THE CASE FOR INTRODUCING STAKEHOLDER CORPORATIONS

Shann Turnbull
sturnbull@mba1963.hbs.edu

ABSTRACT

The objective of this paper is describe how the nature of corporations can and should be reformed to make them an explicit instrument for building an efficient, equitable and sustainable society that is locally controlled. The paper traces how the current concerns over the role of the modern corporation arose from their origin as an explicit instrument of political and economic colonisation. While rights of perpetual succession were consistent with the political origins of corporations, this allows investors to get overpaid with "surplus profits" that exacerbates global inequality in income and wealth. Another problem arises from democracy being undermined by family ownership and/or through what Peter Drucker describes as "pension fund socialism". Tax incentives are proposed to provide shareholders a bigger, quicker less risky short term profit in return for changing corporate constitutions to transfer their property rights to stakeholders over 20 years. The competing interests arising from stakeholder governance introduces self-governance, sustainable competitive advantages and enriches democracy. A Global Community Investment Code to promote the adoption of incentives to create stakeholder corporations is suggested in multi-national forums to counter concerns over globalisation.

JEL Classifications: D21, D31, E61, F02, G38, L16, N20

Key words: Community Investment Code, Corporations, Democracy, Globalisation, Ownership transfer, Stakeholders, Surplus profits

Authors affiliations: Dr. Shann Turnbull is the Principal of the International Institute for Self-governance based in Sydney Australia and a Fellow of the Institute for International Corporate Governance and Accountability based at the George Washington University Law School in Washington, D.C. He is an Honorary Associate of the Asia Pacific Research Institute at Macquarie University and an adjunct at the University's Graduate School of Management in Sydney, Australia.

PO Box 266,Woollahra, Sydney, Australia, 1350
Ph: +612 9328 7466, Fax: +612 9327 1497, Mobile +0418 222 378
http://members.optusnet.com.au/~sturnbull/index.html

This paper can be downloaded without charge from the
Social Science Research Network Electronic Paper Collection at:
http://ssrn.com/abstract=436400

The Case for Introducing Stakeholder Corporations

Introduction

The current concerns over the role of the modern corporation can be traced to their origin as an explicit instrument of political and economic colonisation. The objective of this paper is describe how the nature of corporations can and should be reformed to make them an explicit instrument for building an efficient, equitable and sustainable democratic society that is locally controlled. The next Section of this paper provides a brief overview of the historical origins and nature of corporations.

In the following third section the problem of corporate investors getting overpaid with "surplus profits" is identified as a process that exacerbates the global inequality in income and wealth. The fourth section explains how family and fiduciary ownership of corporations is undermining democracy.

The fifth section describes how the Anglophone model of corporate governance corrupts executives, corporate performance and the relationships between the company and its stakeholders on whom corporations depend for their existence. An analysis of the advantages of introducing a division of power through the establishment of a conflict watchdog board and different types of stakeholder councils is presented.

The sixth section describes how tax incentives could be used to introduce stakeholder ownership and the profound way in which this would change the size and operations of corporations. This section suggest that just as the life of patents has been limited to 20 years by nations of the world, the life of corporate shares should also terminate over the same period.

The concluding seventh section summarises the arguments for promoting stakeholder corporations through a Community Investment Code (CIC) to localise and democratise corporate capitalism. A call is made to governments to promote this reform through the United Nations, World Trade Organisation and/or by other international agreements.

Corporate origins and concepts

The corporate concept had it origins in the Letters Patent and Charters granted by the English Sovereign to delegate administrative discretions to monasteries, towns, universities, guilds and trading ventures. In 1494 the Pope decreed that the Spanish could colonise lands west of 51 degrees west longitude to 129 degrees east longitude with the latter later becoming the Western Australian border. The Portuguese obtained the other half of the World to explain why Brasilians and Timorese speak Portuguese while Spanish is spoken in the Western portion of South America and in the Philippines. The Pope's decree provided an incentive for England to establish its own Church in 1536 and acquire colonies by force. However, unlike other colonising powers, the English Sovereign "privatised" the process by granting charters to merchants to fund the operations that also provided tax revenues on the goods imported.

In the Sixteenth century the English Sovereign issued charters for exclusive trade with Russia (1553) Africa (1553), Turkey (1578), Scandinavia (1579) and Guinea (1588). It was the granting of a charter in 1600 to the 218 persons who became associated as *The Governor and Company of Merchants of London trading into the East Indies,* which firmly established the process of private money financing colonisation. It was not until 1813 that the East India Company lost its monopoly rights in India.

