ANALYZING THE BUSINESS ROUNDTABLE STATEMENT ON THE PURPOSE OF A CORPORATION AND LINKING IT TO CORPORATE GOVERNANCE

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Abstract

The 2019 Business Roundtable Statement on the Purpose of a Corporation, endorsed by 183 CEOs of major U.S. companies, is not such a dramatic break from the past, but rather the next step in a steady retreat from a purely financial approach and an evolution to embrace a stakeholder approach, which is now gaining more and more lip service. The major purpose of this paper is to analyze this Business Roundtable Statement and relate it to three major corporate governance issues: CEO pay, non-financial performance metrics, and sustainability reporting. Then the paper introduces the Commonsense Corporate Governance Principles, which were initially published in 2016 and updated with Version 2.0 in 2018, sponsored by 21 CEOs of major U.S. companies. These Principles provide significant guidance and recommendations for corporations, boards of directors, shareholders, and other stakeholders to follow if they want to create an environment-friendly to meet the fundamental commitments in the Business Roundtable Statement. Accordingly, the major sections of this paper are introduction, CEO pay issues, non-financial performance metrics, sustainability reporting, corporate governance impacts, key points in both versions of the Commonsense Principles, key changes in the Commonsense Principles 2.0, discussion, and conclusions.

Keywords: Business Roundtable, Purpose of a Corporation, Commonsense Corporate Governance Principles, Corporate Governance

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1. INTRODUCTION

On August 19, 2019, the Business Roundtable (BR), representing the most powerful Chief Executive Officers (CEOs) in the United States, issued a 300-word Statement on the Purpose of a Corporation. Since 1978, BR has periodically issued Principles of Corporate Governance. Since 1997, each version of the document has endorsed principles of shareholder primacy, i.e., that corporations exist principally to serve shareholders. This new Statement supersedes previous statements and outlines a modern standard for corporate responsibility. It says that "BR members share a fundamental commitment to all our stakeholders and commit to doing well by our customers, employees, suppliers, and local communities. Each of our stakeholders is essential and we commit to deliver value to all of them, for the future success of our companies, our communities, and our country" (BR, 2019a). This new Statement includes signatures by 183 of the 192 current CEO members of the BR.

The Statement says: "While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:

- Delivering value to our customers. We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
- Investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.
- Dealing fairly and ethically with our suppliers. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.
- Supporting communities in which we work. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.
- Generating long-term value for shareholders, who provide the capital that allows companies to invest, grow, and innovate. We are committed to transparency and effective engagement with shareholders".

The Chairman of the BR and CEO of JPMorgan Chase & Co., Jamie Dimon, summarized this Statement: "Major employers are investing in their workers and communities because they know it is the only way to be successful over the long term. These modernized principles reflect the business community's unwavering commitment to continue to push for an economy that serves all Americans" (BR, 2019b). The Chair of the BR Corporate Governance Committee and CEO of Johnson & Johnson, Alex Gorsky, commented: "This new Statement better reflects the way corporations can and should operate today. It affirms the essential role corporations can play in improving our society when CEOs are truly committed to meeting the needs of all stakeholders. This Statement isn't an achievement; it's a call to action" (BR, 2019b).

The world's two largest asset managers also signed this Statement: Laurence Fink, CEO of Blackrock with $6.4 trillion of assets under management with offices in 30 countries and clients in over 100 countries, and Mortimer Buckley, CEO of Vanguard with $5.3 trillion of assets under management. In January 2018, Laurence Fink sent a letter to all CEOs of publicly listed companies around the world urging them to start accounting for the societal impact of their companies and to focus upon economic growth that is sustainable and inclusive for the majority of people (Fink, 2018). Thus, there should be an expanded social and sustainable focus for the long-term value of corporations with implications for the evolution of corporate governance towards that end (Grove & Lockhart, 2019). The former CEO of Vanguard, Bill McNabb, observed: "I welcome this thoughtful statement by BR CEOs on the Purpose of a Corporation. By taking a broader, more complete view of corporate purpose, boards can focus on creating long-term value, better serving everyone – investors, employees, communities, suppliers, and customers" (BR, 2019b).

