THE DEBATE SURROUNDING THE COMPANY PURPOSE IN THE POST-PANDEMIC AGE

Leon Anidjar†

ABSTRACT

The recent COVID-19 pandemic crisis produced many creative responses to confront its adverse results. Many companies worldwide were required to adopt innovative thinking by altering their business activities and revising their entire supply chain by attracting different types of resources delivered by various stakeholders. This Article explores the implications of this fundamental change on central theoretical assumptions of corporate governance. It articulates a new stakeholders-resources theory that explores governance norms as part of the firm's quest for inputs required to generate a competitive advantage. It applies this analytical framework in the debate on corporate purpose. This Article argues that companies have to consider the interests of diverse constituencies, as long as it affects the company's ability to produce value as an independent and separate legal entity. Moreover, it advocates a novel contingent interpretation for formulating a purpose that acknowledges the dynamic nature of business needs and incorporates the life cycle and the industry patterns to form an instructive tradeoff between efficiency, fairness, moral, and public policy considerations of understanding a company's purpose. Consequently, this Article's reformulation of the debate brings closer companies'' business challenges and the law and regulation governing companies' multi-level interactions with various constituencies to address unique encounters effectively.

† Assistant Professor, IE Law School-IE University, Madrid; Ph.D. (The Hebrew University Faculty of Law); Doctoral Candidate at the Rotterdam School of Management, Erasmus University. I wrote this paper as a Fellow at the Center for Advanced Studies on the Foundations of Law and Finance, Goethe University, Frankfurt am Main (April-June 2021). I thank Bernard Sharfman and Casimiro Nigro for their valuable comments and suggestions on earlier drafts of this paper. I am grateful to the editorial team: Julia Pjevach, Megan McCurdy, Camilla Oliva, Catherine Naas, and Henry Thomas for their superb assistance.

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I. INTRODUCTION

Following the worldwide spread of COVID-19 and the pandemic crisis, extreme policy strategies have been employed to reduce the significant infection rates and prevent the economic recession from shifting to a global depression.[1] The development of effective vaccines against the disease and the constant increase in the immunization of large populations in several European countries resulted in removing significant restrictions on movement, commerce, and social interactions among individuals. At the same time, corporations have been

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[1] *The EU Economy After COVID-19: Implications for Economic Governance*, EUR. COMM'N 1, 4 (2021), https://bit.ly/3CDgF2H [https://perma.cc/P9NC-PBYP].

confronted with the challenge of designing business strategies to address the pandemic's adverse economic and social effects. Many companies were required to adopt innovative business models which revised their entire supply chain to produce value in times of financial distress.[2] Companies have begun to rearrange their business activities and modes of operations by adopting innovative thinking that involves attracting "different types of knowledge, capabilities, skills, and resources" required to generate revenues and profit.[3]

This Article is devoted to exploring the implications of business organization transformations following the epidemic crisis for reforming fundamental assumptions of corporate governance. It uncovers a probable shift in corporate law theory due to innovative responses to the pandemic's challenges. These responses focus on increasing the collaborative efforts and knowledge-sharing between the company and multiple constituents to create value.[4] In particular, this Article argues that the crisis might produce a move in company law discourse from focusing on the traditional agency costs perspective to stakeholders-resources based theory. This last perspective explores governance norms and decision-making arrangements resulting from firms' quest for internal and external resources that they require to generate a competitive advantage.[5]

Furthermore, this Article explores the implications of the expected theoretical move by discussing the company purpose debate and distinguishing between three prominent positions in the literature.[6] According to the first approach – *weak* stakeholderism – the company's goal is to increase value for shareholders exclusively and consider stakeholders' interests for the benefit of shareholders alone.[7] The second approach – *robust* stakeholderism – considers company law devoted to tackling grand societal challenges, such as promoting

2 Stavros Gadinis & Amelia Miazad, *A Test of Stakeholder Governance*, 47(1) J. CORP. L. 47, 50–59 (2021).

3 Jan Fagerberg, *Innovation: A Guide to the Literature*, *in* THE OXFORD HANDBOOK OF INNOVATION 1, 4 (Jan Fagerberg, David C. Mowery & Richard R. Nelson eds., 2006).

4 Gadinis & Miazad, *supra* note 2, at 7 ("Our interviewees uniformly report that, as Covid disrupted modes of production long taken for granted, like office work, they came to realize how deeply interdependent their firm was to their stakeholders and sought to recreate and transform these relationships where possible.").

5 Jay Barney, *Firm Resources and Sustained Competitive Advantage*, 17 J. MGMT. 99, 102–03 (1991).

6 ANDREW KEAY, THE CORPORATE OBJECTIVE (2011).

7 *Id.* at 40.

equality, access to health care services, and, more generally, ensuring distributive justice.[8] The third approach – *moderate* stakeholderism – calls for companies to consider the interests of diverse constituencies if it affects the company's ability to create value for itself as an independent and separate legal entity.[9]

Grounded in the moderate stakeholderism understanding, this Article unveils the indeterminate patterns of the company purpose debate by advocating a contingent interpretation that balances the interests of the company's shareholders and various constituencies according to the fundamental challenges inherent in business activities. While the common discussion assumes that the goal a company has to realize is constant, this Article advances a different idea that recognizes the dynamic features of business operations and embraces the implications of the life cycle's and industry's aspects for articulating a nuanced understanding of the company purpose.

This Article proceeds as follows. It provides a brief and general overview of the innovation and business model research in Part I. Part II is devoted to exploring companies' innovative responses to recovering from adverse pandemic outcomes. These actions are expressed in two primary arrangements: (1) public-private collaboration for delivering healthcare and keeping the economy going during the pandemic, and (2) novel technology and business solutions for overcoming the pandemic's challenges. Part III, argues that business developments following the recent pandemic might result in a theoretical shift from the agency perspective to a stakeholders-resources-based view. Part IV, explores the implications of the expected theoretical move by focusing on the company goal debate and explaining why business operations' dynamics justify designing a company's purpose following the moderate stakeholderism approach that focuses on the company's interests as an independent legal persona. Part V, explains how to practically implement the moderate stakeholderism strategy by considering the life cycle and sector in which the company operates. This Article applies these considerations to explore how to articulate the purpose of financial institutions and high-tech entrepreneurial firms at different stages of their development and growth. Then, conclusions are summarized.

[8] *Id.* at 114.
[9] *Id.* at 173.

II. A PRIMER ON THE RESEARCH AND POLICY OF INNOVATION AND BUSINESS MODELS

A. *The Foundations of Innovation Strategy in the Technology Age*

Innovation is perceived as bringing new products and services to the market by increasing the quality of goods and lowering costs, thus meeting various consumers' needs.[10] By suggesting novel solutions to technological or business problems, innovation can disrupt previous markets and create new ones for the benefit of consumers and society. Moreover, innovation can decrease a product's marginal costs, which reduces pricing and increases market shares. The idea of innovation and its connection with value creation is associated with the work of Schumpeter, who introduced the concept of "creative destruction."[11] This idea refers to a "process of industrial mutation . . . that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one."[12] His theory assumes that traditional arrangements must be destroyed to free up and direct resources for creating innovation.[13] Accordingly, economic development results from internal market forces. It is produced by the opportunity to seek profit by entrepreneurs whose primary role is to allocate existing resources to new uses and combinations. Thus, creative destruction is regarded as the "essence of capitalism."[14]

The process of "creative destruction" generally involves a constant concern for firms to compete in the short-term on price and quality by marginally improving.[15] In the longer term, they also must overcome:

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10 MARK DODGSON & DAVID GANN, INNOVATION: A VERY SHORT INTRODUCTION 40-44 (Oxford Univ. Press, 2d ed. 2018).

11 JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM AND DEMOCRACY 81 (1942) [hereinafter: CAPITALISM, SOCIALISM, AND DEMOCRACY]; JOSEPH A. SCHUMPETER, THE THEORY OF ECONOMIC DEVELOPMENT: AN INQUIRY INTO PROFITS, CAPITAL, CREDIT, INTEREST, AND THE BUSINESS CYCLE 116 (1934) [hereinafter: THE THEORY OF ECONOMIC DEVELOPMENT].

12 SCHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY, *supra* note 11, at 83.

13 *Id.*

14 *Id.*

15 *Id.*

> competition which commands a decisive cost or quality advantage and . . . strikes not at the margins of the profits and the outputs of the existing firms but at their foundations and their very lives. This kind of competition is as much more effective than the other as a bombardment is in comparison with forcing a door.[16]

Creative destruction is a source of economic growth more than the traditional incremental improvements of resource allocation under price competition.[17] This is because it provides a long-run expansion of production by placing goods and services previously available only to wealthy people into the hands of all.[18]

Following Schumpeter's classification of different types of innovation,[19] the Oslo Manual distinguishes between four types of innovation[20]: (1) product innovation that refers to a good or service that is novel or significantly improved; (2) process innovation that focuses on substantially improving the methods of production or delivery; (3) marketing innovation that includes a new marketing method that involves changes in product design, promotion, or pricing; and (4) organizational innovation that suggests a novel organization method in business practices or work environment relating to the relationship between the firm and various stakeholders.[21] Therefore, innovation focuses on how the firm's activities integrate new technology or

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16 *Id.* at 84–85.

17 PHILIPPE AGHION, UFUK AKCIGIT AND PETER HOWITT, THE POWER OF CREATIVE DESTRUCTION: ECONOMIC UPHEAVAL AND THE WEALTH OF NATIONS116 (Harvard University Press, 2021).

18 Rasmus K. Hartmann, *Footnotes to Schumpeter: Foundations and Futures of Innovation Management* 11 (Feb. 17, 2021), https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3169147 [https://perma.cc/6D9H-FNSQ].

19 *See* SCHUMPETER, THE THEORY OF ECONOMIC DEVELOPMENT, *supra* note 11, at 66 (Schumpeter discerned between five types of innovation, such as introducing a new product or new product quality, introducing a unique production process, forming a new market, securing a new source of raw materials, and creating a new organizational structure in the industry.).

20 OSLO MANUAL, GUIDELINES FOR COLLECTING, REPORTING AND USING DATA ON INNOVATION 20–21 (4th ed., 2018).

21 Fariborz Damanpour, *Organizational Innovation*, OXFORD RSCH. ENCYC. OF BUS. & MGMT. 1, 2 (Aug. 22, 2017), https://oxfordre.com/business/oso/viewentry/10.1093$002facrefore$002f9780190224851.001.0001$002facrefore-9780190224851-e-19 [https://perma.cc/8558-SGUH] ("Organizational innovation research examines what external and internal conditions induce innovation, how organizations manage innovation process, and in what ways innovation changes organizational conduct and outcome.").

business ideas to generate novel products, practices, and processes across the value chain. Any innovation strategy or business model refers to how technological change can fulfill consumers' needs and increase competition by articulating the internal capabilities and collaborations required to achieve social and economic goals. Therefore, these strategies and models can be distinguished by their *outcomes, processes, and measures*. Parallel distinctions are employed between incremental versus radical (or disruptive) innovation, architectural versus component innovation, and closed versus open innovation.

Outcomes: Incremental v. radical v. disruptive innovation.[22] The incremental innovation strategy refers to a series of minor improvements made to a venture's existing products or services, extending its offerings to consumers.[23] It utilizes existing technology to fulfill consumers' demands within the current market and reinforces the dominance of established firms.[24] In contrast, a radical innovation strategy formulates a technology that generates revolutionary markets through commercializing breakthrough ideas and creating a dramatic change in market consumption patterns.[25]

In this respect, Clayton Christensen of Harvard Business School has offered the notion of disruptive innovation.[26] This refers to a process in which new ventures challenge established firms despite the former holding substantially limited resources compared to the latter.[27] In particular, "entrants may target overlooked segments of the market with a product considered inferior by incumbent's most-demanding customers and later move up-market as their product improves. Or they may create markets where no market exists and turn non-

22 CRISTIE FORD, INNOVATION AND THE STATE: FINANCE, REGULATION, AND JUSTICE 166 (2017).

23 Paul L. Robertson, G. L. Casali & David Jacobson, *Managing Open Incremental Process Innovation: Absorptive Capacity and Distributed Learning,* 41(5) RSCH. POL'Y 822, 823 (2012) ("[A]ny innovation that is not discontinuous or radical is defined as incremental. Incremental innovations, therefore, do not involve substantial changes in technical skills, knowledge, design.")

24 CHRISTOPHER FREEMAN, JOHN CLARK & LUC SOETE, UNEMPLOYMENT AND TECHNICAL INNOVATION: A STUDY OF LONG WAVES AND ECONOMIC DEVELOPMENT 69–70 (1982).

25 Stijn Smismans & Elen Stokes, *Innovation Types and Regulation: The Regulatory Framing of Nanotechnology as "Incremental" or "Radical" Innovation*, 8 EUR. J. RISK REGUL. 364, 368 (2017).

26 CLAYTON M. CHRISTENSEN, THE INNOVATOR'S DILEMMA: WHEN NEW TECHNOLOGIES CAUSE GREAT FIRMS TO FAIL 97 (1997).

27 *Id.*

consumers into consumers."[28] Thus, while radical innovation focuses on the ability of technology and the organization's capabilities to create groundbreaking change, disruptive innovation relates to the goal of the business model to target overlooked market segments and deliver products that match consumers' preferences.[29]

Process: Architectural v. component innovation. Architecture innovation focuses on improving the efficiency of the product's features instead of changing the entire system's design or function.[30] This is done by changing how the components of a product are linked together while allowing the core design concepts and the basic knowledge underlying the features to remain intact.[31] In contrast, the innovation of components occurs when changes are carried out in the materials, parts, or new modules within the same architecture.[32]

Measures: Closed v. open innovation. This distinction refers to the measures employed by companies for executing innovation.[33] While closed innovation is carried out within the corporate boundaries and is exclusively based on its internal resources, open innovation connects external knowledge and networks as part of innovation management and performance.[34] For instance, Henry Chesbrough introduced six propositions for differentiating between closed and open innovation.[35]

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28 Christian Hopp, David Antons, Jermain Kaminski & Torsten Oliver Salge, *What 40 Years of Research Reveals About the Difference Between Disruptive and Radical Innovation*, HARV. BUS. REV. (Apr. 9, 2018), https://hbr.org/2018/04/what-40-years-of-research-reveals-about-the-difference-between-disruptive-and-radical-innovation [https://perma.cc/HP3N-FUVW].