The Case for Introducing Stakeholder Corporations

The East India Company had a licence to not only trade but to raise its own armies to protect is activities and rule in the name of the Sovereign and even coin money and make its own laws. Initially, no corporate entity was created and no shares issued as the concept of permanent equity had yet to be invented. Investors contributed funds to finance each trading ship to seek both returns OF and ON their money when the ship was sold with all its goods after each voyage. In 1662 limited liability was provided to protect investors not from creditors but from their directors calling up additional funds to finance new ships.

After the collapse of the South Sea Bubble with companies that had been established under common law, the association of more than 20 investors was made illegal in 1720 unless approved by an Act of Parliament. It remains illegal in England and many of her former colonies today forcing investors to incorporate.

Other colonising companies chartered in England were the Virginia Company (1606), Bermuda (1611), and the Hudson Bay company (1648). The first domestic English company was established in 1619 to provide water to London. Like road toll-ways this allowed private money to fund public infrastructure that later became owned by the crown. During the last thirty years this process of private investors Building, Owning Operating and Transferring (BOOT) infrastructure to the State has been re-discovered as a means for governments to finance projects like the tunnels under Hong Kong and Sydney Harbours.

Both historical and contemporary practices illustrate that investors do not require the rights of perpetual succession that are currently provided to modern corporations[i]. Sovereigns had the rights of perpetual succession and they wanted the companies they created to likewise serve them and their heirs in perpetuity to colonise and rule foreign lands in their name. It is this political attribute of corporations that is today subrogating both national sovereignty and democracy to fuel the concerns of globalisation protestors.

The current concerns are not new. They existed with American citizens after their war of independence from England. Having fought for their political independence they did not want to loose it again by being ruled by corporations controlled in England[ii]. To avoid this possibility any corporation established by a State Legislature would only be chartered for a limited time period to carry out specified activities. The States reserved the right to revoke the charter of any company that undertook unauthorised activities or those that introduced harms or injuries. Legislators usually denied charters to would-be incorporators when communities opposed their prospective business project.

By the beginning of the 19th century some 200 companies had obtained charters in the USA to carry out necessary public works. All of these charters limited the life of the company to 20 or fewer years including the Second Bank of United States established in 1816. Its charter was not renewed in 1836 even though its manager provided bribes to the media and members of Congress[iii].

However, the ability of companies to buy both judges and legislators increased as companies became richer and more influential[iv]. As a result, by the middle of the 19th century corporate law in most States of the USA placed no limits on either the life of companies or the activities in which they could undertake. In 1886 the Supreme Court recognised that corporations had the same rights as natural person under the US constitution, even though unlike a citizen they had unlimited life.

Companies in Europe were established under common law that denied the ability to create an artificial entity with unlimited life. The deed of association between investors made provision for the enterprise to be wound up or reconstituted after a specified number of years or when shareholders funds were reduced by a specified amount. The latter provision protected the managers from becoming liable for the debts of the business. Investors avoided personal liability by not being involved in the business operations by controlling the managers through a supervisory board.

When European governments introduced civil laws for corporations in the 19th century the supervisory board feature was adopted with the granting of unlimited life to the company. Likewise the common law precedent of not allowing trading liabilities to flow through to partners not involved in management was adopted by civil laws establishing limited liability partnerships. However, many such partnerships had limited life to provide investors with a way to exit the business without the need for a public exchange to dispose of their interest.

Limited life business equity investments also had important governance implications. Managing partners or directors that did not treat their investors fairly did not get re-hired to manage the successor enterprise established to provide continuity for the business operations. Another problem arising from the ability of enterprise to exist with unlimited life is that it allows investors to obtain profits in excess of the incentive to invest described as “surplus profit”. This problem is considered in the following Section.

Surplus profits

The author identified the concept of surplus profits when he worked as a financial analysis for an affiliate of the Standard Oil Company in New York City in 1962. At that time it was then the largest corporation in the world and I was undertaking a summer job between the two years of study for a MBA at Harvard. It took another ten years to discover that economists were not aware of surplus profits and related concepts like self-financing assets that can make economic development self-financing[v]. Economists are not likely to accept that surplus profits exist, as knowledge of them has not been required for them to gain their qualifications and reputations.

