepted by the courts as good reasons for the consideration of stakeholders interests in corporate operations.[56] In *Teck Corp. v Millar*[57] Berger J observed:

A classical theory that once was unchallengeable must yield to the facts of modern life…. If today the directors of a company were to consider the interests of its employees no one would argue that in doing so they were not acting bona fide in the interests of the company itself. Similarly, if the directors were to consider the consequences to the community of any policy that the company intended to pursue, and were deflected in their commitment to that policy as a result, it could not be said that they had not considered bona fide the interests of the shareholders.

In *A P Smith Manufacturing Co v Ruth F Barlow*[58] Stein JSC had, while approving a modest donation of the company's fund by the directors to a University for educational purposes, reflected the

52 Michael J. Mauboussin, 'What Shareholder Value is Really About' available at *http://blogs.hbr.org/cs/2011/10/ ceos_must_understand_what_crea.html* accessed on 14/12/13.

53 Martin, op cit note 32. The correct approach is reflected in the statement of purpose by Proctor & Gamble as follows: 'We will provide branded products and services of superior quality and value that improve the lives of the world's consumers, now and for generations to come. As a result, consumers will reward us with leadership sales, profit and value creation, allowing our people, our shareholders and the communities in which we live and work to prosper.' For P&G, consumers come first and shareholder value naturally follows. Per the statement of purpose, if P&G gets things right for consumers, shareholders will be rewarded as a result.' Available at *http://www.forbes.com/ sites/stevedenning/2011/11/28/maximizing-shareholder-value-the-dumbest-idea-in-the-world/4/* accessed on 14/04/12.

54 See 'Shareholder value' available at *http://en.wikipedia.org/ wiki/Shareholder_value* accessed on 13/12/13.

55 The Marikana mine workers' strike leading to the massacre of thirty four mine workers and injuring seventy eight others in 2012 by the South Africa police in a bid to quell the violent strike by the protesting workers remains fresh in the minds of the people. See 'Marikana massacre: SAPS, Lonmin, Ramaphosa & time for blood. Miners' blood' available at *http://www.dailymaverick.co.za/article/ 2013-10-24-marikana-massacre-saps-lonmin-ramaphosa-time-for-blood-miners-blood/* accessed on 08/03/2014.

56 See *Steinway v Steinway & Sons* 17 Misc. 43, 40 NYS 718, 720 (1896).

57 (1972), 33 D.L.R. (3d) 288 (B.C.S.C.) at 314.

58 26 NJ Super 106 (1953) 97 A 2d 186 (Superior Court of New Jersey, Chancery Division). See also *Theodora Holding Corp. v Henderson* 257 A.2d 398 (Del.Ch. 1969) where Mervel VC reiterated the long-term value of corporate donation as follows: 'It is accordingly obvious, in my opinion, that the relatively small loss of immediate income otherwise payable to plaintiff and the corporate defendant's other stockholders, had it not been for the gift in question, is far out-weighed by the overall benefits flowing from the placing of such gift in channels where it serves to benefit those in need of philanthropic or educational support, thus providing justification for large private holdings, thereby benefiting plaintiff in the long run.'

long-term value to the corporation of such corporate philanthropy as follows:

It is from the millions of young men and women who are the products of higher American education that industry has picked, and will have need to pick, its scientists and its business executives. It is the youth of today which also furnishes tomorrow's leaders in economics and in government, thereby erecting a strong breastwork against any onslaught from hostile forces which would change our way of life either in respect of private enterprise or democratic self-government…. I cannot conceive of any greater benefit to corporations in this country than to build, and continue to build, respect for and adherence to a system of free enterprise and democratic government, the serious impairment of either of which may well spell the destruction of all corporate enterprise.

These realisations informed the redefining of corporate purpose by Lord Wilberforce who held in *Howard Smith Ltd v Ampol Petroleum Ltd and Others*[59] that where the issue borders on the purpose for which power is exercised, the court should begin by considering the power whose exercise is in question and then, having defined the limits within which it may be exercised, ascertain the *substantial purpose* for which it was exercised in the particular case to determine whether it was a proper purpose or not. In so doing, the court would necessarily give credit to the bona fide opinion of the directors and respect their business judgment as to matters of management.