29 *Id.*

30 Rebecca M. Henderson & Kim B. Clark, *Architectural Innovation: The Reconfiguration of Existing Product Technologies and the Failure of Established Firms*, 35 ADMIN. SCI. Q. 9, 12 (1990).

31 *Id.* at 13.

32 Ashish Sood & Gerard J. Tellis, *Technological Evolution and Radical Innovation*, 69 J. MKTG. 152, 153 (2005).

33 *See generally* HENRY WILLIAM CHESBROUGH, OPEN INNOVATION: THE NEW IMPERATIVE FOR CREATING AND PROFITING FROM TECHNOLOGY (2003).

34 *See generally id.*

35 Henry W. Chesbrough, *The Era of Open Innovation*, 44 MIT SLOAN MGMT. REV. 35, 38 (2003).

Table 1. Closed v. Open Innovation[36]

#	Closed Innovation	Open Innovation
1	The smart people in the field work for the company.	Not all smart people work in the company, so it must find and rely on the knowledge and expertise of bright individuals outside the company.
2	To profit from R&D, we must discover, develop, and supply everything ourselves.	External R&D can create significant value; internal R&D is needed to claim some portion of that value.
3	If the company innovates by itself, it will get it to market first.	The company does not have to originate the research to profit from it.
4	If the company is the first to commercialize an innovation, it will beat its rivals.	The company has to be involved in basic research to benefit from it, but the discovery does not necessarily have to be made by itself.
5	It will prevail if the company creates the best ideas in the industry.	It will prevail if the company makes the best use of internal and external ideas.
6	If the company has complete control over the innovation process, its rivals will be unable to profit from its innovative ideas.	The company should profit from others’ use of its IP and buy others’ IP whenever it advances its business model.

36 *Id.*

The design of an effective business model is highly dependent on the internal capabilities of the company, such as research and development ("R&D") competencies, outside resources available from stakeholders, the external business and regulatory conditions, and the firm's risk preferences in each stage of its life cycle.[37] These risk preferences are expressed on the demand side (consumers will not consume the product of the company); on the supply side (risks associated with the management team, the product/service, the technology, and the partners); via competition risks (imitation of the products by competitors); and via capital market risks and environmental risks (such as macroeconomic, regulatory, and political concerns).[38] The business or innovation strategies consider the activities and operations required for generating value for the firm, given its risk preferences.

B. *Innovation and Business Models*

Generally, business models are defined as an "architecture of value creation, delivery, and capture mechanism" resulting from running business activities.[39] Management scholars have attributed several interpretations to the term "business model."[40] According to one interpretation, a business model is perceived as an empirical phenomenon or attribute of actual firms.[41] Business models direct "the set of activities that a firm chooses to perform, when it performs them, how it performs them, who performs them, and the resources/capabilities that it chooses to use determine the outcome."[42] As such, business models are conceptual representations of the organization's activities and how the company does business and proposes to accomplish its goals. According to another interpretation, a business model should be conceptualized as a cognitive structure that organizes managerial understanding of the design of firms' value-creating activity systems.[43]

37 OSLO MANUAL, *supra* note 20, at 103–26, 145–62.

38 RAPHAEL AMIT & CHRISTOPH ZOTT, BUSINESS MODEL INNOVATION STRATEGY: TRANSFORMATIONAL CONCEPTS AND TOOLS FOR ENTREPRENEURIAL LEADERS 333 (2020).

39 David J. Teece, *Business Models, Business Strategy and Innovation*, 43 LONG RANGE PLAN. 172 (2010).

40 Lorenzo Massa, Christopher L. Tucci & Allan Afuah, *A Critical Assessment of Business Model Research*, 11 ACAD. MGMT. ANN. 73 (2017).

41 *Id.* at 77–78.

42 *Id.* at 78.

43 Luis L. Martins, Violina P. Rindova & Bruce E. Greenbaum, *Unlocking the Hidden Value of Concepts: A Cognitive Approach to Business Model Innovation: A*

It is a thinking pattern held by executives and directs their decision-making process and outcomes.[44]

Recently, Amit and Zott provided a comprehensive understanding of the term "business model" to account for the interactions between the firm and customers, partners, mediators, suppliers, and others for value creation and appropriation.[45] They integrate the notion of innovation within the design of the business model by focusing on its novelty in terms of its content, structure, governance, and value logic to the product-market sphere in which companies compete.[46] A company can innovate at any of the four key dimensions of its business model by considering several elements.[47] These include: (1) *what* are the specific activities governed by the model (novel content);[48] (2) *how* these activities are connected (novel governance);[49] (3) *who* is carrying out each of the activities for generating value (novel structure); and (4) *why* value is created and captured according to a specific revenue model (novel value logic).[50] Because the business model considers the firm's business activities as a collaborative enterprise between the company and its stakeholders, there is a need to understand how it functions in times of financial distress that entail risks to its survival. To do so, this Article explores the pandemic's effects on transforming companies' entire activity system to ensure their resilience and stability in an unprecedented era.

III. THE INNOVATION RESPONSES TO THE PANDEMIC'S CHALLENGES AND THEIR IMPLICATIONS FOR BUSINESS MANAGEMENT

Innovation is an essential mechanism for recovering from the pandemic's adverse outcomes.[51] The innovation redress of the

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Cognitive Approach to Business Model Innovation, 9 STRATEGIC ENTREPRENEURSHIP J. 99, 105 (2015).

44 Ricardo Costa Climent & Darek M. Haftor, *Value Creation Through the Evolution of Business Model Themes*, 122 J. OF BUS. RSCH. 353, 354 (2021).

45 AMIT & ZOTT, *supra* note 38, at 47.

46 *Id.* at 96.

47 *Id.* at 22 ("Business Model Innovation Strategy four interrelated dimensions: content (What), structure (How), governance (Who), and value logic (Why).").

48 *Id.* at 88.

49 *Id.*

50 *Id.* at 95.

51 Ben Ramalingam & Jaideep Prabhu, *Innovation, Development and COVID-19: Challenges, Opportunities and Ways Forward*, ORGANISATION FOR ECON. COOP. & DEV. (OECD) (Dec. 1, 2020), https://www.oecd.org/coronavirus/policy-responses/innovation-development-and-covid-19-challenges-opportunities-and-

pandemic's consequences is expressed in two primary forms: (1) public-private collaboration and stakeholders' contributions for delivering healthcare services and keeping the economy going during the crisis;[52] and (2) novel technology and business solutions for overcoming the pandemic's challenges.[53]

A. *Public-Private Collaborations and Stakeholders' Engagement for Generating Value*

Public-private partnerships played a central role in fighting against the pandemic. These collaborations include the creation of open data-sharing platforms that provide access to epidemiological, clinical, and genomics data on the coronavirus spread among different population groups.[54] Public authorities have collaborated with private actors to conduct clinical research and trials on COVID-19. One example of such an initiative is the American Healthcare Coalition which assembled resources and expertise from large organizations, private industries, and academic institutions.[55] By coordinating the use of healthcare data and advanced analytics, this partnership aimed to reduce infection and mortality rates and enable hospitals to respond to patient needs efficiently and equally.[56] The public-private partnership also provided extensive funding to many technology ventures and

ways-forward-0c976158/ [https://perma.cc/8DGZ-AWF9]; *see also*, Sam Swapn Sinha, *How the Pandemic Has Served As A Catalyst For Innovation*, FORBES (Dec. 28, 2020), https://www.forbes.com/sites/forbestechcouncil/2021/12/28/how-the-pandemic-has-served-as-a-catalyst-for-innovation/?sh=38e596b4812d [https://perma.cc/LX85-9VT9].

52 Andrew Crane & Dirk Matten, *COVID-19 and the Future of CSR Research*, 58 J. MGMT. STUD. 280, 280 (2021).

53 OECD, SCIENCE, TECHNOLOGY AND INNOVATION OUTLOOK 2021: TIMES OF CRISIS AND OPPORTUNITY ch. 5 (2021) (ebook), https://www.oecd-ilibrary.org/sites/75f79015-en/1/3/5/index.html?itemId=/content/publication/75f79015-en&_csp_=408df1625a0e57eb10b6e65749223cd8&itemIGO=oecd&itemContentType=book [https://perma.cc/S9FN-4WEZ].

54 *Id.*

55 *24 Hours a Day, Seven Days a Week, Hospitals Care for Millions of Patients all Over America*, COAL. TO PROTECT AMERICA'S HEALTHCARE, https://protecthealthcare.org/threat [https://protecthealthcare.org/threat] (last visited Nov. 12, 2022).

56 *See COVID-19 Standards for Federated Analytics*, COVID-19 HEALTHCARE COAL., https://mcovid.org/ [https://perma.cc/VJZ7-LPKK] (last visited Oct. 23, 2022); *see also Delivering Impact and Value: COVID-19 Healthcare Coalition Members Report*, COVID-19 HEALTHCARE COAL. (July 2020), https://c19hcc.org/impact-report/ [https://perma.cc/B73Z-S4BW].

companies operating in the healthcare industry to develop diagnostics, vaccines, and other treatments against the disease.[57]

Moreover, governments have reduced the uncertainties for the private sector to become involved in combating the pandemic by investing in manufacturing capacity and advancing market commitments.[58] These measures are perceived as more effective than the traditional patent-centric innovation model to incentivize research.[59] For example, governments, private actors, and philanthropies engaged in procurement agreements committed to purchasing large volumes of the vaccine from pharmaceutical firms to encourage the development of vaccines and appropriate therapies.[60] Countries, such as the United States, the United Kingdom, Australia, Canada, Israel, and Japan contracted to purchase large amounts of vaccines that encouraged the acceleration of the development efforts among participating firms and, at the same time, secured priority access to them at the global level.[61]

While these initiatives mainly address urgent emerging needs and rely on the collaborative goodwill of the public and private sectors, several scholars have argued that the pandemic created a fertile ground for establishing medium and long-term partnerships.[62] These should tackle significant public health challenges, such as public education and advocacy, global coordination, improving healthcare access, and

57 *See Policy Responses to COVID-19*, INT'L MONETARY FUND, https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#E [https://perma.cc/E3JG-MP78] (July 2, 2021). For a policy study of the private-public partnership during the pandemic in the United Kingdom, *see* Aidan Shilson-Thomas & William Mills, *All Hands On Deck: Public-Private Partnerships During COVID-19*, REFORM (Dec. 7, 2020), https://reform.uk/research/all-hands-deck-public-private-partnerships-during-covid-19 [https://perma.cc/5AL6-6PRK].

58 *See Policy Responses to COVID-19*, *supra* note 57.

59 Robert Burrell & Catherine Kelly, *The COVID-19 Pandemic and the Challenge for Innovation Policy*, 71 N. IR. LEGAL Q. 89, 91 (2020) ("We believe the challenge lies in moving towards a more 'proactive' innovation policy: one that recognizes that a patent-centric and market-focused innovation model may result in underinvestment in promising treatment opportunities until a crisis is upon us . . . .").

60 *Enhancing Public Trust in COVID-19 Vaccination: The Role of Governments* (May 10, 2021), https://www.oecd.org/coronavirus/policy-responses/enhancing-public-trust-in-covid-19-vaccination-the-role-of-governments-eae0ec5a/ [https://perma.cc/HN8N-L3BZ].

61 Bhaven N. Sampat & Kenneth C. Shadlen, *The COVID-19 Innovation System*, 40 HEALTH AFF. 400, 404 (2021).

62 Florian Tille, Dimitra Panteli, Nick Fahy, Ruth Waitzberg, Nadav Davidovitch & Alexander Degelsegger-Márquez, *Governing the Public-Private-Partnerships of the Future: Learnings from the Experiences in Pandemic Time*, 27(1) EUROHEALTH 49 (2021).

developing R&D programs where the private sector is rewarded for serving as a long-term partner.[63]

Furthermore, these innovative efforts have reconfigured companies' supply chains to be more efficient and resilient to societal challenges. For instance, healthcare, food service, and public transportation workers were critical for conveying healthcare treatments and resuming economic activities.[64] These innovation efforts included rearranging individuals' work engagements by delivering services that would allow a healthy home-work balance in times of crisis.[65] In the future, to overcome work-family conflict, employers will be required to be more attentive to the well-being of employees rather than just ensuring that their employment rights and benefits are not infringed.[66] Because corporations' successes in overcoming the pandemic's economic turmoil were mainly based on the essential contributions of various stakeholders, it can be anticipated that future business models will consider their interests and functions more seriously. For example, business strategies could redefine the agents in charge of performing business activities and formulate fair arrangements for the value distribution between the corporation as a separate entity and its stakeholders.

63 David Baxter & Carter B. Casady, *Proactive and Strategic Healthcare Public-Private Partnerships (PPPs) in the Coronavirus (Covid-19) Epoch*, 12 SUSTAINABILITY 5097 (2020); Ramalingam & Prabhu, *supra* note 51, at 13; *see also OECD Science, Technology and Innovation Outlook 2021: Times of Crisis and Opportunity*, https://www.oecd-ilibrary.org/sites/e7747a75-en/index.html?itemId=/content/component/e7747a75-en [https://perma.cc/CMY4-7BBM] (last visited Oct. 22, 2022) ("[F]urther opened access to data and publications, increased the use of digital tools, enhanced international collaboration, spurred a variety of public-private partnerships, and encouraged the active engagement of new players.").