One reason why economists and others cannot learn about surplus profits is because they are not identified or measured by accountants. Accountants identify and measure profits within an annual accounting period. Surplus profits usually do not arise until a later time. Another problem is that accounting information obscures the fact that all wealth creating business investments not only pay for themselves but also generate additional values, which represent a “free lunch” for society. Many economists also dismiss the existence of free lunches to deny them insight into how economic development occurs.

Accounting doctrines are misleading and deceptive by allowing “profits” to be reported before the cost of an investment has been recovered. This practice also obscures the ability of business investments to become self-financing because they treat a return OF the investment as a cost before estimating the return ON the investment. The so-called profits reported before the investment has paid for itself is reduced by an artificial cost called “depreciation”. This helps to make it look unlikely that profits will be sufficient to recover the cost of the investment and it also attenuates the reporting of any “excessive” profits. There are endless debates as to what represents an excessive profit but surplus profits are a different concept as explained below.

The Case for Introducing Stakeholder Corporations

The Standard Oil Company in 1962 obtained multi-million dollar investment proposals from affiliates around the world to build oil refineries, chemical plants, and so on. Projected cash flows were submitted over the projects operating life of 20 years or more. However, the value of future cash was discounted at a compound rate of at least 15% per year that reduced the economic value of any expected returns after ten years to a negligible value[vi]. But there were political, social and foreign exchange risks that made reliance on receiving sufficient cash over ten years unacceptable. So investments were made only on the cash expected within the foreseeable future described as the "investment time horizon". For some high-risk countries their investment time horizon was as short as three or four years. For the least risky countries it was ten years. All cash emerging after the investment time horizon is by definition a "surplus profit".

All investments were made on the expectation that all the cost of the investment and a competitive profit to compensate for the risk of loss would be obtained within the time horizon. This was true no matter how large the investment. For an investment with an operating life of 20 years in a country with a four-year time horizon, this meant that surplus profits would be generated for 16 years! So surplus profits, defined as the profit in excess of that needed to provide the incentive to invest, can typically be two, three, or more times the original cost of the investment. This is the extent to which multinational corporations can extract surplus profits from their host countries to suck out economic value, living standards and their foreign exchange earnings.

The concept of surplus profits may at first appear to be an oxymoron as there is no limit to human greed and so no limit to the profits sought by investors. However, it is the human drive to maximise the size of short-term profits that investors will select a limited life investment in preference to those with smaller short-term profits that do not limit the time of obtaining long-term and so more uncertain returns.

A limited life equity investment does not limit the size of the profit that an investor can obtain during the life of the investment. So arguments about "excessive" profits before the investment time horizon can continue. Surplus profits are different because they depend upon the investors time horizon and cash flows while judgements about profits being excessive are based on accounting concepts and the deceptive information they produce.

The life of all physically productive assets is limited because the productive process wears them out or depletes their capability to produce be they man-made or natural assets. This is commonly recognised by tax laws by providing depreciation and depletion deductions over the estimated productive life of the asset. While intellectual property cannot wear out it can be become obsolete. In any event all productive intellectual property rights have limited life with patents rights limited to twenty years. While investors are allowed to write off the cost of their investment for tax purposes they are not necessarily required to also write off their ownership rights. The availability of the tax deductions could be made conditional upon the pro-rata transfer of the ownership as proposed below through an international CIC.

Time limits on the life of equity investment in productive, natural and intellectual assets are universally accepted. The only exception to limited life investments is in the ownership of realty and corporate stock. Both of these exceptions make contemporary forms of capitalism inefficient and unequitable as investors can get overpaid. It is also unstainable without governments redistributing income to consumers to maintain production. Governments are also needed to protect their citizens and the environment because of the lack of corporate accountability discussed later.

The nature of property rights created by society can be changed by society. How this might be achieved on a politically attractive basis for both realty and corporate property rights is also set out in my 1975 book, *Democratising the Wealth of Nations*[vii] and in many other writings[viii].

The present system of corporations issuing shares with unlimited life needs to be terminated to reduce the overpayment of investors and the concentration of wealth. A major problem is that economists have neither the intellectual tools nor the empirical facts to explain how corporations concentrate wealth. Without the full knowledge of how wealth inequality is exacerbated governments are forced to redistribute wealth through taxes and welfare. This in turn increases the size, power and dead weight of government to increase the alienation of citizens. Citizens are also alienated from the control of corporations as is described in the following section.

