

A Multi-stakeholder Approach: Is the Role of the Modern Stakeholder Changing to one with Corporate Influence?



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«Understand stakeholder symmetry: Find the appropriate balance of competing claims by various groups of stakeholders»

Warren G. Bennis

1. Introduction

Early in the 1980, Milton Freedman and David Reed for the first time emphasized the need for stakeholder inclusions by the hypothesis that the primacy of shareholder interests at one point in time becomes completely outdated.¹ By introducing the notion of «the wide sense of stakeholder», group or individuals crucial for the achievement of objectives, and «the narrow sense of stakeholder», group or individuals crucial for the continued survival, the corporate actions shall be directed towards all groups and individuals having a stake of interest involved. In that sense, their theory was the antithesis of the at this time leading Milton-doctrine campaigning for «The Social Responsibility of Business is to Increase its Profits».²

As of today, beyond the pure interest of generating profit, the board of directors is strongly required to involve the multistakeholder-community. The positive aspect of its inclusion is that it will have an enormous impact to drive future-oriented actions forward. ESG, political risk, and resource-saving actions are just three examples. The negative aspect is that engaging with multifaceted stakeholders is also a balancing act in-between conflicting interest. Finding an adequate sense of balance between the commercial and the non-commercial interest of the various stakeholder views and the resulting requests/demands increases the complexity of the board's work.³ In addition to the economic-social-political environment that has already highly challenged the board in recent years, the stakeholder-inclusion trend is expected to intensify.

1 Freeman, R. & Reed, D. (1983). Stockholders and Stakeholders: A New Perspective on Corporate Governance. California Management Review, 25(3), 88–106.

2 Friedman, Milton (1970, September 13). The Social Responsibility of Business is to Increase its Profits. The New York Times.

3 Ingenbleek, P. T. M. and Immink, V. M. (2010). Managing Conflicting Stakeholder Interests: An Exploratory Case Analysis of the Formulation of Corporate Social Responsibility Standards in the Netherlands. Journal of Policy & Marketing, 29(1), 52–65.

However, the higher complexity the board faces is not the crucial point this article wants to emphasize. On the contrary, it is desirable to achieve the best for the organisation, the society, and the environment from a dialogue based on partnership.⁴ From the author's perspective, yet it is rather the increased (over-)influence on the board's area of responsibility by some stakeholders that this article views with skepticism. In practice, it is increasingly seen that the board is 'bound by instructions' to follow third-party recommendations to avoid criticism/potential breach of regulations. This particularly intends the forthcoming article to highlight by accentuating it with practical examples.

2. The Key Stakeholders Perspective

In principle, defining key stakeholders is company-specific and should be determined strategically by the board and the senior management. This is not a one-time but should be a constantly repeating process. Despite the company-specific individuality addressed, for the board four stakeholders have become increasingly important over the course of time that in the following it is briefly touched upon:

2.1 Institutional investors set the pace with the small shareholder becoming inventive

Since the dot-com crisis, institutional investors have greatly outnumbered private individuals and family shareholders (see figure 1). Although at the AGM the exercise of the voting right is decisive, with prerequisite to prior share register entry (30–40% of shareholders forego the entry as they invest only for dividend-purpose reasons), the trend towards over-proportionate (institutional shareholders) or under-proportionate (family or small shareholders) voting power will continue to increase.⁵ For the board/management of the companies concerned, this will cause additional work. The most obvious example is the form of influence, which can range from shareholder-friendly corporate governance structures («adapt»), the sale of shares in the event of dissatisfaction («exit»), the activist exercise of shareholder rights («voice»), or a board seat request («enter»). On the other hand, with the loss of share votes, small shareholders lack the power to effectively defend their interests, which is reflected in the formation of advisory pools («infomedaries») or protective voting associations («vote pooling»).