64 Crane & Matten, *supra* note 52, at 280.

65 Clark D. Asay & Stephanie Plamondon Bair, *COVID-19 and Its Impact(s) on Innovation*, 2021 UTAH L. REV. 805, 825–26 (2021).

66 Tim Allen, *The Pandemic Is Changing Employee Benefits*, HARV. BUS. REV. (Apr. 7, 2021), https://hbr.org/2021/04/the-pandemic-is-changing-employee-benefits [https://perma.cc/6DF9-8WMM]; Adrienne Eaton & Charles Heckscher, *COVID's Impacts on the Field of Labour and Employment Relations*, 58 J. MGMT. STUD. 275, 277 (2021) (observing that large percentages of the workforce are now working from home and this may have a large negative impact on the ability of employees to create a healthy balance between their work duties and family life).

B. *Transforming the Role of Corporate Constituencies*

Corporations that prepare themselves for a post-pandemic world must adjust their business models by identifying critical stakeholders. Their inputs are required to produce goods and continue the flow of information to increase value and performance. As Patnaik, Loret de Mola, and Bates put it —

> Ultimately, planning for a post-pandemic world means answering three questions. The first is: How does your business really make money? Many companies haven't taken the time to articulate their critical strategic differentiators or map out how money, goods, and information flow from their suppliers to their consumers. Next, who do you depend on to drive the business? Define your most important stakeholders and their behaviors that affect your business model.[67]

Recognizing stakeholders' contributions to business management is essential because it enables company leaders to prioritize different constituencies' interests to ensure firms' resilience in difficult times. Any business model "has stakeholder trade-offs embedded within it. Some groups win (maybe consumers, bondholders, or shareholders), and other interests lose (the environment, vulnerable workers, or communities)."[68] Thus, managers have to engage in a systematic innovation exploration of stakeholders' interests as part of "strategy-making, business planning, new product designs, or reorganization efforts."[69] This exploration is perceived as a transformative shift in how companies should run their businesses in the coming years in an environment that is highly dependent on the contribution of external constituencies.

C. *Fair Provisions for Value Distribution*

The pandemic crisis revealed the interdependency between the firm and its stakeholders for the company's ability to function, let alone create value in a time of distress. Because companies have struggled to survive in the face of significant disruptions in their supply

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[67] Dev Patnaik, Michelle Loret de Mola & Brady Bates, *Creating a Post-Covid Business Plan*, HARV. BUS. REV. (Jan. 8, 2021), https://hbr.org/2021/01/creating-a-post-covid-business-plan [https://perma.cc/JU35-6DCN].

[68] Sarah Kaplan, *Why Social Responsibility Produces More Resilient Organizations*, 62 MIT SLOAN MGMT. REV. 86 (2020).

[69] *Id.* at 87.

chain,[70] the contribution of the most "essential" stakeholders to business activities was reassessed.[71] The business model not only considers the activities of the firm and the factors in charge of performing them but also determines the expected value creation and how it will be appropriated between the company and its stakeholders. The value division between the firm and its partners is primarily a result of the parties' relative bargaining power and risk preferences. Thus, the size of the profit appropriated by stakeholders is not determined by markets but is based on formal governance arrangements – whether through contractual agreements or internal corporate decision-making – that guide the bargaining process.[72] These governance devices resolve conflicts among stakeholders over the surplus created due to their contributions.[73]

The relationship between the company and its stakeholders concerning value creation and appropriation is generally governed by arms-length contractual terms.[74] The business model also addresses it. However, taking stakeholders' interests seriously in the post-pandemic arena will require companies to ensure procedural contractual justice when articulating the value appropriation arrangements and substantive contractual justice that provides a balance allocation of risks, rewards, and chances between the parties. This can be done only after the company "reconsider[s] how value is assessed and allocated" and give stakeholders deemed most essential for business activities a fair slice of the economic pie.[75]

D. *Novel Technology and Business Solutions*

The pandemic crisis has brought about the development of new and practical solutions to fight against health emergencies and maintain (to some extent) the regular functioning of business and social

70 Lynn S. Paine, *Covid-19 Is Rewriting the Rules of Corporate Governance*, HARV. BUS. REV. (Oct. 6, 2020), https://hbr.org/2020/10/covid-19-is-rewriting-the-rules-of-corporate-governance [https://perma.cc/8EVG-2GB8].

71 Crane & Matten, supra note 52, at 281.

72 J.W. Stoelhorst, *Value, Rent, and Profit: A Stakeholder Resource-based Theory*, STRATEGIC MGMT. J. (2021); AMIT & ZOTT, *supra* note 38, at 243 (arguing the positive effect of the firm's novel business model on creating idiosyncratic value may reinforce its ability to capture larger parts of it).

73 Stoelhorst, *supra* note 72, at 12.

74 *Id.* at 11.

75 Crane & Matten, *supra* note 52, at 281.

activities.[76] This is expressed in the creation of technologies and novel business arrangements for saving the lives of people infected with COVID-19 and improving their quality of life during lockdowns.[77] For instance, many pharmaceutical companies worldwide have been racing to develop a vaccine against the disease.[78] To accelerate the development of various treatments, these companies used crowdsourcing data combined with big data analytics and Artificial Intelligence ("AI") technology to identify essential proteins that could become drug or vaccine targets.[79] Moreover, because people were obligated to confine in their homes during the pandemic, new technologies emerged for sustaining education, employment, commerce, and social exchanges between individuals despite the absence of face-to-face interactions.[80] In many parts of the world, schools and universities could not conduct face-to-face learning activities and had to shift their entire operations to online learning.[81] This included presenting lectures digitally and assigning work remotely.[82] In addition, most workplaces had to allow employees to work remotely from their homes through video conferencing tools such as Apple's FaceTime, Cisco's Webex, Microsoft's Teams, and Zoom Video Communication.[83] Finally, in times of lockdowns, consumers increased the demand for advanced platforms for e-commerce, mainly in food and clothing businesses.[84] Although many of the technologies discussed here were already in place

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76 Alexander Brem, Eric Viardot & Petra A. Nylund, *Implications of the Coronavirus (COVID-19) Outbreak for Innovation: Which Technologies will Improve our Lives?*, 163 TECH. FORECASTING & SOC. CHANGE 1 (2021).

77 *Id.*

78 MoneyShow, *Pharmaceutical Companies Racing For A COVID-19 Vaccine*, FORBES (June 16, 2020), https://www.forbes.com/sites/moneyshow/2020/06/16/9-pharmaceutical-companies-racing-for-a-covid-19-vaccine/?sh=77bdeaa176ad [https://perma.c/A3Q5-HK6V].

79 *See* Wu He, Zuopeng (Justin) Zhang & Wenzhuo Li, *Information Technology Solutions, Challenges, and Suggestions for Tackling the COVID-19 Pandemic*, 57 INT'L J. INFO. MGMT. 1 (2021) (for an overview of the various technologies used to mitigate the threats of COVID-19).

80 Brem, Viardot & Nylund, *supra* note 76.

81 Jitendra Singh, Keely Steele & Lovely Singh, *Combining the Best of Online and Face-to-Face Learning: Hybrid and Blended Learning Approach for COVID-19, Post Vaccine, & Post-Pandemic World*, 50(2) J. EDUC. TECH. SYS. 140 (2021).

82 *Id*.

83 *Id*. at 152.

84 *OECD Policy Responses to Coronavirus (COVID-19): E-commerce in the Time of COVID-19* (Oct. 7, 2020), https://www.oecd.org/coronavirus/policy-responses/e-commerce-in-the-time-of-covid-19-3a2b78e8/ [https://perma.cc/56DR-HN7U].

before the pandemic, the crisis has pushed for their diffusion and adoption in many other areas, resulting in sharing knowledge, experience, and expertise among various sectors and industries.[85]

Consequently, scholars have argued that the developments described above have transformed the traditional understanding of the place of innovation in business management. For example, Chesbrough maintained that open innovation could assist not only in responding immediately to the adverse outcomes of the emergency but also has a vital role in redressing its damages.[86] In particular, open innovation involves "purposive knowledge flows across organizational boundaries for monetary or non-monetary reasons" that enables companies to take advantage of the knowledge of others in running the company business (outside-in), as well as allows others to exploit the knowledge of the company in their business (inside-out).[87] Accordingly, other scholars call for adopting open innovation thinking to transform entire firms' supply chain in various industries, which will produce "many more ways to create value, be it through new partners with complementary skills or by unlocking hidden potential in long-lasting relationships."[88]

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The discussion so far demonstrated the essential value of collaboration, sharing of knowledge, resources, and expertise among companies, their constituencies, and the State in times of distress. This observation has also captured corporate leaders' attention on how to run their businesses for generating and distributing value.[89] Now, this Article discusses how these significant changes in business management may affect the design of corporate governance arrangements for regulating the power relations between the company's insiders and

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85 Singh, Steele & Singh, *supra* note 81.

86 Henry W. Chesbrough, *To Recover Faster from Covid-19, Open Up: Managerial Implications from an Open Innovation Perspective*, 88 INDUS. MKTG. MGMT. 410 (2020).

87 *Id.* at 412.

88 Linus Dahlander & Martin Wallin, *Why Now is the Time for "Open Innovation"*, HARV. BUS. REV. (June 5, 2020), https://hbr.org/2020/06/why-now-is-the-time-for-open-innovation [https://perma.cc/S9GW-DDA9].

89 Francois Bonnici & Carolien de Bruin, *What COVID-19 Taught us About Collaboration – 7 Lessons From the Frontline*, WORLD ECON. F. (Apr. 21, 2022), https://www.weforum.org/agenda/2022/04/what-covid-19-taught-us-about-collaboration-7-lessons-from-the-frontline/ [https://perma.cc/4KYR-CZUE].

outsiders. As the entire focal firm's activity system is prone to fundamental alterations, it can be assumed that they will also reformulate traditional understandings of the theory of company law. These developments may create a significant synchronization between how business activities are perceived from a managerial perspective and how the relationship between the company and its stakeholders – for performing various business functions – is regulated from a legal perspective.

IV. A POST-PANDEMIC AGENDA FOR SUSTAINABLE CORPORATE GOVERNANCE REGIMES: THE THEORETICAL FRAMEWORK

This part is devoted to exploring a theoretical shift from the traditional agency costs perspective to a resource-based view of the company and its implications for the purpose a company must pursue in the post-pandemic era. The predominant approach for analyzing company power relations focuses on alleviating agency costs by preventing rent-seeking behavior and inducing responsible conduct of managers toward shareholders.[90] The shareholder value model emphasizes the incentives and control systems required to encourage managers to engage exclusively with strategies that maximize owners' value.[91] Moreover, the model perceives company innovation efforts as means for generating value that will eventually be allocated to shareholders alone.[92] Thus, the interests of stakeholders and society are not considered part of corporate decision-making.[93]

90 Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305, 310 (1976); John Armour, Henry Hansmann & Reinier Kraakman, *Agency Problems and Legal Strategies*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 29–30 (3d ed. 2017) ("The first [agency problem] involves the conflict between the firm's owners and its hired managers . . . . The problem lies in assuring that the managers are responsive to the owners' interests . . . .").

91 Lucian Arye Bebchuk & Jesse M. Fried, *Executive Compensation as an Agency Problem*, 17 J. ECON. PERSP. 71, 72–75 (2003).

92 William Lazonick, *How "Shareholder Value" is Killing Innovation*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 8, 2017), https://corpgov.law.harvard.edu/2017/08/08/how-shareholder-value-is-killing-innovation/ [https://perma.cc/CR9U-ANAG].

93 Andreas Georg Scherer & Christian Voegtlin, *Corporate Governance for Responsible Innovation: Approaches to Corporate Governance and Their Implications for Sustainable Development*, 34 ACAD. MGMT. PERSP. 182, 190 (2020) ("[E]xternal stakeholders whose interests lie in promoting social or environmental welfare are normally excluded from corporate decisions.").

However, the essential capability of managers to carry out innovative business activities that increase value is highly dependent on the ability of the company to cooperate and exchange resources, knowledge, and expertise with various constituencies. Under this setting, the misalignment between how the company creates novel business activities and how internal power relations between insiders and multiple stakeholders are regulated is puzzling. In the post-pandemic world, which highlights the values of collaboration and diffusion of knowledge, it is doubtful whether the shareholder value model will continue to dominate company law and theory.

Therefore, this Article suggests an alternative theoretical framework that focuses on the legal implications of the company's need to attain resources from various stakeholders for creating value and generating competitive advantages. Because firms are "constrained and affected by their environment and act to attempt to manage . . . resource dependencies," the board of directors must contract with the external surroundings to access critical inputs to increase firm performance and value.[94] The resource-based theory declines the preference given shareholders' claims because of being the residual carriers of the risks involved in the business activities.[95] Because the maximization of firm value is based on the resources provided by various stakeholders, the theory rejects the idea of giving special protection to shareholders' interests.[96]

The resource-based theory contends that profits can be created only when companies with access to unique resources have more accurate expectations about the future revenues created by those resources than other companies or constituencies operating in the market.[97] The selling and acquiring resources between the company and

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94 JEFFREY PFEFFER & GERALD SALANCIK, THE EXTERNAL CONTROL OF ORGANIZATIONS: A RESOURCE DEPENDENCE PERSPECTIVE xxxiii (2003) (suggesting that directors produce four advantages to organizations: (a) information in the form of advice, (b) access to flows of information between the firm and environmental contingencies, (c) favorite access to resources, and (d) legitimacy); *see also* Johannes M. Drees & Pursey P. M. A. R. Heugens, *Synthesizing and Extending Resource Dependence Theory: A Meta-Analysis*, 39 J. MGMT. 1666, 1667 (2013).