Corporations undermine democracy

A relatively small minority of wealthy families control most corporations in the world whether or not they are publicly traded. Corporations create the larger share of the wealth of nations and determine the manner in which it is created yet they are not directly accountable to the people on who they depend for their existence.

It is only in the USA, Canada, and the UK that institutional investors own a majority in value of publicly traded corporations[ix]. Even in the USA, the founding entrepreneur or a family dynasty controls around 20% in number of the 500 largest companies[x]. In Japan, Germany, France, Italy and other mature industrialised economies, family companies control many others through complex corporate cross ownership arrangements[xi]. The complexity of the arrangements results in the corporate managers exercising control over many companies rather than the ultimate owners.

Institutional ownership is growing rapidly in many countries as governments encourage their citizens to rely on privately funded pensions to reduce the need for taxpayer funded pensions. But institutional ownership introduces what Peter Drucker[xii] described in 1976 as "Pension fund socialism". At that time US institutions owned less than half as much in value of publicly traded corporations than 25 years later. Institutions obtain much of their investment advisory and management business from the corporations in which they invest for their clients. This creates an unholy alliance between fund managers and corporations to not blow the whistle on each other. The result is that institutional investors are reluctant to vote at annual general meetings against proposals put forward by management. As a result, institutions become negligent owners who do not fully exercise their ownership responsibilities. Managers become accountable only to themselves.

The impotence of institutions to act as owners is compounded by most of them being fiduciary agents for pension plans and other beneficiaries. By law a fiduciary agent cannot take into account any other issue but the economic welfare of the beneficiaries. This means that fiduciary shareholders do not have a mandate to make corporations accountable in regards to non-economic issues like their political, ethical, social and environmental behaviour. This is why it is important that the shareholders of record in corporations are real people who can make management accountable for non-financial issues that may concern them.

Citizens who have their savings in pension plans, employees who own shares in their employer through a trust and others who hold their shares through nominee companies become second class owners. This is because they are not members of record of the company. A fiduciary agent represents them with a narrow remit for making managers accountable. In many cases the agent has

conflict of interest in making management accountable. While some countries require employee share plans to pass through the right of employees to vote their shares this introduces administrative difficulties exacerbated by many plan trustees having conflict from being management or beholden to management. In any event some rights of ownership cannot pass through. For example, the right to be included in a quorum of a shareholders meeting or the right to participate in requisitioning a meeting when this is determined by the number of shareholders of record.

The need to democratise the political and economic power of corporations is most compelling. The ability of corporations to "buy governments", as occurred in the USA in the 19th century, has not diminished in the 21st century. Indeed, it may have increased with around half the largest economies in the world being transnational corporations. Just 500 corporations control 70% of global trade and 1% of the transnational corporations on the planet own half the total stock of foreign direct investment[xiii]. That so much economic activity is controlled by so few means that both democracy and sovereignty has been hollowed-out in nations around the world.

While family ownership of corporations eliminates corporate managers from being accountable only to them selves it allows corporate wealth to be applied to buy judges, politicians and media influence to establish a plutocracy. Government ownership allows the private interests of politicians to dictate corporate activities. Institutional ownership denies meaningful corporate accountability to their ultimate owners and citizens in general. The direct ownership of corporate stock by citizens provides one step in making corporations both accountable and responsive to the will of the people.

However, direct ownership can raise a number of problems for sovereignty and democracy. National, regional and community sovereignty can be undermined by corporations operating across political jurisdictions. This also confounds democracy. Democracy can also be undermined by the lack information, will and capability for citizens to take collective action. To mitigate these problems the reform of corporations needs also to reduce their size and scope to allow their ownership and control to be more focused on national and sub-national political constituencies.

One way to localise the control of corporations, if not also their ownership, is through involving their various stakeholder constituencies. No Company can exist without workers, customers and suppliers, including those providing infrastructure services in the host community. For this reason they will be described as "strategic stakeholders". How the control, and also the ownership of corporations, can be vested in its strategic stakeholders with tax incentives supported by a CIC is next considered.

Democratising corporate control

The dominant form of corporate control is through a unitary board that concentrates corporate power and conflicts of self-interest of its members[xiv]. This Anglophone model of a centralised corporate command and control system is little different from that of many former socialist nations whose economic activity might not have exceeded that of some of the larger transnationals enterprises.