Figure 1: Shareholder Structure of SMI Expanded Organisation⁶

SMI Expanded (2017)	SIX notification (weighted market cap.)	SIX notification (unweighted)
By investor category:		
Institutional*	57,8	69,4
Public / state fund	4,6	5,5
Private	27,9	12,3
Non-categorizable	9,7	12,8
By institutional*:		
Investment company	29,1	51,7
Ownership / participation**	15,9	1,4
Companies	7,7	5,4

* Institutional includes: Investment companies, banks, proprietary / shareholdings, hedge funds, pension funds / funds, foundations, corporations, insurance companies.

** Companies with own-equity shares and, if applicable, in other companies.

4 Silverstein, K. (2019, 26. July). Institutional Investors Have More Power than Governments to Shape Climate Future. Forbes.

5 Horber, F. (2022, Juni). Wenn eine Minderheit eine AG kontrolliert. The Reporting Times.

6 Seiler Zimmermann, Y. & Zimmermann, H. (2019, 18. Juni). Wem gehören die schweizerischen börsenkotierten Gesellschaften? Die Volkswirtschaft.

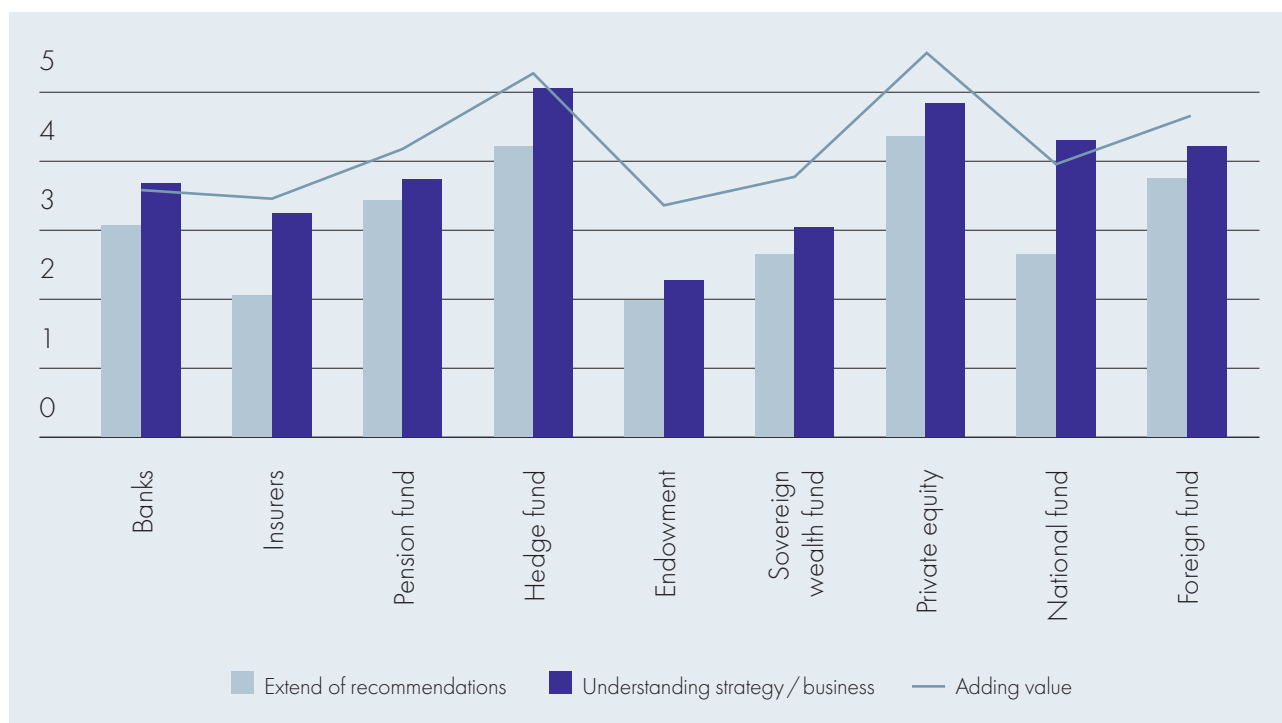
The handling of the two shareholder groups should follow the principle of equal treatment, which in practice yet increasingly ends in a patchwork problematic. Larger institutional investors often can question the strategy and provide input at the specific organized roadshows, leading to a greater proximity to board and management members and a higher information base. Having the opportunity to give company-specific feedback allows, on the one hand, to exert pressure on the board/management and, on the other hand, to align the corporate strategy with the investor-specific investment targets developed. The latter, in turn, can put the board/management in a quandary, as they have the difficult task of constantly distinguishing between goal-oriented from non-goal-oriented inputs. Consequently, there are three important questions that companies need to ask:

- What kind of institutional investors are influencing («investment style and horizon»)?

- How well do they understand the business («expertise»)?
- How strong is their added value in the feedback process («engagement»)?

In principle, all three factors are a question of (human) resources. A study that reviewed the role of the institutional investor in Germany identified that especially profit-driven investors exert high influence/pressure (see figure 2). The most prominent players among them are hedge funds, private equity, pension/national funds, and banks. Following those insights, company representatives who are in touch with institutional investors should collect the information they receive and «store» it in a central system point. This makes it possible to bundle the information and, after a strategic discussion by the board/management, to implement or discard the input accordingly.⁷

Figure 2: Institutional Investor Activity and Value-Add in a Company Perspective⁷



Note: Figure 2 shows the survey response-mean of a 6 Likert-scale (0 = none at all, 5 = very strong; N = 20)

⁷ Nix, P. (2012). The Role of the Institutional Investor in Corporate Governance: Evidence from German Corporations [Dissertation, University of Surrey].

2.2 Regulator and politics intervene in entrepreneurial decision-making

Since the financial crisis 2008/2009, the influence of the regulatory (financial services) and political (parliament, initiative) side has increased and, in some cases, has (over)crossed the board's area of responsibility. The reasons for this are manifold but can be traced back to operational limitations, the handling of capital flows, and the perception of social interests. Companies are required to implement these measures, even if they are referred to as «voluntary», because they can result in potential legal and enforcement proceedings. Well-known examples of this in recent years include (list not exhaustive):

- Business operations: In the wake of several money laundering deficiencies, FINMA for certain banks enforced the adjustment of recruitment and remuneration/sanctions policy, the prohibition for M&A transactions, and the review of independent third-party auditors;⁸
- Dividends: To restrict the decision-making power, the Cantonal parliaments submitted a motion to disempower the board of their Cantonal Banks in determining the appropriation of profits (dividend amount) and use (dividend purpose);⁹
- Board candidacy assessment: To ensure the board of director has the necessary competences as supervisory and control body, FINMA assesses every potential new board member prior to election proposal to the Annual General Meeting or the Cantonal Parliaments;¹⁰
- Board appointment: In financial services alleged to have been part of investor fraud, FINMA took control of the business management and appointed an investigative lawyer as board member;¹¹

8 FINMA (2020, 20. Februar). Schwere Mängel in der Geldwäschereibekämpfung bei Julius Bär [Medienmitteilung].

9 finews (2022, 25. April). Kanton will mehr Macht über die Dividende der ZKB. finews.ch.

10 Städeli, M. (2012, 23. Dezember). Finma greift bei ZKB ein. Neue Zürcher Zeitung.

11 Gilb, C. (2019, 13. Januar). Zug: Finma greift bei mutmasslicher Betrügerfirma ein. Luzerner Zeitung.

- Capital flow: In the wake of the COVID crisis, FINMA and the ECB demanded the temporary suspension of dividend and share buyback programs to support the economy, despite already existing capital buffers;¹²
- Human resources allocation: Due to Brexit and the exodus of investment/trading activities to other European cities such as Paris or Frankfurt, the ECB requires banks to increase their human resources and lower the passporting-exposure (cross-border transaction support from UK-based to EU-based banks and/or service providers).¹³