95 Frank H. Easterbrook & Daniel R. Fischel, *Voting in Corporate Law*, 26 J.L. & ECON. 395, 403–06 (1983) (arguing that "shareholders are the residual claimants to the firm's income" and thus have the best economic incentives to vote in the best interests of the company).

96 Jay B. Barney, *Why Resource-Based Theory's Model of Profit Appropriation Must Incorporate a Stakeholder Perspective*, 39 STRATEGIC MGMT. J. 3305, 3306 (2018).

97 *Id.* at 3309.

its stakeholders are carried out under the assumptions of information asymmetry and transaction-specific investments.[98] This means that stakeholders who provide help and companies that obtain access to resources do not know the accurate quality of the resources provided, the revenues these resources will generate, and the actual payments stakeholders will receive.[99] Thus, the theory's basic idea of how value is made in the first place is based on an incomplete contracting process as part of obtaining external resources.[100]

As several authors argued,[101] the resource-based theory has to be combined with the stakeholders' perspective, which recognizes the company's duty to share the value it attained due to its unique contributions.[102] Thus, any division of value among various constituencies perceived to be inequitable could undermine "the stability of a particular bundle of co-specialized resources" because "stakeholders may withdraw, or threaten to withdraw, their resources and make them available to other bundles of resources."[103] Moreover, combining resource-based theory with a stakeholder perspective emphasizes the board of directors' central role in harmonizing the conflicting demands of stakeholders regarding value allocation and ensuring future collaboration between the parties.[104]

This conclusion fits well with the team production theory that defines the board's role as a "mediating hierarch" that has to balance the interests of the corporation's various constituencies in a manner that "[fosters] productive activity requir[ing] . . . combined investment and

98 *Id.* at 3309–10.

99 *Id.* at 3310–12.

100 *Id.* at 3312–13.

101 R. Edward Freeman, Sergiy D. Dmytriyev & Robert A. Phillips, *Stakeholder Theory and the Resource-Based View of the Firm*, 47 J. MGMT. 1757, 1758 (2021) ("To date, scholars have incorporated some elements of stakeholder theory in RBV, including accounting for stakeholders in RBV's model of rent appropriation [] and exploring stakeholders as resources leading to competitive advantage.").

102 Anita M. McGahan, *Integrating Insights From the Resource-Based View of the Firm Into the New Stakeholder Theory*, 47 J. MGMT. 1734, 1735 (2021) ("The NST [New Stakeholders Theory – L.A] relies primarily on economic and legal arguments that stakeholders will sustain their connection to an organization only if they expect and ultimately receive appropriate returns on their contributions. Much of the theory seeks to deal precisely with what this means.").

103 Barney, *supra* note 96, at 3316.

104 *Id.* at 3320.

coordinated effort."[105] However, there are still fundamental differences between these two streams of thought when explaining governance norms in company law. *First,* the team production theory perceives the role of the board of directors to be focused on balancing the conflicting interests of all team members "in a fashion that keeps everyone happy enough that the productive coalition stay together."[106] In contrast, the stakeholder-resources theory emphasizes the view that directors provide advice, service, and access to a variety of networks to attract valuable external resources required to enhance company value.[107] While there is no doubt that mitigating conflicts between corporate constituencies can be regarded as one of the board's roles, it is nevertheless questionable whether this is a central function shared among all members of the board rather than by those who are considered independent and not related to company insiders.[108]

Second, it can be argued that the team production theory can explain only the governance devices of public companies with a diffuse ownership structure. However, when it comes to public companies with a concentrated ownership structure directed by controlling shareholders, the board of directors may generally be inclined to advance those shareholders' interests rather than ensuring the continuation of stakeholders' collective production.[109] Because in most countries around the world, the ownership structure of public companies is concentrated, the applicability of the team production theory to understanding corporations' reality is to some extent limited.[110] In contrast,

105 Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 249 (1999) (quoting); Margaret M. Blair, *Boards of Directors as Mediating Hierarchs*, 38 SEATTLE UNIV. L. REV. 297, 309 (2015).

106 Blair & Stout, *supra* note 105, at 281.

107 Stephen M. Bainbridge, *Why a Board? Group Decisionmaking in Corporate Governance*, 55 VAND. L. REV. 1, 8 (2002); *see also* Amy J. Hillman, Michael C. Withers & Brian J. Collins, *Resource Dependence Theory: A Review*, 35 J. MGMT. 1404, 1408–11 (2009).

108 Steven Boivie, Michael C. Withers, Scott D. Graffin & Kevin G. Corley, *Corporate Directors' Implicit Theories of the Roles and Duties of Boards*, 42 STRATEGIC MGMT. J. 1662 (2021) (Providing qualitative evidence that suggests that "directors view their CEOs as generally acting in the best interests of their firms." Thus, directors do not necessarily view their responsibility as explicitly monitoring managerial opportunism. Instead, "directors consider strategically collaborating with their CEOs as critical to their board service.").

109 YEDIDIA Z. STERN, THE GOAL OF THE BUSINESS CORPORATION 296 (BAR-ILAN, 2009) [in Hebrew].

110 Julian Franks & Colin Mayer, *Evolution of Ownership and Control Around the World: The Changing Face of Capitalism*, *in* THE HANDBOOK OF THE ECONOMICS

because the stakeholders-resources approach focuses on attaining the inputs required to generate value,[111] it can be applied *prima-facie* to all types of corporations, whether publicly or privately held and whether their ownership structure is diffused or concentrated.

Third, the team production theory declines the priority provided by Anglo-American law to the interests of shareholders by considering the relative contributions of all stakeholders to the production function. However, it is questionable whether this argument is compatible with how the board of directors perceives the separate contributions of shareholders and stakeholders to value creation. Specifically, while stakeholders provide idiosyncratic and firm-specific investments, shareholders provide capital that can be directed easily and cheaply to other companies through the market mechanism.[112] Because stakeholders provide firm-specific assets, they are substantially prone to a company's opportunism which often cannot be removed by contractual safeguards alone.[113] This is especially true when shareholders have preferable political power and influence over the allocation of value produced by the firm. In this case, the board of directors will be more attentive to shareholders' interests than other constituencies' demands.[114]

In contrast, the stakeholders-resources based view focuses on generating the firm's value as a separate and independent entity. At times, it can provide special protection to shareholders' interests if required to increase the firm's value. Therefore, while the team production model is more focused on mitigating conflicts between various constituencies by considering their relative contribution, the stakeholders-resources view is more focused on how to generate a

OF CORPORATE GOVERNANCE 685, 717 (Benjamin E. Hermalin & Michael S. Weisbach eds., 2017).

111 McGahan, *supra* note 102, at 1735.

112 David Millon, *New Game Plan or Business as Usual? A Critique of the Team Production Model of Corporate Law*, 86 VA. L. REV. 1001, 1024–27 (2000).

113 Oliver E. Williamson, *Assessing Contract*, 1 J.L. ECON. & ORG. 177, 182–201 (1985) (discussing "alternative conceptions of the process of contract and relat[ing] these to . . . the condition of asset specificity"); Ronald J. Gilson, Charles F. Sabel & Robert E. Scott, *Braiding: The Interaction of Formal and Informal Contracting in Theory, Practice, and Doctrine*, 110 COLUM. L. REV. 1377, 1388 (2010) ("If the threat of opportunism can be addressed by specifying state-contingent outcomes or by assigning decision rights among the parties, then we observe formal contracting; if not, then we observe either self-enforcing informal contracts supported relationally or, if informal contracting cannot protect specific investment, we observe vertical integration.").

114 STERN, *supra* note 109, at 297–300.

competitive advantage by employing the resources at the company's disposal efficiently.

V. THE DEBATE SURROUNDING THE COMPANY PURPOSE

The modern corporation is under extensive pressure to shift its purpose from protecting the primacy of shareholder profits to directing its core operations to benefit public interests.[115] Accordingly, companies must be attentive not only to the interests of shareholders but also to the interests of various stakeholders.[116] One clear expression of this movement is the recent statement on the corporate purpose from the Business Roundtable that comprises the CEOs of the 200 largest U.S. public firms.[117] Although providing attention to stakeholder interests is undoubtedly a worthwhile policy goal, it is unclear how to integrate these interests into regular decision-making. Below are three possible models for incorporating stakeholders' agendas in business decision-making to tackle this issue.

A. *Weak Stakeholderism*

This model perceives stakeholders' interests as entitled to legal protection, not for their own sake but for increasing shareholders' profits and securing their preferences.[118] This approach emphasizes that stakeholders' views are instrumental in increasing shareholder

115 Lucian A. Bebchuk & Roberto Tallarita, *The Illusory Promise of Stakeholder Governance*, 106 CORNELL L. REV. 91, 108 (2020).

116 *Id.* at 105.

117 *Statement on the Purpose of a Corporation*, BUS. ROUNDTABLE, https://s3.amazonaws.com/brt.org/2022.08.01-BRTStatementonthePurposeofaCorporationwithSignatures-Compressed.pdf [https://perma.cc/S4R9-PVDS] (July 2022). Moreover, the agenda to incorporate stakeholders' interests as part of business decision-making was also put forward by management scholars. *See, e.g.*, COLIN MAYER, PROSPERITY: BETTER BUSINESS MAKES THE GREATER GOODS 109 (2018) (In lieu of the foundational principle of shareholder primacy, Mayer proposes a "purpose primacy" which "produce solutions to problems of people and planet and in the process to produce profits, but profits are not per se the purpose of companies.").

118 Lucian A. Bebchuk, Kobi Kastiel & Roberto Tallarita, *For Whom Corporate Leaders Bargain*, 94 S. CAL. L. REV. 1467, 1471 (2021) ("This analysis concludes that corporate leaders have incentives not to protect stakeholders beyond what would serve shareholder value. In this view, acceptance of stakeholderism would be counterproductive: rather than protecting stakeholders, stakeholderism would serve the private interests of corporate leaders by increasing their insulation from shareholder oversight.").

value.[119] The law and practice in Anglo-American countries have long embraced the shareholder primacy approach as the primary goal that corporate law and governance have to achieve.[120] In the United States, Delaware case law has adopted the view that corporate officers can promote stakeholders' interests as long as they are rationally beneficial to shareholders.[121] Moreover, when courts needed to resolve conflicts between the interests of stakeholders and shareholders, they clarified that shareholders' interests should prevail over any other claims.[122] As stated by the Delaware Supreme Court in *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.* — "while concern for various corporate constituencies is proper when addressing a takeover threat, that principle is limited by the requirement that there be some rationally related benefit accruing to the stockholders."[123]

The United Kingdom endorses a multi-stakeholder decision-making rule that makes management indirectly accountable to stakeholders' interests.[124] However, the director's duty to promote the

119 A. A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049, 1049 (1931) ("[A]ll powers granted to a [company board] . . . are . . . exercisable only for the ratable benefit of all the shareholders as their interest appears.").

120 LYNN A. STOUT, THE SHAREHOLDER VALUE MYTH 21 (2012); Robert J. Rhee, *A Legal Theory of Shareholder Primacy*, 102 MINN. L. REV. 1951 (2018) (presenting an empirical study which shows that "shareholder primacy has become a Hartian obligation and a rule of law").

121 Eduardo Gallardo, *On an Expansive Definition of Shareholder Value in the Boardroom*, THE CLS BLUE SKY BLOG (Oct. 22, 2019), https://clsbluesky.law.columbia.edu/2019/10/22/on-an-expansive-definition-of-shareholder-value-in-the-boardroom/ [https://perma.cc/YW4T-VHPP] ("Directors of a Delaware corporation must act in the best interest of the corporation and its *shareholders*. Other *stakeholders* – such as employees, creditors, customers, and suppliers – may only be considered by directors to the extent there are rationally related benefits to the welfare of shareholders.").

122 Edward B. Rock, *For Whom Is the Corporation Managed in 2020? The Debate over Corporate Purpose*, 76 BUS. LAW. 363, 372 (2021) ("Whenever courts have been confronted with an inescapable conflict between the interests of shareholders and the interests of other stakeholders, and have not been able to dodge the question by deference to board discretion under the business judgment rule, the courts have affirmed the primacy of shareholder interests.").

123 Revlon, Inc. v. MacAndrews & Forbes Holding, Inc., 506 A.2d 173, 176 (Del. 1986); *see also* Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1264 (Del. 1989) ("Our decision in Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., Del. Supr., 506 A.2d 173 (1986), requires the most scrupulous adherence to ordinary standards of fairness in the interest of promoting the highest values reasonably attainable for the stockholders' benefit.").

124 Companies Act 2006, c. 46, § 172(1) (Eng.); *see also* Richard Williams, *Enlightened Shareholder Value in UK Company Law*, 35 UNIV. NEW S. WALES L.J. 360, 362 (2012).

company's success is towards its shareholders, and the responsibility to consider stakeholders' interests is merely *derivative*.[125] Hence, considering stakeholders' interests is possible only when it is necessary to promote shareholder wealth.[126] To illustrate this model, two main implications are discussed: (1) maximizing shareholders' profits and (2) securing their actual preferences. As explored below, even if the importance of shareholder value is accepted, these aspects involve questionable assumptions that cast doubt on the ability of corporate insiders to execute effective decision-making.