The symbiotic self-serving relationship between board members and corporate executives allows both to overpay themselves when institutional and other minority investors are the dominant owners. To avoid the corruption of directors and corporate performance a division of power is required as is mandated in some jurisdictions that require corporations to have a supervisory and/or a watchdog board. However these may or may not achieve their purpose according to how they are

constituted. When a dominant family or other shareholder is present, they may provide a watchdog role on executive pay and performance. However, dominant investors can also use their power to transfer value from a public company to their own private interests to oppress minority shareholders.

To both democratise corporate control and introduce political, social and operational competitive advantages at least two types of watchdog boards are required. To counter what Lord Hailsham[xv] described as an "elective dictatorship" investors need to appoint a conflict of interest watchdog on a democratic basis of one investor one vote to counter the plutocratic control of corporations by a dominant shareholder with one share per vote.

However, so as to protect and not disenfranchise the property rights of investors the conflict watchdog would not obtain operational executives powers. It would only have power to blow the whistle directly to investors on the oppression of minority interests from related party transactions or any other type of conflict of interest. These conflicts are intrinsic in all board decisions concerning the remuneration and nomination of directors or the accounting procedures used to meet accounting standards in audited reports. Details of how these arrangements could work are set out in my article posted on the World Bank anti-corruption strategies web page on Improving Corporate Structure and Ethics: A Case for Corporate "Senates"[xvi]. The conflict board or "Corporate Senate" would also control the conduct of shareholder meetings and the election of directors to avoid directors having a conflict in being accountable to investors.

Even with a conflict board the role of the operational board is fundamentally flawed in its fiduciary duty to monitor, control, evaluate, remunerate and/or dismiss management. To carry out this role with any creditable due diligence and vigilance, operational information independent of management is required to evaluate the Strength Weaknesses, Opportunities and Threats (SWOT) of both the managers and the business. It is not practical for non-executive directors to spend the time to do so. Even if they spent the time they could jeopardise their relationship and tenure of themselves or their informants with management. It suits management for corporate governance codes and experts to seek the appointment of directors who are not associated with the company to monitor management as these people have the least knowledge or authority so to do.

The individuals that have the most inside knowledge and authority about the integrity of a business, its managers and its SWOT, are its strategic stakeholders as defined above. Separate councils elected independently by the different classes of stakeholder constituencies provide a basis for establishing operational watchdogs. But more importantly they provide a basis to provide operational feedback information to sustain competitive advantages. In addition they provide a forum for corporations to constructively engage with the individuals on who they depend to sustain their operations and existence. Perhaps the most valuable consequence of corporations politically engaging with their stakeholder constituencies is that it would counter the alienation created by globalisation. The councils would provide representation and a voice for citizens effected by the operations of the company. In this way corporations would enrich democracy instead of undermining it.

There is a compelling case for stakeholder councils to be mandated in any industry in which a government regulates to protect investors and or stakeholders[xvii]. Contemporary corporate activities are far too complex and fast moving for any centralised command and control bureaucracy to identify and react sufficiently fast to protect citizens from the any risks to their health, safety and financial security from corporate actions or in-actions. Regulation of complexity is not possible without a matching variety of information feedback and control that an appropriate mix of

stakeholder councils can provide[xviii]. This approach also simplifies regulatory law and the cost of regulation.

Another role of stakeholder councils is mitigating the capture by corporate management of price and other regulators in ways that disadvantage stakeholders. Citizen Utility Boards (CUB's)[xix] established by customers of privately US owned power and gas corporations illustrate how customer councils can protect stakeholders. CUBs also illustrate the practicality of forming and operating stakeholder councils when millions of constituents may be involved.

The practicality of also distributing economic value to a large numbers of stakeholders is illustrated by "frequent flyer" and fly-buy loyalty promotions. The distribution of corporate ownership rights to stakeholders with such types of arrangements provides a way to greatly enhance the engagement of them in corporate control. How this can be achieved is now considered.

Democratising and localising ownership

The reversion of ownership from investors to stakeholders would both democratise and localise ownership as at least the employees and those supplying infrastructure services would represent the host community. In addition, there could be other local suppliers as well as locally based customers.