The reference to *substantial purpose* for which power is exercised is a reaffirmation of favourable judicial disposition to the consideration of stakeholders interests by the directors in the exercise of their powers, so long as the decision reached would, in the bona fide opinion of the directors, ultimately advance the interests of the company and not informed by some by-motive, possibly of personal advantage, or for any other reason.[60] In *BCE Inc v 1976 Debentureholders*[61] the Canadian Supreme Court reiterated the essence of the business judgment rule as deferring to a business decision so long as it lies within a range of reasonable alternatives. It reflects the reality that directors who manage the corporations business and affairs are better suited to determine what is in the best interests of the corporation, and extends to decisions on stakeholders' interests, as much as other directorial decisions.

The legislature is not left out on this innovative path espoused by the judiciary. The Nigerian Companies and Allied Matters Act of 1990 provides in section 279(4) that 'the matters which the director of a company is to have regard in the performance of his functions *include* the interests of the company's employees in general, as well as the interests of its members.'[62] The word 'include' as used in that provision, suggests the expansive nature of the interests that could be considered by the director. The interests are not restricted to those specifically mentioned, so long as the ultimate end would serve the interests of the company.

The UK Companies Act of 2006 embodies provisions illustrating the expansive nature of stakeholders interests which the director shall consider in the exercise of his duty. Such matters and interests as shown in section 172(1) of the Act include the following: '(a) the likely consequences of any decision in the long term, (b) the interests of the company's employees, (c) the need to foster the company's business relationships with suppliers, customers and others, (d) the impact of the company's operations on the community and the environment, (e) the desirability of the company maintaining a reputation for high standards of business conduct, and (f) the need to act fairly as between members of the company.'

The snag here is that the duties are not enforceable by any of the stakeholders. This is shown by the provision in section 170 that duty is owed by a director, not to any of the stakeholders mentioned in section 172(1), but to the company.[63] The real essence of the statutory formulation is that the director is now under positive duty to consider the interests of the stakeholders unlike at common law where the consideration of such interests is merely permissive,[64] as such where a director in good faith and in pursuit of the company's interests, makes a decision in the wider interests of the community or the environment he would be protected from blame.[65]

In Lesotho, section 63(1) of the Companies Act of 2011 requires a director to act in good faith and on 'reasonable grounds' in the interests of the company. The Act does not define what it refers to as 'reasonable ground' under that provision. Section 63(1) is, however, subject to subsection 2 of that section which requires a director to act in the same manner as a reasonable director would act in comparable circumstances. A reasonable director would ordinarily be expected to keep abreast with the business and societal dynamics, always feel the pulse of the community and the environment where the company's operation is conducted. In pursuing the company's interests, such other stakeholders interests must be factored in as 'reasonable grounds' for corporate decision making. A director that takes such decision would not be seen to have breached the

[59] [1974] AC 821 at 835 (PC), [1974] UKPC 3 at 7 emphasis supplied.

[60] See *Hindle v John Cotton Ltd* (1919) 56 SLR 625 (HL) at 631 per Viscount Finlay.

[61] 2008 SCC 69 (CanLII), [2008] 3 SCR 560. See also *Maple Leaf Foods Inc v Schneider Corp* 1998 CanLII 5121 (ON CA), *Kerr v Danier Leather Inc* 2007 SCC 44 (CanLII).

[62] Emphasis supplied.

[63] See Mortimore op cit note 31.

[64] See Davies op cit note 48.

[65] See Mortimore op cit note 63 p 260.

provision of section 63, rather caring for the long-term interests of the company.

South Africa, like Lesotho, does not have any equivalent of the UK Companies Act provision in the sense of providing guide to the director on what should be considered in the performance of his duty. But the law in South Africa has gone a step further in ensuring that corporations are socially responsible by conferring power on the Minister of Trade and Industry to make regulations requiring certain companies identified by their annual turnover, the size of their workforce or the nature and extent of their activities to have a social and ethics committee. The Minister has accordingly responded as shown by regulation 43(1) of the Companies Regulations, 2011 which requires all state-owned companies, listed public companies or companies that have in any two of the previous five years scored 500 points in terms of the regulation to appoint a social and ethics committee whose responsibilities, as set out in regulation 43(5)(a), include the monitoring and reporting on the company's compliance with any relevant legislation, other legal requirements or prevailing codes of good practice on issues of, among others, the environment, health and public safety, including the impact of the company's activities and of its products or services.[66] This regulation which implicitly elevates the status of directors' duties to stakeholders, beyond a mere exhibition of magnanimity and to a mandatory level, failed short of explicitly empowering the directors in that regard.