From the perspectives of business and industry representatives, such measures are not target-oriented. As a consequence, beyond Switzerland, the regulators work is not without criticism. Some journalists, for example, are speaking of a loss of reality on the part of the ECBs inflation policy.¹⁴ ECB policies yet have had already been criticized years before (e.g. John Cryan Ex-CEO Deutsche Bank). Another specific instance many times mentioned is the requirement to waive minus interest, penalizing safety-oriented banks with a high capital buffer.¹⁵ Also, Deutsche Industriebank (IKB) critically reflected in a blog the ECB for abusing its operational independence, which is partly due to the packages of measures that have exceeded their effectiveness (especially with regard to its influence on the real economy).¹⁶ Therefore, especially in view of the examples provided above, one has to ask: How much power can the regulator exert on entrepreneurial decisions if they miss/not fully achieve their target?

12 Finma. (2020, 25. März). FINMA unterstützt das Liquiditätspaket des Bundesrats und rollt weitere Massnahmen aus [Medienmitteilung].

13 Enria, A. (2022, 19. May). The desk mapping review – integrating Brexit banks into European banking supervision [blog]. Arnold, M. (2022, 19. May). ECB orders banks to beef up 'empty shell' operations set up after Brexit. Financial Times.

14 Rasch, M. (2022, 14. April). Die EZB verliert den Kontakt zur Realität. Neue Zürcher Zeitung.

15 Handelsblatt. (2016, 23. August). Cryan kontra Draghi. Der Deutsche-Bank-Chef hat den Glauben an die Heilungskräfte der EZB-Politik verloren. Cryan warnt, dass die lockere Geldpolitik von Notenbankpräsident Draghi inzwischen mehr Schaden anrichtet als nutzt. Handelsblatt.

16 IKB Deutsche Industriebank (2020, 3. Juli). Unabhängigkeit der EZB: In guten wie in schlechten Zeiten [Blog]?

We think it is time to critically reflect on the regulatory and political influence in corporate governance and to define a stronger dividing line between control/supervision vs. entrepreneurship/responsibility. Especially regarding the revision of Swiss Company Law with effect 1 January 2023, the responsibility of the board of directors has been confirmed and thus also applies to regulator representatives and their organisations. As it is a question often discussed with the external auditor, one has also to reflect critically whether it is time to come up with a supervisory authority that regulates the regulators.¹⁷

2.3 Proxy advisors' power in voting rights and its never-ending discussion of conflict of interests

With the change in the shareholder structure and the associated introduction of proxy voting for institutional investors in the US (2003), France (2005), and Switzerland (2014), proxy advisors have gained enormous influence. Studies have shown that their influence accounts for 10 – 20% of votes, with ISS and Glass Lewis wielding the most power with about 97% of worldwide market share.¹⁸

Despite the strong support for institutional investor in voting decisions, there is a strong voice of criticism against proxy advisors (list not exhaustive):¹⁹

- Fiduciary duty: There are no standards requiring them to demonstrate that recommendations are in the best interest of the company;
- Transparency: Ownership structures are opaque and there is no controlling authority over their actions. There is also a lack of clear criteria on how reporting is done;
- Risks of outcome: Proxy advisor are not elected by shareholders and therefore bear no reputational nor financial risks;
- Conflicts of interest: Conflicting interest occur while simultaneously advising and assessing governance structures;

17 Roy, A. (2012, 2. May). Who Regulates the Regulators? Forbes.

18 Zuckerschwerdt, A-S. (2016, 22. September). Stimmrechtsberater gewinnen an Einfluss. Die Volkswirtschaft. Choi, S., Fisch, J. & Kahan, M. (2010) The Power of Proxy Advisors: Myth or Reality? Emory Law Journal, 59(4), 869-918.