A reduced corporate tax for those companies whose shareholders voted to establish a stakeholder class of shares provides one politically and economically attractive way to democratise and localise ownership. The tax deduction would produce higher quicker profits with less risk with a greater value than the smaller, long-term and more uncertain profits expected without a tax benefit. The compounding discount on the future value of money for investors allows the tax incentive to be quite modest[xx].

The creation of stakeholder shares that were eventually vested as a class with all the property rights of the shares issued to investors would create what I describe as an Ownership Transfer Corporation (OTC). The stakeholder shares would be issued to individuals who were customers or employed by customers, the company or by its suppliers according to their economic contributions. Only voting citizens or their guardians would be eligible to become an owner or record of stakeholder shares, as is the case for fly-buy points.

To create parity with patents, investor shares would loose all their property rights after 20 years. There are various ways this objective could be reached. Some countries might use a tax incentive to require 5% of the ownership rights to be transferred each year. Others might provide little or no a tax incentive with no ownership transfer for ten years but then a 10% pa ownership transfer for the residual ten yeas. In the past investors in some Socialist countries have accepted the lost all ownership at the end of a 20-year period so as be able to invest. While these details could be optional what is needed through bodies like the World Trade Organisation are agreements to limit the property rights of shares to the same time period adopted around the World for patents. The CIC is so named because such agreements would result in the localisation of ownership.

Localisation of ownership would be concentrated by a profound difference that OTC's would introduce to the dynamics of corporate capitalism. With their ownership diluting each year, investors would require that all profits be distributed as a dividend because they would loose equity in retained earnings. This would force managers to become continuously accountable to investors for attracting new funds. Expansion of the business would be financed through the establishment of

"offspring" companies financed by dividend re-investment and new issues to local investors. Some offspring shares might be issued to the Progenitor Company to acquire some of its assets but the diluting equity for its investors would provide a disincentive for such issues to make the offspring a subsidiary.

Besides making corporate executives continuously accountable for new funding, OTC's inhibit the formation of giant firms. Growth is achieved by establishing networks of smaller firms as achieved by the stakeholder controlled cooperatives located around the Spanish town of Mondragón that limits the size of any company to employ only 500 people[xxi]. So like the Mondragón cooperatives, OTC's would form networks of firms that are suppliers or customers of each other. This arrangement is also found in a Japanese Keiretsu where a Council of CEO's of their members supervises the network[xxii]. The Keiretsu Council represents a stakeholder council and provides informed committed feedback information to improve the competitiveness of operations and/or restructuring of firms and their relationship. The involvement of strategic stakeholders in the ownership and control of US firms was recommended in a 1992 report on how to make US firms competitive with those in Japan and Germany by Professor Michael Porter[xxiii].

Most members of a Keiretsu council would not hold sufficient shares to obtain the power to make changes but they provide information to the dominant shareholder to do so. Likewise, stakeholder council may be composed of members that have little of no shares. However, they can be very influential from having the power of information, material and intellectual resources and/or custom for the business. Directors could make management sensitive to stakeholder concerns by tying executive bonuses to performance indicators determined by the stakeholders. The value of stakeholder councils is not depended upon the company being an OTC. However, with an OTC the stakeholders also obtain votes as shareholders. However, stakeholder councils do not subordinate the authority of directors, as power must still be exercised through shareholder meetings[xxiv].

The technical details of OTC's are expanded in a number of professional articles listed in the footnotes. The compelling advantages of establishing stakeholder corporations through the adoption of OTC's are next considered.

Concluding remarks

In summary, the case for the introduction of stakeholder owned and controlled corporations is supported by providing a basis for improvements in efficiency, equity, justice, competitiveness, sustainability, democracy and accountability. There a number of supporting reasons for each of these six considerations as summarised below.

1. Efficiency
   - (a) Minimise overpayments to investors through ownership transfer
   - (b) Minimise overpayments to employees through watchdog boards
   - (c) Re-investment not restricted to corporate activities and subject to market forces
   - (d) Reduced cost of government transferring income through taxes and welfare
   - (e) Improved quality control of goods and services from feedback by stakeholder councils
   - (f) Minimise cost of procuring goods and services by supplier bonding
   - (g) Minimise cost of organising production with employee bonding
   - (h) Other costs minimised by increasing trust between stakeholders

2. Equity
   - (a) From checks and balances against exploitation

(b) Distribute wealth more in accordance with contributions made by stakeholders to build a universal citizen's income/social security