It is fairly settled that the laws of the various jurisdictions in focus allow the directors limited freedom, in the performance of their duties, to consider interests of stakeholders, other than the shareholders,[67] and so long as the promotion of the interest of the company is the ultimate goal. The next question is; how satisfactory is this position of the law? In the modern world, where there is so much industrial activities resulting in pollution, other environmental degradation, health hazards and even death of humans and animals, should there not be positive and enforceable duty within the realms of companies legislation compelling the directors, in the performance of their duties, to consider the interests of stakeholders at equal length with those of the shareholders? These questions invoke the consideration of the pluralist approach to directors' duty.

Pluralist Approach

The pluralist argues for the statutory imposition of enforceable obligation on the director to consider the interests of all the stakeholders in their own rights in the performance of his duty. Shareholders' interests would become merely one of a number of interests the director would weigh against each other when making decisions.[68] This is where the difference lies with the enlightened shareholder value approach, in that the latter concept subordinates the interests of other stakeholders to the shareholders interests, and the statute[69] imposes unenforceable obligation on the directors as failure to comply does not attract any legal reproach.[70] The pluralist advocates a more radical view of a director's duty as focused on the maximization of value for the benefit of all stakeholders and not just shareholders.[71] The point is made that the only way the director would accord equal and fair consideration to all stakeholders is by statutory compulsion attained by broadening the range of groups to whom directors owe a duty. This would dilute the pressure on companies from institutional investors to provide short-term returns and would improve the company's long-term economic performance.[72] The purpose of company law, from the pluralist perspective, is not restricted to the furthering of the interests of the shareholders, but extends to the regulation of the social role of companies which imposes responsibilities on the company to consider the interests of all stakeholders

[66] For a more detailed discussion of the functions of the committee, see HJ Kloppers, 'Driving Social Responsibility (CSR) Through the Companies Act: An Overview of the Role of the Social and Ethics Committee' 2013(16) 1 *Potchetstroon Electronic Law Journal* 166

[67] Berle conceded that much to Dodd where he stated that the argument has been settled (at least for the time being) squarely in favour of Professor Dodd's contention. See AA Berle *The 20th Century Capitalist Revolution* (New York: Harcourt, Brace and Co., 1954) p 169.

[68] See Select Committee on Trade and Industry Sixth Report 'The Role of Directors' available at *http://www.publications.parliament.uk/pa/cm200203/cmhansrd/439/43906.htm* accessed on 17/12/13.

[69] Especially in Nigerian and UK Companies Act provisions respectively.

[70] Section 172(1) of the UK Companies Act has been described by Hollington as 'banality'. This was illustrated by the writer with the following poser: 'Suppose the directors fail to take into account, as part of their thinking process, the listed factors – then what? What will the court do about it? The court will not make the business decision itself and so will send it back to the directors, who will in almost all cases reach the same decision, whilst paying lip-service to the listed factors.' See Robin Hollington QC 'Directors' Duties Under The Companies Act 2006 - Have the Lunatics Taken Over the Asylum?' (Lecture delivered on 22 April 2008 Ian Fairbairn Lecture Theatre University of Buckingham) p 8 available at *http://www.newsquarechambers.co.uk/files/Publications/Directors%20duties%20under%20the%20Companies%20Act%202006%20(Robin%20Hollington%20QC).pdf* accessed on 17/12/13.

[71] See Hollington QC ibid p 5 where the writer drew a distinction between enlightened shareholder value and the pluralist approach stating that "The former is essentially the management mantra that it is good for business to take account of nice cuddly things like the community and the environment:…The Pluralist Approach was more radical: it required a different view of a director's duty as focused on the maximization of value for the benefit of all contributors not just shareholders. This took away ultimate control of a company's destiny from the shareholders.'

[72] See Select Committee on Trade and Industry Sixth Report 'The Role of Directors' available at *http://www.publications.parliament.uk/pa/cm200203/cmhansrd/439/43906.htm* accessed on 17/12/13.

such as the shareholders, employees, customers, the environment and the community.[73]

The antagonists advocate a restrictive view of the purpose of company law as a framework to promote the long-term health of companies, taking into account both the interests of the shareholders and broader corporate social and environmental responsibilities as a matter of corporate convenience. This non-obligatory responsibility of the company to the stakeholders, other than shareholders, is hinged on the conviction that the specific duty of care required of a company to its employees and the society at large are best set out in other legislation covering areas of health and safety, environment and employment.[74]

It is not in dispute that stakeholders have in the past relied, and presently still rely, on the general principles of common law and legislation, other than companies' legislation, to seek protection of their interests against adverse corporate operations. Cases of this nature are regularly found in the reports.[75] The recurrence of such cases cannot be divorced from the absence of any statutorily enforceable obligation on the director to consider the interests of stakeholders in the conduct of the company's business. Carrying along all the stakeholders would instill in the stakeholders a sense of belonging and not alienation which presently is the effect of the exclusion of such interests from companies' legislation. The inclusion of the stakeholders interests in the companies' statutes would increasingly erase antagonism and suspicion which have bedeviled the operations of some corporations, especially in the developing countries where most of the multinational corporations are seen as agents of neo-colonialism. It would create mutual understanding and conducive operating environments bereft of premeditated attacks on company facilities and reduce the number of court cases relating to the adverse consequences of company's operations.