19 Larcker, D. F., Tayan, B. & Copland, J. R. (2018). The Big Thumb on the Scale: An Overview of the Proxy Advisory Industry. Harvard Law School Forum on Corporate Governance.

- Resource constraints: Reporting is often unspecific, developed with underqualified resources, and a tick-the-box design.

Although proxy advisors are not completely resistant to criticism, as evidenced by the fact that companies are now increasingly able comment against a critical proxy vote and/or proxies supporting transparency claims in who funds their activities, conflict of interest issues remain.²⁰ One such example is the intransparent and questionable ownership structure of proxies itself (see figure 3).

Figure 3: Proxy Ownership Structure

Proxy Advisor	Ownership
ISS	Deutsche Börse, Genstar Capital
Glas Lewis	Peleton Capital Management, Stephan Smith
Ethos	Fondation Ethos, Pensionskasse Post, Retraite Populaires, Caisse de Prévoyance de l'Etat de Genève CPEG, Pensionskasse Bühler Uzwil (>2%)
Inrate	Infras AG, NEST Sammelstiftung, SG Analytics, Members of Executive Management

Therefore, there are increasing calls to regulate proxy advisors. With the Minder motion (19.4122, 23.09.2019), there has been a first impulse at the level of the Swiss parliament. However, despite approval of the motion in the Council of States (Ständerat, 16.12.2019) and National Council (Nationalrat, 03.06.2020), for example, Swissholding has spoken out against its adoption. According to them, there should be no specific regulation but rather quality and transparency standards improvement in the voting criteria, in the financing source, and in sending preliminary draft reports.²¹

20 Ethos. (2017, 14. Juli). Ja zu Mehr Transparenz bei den Beratungsmandaten der Proxy Advisors (Stimmrechtsberater) [Medienmitteilung].

21 SwissHoldings (2020, 29. Mai). Empfehlungen SwissHoldings Motion Minder (19.4122) Betreffend Stimmrechtsberater [Report].

In practice, it can be recognized that more and more companies want to follow proxy recommendations because they fear additional negative consequences that could be reflected in a lower voting rate at the AGM. However, studies have shown that companies that follow voting recommendations blindly do not gain any added value.²² On the contrary, most of them had weaker operational performance and higher executive turnover. There, particularly foreign investors tend to follow proxy recommendations more closely in comparison to their national counterparts.²³ The recommendations often lack individual-specificity, clear insights on the variables taken into consideration, and weight specific favors differently (e.g. ISS focuses on governance-related variables, while Glass Lewis focuses on audit/disclosure-related variables). We thus urge companies as well as investor to cautiously decide what recommendations to implement in their voting decision.²⁴ Also, for the voting shareholders it is important to check rather twice and argue against than to blindly follow all recommendations (keyword comply or explain).

2.4 NGOs vehemently push into the boards' action

The voice of NGOs is rising. They are increasingly using social and societal pressure to vehemently insist on compliance with climate, social, and other environmental goals.²⁵ Measures to do so are in the corporate world often unusual and strongly based on guerrilla tactics. «Wir sind hier, wir sind laut, weil ihr uns die Zukunft klaut», speeches like that of Friday for Future activist Clara Mayer at the Volkswagen AGM 2019 will thus become more frequent and more difficult to handle for the chairperson steering the AGM.²⁶

In order to limit reputational risks, companies are thus often forced to seek/foster an active dialogue. This results in new forms of influence and integration features. Two of them, to counteract actionism and make a drastic outside statement, is offering board positions or collaborative partnerships.²⁷