Shareholder Value Maximization. By acknowledging the importance of attracting, retaining, and motivating a company's constituencies to produce value, the law considers stakeholders' interests instrumental in increasing value for shareholders alone. While weak stakeholderism acknowledges that profitability is produced by a variety of inputs provided by investors and stakeholders, it prioritizes shareholder interests over allocating the value created.[127] Thus, the law equates the maximization of firm value with shareholder value, mainly because shareholders are regarded as the sole residual risk-bearers in the firm.[128]

In contrast, stakeholders are fixed claimants who do not have the incentive to increase firm value beyond the point at which their claims are entirely met and repaid.[129] Accordingly, the economic rights assigned to shareholders represent the residual interests of the corporation itself, which are "those left after all corporate obligations, of any kind, to all non-residual claimants, are satisfied, in practice or in capacity."[130] Moreover, stakeholders generally have explicit contracts

125 However, other scholars argue that recognizing the welfare of stakeholders is a mechanism for advancing the company's overall benefit in the long run. Thus, directors are not allowed to promote the interests of the shareholders in a manner that impairs the legitimate interests of stakeholders. *See* Virginia H. Ho, *"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder-Stakeholder Divide*, 36 J. CORP. L. 59, 62 (2010).

126 MAYER, *supra* note 117, at 110–12.

127 Gaff v. Fed. Deposit Ins. Corp., 919 F.2d 384, 392 (6th Cir. 1990).

128 Jensen & Meckling, *supra* note 90, at 314.

129 Jonathan R. Macey, *An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties*, 21 STETSON L. REV. 23, 27–28 (1991).

130 Asaf Raz, *Share Law: Toward a New Understanding of Corporate Law*, 40 U. PENN. J. INT'L L. 255, 276 (2018); Kelli A. Alces, *Balance and Team Production*, 38 SEATTLE UNIV. L. REV. 187, 202 (2015) ("The shareholder primacy norm is more properly stated as a 'residual claim primacy' norm."); Andrew C. Inkpen & Anant K. Sundaram, *The Endurance of Shareholder Value Maximization as the Preferred*

with the firm, and in the event of corporate insolvency, they can rely on the legal system's protection by filling contractual gaps.[131] However, perceiving shareholders as the sole residual risk carrier of the company's obligations is highly controversial.[132] For example, Sung Kim has recently rejected the idea that shareholders are the sole residual claimants of the corporation and called for abolishing the current single criteria (profit residual) view.[133] By suggesting a standard that focuses on the distribution of rewards, the allocation of risks, and the firm's internal relationships, Kim demonstrates that shareholders cannot be considered the only residual claimants of the company.[134] Instead, it must be acknowledged that shareholders are only one of many residual claimants in the reality of the modern corporation, which justify a different allocation of rights and protections attached to such a status.[135]

Furthermore, although the shareholder value maximization rests on the assumption that shareholders are the only residual plaintiffs of the future company's remaining assets, shareholders' claims are far from homogenous.[136] As a result, the normative value of residual claimant argument as the primary justification for shareholders value norm cannot be sustained. In particular, a large body of literature demonstrated that shareholders could not be considered a homogenous constituency with similar interests, values, and preferences.[137] Shareholders generally differ in several ways, such as whether they have a

Corporate Objective, 59 J. MGMT. STUD. 555-68 (2021) (arguing that providing control rights to residual – and not fixed – claimants, shareholder value norm is the only decision rule that maximizes the value of the whole firm, thereby producing the largest corporate pie for all stakeholders).

131 Inkpen & Sundaram, *supra* note 130, at 556 ("Non-shareowning stakeholders typically have explicit contracts with the firm, whereas a shareholder's contract is implicit; in the event of corporate wrongdoings that harm them, the former have legal recourse via contract law, tort law, and regulations, with the judicial system routinely stepping in to fill contract voids.").

132 *See* Lynn A. Stout, *Bad and Not-So-Bad Arguments for Shareholder Primacy*, 75 S. CAL. L. REV. 1189, 1192–95 (2001).

133 Sung Eun (Summer) Kim, *Dynamic Corporate Residual Claimants: A Multicriteria Assessment*, 25 CHAP. L. REV. 67 (2022).

134 *Id.* at 70.

135 *Id.* at 93-96.

136 Grant M. Hayden & Matthew T. Bodie, *Shareholder Voting and the Symbolic Politics of Corporation as Contract*, 53 WAKE FOREST L. REV. 511, 522 (2018).

137 For a large discussion, *see e.g.*, Maria Goranova & Lori Verstegen Ryan, *The Corporate Objective Revisited: The Shareholder Perspective*, 59 J. MGMT. STUD. 526 (2021).

unique business relationship with the firm, hold long-term or short-term investment horizons, use derivatives to decouple voting and economic rights, and engage in shareholder activism.[138] Moreover, most shareholders have their shares indirectly through investment intermediaries, such as pension and mutual funds.[139] This leads to a divergence in investment time-horizon and risk preferences between investment managers and plan beneficiaries. Specifically, their interests differ because investment managers are "compensated based on the short-term performance of their investment portfolios or the size of their funds, and who face significant career risks if their funds underperform."[140] Thus, investment managers act as financial intermediaries between public companies and plans' beneficiaries, who are the ultimate residual-risk investors.[141] Because institutional investors are *not* considered the *direct* residual risk carriers of the company, the same justification cannot be applied to increasing value for all types of investors.[142]

Securing the Actual Preferences of Shareholders. Protecting stakeholders' interests as part of sustaining shareholders' interests can also be expressed by satisfying shareholder preferences concerning social agendas and maximizing profits. Today, "shareholders (in all their diversity) are speaking up about the ability of firms to impact

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138 *Id.* at 540-41.

139 Lucian A. Bebchuk, Alma Cohen & Scott Hirst, *The Agency Problems of Institutional Investors*, 31 J. ECON. PERSP. 89 (2017) ("The rise of institutional investors has led to increased concentration of equity ownership, with most public corporations now having a substantial proportion of their shares held by a small number of institutional investors."). Leo E. Strine termed this phenomenon as the "separation of ownership from ownership," *see* Leo E. Strine, Jr., *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*, 114 COLUM. L. REV. 449 (2014) ("That separation arises because the direct stockholders of private companies are typically not enduser investors, but instead money managers, such as mutual funds or hedge funds, whose interests as agents are not necessarily aligned with the interests of long-term investors.").

140 Goranova & Ryan, *supra* note 137, at 533 (citations omitted).

141 John C. Coffee, Jr., *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk*, 2021 COLUM. BUS. L. REV. 602, 608 (2021) ("Still, a potential conflict may be developing: as diversified institutional investors, utilizing their power of common ownership, begin to make decisions on a portfolio-wide basis (deliberately pursuing strategies that boost the stocks of some firms in their portfolios, while depressing the stocks of others to achieve a net gain), they will be taking actions contrary to the interests of undiversified investors in those firms on which they impose losses.").

142 Strine, Jr., *supra* note 139, at 533-34.

society."[143] For example, the rise of Environmental, Social, and Corporate Governance ("ESG") investing and impact investing "demonstrate that while shareholders care about financial returns, they also hold heterogenous values that extend beyond strict economic value."[144] The majority of investors value not only profits but also environmental, political, religious, and social goals. Nobel Laureates Oliver Hart and Luigi Zingales recently argued that corporations' objective should be to maximize shareholder welfare rather than just profits.[145] This could be accomplished only if executives seriously consider shareholders' social preferences.[146] In particular, shareholders might want the firm to internalize negative externalities, not because they believe themselves to be harmed by them, but rather due to altruistic personal motivations as members of society. Thus, the share price does not reflect shareholders' interests and cannot adequately measure their welfare.[147] This observation declines the common understanding that corporate officers must promote shareholder value as reflected in the share price to achieve overall social welfare.[148]

However, as Adi Libson observed, protecting shareholders' social preferences entails vertical conflicts with the management and horizontal conflicts with other fellow shareholders.[149] Vertical conflicts are a product of a systematic gap between shareholders and management concerning social preference.[150] Specifically, managers are more sensitive to profits than shareholders because their remuneration packages depend highly on the corporation's profitability.[151] Given that human capital is solely invested in one specific company, the "market value of their managerial skills is directly linked to the financial bottom line of the corporation."[152] Thus, managers will resist

143 Bidhan (Bobby) L. Parmar, Andrew C. Wicks & R. Edward Freeman, *Stakeholder Management & The Value of Human-Centred Corporate Objectives*, 59 J. MGMT. STUD. 569, 572 (2021).

144 *Id.*

145 Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L., FIN., & ACCT. 247 (2017).

146 *Id.* at 250–51.

147 *Id.* at 266–67.

148 Henry Hansmann & Reinier Kraakman, *End of History for Corporate Law*, 89 GEO. L.J. 439, 441 (2001).

149 Adi Libson, *Taking Shareholders' Social Preferences Seriously: Confronting a New Agency Problem*, 9 U.C. IRVINE L. REV. 699 (2019).

150 *Id.* at 712–22.

151 *Id.* at 707.

152 *Id.* at 701, 708.

satisfying particular social preferences that do not correspond to increasing shareholders' profit as reflected in the share price. This last argument is reinforced by the fact that large institutional investors have only small-sized teams engaging with ESG policies.[153] Thus, assets managers generally do not challenge incumbent managers' decision to focus only on generating profits instead of advancing social goals.[154] In addition, horizontal conflicts are a result of a divergence in (social) preferences among shareholders, which creates the risk of mutual exploitation and mistreatment, especially when individual shareholders hold significant decision-making rights over business resolutions that may produce policies that are not aligned with the views of the majority of shareholders.[155] Because there is no clear principle on how to address different shareholders' preferences, arguing for their protection is just an invitation for further discussing the governance consequences of diverging priorities rather than the end of the debate itself.

B. *Robust Stakeholderism*

This model considers shareholder value norms as the primary driver for global income inequality and unjust distribution of resources in societies.[156] Triggered by the adverse effects on the economy and society, which were partly exemplified in the financial crisis of 2007-2008, several commentators argued that corporate leaders should not only focus on increasing share prices but also confront public issues that transcend national borders by protecting stakeholders' interests for their own merits.[157] For example, Leo Strine has argued that for decades, corporations solely focused on increasing shareholders' profits, which resulted in an expansion of economic elites' gaining power

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153 Wolf-Georg Ringe, *Investor-led Sustainability in Corporate Governance*, (EUR. CORP. GOVERNANCE INSTITUTE, Working Paper No. 615/2021, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3958960 [https://perma.cc/N824-HPYK].

154 *See, e.g.*, Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029, 2040 (2019).

155 Iman Anabtawi, *Some Skepticism About Increasing Shareholder Power*, 53 UCLA L. REV. 561, 577–93 (2006).

156 BARNALI CHOUDHURY & MARTIN PETRIN, CORPORATE DUTIES TO THE PUBLIC 42–43 (2019).

157 Simon Deakin, *The Corporation as Commons: Rethinking Property Rights, Governance and Sustainability in the Business Enterprise*, 37 QUEEN'S L.J. 339, 367-80 (2012).

at the expense of workers, consumers, and the environment.[158] This observation is reflected in "wage stagnation, growing inequality, climate change that threatens humanity, repeated bailouts by the many of the few, consumer exploitation, increased insecurity, social division, and racial and economic inequality."[159] Accordingly, Strine argues that policymakers and courts should employ corporate governance devices to protect stakeholders' interests by requiring large companies and institutional investors to act socially responsibly.[160] By restoring the balance between shareholders' and stakeholders' interests, American corporate governance could obtain greater harmony with civil legal systems, such as Germany and other Scandinavian countries, which "compete effectively in the global market while producing widespread prosperity."[161]

Following the pandemic crisis, the view that companies need to tackle grand societal challenges, such as promoting equality, access to health care services, fighting poverty, and preventing the degradation of the natural environment and climate, has gained momentum.[162] This is also expressed in legislative reforms recently carried out in Europe. For example, recently, the European Commission published a directive proposal on Corporate Sustainability Due Diligence focusing on due diligence and duty of care rules.[163] Article 25(1) of the proposal states that the board of directors must consider the "consequences of their decisions for sustainability matters, including, where applicable, human rights, climate change, and environmental consequences, including in the short, medium, and long term."[164] The European Commission has introduced the Sustainable Corporate Governance Initiative following the E&Y study on directors' duties.[165] The study argued

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158 Leo E. Strine, Jr., *Restoration: The Role Stakeholder Governance Must Play in Recreating a Fair and Sustainable American Economy – A Reply to Professor Rock*, 76 BUS. LAW. 397 (2020).

159 *Id.* at 398.

160 *Id*. at 432.

161 Strine, Jr., *supra* note 158, at 400.

162 Martin Gelter & Julia M. Puaschunder, *COVID-19 and Comparative Corporate Governance*, 46 J. CORP. L. 557, 607–24 (2021).

163 *Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and Amending Directive (EU) 2019/1937*, COM (2022) 71 final (Feb. 23, 2022).

164 *Id.*

165 *Study On Directors' Duties And Sustainable Corporate Governance Final Report*, EUR. COMM'N (July 29, 2020), https://bit.ly/3xeNFeS [https://perma.cc/R3TK-HNF7].

that European companies focus too much on shareholders' short-term benefits rather than the company's long-term welfare.[166] At the same time, the study recognizes that several European jurisdictions already define directors' duties to extend beyond shareholder primacy.[167] For instance, in Germany, the *stakeholders' governance view* provides employees with a significant role in advancing good and proper corporate governance practices.[168] Its *codetermination model* promotes a democratic decision-making process by giving a voice to financial and human capital contributors for the company's business success.[169] However, the study asserts that adopting a similar position at the European Union ("EU") level will help overcome the problem of the traditional focus on short-term gains.[170]

Nevertheless, several commentators explained that corporate governance's ability to resolve grand societal challenges is limited and often produces counter-productive outcomes.[171] For instance, management could employ a stakeholder perspective to promote their interests by expanding their business discretion and insulating them from shareholder pressure, which could impair firm performance.[172] Since strong stakeholderism obligates managers to consider the interests of multiple and conflicted constituencies without any moral or economic guidance, that could damage the company's ability to make effective

166 *Id.* at 51.