The pluralist approach was, regrettably, found unacceptable in the UK on, among other grounds, that:

From a practical point of view, to redefine the directors' responsibilities in terms of stakeholders would mean identifying all the various stakeholder groups; and deciding the nature and extent of the directors' responsibility to each. The result would be that the directors were not effectively accountable to anyone since there would be no clear yardstick for judging their performance. This is a recipe neither for good governance nor for corporate success.[76]

Identifying stakeholders within the company's operating zone is not such an unaccomplishable task as suggested; neither are the expectations of such stakeholders on the company.[77] The community within the company's operations zone is certainly a stakeholder. Such community would ordinarily expect that the company would in the course of its operations take necessary measures to avoid all incidences of harmful environmental degradation arising from industrial pollution, offer jobs to members of the community and provide them with the essential amenities of life within the company's capacity. Customers would expect that goods which are of good standard would be provided for them by the company at competitive prices. Similarly, the employees would expect to be paid a living wage and provided safe and healthy work procedures. Interestingly, shareholders expectations on the company are equally not expressed in the companies

[73] See 'What would Professors Berle and Dodd make of the new Companies Act 2006 provisions on directors duties?' available at *http://www.ukessays.com/essays/law/berle-and-dodd-companies-act-2006-directors-duties.php* accessed on17/12/13.

[74] See Select Committee on Trade and Industry Sixth Report 'The Role of Directors' available at *http://www.publications.parliament.uk/pa/cm200203/cmhansrd/439/43906.htm* accessed on 17/12/13.

[75] See for instance; *Adams v Cape Industries plc* [1990] 1 Ch 933 (CA), *Lubbe v Cape Industries plc* [2000] 1 WLR 1545 (HL) both cases concern claims for personal injury by employees and the some members of the community in South Africa for asbestos contamination from the same company. In *Connelly v RTZ Corporation plc* [1998] AC 854 (HL) uranium mining company in Namibia sued by employee who contracted cancer for failure of the company to provide safe and healthy work procedure. See *Chinda and 5 others v Shell-BP Petroleum Development Company* (1974) 2 RSLR 1; *Shell Petroleum Development Company v Chief W. W. Amachree and 5 others* (2002) FWLR 1656; *Oronto-Douglas v Shell Petroleum Development Company and 5 Others*, Unreported Suit No. FHC/CS/573/93, Delivered on 17 February 1997; *Jonah Gbemre v Shell Petroleum Development Company of Nigeria and 2 Others*, Unreported Suit No. FHC/B/CS/53/05, Delivered on 14 November 2005, *SPDCN v Edamkue* [2009] 14 NWLR pt. 1160 at 1 (SC), *Shell Dev Co. Ltd v Otoko* [1990] 6 NWLR pt 159 (CA) for actions against multinational oil company in the Niger Delta of Nigeria bordering on environmental issues. A case is at present pending against Shell Petroleum Development Company in the UK court filed by Ogoni community in the Nigerian Niger Delta claiming compensation for environmental degradation arising from many years of oil exploration. See 'Shell in court over Nigeria oil spill compensation' available at *http://www.bbc.co.uk/news/world-africa-17486617* accessed on 13/12/13.

[76] See French, Mayson, & Ryan, op cit note 33 p 492 quoting Committee on Corporate Governance, Final Report (London, Gee, 1997) para 1.17. See also Mortimore op cit note 65 p 254.