3. Justice
(a) Power differentials between stakeholders reduced to minimise exploitation and social alienation
(b) Injustices minimised through disclosure from diverse stakeholder forums to provide the other side of the storey in any disputes
(c) Dispute resolution process built into governance system with a conflict board

4. Competitiveness
(a) Speedier, more accurate and effective feedback on problems
(b) Superior information and resources to improve performance

5. Sustainability
(a) Enhanced identification of risks to the business and stakeholders
(b) Increased resources to manage risks through stakeholder involvement
(c) Enhanced resource management through mutual interdependence
(d) Creditable basis for self-regulation to reduce the role of government

6. Democracy and accountability
(a) Widening the accountability of firms to the people that they affect
(b) Enriching democracy with inclusive civil participation in government or private firms (Creates technique for privatisation and localisation)
(c) Furthering the political and social acceptance and legitimacy of business

The development of the corporate concept was not moulded in any significant way on the need to further any of these six objectives. As result, contemporary concepts of a corporation are inconsistent with the most fundamental assumption justifying a market economy that competition will limit the overpayment of investors. The transfer of these overpayments to stakeholders provides a "third way" to taxes and welfare for distributing the wealth of nations by contributing to a universal minimum income. The transfer of surplus profits mitigates the inequality in wealth without introducing bigger and more intrusive government. OTC's provide a way to privatise the tax and welfare system while enriching democracy instead of undermining it.

The existing colonising static, monopoly and perpetual property rights of corporate stock needs to be replaced with ecological property rights created by OTC's. These are dynamic, inclusive and time limited like all living things.

The hierarchical command and control system of modern business introduces information overload while paradoxically not providing directors with sufficient information to manage the complexity of contemporary business let alone take account social, ethical and environmental concerns. Nor can these non-financial topics be a concern for fiduciary shareholders. To overcome both these problems corporations need to limit their size to human scale and adopt ecological patterns of control as illustrated in the Mondragón cooperatives[xxv]. This objective is achieved with stakeholder corporations. They provide a way to reform the process of globalisation to enrich democracy at all levels and enrich all individuals and society on a sustainable basis. This provides compelling reasons for international agreements, the United Nations and/or the World Trade Organisation to promote the concept of Stakeholder Corporations through a Community Investment Code.

oooOOOooo
5594/04112001

---

[i] Turnbull, S, 1998, 'Should ownership last for ever?', *Journal of Socio-Economics*, 27:3, pp. 341–63, <http://papers.ssrn.com/paper.taf?abstract_id=137382>

[ii] Grossman, R.L. & Adams, F.T. 1993, *Taking care of business: Citizenship and the charter of incorporation*, Charter Ink, Cambridge, MA.

[iii] Galbraith, J.K. 1976, *Money: Whence it came and were it went*, Pelican Books, p. 89.

[iv] Grossman & Adans op cit note ii, p. 16.

[v] A detailed explanation is presented in Turnbull, S. 1992, 'New Strategies for Structuring Society From a Cashflow Paradigm', presented to the Fourth Annual Conference of the *Society for the Advancement of Socio-Economics*, Graduate School of Management, University of California, Irvine, California, USA, March 27, <http://cog.kent.edu/lib/turnbull1/turnbull1.html>

[vi] The Present Value at various discount rates is presented in Turnbull, S. 2000, 'Stakeholder Governance: A cybernetic and property rights analysis', *Corporate Governance*: *The history of management thought*, Ed. R. I. Tricker, pp. 401–13, Ashgate Publishing, London. <http://cog.kent.edu/lib/turnbull6/turnbull6.html>.

[vii] Turnbull, S. 1975, *Democratising the Wealth of Nations*, Company Directors' Association of Australia Limited, Sydney, <http://cog.kent.edu/lib/TurnbullBook/TurnbullBook.htm>.

[viii] Turnbull, S. 1973, 'Time limited corporations', *ABACUS: A Journal of Business and Accounting Studies*, Sydney University Press, 9:1, June, 28–43.

__________ 1991, 'Re-inventing Corporations', *Human Systems Management*, 10:3, pp. 169–86.

__________ 1993, 'Flaws and Remedies in Corporatisation and Privatisation', *Human Systems Management*, 12:3, pp. 227–52.

__________ 1994, 'Stakeholder Democracy: Redesigning the Governance of Firms and Bureaucracies', *Journal of Socio-Economics*, 23:3, Fall, pp. 321–60.