167 *Id.* at annex I.5.

168 Aktiengesetz [AktG] [Stock Corporation Act] section 93(1)(2), Sept. 6, 1965, BGBl I at 1089, last amended by Gesetz [G], Aug. 7, 2021, BGBl I at 3311, art. 7 (Ger.).

169 *See e.g.*, Klaus J. Hopt & Patrick C. Leyens, *The Structure of the Board of Directors: Boards and Governance Strategies in the US, the UK and Germany*, *in* RESEARCH HANDBOOK ON COMPARATIVE CORPORATE GOVERNANCE 116, 139 (Afra Afsharipour & Martin Gelter eds., 2021) (for a comprehensive discussion of the codetermination model).

170 EUR. COMM'N, *supra* note 165, at 23 ("The link between short-termism and poor sustainability outcomes by the companies has been also highlighted in the field of company law research where the shareholder primacy in corporate governance has been pointed out as a key driver of short-termism and a powerful barrier against more environmentally sustainable companies.").

171 Matteo Gatti & Chrystin Ondersma, *Can A Broader Corporate Purpose Redress Inequality? The Stakeholder Approach Chimera*, 46 J. CORP. L. 1 (2021) (arguing that "a stakeholder approach is unlikely to achieve meaningful redistribution of power and resources to weaker constituents and would likely work in the opposite direction").

172 Bebchuk & Tallarita, *supra* note 115, at 92.

decisions.[173] Moreover, due to ownership and governance costs, assigning control rights to more than one constituency will prevent the board of directors from running the company effectively.[174] While these explanations focus on the difficulties that robust stakeholderism imposes on corporate intra-relationships, others emphasize that the benefits of the stakeholder governance approach cannot be attained in Anglo-American countries due to "the different institutional, social, and economic environment."[175] Therefore, to tackle social challenges, other sources of law, such as antitrust, labor, and tax law are more appropriate for this purpose.[176] Following the difficulties inherent in the weak and robust models of stakeholderism, this Article advocates for a moderate model of stakeholderism that considers the interests of stakeholders or shareholders when it corresponds to the focal firm's interests for increasing social and financial value according to its business interests.

C. *Moderate Stakeholderism*

This model stipulates that the company's structure, functions, and activities should not be confined to increasing shareholder or stakeholder value but promoting the firm's separate and special interests to increase its value and performance. This framework implies that the management should consider the interests of the diverse constituencies that it interacts with, as long as it fundamentally affects the value of the company as a *separate and independent legal entity*.[177]

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173 Andrew Keay, *Shareholder Primacy in Corporate Law: Can it Survive – Should it Survive*, 7 EUR. CO. FIN. L. REV. 369, 383 (2010).

174 Henry Hansmann, *Ownership and Organizational Form*, *in* THE HANDBOOK OF ORGANIZATIONAL ECONOMICS 891, 904 (Robert Gibbons and John Roberts eds., 2013) (Not only is ownership confined to a single class of patrons – such as investors of capital, employees, suppliers of some other factor of production, or customers – but, even within that class, ownership interests are, or are structured to be, highly homogeneous. Thus, business corporations with more than a very small number of owners are typically owned only by investors of capital, and all owners are given common interests via shares of entirely homogeneous common stock.); *see also* Andreas Kokkinis & Konstantinos Sergakis, *A Flexible Model for Efficient Employee Participation in UK Companies*, 20 J. CORP. L. STUD. 453, 457 (2020).

175 Jens Dammann & Horst Eidenmüeller, *Codetermination: A Poor Fit for U.S. Corporations*, 2020 COLUM. BUS. L. REV. 870, 940 (2021).

176 Gatti & Ondersma, *supra* note 171, at 9–10.

177 This idea follows the research of Andrew Keay. *See* Andrew Keay, *Ascertaining the Corporate Objective: An Entity Maximisation and Sustainability Model*, 71 MOD. L. REV. 663 (2008) (discussing the company as a separate legal entity and

Accordingly, corporate leaders should not adopt the predominance of shareholder or stakeholder interests concerning business resolutions. They should instead direct companies' business activities to maximize its value and not necessarily the value of any of its constituencies.[178] Therefore, although the board of directors must consider the implications of its business actions on different constituencies' interests, the company must adopt modes of operations and conduct that are in its interests. As Professor Andrew Keay puts it —

> The theory means that the directors are not under the direct control of the shareholders or any other stakeholder group. This allows the directors to make decisions which are best for the entity and not any shareholder or stakeholder. So, in making any decisions the directors must ask: what will benefit the company? Under EMS [entity maximization and sustainability theory], the company is not run for the benefit of the shareholders or any other stakeholders, but for itself.[179]

Therefore, the company cannot be considered a mere reflection of its shareholders' or stakeholders' interests or rights.[180]

Generally, a business model entails the value the company wishes to maximize and how it will be allocated between the firm and its various constituencies that contribute to its production.[181] A fair allocation of value will ensure the continuing efforts of the collaborative enterprise. Because moderate stakeholderism considers the interests of various stakeholders only if they correspond to the sole interests of the company, managers and directors need to choose clear courses of action that maximize entity value and promote sustainability.[182] To

maintaining that the objective of the company is to maximize its wealth and, at the same time, ensure that the company is sustained financially).

178 *Id.* at 685 ("Entity maximization involves the fostering of entity wealth, which will entail directors endeavoring to increase the overall long-run market value of the company as a whole, taking into account the investment made by various people and groups.").

179 Andrew Keay, *Board Accountability and the Entity Maximization and Sustainability Approach*, *in* UNDERSTANDING THE COMPANY: CORPORATE GOVERNANCE AND THEORY 271, 276-77 (Barnali Choudhury & Martin Petrine eds., 2017).

180 *See* STERN, *supra* note 109 (A similar view was advocated in Israel by Yedida Stern, who argued that considering the interests of the various constituencies has a purely instrumental nature for increasing the sole value and profits of the *company* as an independent and separate entity without any legal owners.).

181 AMIT & ZOTT, *supra* note 38, at 20.

182 Keay, *supra* note 177, at 687.

illustrate the moderate stakeholderism model, several examples and their implications are provided.[183]

Example 1 — Transfer of control: A prevalent way to transfer control in public companies is through selling the shares held by controlling shareholders. Generally, such a transaction does not require the involvement of minority shareholders; the company's insiders carry it out independently.[184] However, several jurisdictions impose a fiduciary duty on controlling shareholders that prevents them from advancing their business interests without considering the best interest of the company.[185] Any transfer of control imposes risks on various constituencies, such as bankruptcy hazards or an increase of dismissal chances. This is also reflected in having the new controlling shareholder who finds the controlling interest appealing because it may allow them to appropriate private benefits of control at the expense of minority shareholders and stakeholders. As a result, the latter might refrain from providing contributions to the firm. However, such transactions could entail considerable benefits to the corporation when the new controlling shareholders hold special competence, skill, knowledge, and expertise.[186] Therefore, from a firm-specific perspective, directors must balance the company's costs due to a decrease in

183 These examples are heavily based on Yedidia Z. Stern, *The Goal of the Business Corporations: Interpretation and Practical Implications*, 32(2) MISHPATIM 327, 346–47 (2001) (in Hebrew).

184 *See e.g.*, Frank H. Easterbrook & Daniel R. Fischel, *Corporate Control Transactions*, 91 YALE L.J. 698, 715-19 (1981) (exploring different views on whether the ability of controlling shareholders to transfer their control should be limited).

185 For the position of Delaware law, *see, e.g.*, Abraham v. Emerson Radio Corp., 901 A.2d 751, 753, 758 (Del. Ch. 2006) (controlling shareholders have a right to sell his control at a premium subject to the limit on selling control to a looter); WILLIAM T. ALLEN, REINIER KRAAKMAN & VIKRAMADITYA S. KHANNA, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATION 488-90 (Rachel E. Barkow et al. eds., 6th ed. 2021).

186 The legal and management literature has recently explored the positive contribution of controlling shareholders and more generally equity owners to increase firm value and performance for the benefit of all stakeholders. *See e.g.*, Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 YALE L.J. 560 (2016); Nicolai J. Foss, Peter G. Klein, Lasse B. Lien, Thomas Zellweger & Todd Zenger, *Ownership Competence*, 42 STRATEGIC MGMT. J. 302, 302 (2021) ("[C]ontrol afforded by ownership allows owners to deploy resources in novel ways: acquiring and selling resources, investing in them, or recombining them according to the owners' unique, idiosyncratic, and ultimately inalienable beliefs about paths to value creation. . .we develop the argument that ownership can be exercised with greater or lesser competence and that this matters to value creation.").

stakeholders' contributions following a transfer of control with the benefits resulting from the new controlling shareholder's expertise.

Example 2 — Research and development investment. Companies need to decide whether to make significant investments in research and development which their expected contribution for firm value and performance is often not known. This decision reflects a business challenge mainly when the stock markets do not know how to price the proposed investment appropriately. While shareholders' short-term returns could be damaged due to such an investment, stakeholders and, more importantly, society at large will substantially benefit from it. Moreover, other companies in the industry will also enjoy any investment in research and development made by the focal firm due to knowledge and the spillover of ideas.[187] While the weak and robust stakeholderism reach different conclusions on which course of action the company must adopt, moderate stakeholderism urges corporate leaders to balance the costs and benefits from a firm perspective. On the one hand, they have to consider the costs if shareholders choose to sell their stocks and disconnect from the company's activities; on the other hand, they need to estimate the benefits the company materializes if its efforts will eventually yield a competitive advantage.

VI. A CONTINGENT INTERPRETATION OF THE COMPANY PURPOSE: STRATEGIES AND GUIDELINES

Moderate stakeholderism adopts the view that insiders must make decisions that maximize the corporation's benefits. As the company's course of action may sometimes be in the interests of shareholders or stakeholders, principles are needed to guide directors and managers in balancing competing interests. Most scholars perceive company purpose as constant arrangements that apply to any business decision insiders make. Alternatively, advanced here is a different view that acknowledges the dynamic nature of business activities that justifies a contingent understating of the company purpose. As Professor Jonathan Doh puts it —

> From a practical vantage point, the relevance and applicability of each of these corporate objectives is contingent on the

[187] Raymond Van Wijk, Justin J. P. Jansen & Marjorie A. Lyles, *Inter- and Intra-Organizational Knowledge Transfer: A Meta-Analytic Review and Assessment of its Antecedents and Consequences*, 45 J. MGMT. STUD. 830, 835-36 (2008) (discussing how resource exchange and knowledge transfer facilitate organizational innovativeness and performance).

> national institutional context, the relevant sector and industry of the corporation in question, the strategy of the individual corporation, and the vision of the leader or leaders of that organization. . . . [T]here is no one corporate objective; rather the objective is variable based on a range of conceptual lenses, contextual factors, interests, and situational influences.[188]

For example, a recent revision to the U.K. Corporate Governance Code in July 2018 states, "[t]he board should establish the company's purpose, values, and strategy, and satisfy itself that these and its culture are aligned."[189] However, the Code has not further defined what is meant by company purpose. Moreover, the relationship between the Code's provision and section 172(1) of the Companies Act, which adopts the enlightened shareholder view, is unclear.[190] Recently, Kershaw and Schuster argued that we should understand the term "purpose" in the U.K. Corporate Governance Code in a limited manner that refers only to a mission purpose.[191] Specifically, it relates to "an animated version of what it does —– a corporate and societal mission which levitates out of what it prosaically does and around which the actions of its directors, managers, and employees can coalesce."[192] The proposed view differs in that it assigns far-reaching implications to the Code provisions, which reflect a firm-specific approach to the purpose debate. According to the conventional meaning of Principle B in the section on "Board Leadership and Company Purpose," the board of directors may tailor the firm's purpose to its unique business dynamics and challenges.[193] However, to provide a meaningful interpretation of corporate purpose designed from a firm-specific perspective, two *critical* aspects that policymakers and corporate leaders must contemplate

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188 Jonathan Doh, *Introduction to the Point-Counterpoint: The Corporate Objective as a Contingency*, J. MGMT. STUD. 518, 519-20 (2021) (citing R. Edward Freeman, Andrew C. Wicks & Bidhan Parmar, *Stakeholder Theory and 'The Corporate Objective Revisited'*, 15 ORG. SCI. 259, 364-69 (2004)).

189 *The UK Corporate Governance Code*, FIN. REPORTING COUNCIL 4 (July 2018), https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-uk-corporate-governance-code-final.pdf [https://perma.cc/2TTF-VQAH].

190 *See also* Holger Fleischer, *Corporate Purpose: A Management Concept and its Implications for Company Law*, 18(2) EUR. COMP. & FIN. L. REV. 161, 174 (2021).

191 David Kershaw & Edmund-Philipp Schuster, *The Purposive Transformation of Company Law*, 69 AM. J. COMP. L. 478, 478-79 (2021).

192 *Id.* at 490.

193 *The UK Corporate Governance Code, supra* note 189, at 4–5.

as part of making a tradeoff between moral, fairness, efficiency, and public policy rationales devoted to maximizing a firm's benefit are discussed. This approach advances the idea that to form an instructive balance between different considerations, a contextualized understanding of the debate's purpose should be adopted to bring closer the actual business reality with its core regulation.