[77] The stakeholders and their interests were captured with relish in the statement of Patricia Hewitt (then Secretary of State for Trade and Industry) as follows: 'We expect companies to generate the wealth that provides good public services and a decent standard of living for everyone. We need continuing recognition that wealth-creation demands honest and fair dealings with employees, customers, suppliers and creditors. Good working conditions, good products and services and successful relationships with a wide range of other stakeholders are important assets, crucial to stable, long-term performance and shareholder value. We expect companies to create wealth while respecting the environment and exercising responsibility towards the society and the local communities in which they operate. The reputation and performance of companies which fail to do these things will suffer.' See French, Mayson, & Ryan ibid p 32 quoting Draft Regulations on the Operating and Financial Review and Directors' Report: A Consultative Document (URN 04/1003) (London, DTI, 2004).

statute, yet the directors consciously pursue the goal of profit making in realization that the reasonable expectation of every investor is to have some returns on his investment.[78]

In India, unlike in the UK, parliament has taken a bold step by introducing a model provision in section 166 of the Indian Companies Act of 2013 expanding duties of directors to include stakeholders' interests. Section 166(2) provides that '[a] director of a company shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment.' Section 135(1)(5) of the Act ensures that the consideration of the listed stakeholders interests are not merely directory by providing that every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its corporate social responsibility policy with primary attention given to the company's local area and areas around it where it operates.

An interesting feature of this provision is that it does not only require companies to engage part of their earning on social welfare but lays emphasis on the community or environment in which the operations of the company are centered. Although the specified percentage of the profits to be applied for social goals may seem not too significant, it is at least a good starting point for a mandatory corporate involvement in the development of its operational zones and caring for the environment.

Ensuring full compliance with such statutory provision would obviously require stakeholders representation on the board. This may seem incongruous with the general view of the shareholders status as the owners of the company. But such narrow perception of the company is now outmoded. It has given way to the modern view of corporation as a corporate citizen and, as such, has social roles which must be performed within the confines of the law.

The other arm of the objection to pluralist approach suggesting that the director's duty would be difficult to enforce is not indefeasible. Under the existing law, the director does not owe duty to the shareholders individually but to the company which is seen as the body of the shareholders and, as such, duty owed to the company is a duty owed to the shareholders as a whole. Inclusion of the stakeholders would not alter this settled legal principle as the stakeholders, like the shareholders, would be subsumed within the connotation of company as a whole and protected alike. Enforcement of the duty would remain the same as the stakeholders would seek reliefs only in those circumstances in which the shareholders are empowered by the law, ie to the extent that the interest of such stakeholder is adversely affected.

Incorporating stakeholders' interests in the companies' legislation is made easier by the various courts decisions and other legislation providing for such duty which the opponents of the pluralist approach contend should be the only sources of protection for the stakeholders. Those courts decisions and legislation could be adapted in the companies' legislation, and by so doing, bring the stakeholders into the realms of company's operations as insiders having equal stakes in the success of the company with the shareholders.

Conclusion

The concept of shareholders profits maximization which is founded on the corporate pursuit of short-term shareholder value, is increasingly yielding ground to a more expansive and inclusive concept of enlightened shareholder value. The latter approach is forward looking, aimed at protecting the future or long-term interests of the company as a body of all the shareholders and stakeholders including the employees, customers, environment and the community where the company operates.

Enlightened shareholder value is accepted by the courts and companies' legislation in various jurisdictions to the extent that the interests of stakeholders are subordinated to that of the shareholders, and that any consideration of the stakeholders' interests would ultimately result in the furthering of the long-term interests of the company. What this minimal concession to stakeholders amounts to in reality is simply a legal recognition of corporate philanthropy. This is obviously inadequate to stand as a protection to the interests of the stakeholders.

What is required in modern times is a corporate governance policy that would place the stakeholders' interests at the same length as that of the shareholders. This is in realization of the fact that the stakeholders equally bear the burden of corporate operations in the same manner as the shareholders bear the burden of corporate failure. The community suffers from pollution and other environmental degradation. The lives of the employees are endangered by the absence of safe and healthy work procedures. The customers feel the impacts of substandard goods and price exploitation in the quest for profits maximization by the corporations. All these lead to court actions and sometimes communal

[78] Jia Lynn Yang attributed the pursuit of shareholders' interests by directors to the works of free-market academics in the 1970s which was picked up by business leaders and the media until it became an oft-repeated mantra in the corporate world. See 'Maximizing Shareholder value' op cit note 45.

revolts and attacks on company's property and personnel.

The solution lies on the pluralist approach to corporate governance bordering on statutorily enforceable obligation on the directors to consider the interests of the stakeholders at the same length as those of the shareholders. India has shown the way, albeit modestly, by prescribing the ploughing back of two per cent of the corporation's profits to the service of the community and the environment. It is believed that the adoption of this approach would instill in the stakeholders a sense of belonging, create harmonious relationship between the company and the stakeholders which would result in an operating environment conducive for the company for the benefit of all the stakeholders including the shareholders.