However, a partnership should not be entered into blindly. The morals/ethics of such a partnership should be in strong agreement to set up a co-creation of engagement, for the company and the NGO.²⁸ It is also critical of offering a board position to an activist for the sole purpose of sending a sign to the outside that the company/the board takes the matter seriously. From this perspective, within board actionism will disrupt the company/board culture.²⁹ The board, which is not consensus-oriented per se but strives to present itself unified to the outside, would increasingly struggle with internal conflicts. Such conflicts would make the strategic and administrative board work more difficult and more complicated, which would further complicate the circumstance of handling the flood of information to which the board is exposed to.³⁰ As a result, in the long run, offering board positions to activists would rather harm than benefit the initial purposeful intention. From this perspective, it would thus be recommendable to compose the board with NGO/CSR expertise to proactively address the wider stakeholder community demands. There studies have shown that third-parties will start to positively acknowledge the impact post three years the expert joined the board.³¹

- 22 Larcker, D. F., McCall, A. L. & Ormazabal, G. (2013). Proxy advisory firms and stock option repricing. *Journal of Accounting and Economics*, 56(2-3), 149-169.
- 23 Balp, G. (2017). Regulating Proxy Advisors Through Transparency: Pros and Cons of the EU approach. *European Company and Financial Law Review*, 14(1), 1-36.
- 24 Mooney, A. (2019, 21 October). Proxy advisers under regulators' glare over transparency concerns. *Financial Times*. Doyle, M. (2018). The Conflicted Role of Proxy Advisors. *Harvard Law School Forum on Corporate Governance*. Choi, S. J., Jill, E. F. & Kahan, M. (2009). Director Elections and the Role of Proxy Advisors. *Southern California Law Review*, 82, 649-702.
- 25 Bruner, R. F. & Warburg, G. F. (2018). Governing NGOs: A Challenge in Four Acts. *Stanford Social Innovation Review*.
- 26 Welt.de. (2019, 15. Mai). 18-jährige Aktivistin greift VW scharf auf der Hauptversammlung an. *Welt*.

- 27 Ceesay, L. B. (2020). Exploring the influence of NGOs in Corporate Sustainability Adoption: Institutional-Legitimacy Perspective. *Journal of Business Research*, 9(2), 135-147.
- 28 Baur, D. & Palazzo, G. (2011). The Moral Legitimacy of NGOs as Partner of Corporations. *Business Ethics Quarterly*, 21(4), 579-604. Nahi, T. (2018). Co-creation for sustainable development: The bounds of NGO contributions to inclusive business. *Business Strategy and Development*, 2(1), 88-102. Hoepner, A. G. F. (2021). The Impact of NGO activism. In: Mayer, C. & Roche, B., *Putting Purpose Into Practice: The Economics of Mutuality*. Oxford University Press.
- 29 Bebchuk, L. A., Brav, A. Jian, W. & Keusch, T. (2020). Dancing with activists. *Journal of Financial Economics*, 137, 1-41.
- 30 van Ees, H., Gabriellsson, J. & Huse, M. (2009). Toward a Behavioral theory of Boards and Corporate Governance. *Corporate Governance: An International Review*, 17(3), 307-319.
- 31 Chen, S. & Hermes, N. (2022). Corporate Social Responsibility and NGO Directors on Boards. *Journal of Business Ethics*, 175, 625-649.

3. Conclusion

As have Milton Freedman and David Reed be hesitant to suggest specific strategies on how to approach the multi-faceted stakeholders, this article also foregoes to provide a best practice approach. Yet despite not having the one solution ready, the author is convinced that for addressing the emerging demands stakeholders have, to return to Warren G. Bennis's quote at the beginning, it requires an adequate balance to deal with that symmetry. As in mathematics, symmetry can be observed in time, as a spatial relationship, through geometric transformations, and through other types of functional transformations. It is therefore also important in business to adopt to different perspectives to unite the symmetrical relationships.³² This means, from a board-perspective, to find compromises to fulfil the duties and make beneficial entrepreneurial decisions and, from a stakeholder-perspective, to drive initiatives forward and establish business-environmental-friendly conditions.

32 Mainzer, K. (2005). *Symmetry and Complexity: The Spirit and Beauty of Nonlinear Science*. World Scientific.