A. *Life-Cycle*

This aspect considers the balance between financial and social (or pluralistic) rationales for the corporate purpose to be affected by the specific stage in the company's business development. Because the company's growth depends on the contribution of different stakeholders, the management must consider the constituency whose contribution is critical for generating value at each stage of its life cycle. The literature discussed several models of a company's life cycle and acknowledged that each stage of its growth involves different business challenges that require distinctive stakeholders' inputs.[194] For example, Lippitt and Schmidt argued that companies progress through three stages of development that involve particularly managerial challenges.[195]

At early stages, critical concerns include the formation of the company and obtaining the essential resources needed for achieving a survival threshold.[196] During youth, the company's main interests are to ensure stability and reputation; and, during maturity, the main interests become to attain "uniqueness and respond to diverse societal needs."[197] According to this view, the management has to consider the critical dependency on resources conveyed by each constituency at

194 *See e.g.*, Luigi Mosca, Martina Gianecchini & Diego Campagnolo, *Organizational Life Cycle Models: A Design Perspective*, 10 J. ORG. DESIGN 3 (2021) (for a review of the major organizational life-cycle models in the management literature).

195 Gordon L. Lippitt & Warren H. Schmidt, *Crises in a Developing Organization*, 45 HARV. BUS. REV. 102 (1967). *See* Neil C. Churchill & Virginia L. Lewis, *The Five Stages of Small Business Growth*, 61 HARV. BUS. REV. 30 (1983) (The authors identify five stages of a company's life cycle: conception/existence, survival, profitability and stabilization/growth, take-off, and maturity. They argue that "each stage is characterized by an index of size, diversity and complexity, as described by five management factors: managerial style, organizational structure, extent of formal systems, major strategic goals and the owner's involvement in the business."); *see also* Mosca, Gianecchini & Campagnolo, *supra* note 194, at 5-6.

196 Aracely Soto-Simeone, Charlotta Siren & Torben Antretter, *New Venture Survival: A Review and Extension*, 22 INT'L J. OF MGMT. REVS. 378, 378–79 (2020).

197 Mosca, Gianecchini & Campagnolo, *supra* note 194, at 5.

each stage of the firm development and choose a course of action that considers the interests of the stakeholder whose contribution is essential for producing value for the benefit of the company as an independent entity. Thus, because the needs of the company vary over time, the company will assign a different weight to constituencies' contributions at separate stages of its growth.[198] For example, because managers are mainly concerned with ensuring the firm's survival chances at the company's formation stage, they should prioritize the interests of investors and creditors whose financial contributions are essential. However, as the company grows and expands its business activities, it recognizes the valuable contributions of other stakeholders for producing value, such as employees, suppliers, and local communities.[199] Therefore, the balance between various policy considerations depends on the particular stage of the company's life cycle according to the relative importance of multiple constituencies' contributions to producing value for the company.[200]

Furthermore, the company's reliance on firm-specific investment ("FSI") also affects the relative consideration it will provide to stakeholders' interests as part of its purpose. FSI refers to a unique contribution that allows the firm to achieve a sustained economic advantage through bundles of resources created by stakeholders.[201] However, because these resources are tailored to the company's needs, the firm can engage in behavioral opportunism vis-a-vis its stakeholders.[202] Specifically, the company can "appropriate value and quasi-rents using its bargaining position, since stakeholders, once having made an FSI, cannot obtain value from outside the focal firm."[203] As explained by Coff and Raffiee, "a dilemma exists because the very same reasons that firms want employees [or other stakeholders] to develop firm-specific skills may simultaneously make employees [or other

198 *See* I. M. Jawahar & Gary L. McLaughlin, *Toward a Descriptive Stakeholder Theory: An Organizational Life Cycle Approach*, 26 ACAD. MGMT. REV. 397 (2001).

199 *Id.* at 406–10.

200 David G. Sirmon, Michael A. Hitt, R. Duane Ireland & Brett Anitra Gilbert, *Resource Orchestration to Create Competitive Advantage: Breadth, Depth, and Life Cycle Effects*, 37 J. MGMT. 1390, 1400–03 (2011).

201 Robert E. Hoskisson, Eni Gambeta, Colby D. Green & Toby X. Li, *Is My Firm-Specific Investment Protected? Overcoming the Stakeholder Investment Dilemma in the Resource-Based View*, 43 ACAD. MGMT. REV. 284 (2018).

202 *Id.* at 284.

203 *Id.*

stakeholders] reluctant to do so."[204] The firm must create certain formal and informal safeguards to overcome the holdup problem and induce stakeholders to continue collaborating with the company.[205] The standard protections are usually expressed through contractual terms that regulate the interaction between the company and its stakeholders. Informal protections could be provided by considering stakeholders' interests as part of the managerial decision-making, especially when their FSIs are crucial for generating a competitive advantage in the market.[206]

Previous empirical examination supports the argument here that conditions the protection of shareholders' or stakeholders' interests in the relevant business challenges associated with the firm's development. For instance, Diebecker, Rose, and Sommer use a comprehensive international sample to demonstrate that corporate sustainability performance ("CSP") varies according to different stages of the company's life cycle.[207] They show that for companies:

> in the introduction stage of the life cycle, scarce resources leave little room for CSP because the top priority is mere survival. However, in the growth stage CSP can be used as a tool in order to attract external resources. In later stages of the life cycle, such as the mature and shake-out stages . . . CSP might be a tool with which. . . to build a reputation and gain competitive advantages, which in turn might lead to superior financial performance.[208]

Therefore, because companies' main ambition is to produce value and ensure survival in a complex business environment, corporate leaders should adopt a dynamic approach to the company purpose that provides preferences to the constituency's demands that secure that

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204 Russell Coff & Joseph Raffiee, *Toward a Theory of Perceived Firm-Specific Human Capital*, 29 ACAD. MGMT. PERSP. 326, 328 (2015).

205 The holdup problem arises "when one party makes a sunk, relationship-specific investment and then engages in bargaining with an economic trading partner. That partner may be able to appropriate some of the gains from the sunk investment, thus distorting investment incentives, either toward too little investment or toward investments that are less subject to appropriation." *See* Benjamin E. Hermalin & Michael L. Katz, *Information and the Hold-Up Problem*, 40 THE RAND J. ECONS. 405, 405 (2009).

206 Hoskisson, Gambeta, Green & Li, *supra* note 201, at 296–99.

207 Jan Diebecker, Christian Rose & Friedrich Sommer, *Corporate Sustainability Performance Over the Firm Life Cycle: Levels, Determinants, and the Impact on Accounting Performance*, SSRN ELEC. J. (2017).

208 *Id.* at 3.

company's motivations are accomplished at different stages of its development.

B. *Industry*

As illustrated below, to understand the balance of shareholders' and stakeholders' interests, one must consider the unique characteristics associated with regulating a particular sector in which a company operates. This is because a firm generally interacts with consumers, competitors, and regulators, who are influenced by formal and informal industry practices.[209] Thus, "the success or failure of a firm is to a certain degree conditioned by its industry."[210] The nature and magnitude of the company's interactions with various constituencies in different industries and their implications for conceptualizing the company goal and its resulting internal governance norms are discussed. To illustrate this argument, the discussion focuses on the financial services sector and the high-tech entrepreneurial industry.[211]

C. *Financial Services Sector*

Generally, Anglo-American law considers the purposes and the governance norms that dictate the operations of financial institutions to maximize return for shareholders exclusively and enlists stakeholders' interests in accomplishing this goal.[212] Thus, directors are required to act in the best interests of the creditors and other stakeholders only in the vicinity of insolvency.[213] However, as several commentators have argued, shareholder primacy in the governance of financial institutions may carry out systematically significant negative externalities

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209 Climent & Haftor, *supra* note 44, at 357.

210 *Id.*

211 Doh, *supra* note 188, at 523.

212 Steven L Schwarcz, Aleaha Jones & Jiazhen Yan, *Responsibility of Directors of Financial Institutions*, *in* GOVERNANCE FINANCIAL INSTITUTIONS: LAW, CONDUCT, AND CULTURE 3, 4 (Danny Busch, Guido Ferrarini, & Gerard van Solinge, eds., 2019).

213 *See* Insolvency Act of 1986, c. 45, § 214 (UK); Insolvency Act of 1986, c. 45, § 246ZB (UK); Liquidator of West Mercia Safetywear Ltd v. Dodd, 1988 WL 624053 (UK). The rationale advanced is that creditor-oriented duty-shifting rules may deter directors from disposing of assets in high-risk, high-reward projects in insolvency and its vicinity even though shareholders may support these strategies. *See also* Kristin van Zwieten, *Director Liability in Insolvency and Its Vicinity*, 38 OXFORD J. LEGAL STUD. 382, 388 (2018).

on the rest of the economy, especially during times of crisis.[214] In such cases, the entire economy bears the residual risks of the corporation's failure, and unlike creditors or employees, it cannot negotiate for contractual protections.[215] Thus, during financial crises, fiduciary duties — duties of care and loyalty — owed by directors and officers to shareholders should be extended to encompass the interests of the broader economy.[216] Assigning importance to the industry pattern indicates that in times of a pandemic that involves immense economic distress, financial institutions should adopt a more inclusive objective for arranging their business functions and activities. Such a wide-ranging goal is essential due to shareholders' pressure to increase the leverage that could eventually result in the corporation's insolvency and a failure of the economy. These institutions should consider the interests of various constituencies that collaborate in generating value for the corporation, even if their economic condition is not under explicit ongoing concern. Moreover, other commentators argued that favoring the interests of the financial institution's shareholders over any other constituency is problematic even in ordinary times.[217] Financial institutions profit from the difference between short-and long-term interest rates and disproportionately rely on various debt instruments to finance their activities.[218] Because banks' profits are mainly derived from lending money to others at higher rates than those they borrow at, they can increase their returns by magnifying their leverage. Since shareholders are interested in maximizing profit, they will encourage the financial institution, through its managers, to increase leverage at the expense of the creditors and the rest of the economy.[219] This incentive can be even more compelling due to the promise of expensive

214 John Armour & Jeffrey N. Gordon, *Systemic Harms and Shareholder Value*, 6 J. LEGAL ANALYSIS 35, 35-36 (2014) (arguing that the recent financial crisis has demonstrated that the norm that managers should seek to maximize shareholder value, as measured by the stock price, is a faulty guide for managerial action in systemically essential firms).

215 *See also* DEMETRA ARSALIDOU, RETHINKING CORPORATE GOVERNANCE IN FINANCIAL INSTITUTIONS 105–08 (2015).

216 Yair Listokin & Inho Andrew Mu, *Rethinking Corporate Law During a Financial Crisis*, 8 HARV. BUS. L. REV. 349, 354 (2018).

217 See *generally* Steven L. Schwarcz & Aleaha Jones, *Corporate Governance of SIFI Risk-Taking: An International Research Agenda*, *in* RESEARCH HANDBOOK ON CROSS-BORDER BANK RESOLUTION 177 (Bob Wessels & Matthias Haentjens eds., 2019).

218 Michael Marin, *Disembedding Corporate Governance: The Crisis of Shareholder Primacy in the UK and Canada*, 39 QUEEN'S L.J. 223, 230–33 (2013).

219 Schwarcz & Jones, *supra* note 217, at 179.

public support in the manner of a "bailout to make sure that a really large bank does not inflict serious economic damage through its failure."[220] Thus, it was suggested to modify the rule that limits the liability of systemically important financial institutions ("SIFI") shareholders to the amount of their investment and instead imposes on them an additional fixed amount of potential liability in case the SIFI is resolved or bailed out.[221]

To understand more accurately how to balance the interests of shareholders and stakeholders (especially financial consumers) in the financial sector, one should consider how governments intervene in the function of financial markets and to what extent. The literature suggested several arguments for supporting different types of government intervention.[222] From an economic perspective, regulation is required only when market failures, such as asymmetric information,[223] negative externalities, imperfect competition, and irrational consumer decision-making occur.[224] Accordingly, financial regulation aims to redress these shortcomings to allow economic growth.[225] For example, to alleviate investors' costs resulting from the tendency of public

220 Yesha Yadav, *Too-Big-to-Fail Shareholders*, 103 MINN. L. REV. 587, 650 (2018).

221 Alessandro Romano, Luca Enriques & Jonathan R. Macey, *Extended Shareholder Liability for Systemically Important Financial Institutions*, 69 AM. U. L. REV. 967 (2019).

222 *See, e.g.*, Rashmi Arora, *Government Intervention and Financial Sector Development*, *in* DEVELOPMENT FINANCE: OPPORTUNITIES AND CHALLENGES 53 (Gianluigi Giorgioni ed., 2017).

223 *See generally* Donald D. Bergh, David J. Ketchen, Jr., Ilaria Orlandi, Pursey P. M. A. R. Heugens & Brian K. Boyd, *Information Asymmetry in Management Research: Past Accomplishments and Future Opportunities*, 45 J. MGMT. 122, 128 (2019) ("Information asymmetry was most frequently depicted as present when a party has access to privileged or private information.").

224 JOHN ARMOUR, DAN AWREY, PAUL DAVIES, LUCA ENRIQUES, JEFFREY N. GORDON, COLIN MAYER & JENNIFER PAYNE, PRINCIPLES OF FINANCIAL REGULATION 55–61 (John Armour et al. eds., 1st ed. 2016); Christopher P. Buttigieg, John A. Consiglio & Gerd Sapiano, *A Critical Analysis of the Rationale for Financial Regulation Part I: Theories of Regulation*, 17 EUR. COMP. & FIN. L. REV. 419, 430 (2020) ("In the field of financial regulation the mitigation of information asymmetries is one of the main investor protection objectives. Regulation is instrumental for the correction of market failures and a means to maximise general welfare and society's common economic interests.").