__________ 1997, 'Stakeholder Co-operation', *Journal of Co-operative Studies*, Society for Co-operative Studies, 29:3, pp 18–52, (no.88), Manchester, January.
<http://papers.ssrn.com/sol3/papers.cfm?cfid=196284&cftoken=90592070&abstract_id=26238>

__________ (1998), op. cit.

__________ (2000), op. cit.

[ix] Shleifer, A. & Vishny, R.W. 1996, *A survey of corporate governance,* National Bureau of Economic Research, Working paper 5554, Cambridge, MA.

[x] Zey, M. 1999, 'Major changes in corporate strategy and structure of the Fortune 500 in the 1990s', Paper presented to the 11th Annual Meeting of the Society for the Advancement of Socio-Economics, University of Wisconsin, July 11th, Madison, (Working paper available from author at Texas A&M University).

[xi] Becht, M. & Röll, A. 1999, 'Blockholding in Europe: An international comparison'*, European Economic Review,* 43, 1049–56. Japan is included in Analytica 1992, *Board directors and corporate governance: Trends in the G7 countries over the next ten years,* Oxford Analytica Ltd., England.

[xii] Drucker, P. 1976, *The unseen revolution: How pension fund socialism came to America*, Harper & Row, New York.

[xiii] <http://www.afsc.org/pwork/1099/1008.htm> visited November 3, 2001.

[xiv] Turnbull, S. 2000, 'Why unitary boards are not best practice: A case for compound boards', presented to the First European Conference on Corporate Governance, Belgian Directors' Institute, November 16th, Belgium's National Bank Brussels. <http://papers.ssrn.com/paper.taf?abstract_id=253803>

[xv] Hailsham, Lord, 1978, *The Dilemma of Democracy: Diagnosis & Perscription*, p. 127, Collins, London.

[xvi] Turnbull, S. 1993, 'Improving Corporate Structure and Ethics: A Case for Corporate "Senates"', *Director's Monthly*, National Association of Company Directors, 17:5, pp. 1-4, May, Washington, D.C. <http://www.worldbank.org/devforum/files/struc-and-eth.pdf> A detailed description is presented in Turnbull, S. 2000, Corporate Charters with Competitive Advantages', *St. Johns Law Review*, St. Johns University, New York City, 74:44, pp. 101–159, Winter, 2000.<http://papers2.ssrn.com/paper.taf?ABSTRACT_ID=245691>

[xvii] 'Why regulation of financial institutions cannot be assured with a unitary board', 14th Australasian Finance and Banking Conference, The ANA Hotel, Sydney, December 18th, 2001, <http://papers.ssrn.com/paper.taf?abstract_id=310501>.

[xviii] This statement is based on Ashby's Law of requisite variety, Beer S. 1995, *The heart of the enterprise,* pp. 84–96, John Wiley & Sons, Chichester, England

[xix] Givens, B. 1991, *Citizens' Utility Boards: Because utilities bear watching,* Centre for Public Interest Law, University of San Diego, School of Law, California.

[xx] Worked examples are provided in Turnbull 2000 op cit note vi.

[xxi] Turnbull, S. 1995, 'Innovations in Corporate Governance: The Mondragón Experience', *Corporate Governance: An International Review*, 3:3, 167-180, July, <http://cog.kent.edu/lib/Turnbull6.htm>.

[xxii] Analytica, 1992 p. 132, op. cit. Note xi.

[xxiii] Porter, M. 1992, *Capital choices: Changing the way America invests in industry*, A research report presented to the Council on Competitiveness and co-sponsored by The Harvard Business School, Boston.

[xxiv] The arrangements are discussed in Turnbull, S. 2001, 'The competitive advantage of stakeholder mutuals' in *The New Mutualism in Public Policy*, ed. J. Birchall Chapter 9, pp. 171–201, Routledge, 2001, London. http://papers.ssrn.com/sol3/papers.cfm?cfid=196284&cftoken=90592070&abstract_id=242779

[xxv] The "ecological patterns of control" are described as "holons" as explained in Turnbull, S. 2001, 'Design criteria for a global brain', *The First Global Brain Workshop (Gbrain O)*, Vrije Universiteit Brussei, Brussels, Belguim, Thursday, July 5, 2001. <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=283715> Video of presentation linked to <http://www.comdig.de/Conf/GB0/pr010705327.html>