225 Buttigieg, Consiglio & Sapiano, *supra* note 224, at 437. ("it is generally accepted that financial regulation is an instrument of economic policy. Financial regulation has been found to have a significant influence on the output and productivity growth within an economy.").

corporations to provide partial information to the markets, financial regulation imposes strict disclosure obligations that protect investors' rational decision-making.[226] These obligations are in place to remove information asymmetries between financial institutions and their beneficiaries and consequent agency costs.[227] Since the primary goal of government intervention is to ensure market efficiency, the interests of stakeholders and deprived socio-economic populations will be integrally protected due to the overall increase in social welfare.[228] Moreover, because the economic approach perceives the protection afforded by financial regulation to be focused on retail investors, there is no difference between corporate law and financial regulation regarding the identity of the ultimate beneficiary. While financial regulation aims to protect the investors' interests during trade, corporate law protects their interests immediately after officially being owners of the company's shares.[229]

However, other views assign pluralist accounts for regulatory intervention in the operation of the financial system. For example, several scholars argue that financial regulation could reduce inequalities and provide economic opportunities and justice for a disadvantaged population.[230] Financial regulation should improve inclusion by "expanding account ownership to provide basic banking services" and increasing access to credit to simplify lending instruments.[231] Moreover, the recent pandemic emphasized the societal functions of financial regulation because many low-income individuals in the United States and elsewhere lack bank accounts to receive direct deposits and do not have access to credit that could assist them in redressing the unexpected costs of the crisis.[232]

226 Armour, Hansmann & Kraakman *supra* note 90, at 256–61.

227 ARMOUR, AWREY, DAVIES, ENRIQUES, GORDON, MAYER & PAYNE*, supra* note 224 at 64.

228 Therefore, while the economic view of financial regulation acknowledges that "[a] highly competitive economy may be a highly unequal one," government intervention in other areas of law will be required to allow a just allocation of resources. *Id.* at 54–55. *See also* A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 158–61 (4th ed. 2011); Richard L. Revesz, *Regulation and Redistribution*, 93 N.Y.U. L. REV. 1489, 1489 (2018).

229 For a similar argument, *see* James J. Park, *Reassessing the Distinction Between Corporate and Securities Law*, 64 UCLA L. REV. 116 (2017).

230 *See e.g.*, Steven L. Schwarcz & Theodore L. Leonhardt, *Scoping and Defining Financial, Access to Credit, and Sustainable Finance*, 84 L. & CONTEMP. PROBS. 1 (2021).

231 *Id.* at 5, 7.

232 *Id.* at 12–13.

The financial regulation's economic and social rationales may suggest different proposals on how to combine stakeholders' and shareholders' perspectives as part of articulating the purpose the corporation has to attain. Accordingly, the protection of stakeholders' and shareholders' interests through financial institutions' governance cannot solely be determined from a corporate law perspective. To construct a meaningful balance between these interests, corporate leaders and policymakers should examine institutions' internal decision-making concerning the *type and risk of financial products and consumers' backgrounds and needs*.

To accomplish such an examination, the *'product governance'* approach should be adopted, which was recently embraced by the EU authorities.[233] This approach introduced the idea of "know your customer" concerning the design and marketing of new products.[234] Financial firms are obligated to establish, implement, and maintain procedures designed to meet the needs of an identified target market of the end client.[235] In particular, they need to specify the types of clients for whose needs, characteristics, and objectives the product is compatible with using the following categories: (i) types of clients for whom the product is intended; (ii) their knowledge and experience; (iii) their financial situation, with a focus on the ability to bear losses; (iv) their risk preferences and the compatibility of the risk/reward profile of the product with the target market; (v) their objectives and needs.[236] Moreover, financial firms are obligated to constantly review their products by considering any "event that could materially affect the potential risk to the identified target market and consider if the financial

233 Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to the safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits, 2017 O.J. (L 87) 500 (Art. 16(3) and 24(2) MiFID II, art. 9-10). For an overview, *see* Antonio Marcacci, *European Regulatory Private Law Going Global? The Case of Product Governance*, 18 EUR. BUS. ORG. L. REV. 305, 313 (2017).

234 Veerle Colaert, *Product Governance: Paternalism Outsourced to Financial Institutions?*, 31 EUR. BUS. L. REV. 977, 977 (2020).

235 *See also Guidelines on MiFID II Product Governance Requirements*, EUR. SEC. & MKT. AUTH. 7 (May 2, 2018) [hereinafter *Guidelines on MiFID II Product Governance Requirements*], https://www.esma.europa.eu/sites/default/files/library/esma35-43-620_guidelines_on_mifid_ii_product_governance_requirements_0.pdf [https://perma.cc/7LS5-XZKN].

236 Colaert, *supra* note 234, at 979-80.

instrument remains consistent with the needs, characteristics, and objectives of the target market."[237]

While the EU's product governance rules are focused on tailoring the products' features to the target market's needs, its analytical framework could be extended to shaping the entire firm's internal decision-making concerning the balance between shareholders' and stakeholders' interests. These rules employ essential terms, such as "risk tolerance" and "objective and needs," that must be understood according to the economic and pluralist justifications for financial regulation.[238] For example, when the firm's decision-making relates to complex financial products that entail significant failure risks for unsophisticated clients, the terms consumer's objective and needs should receive an elaborated interpretation. Such an understanding will obligate firm insiders to protect not only mere consumers' investment expectations but also ensure their ultimate welfare following the pluralist rationales of financial regulation. This conclusion holds to any resolutions relating to designing, distributing, and marketing the financial product even if they are not explicitly required (or addressed) by the relevant regulation.

Moreover, this is especially true in times of financial distress in which the vulnerability of financial consumers is significant.[239] For example, in early 2021, the U.K. Financial Conduct Authority ("FCA") found the COVID-19 pandemic left over a quarter of U.K. adults with low financial resilience.[240] A similar result was found in other countries.[241] However, when it comes to traditional financial products that do not require a high level of competence to understand their core characteristics, the firm's insiders can direct the internal

237 *Id.* at 981.

238 *Guidelines on MiFID II Product Governance Requirements*, supra note 235, at 7-8.

239 Iris H-Y Chiu, *More Paternalism in the Regulation of Consumer Financial Investments? Private Sector Duties and Public Goods Analysis*, 41 LEGAL STUD. 657, 673 (2021) (arguing that product governance is "insufficiently connected with 'welfare outcomes'").

240 *Financial Lives 2020 Survey: The Impact of Coronavirus*, FCA (Nov. 2, 2021), https://www.fca.org.uk/publications/research/financial-lives-2020-survey-impact-coronavirus [https://perma.cc/CL8Y-QBZB].

241 *See, e.g.*, *G20/OECD Report on Lessons Learnt and Effective Approaches to Protect Consumers and Support Financial Inclusion in the Context of COVID-19* (2021), https://www.oecd.org/daf/fin/financial-education/G20-OECD-report-on-financial-consumer-protection-and-financial-inclusion-in-the-context-of-covid-19.pdf [https://perma.cc/BM2E-3DCV].

decision-making to protect shareholders' interests by only considering the basic investment expectations of financial consumers. *Although the product governance strategy focuses on constructing internal firms-process devoted to matching product characteristics and consumers' backgrounds, its (methodological) scope could be extended to any corporate resolution that entails a conflict between shareholders' and stakeholders' interests*. While shareholders want insiders to maximize the rent the firm receives from consumers, stakeholders, and especially consumers, demand the firm protect their welfare needs and claims, even at the cost of short-term losses for the company. The product governance understanding can mitigate the conflict between these constituencies and allow corporate governance and financial regulation to accomplish similar goals.

D. *High-Tech Entrepreneurial Industry*

Unlike established public firms, one prominent feature of privately held companies' business activities in the high-tech industry is resource scarcity. A lack of resources impedes entrepreneurial activities and contributes to start-up failures.[242] It is common to say that the primary inputs required for achieving innovation and generating value are finance, human capital, knowledge, and physical infrastructure.[243] Whereas private investors, such as venture capitalists ("VCs") and angels,[244] are the traditional primary sources for injecting equity, knowledge, and training at the nascent stages of development,[245] the availability of other sources of inputs provided by critical stakeholders is dependent on the economic and institutional conditions of a given market.[246] At the beginning of the company's activities, the separation

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242 *See* Sam Garg, *Venture Governance: A New Horizon for Corporate Governance*, 34 ACAD. MGMT. PERSP. 252, 255–56 (2020); *see also* SIMON WITNEY, CORPORATE GOVERNANCE AND RESPONSIBLE INVESTMENT IN PRIVATE EQUITY 197–200 (2021).

243 Zhe Cao & Xianwei Shi, *A Systematic Literature Review of Entrepreneurial Ecosystems in Advanced and Emerging Economies*, 57 SMALL BUS. ECON. 75, 81 (2021).

244 Will Gornall & Ilya A. Strebulaev, *The Contracting and Valuation of Venture Capital-Backed Companies*, HANDBOOK OF THE ECON. OF CORP. FIN., VOL 1: PRIV. EQUITY & ENTREPRENEURIAL FIN. *6 (2022) ("Companies have a variety of options to fill this financing gap. Angel investors, who are often wealthy individuals investing their own money in arms-length startups, are a common option.").

245 *See generally* PAUL ALAN GOMPERS & JOSHUA LERNER, THE VENTURE CAPITAL CYCLE (2004).

246 Cao & Shi, *supra* note 243, at 85.

between ownership and control is less evident because entrepreneurs-CEO typically own significant shares in their companies.

Consequently, there is less concern for founders' opportunistic behavior against the interests of VCs and angels because such conduct will impair their financial interests, given the firm's limited resources and small cash flow.[247] Moreover, since the early stages, companies have a critical dependency on financiers, perceiving their goals as devoted to increasing shareholder value solely corresponds to their business needs. However, because high-potential innovative start-ups generally need far more substantial resources than founders and financiers can usually deliver, they seek additional sources of inputs that produce complex ownership structures with preferable rights, varied investment time horizons, and different exit preferences.[248] Because the later stages of the company development require additional and idiosyncratic inputs for innovation, confining business activities to increase shareholder value impairs the ability of the company to generate value for its benefit. Stakeholders aware of the conclusive priority provided to shareholder interests will refrain from giving firm-specific assets to the company unless they are given valuable guarantees that secure their rights against any possible opportunism by the company's insiders.[249] As the protection of the interests of shareholders intensifies, the company will eventually obtain the resources required for innovation, but in unfavorable terms reflecting the urgent business needs (especially in periods of crisis) and the preferable bargaining powers of stakeholders.

Furthermore, securing shareholders' interests and designing governance norms for their ultimate protection, without allowing stakeholders to participate in the company's decision-making, could entrench the entrepreneurs-CEO who refuse to surrender control even if it damages value. This last argument was explored empirically by Noam Wasserman, who argued that founders face a "control dilemma" in which a start-up's resource dependence drives a wedge between the start-up value and the founder's ability to continue retaining control

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247 Jonathan D. Arthurs & Lowell W. Busenitz, *The Boundaries and Limitations of Agency Theory and Stewardship Theory in the Venture Capitalist/Entrepreneur Relationship*, 28 ENTREPRENEURSHIP THEORY & PRAC. 145, 147–54 (2003).

248 *See e.g.*, Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155 (2019) (for a comprehensive discussion).

249 For an extensive discussion of the variety of entrepreneurial finance instruments, *see e.g.*, J. Brad Bernthal, *The Evolution of Entrepreneurial Finance: A New Typology*, BYU L. REV. 773, 789–817 (2018).

over the decision-making process.[250] While during the early stages of the firm's lifecycle, the founder's skills and inputs are better suited to the challenges faced by the young start-up and his contribution is conceived as fundamental for producing value for the corporation, as the start-up's needs extend beyond technical or scientific challenges, the founders' skills are less suited to these new challenges. At later stages, attaining valuable external resources is essential for the ability of the company to generate value. Because entrepreneurs' contributions have diminishing marginal utility, entrepreneurs whose business decisions prioritize maintaining control of the start-up by securing the sole interests of shareholders may grow less value than the entrepreneurs whose founding decisions prioritize the attraction of valuable resources.[251]

The above discussion implies the need to distinguish between the earlier and later stages of a start-up's life cycle when one articulates its purpose as an independent legal entity, and as a result, understands the nature of directors' fiduciary duties of care and loyalty. When considering imposing liability on directors of venture-backed firms for breach of fiduciary duties, several matters should be considered. On the one hand, there is a need to incentivize directors to engage in innovative decision-making under uncertain conditions by mitigating concerns for judicial ex-post hindsight bias. On the other hand, any start-up needs to attract a wide range of resources to allow the creation of social and economic values in highly competitive and uncertain markets. Because companies may have incentives to externalize costs on stakeholders who generally do not have a direct voice in the company's decision-making, the law must provide additional protection to stakeholders who cannot rely on the contractual assurances solely. This is especially prevalent when the company reaches maturity and asks stakeholders to provide firm-specific investments to attain far-reaching innovation goals. At this later stage of the firm's life cycle, insiders' fiduciary duties must reflect the move from increasing shareholder value to protecting the interests of all stakeholders involved.

250 Noam Wasserman, *The Throne vs. the Kingdom: Founder Control and Value Creation in Startups*, 38 STRATEGIC MGMT. J. 255 (2017).
251 *Id.* at 273.

VII. Conclusion

The recent pandemic has changed how companies run their businesses: it has forced companies to adopt an innovative philosophy to tackle financial and social challenges. This Article explored the implications of this change by reassessing core assumptions of company law and theory by focusing on the company purpose debate. It suggested reformulating the discussion by acknowledging the dynamic nature of business activities and needs. By recognizing the multi-level characteristics of business challenges, this Article demonstrated the flexibility of the goals a company may realize. Specifically, this approach integrates the implications of the company's life cycle and the industry in which it operates to balance the interests of numerous constituencies to generate value for the corporation as an independent and separate legal entity.