Although the BR group should be commended for coming around to this broader stakeholder focus, it is undeniably late. It wasn't shareholder democracy that created this new enlightened moment. Public outrage pushed this forward as did anger in Washington D.C. and regulatory scrutiny that is finally coming into focus. Also, Democratic politicians have argued that the narrow focus on shareholder returns has worsened economic inequality, enriching wealthy investors at the expense of workers (Benoit, 2019). Thus, the BR Statement should be seen as a prudent decision as the BR CEOs rightly see the direction the country is headed and have decided to get in front of the parade if they don't want to be trampled by it (Olsen, 2019). Also, most shareholders did not come around until they had no choice but to realize that this oncoming parade could have a negative impact on their investments. However, the Council of Institutional Investors disagreed with the BR Statement and said: "Accountability to everyone means accountability to no one. It is government, not companies, that should shoulder the responsibility of defining and addressing societal objectives with limited or no connection to long-term shareholder value" (Sorkin, 2019a).

The major purpose of this paper is to analyze this Business Roundtable Statement on the Purpose of a Corporation and relate it to three major corporate governance issues: CEO pay, non-financial performance metrics, and sustainability reporting. Then, the paper introduces the Commonsense Corporate Governance Principles, which were initially published in 2016 and updated with Version 2.0 in 2018, sponsored by 21 CEOs of major U.S. companies. These Principles provide significant guidance and recommendations for corporations, boards of director, shareholders, and other stakeholders to follow if they want to create an environment-friendly to meeting the fundamental commitments in the Business Roundtable Statement. Accordingly, the major sections of this paper are CEO pay issues, non-financial performance metrics, sustainability reporting, corporate governance impacts, key points in both versions of the Commonsense Principles, key changes in the Commonsense Principles 2.0, discussion, and conclusions.

2. CEO PAY ISSUES

On a cautionary note, this Statement comes amid a growing debate in the United States about the responsibilities of corporations in a time of stark economic inequality. Similar to the stakeholder perspective of European countries, some U.S.

politicians have proposed a plan that would require U.S. corporations to turn over part of their board of directors to members chosen by employees. The prior BR focus on shareholder-first or shareholder primacy grew to prominence in the mid-1980s and has since become a widely accepted corporate governance norm. Critics say such a focus has driven a fixation on short-term results and helped balloon the size of CEO pay packages, fueled by outsized stock awards. This new BR Statement comes as the gap between the compensation growth of corporate executives and American workers has grown at staggering rates. An August 2019 study by the Economic Policy Institute found that CEO compensation had grown 940 percent since 1978 while typical worker compensation had risen just 12 percent over that same period. One critic said these CEOs created such pay gaps and should volunteer to cut their own salaries by two-thirds and give it back to employees if they really believe in this new Statement (McGregor, 2019a).

On a similar vein, another critic said boards of directors should dramatically increase how much CEOs' compensation is tied to goals outside of financial metrics. Currently, when such non-financial metrics are considered for executive pay, their weightings are typically "infinitesimal" compared to financial metrics weightings. There is also an enormous amount of discretion in how boards consider such non-financial metrics. Currently, any material impact on CEO pay is unclear when other stakeholders are not accounted for (McGregor, 2019a).

Using just financial metrics for CEO pay is still being advocated. For example, International Shareholder Services (ISS) is the U.S.'s leading proxy advisory firm with over 61 percent of the business. Its clients are hedge funds, mutual funds, and asset management firms that own shares of multiple companies, and they pay ISS to advise and often vote their shares regarding all shareholder votes (Wikipedia, 2019). ISS is the most powerful voice in advising investors to vote up or down each year on pay-for-performance plans, as well as board candidates and other initiatives that require shareholder approval. In the past, ISS has been using the following financial criteria to evaluate executive compensation: total shareholder return (TSR) and several traditional accounting measures, like return on equity and EBITDA (earnings before interest, depreciation, and amortization).

However, Bennett Stewart, a senior advisor to ISS, has commented that EBITDA is the world's least accountable financial metric, since it imposes no capital charge. Bennett's firm, Stern Stewart, pioneered the economic value added (EVA) metric that prevents CEOs from gaming the system by using short-term profits, piling on debt, or expanding via pricy acquisitions to increase their own compensation. Among the major public companies that use EVA as a management tool are Coca-Cola, Borg Warner, Ball Corporation, DowDuPont, Clorox, and Deere & Co. In March 2019, ISS announced that it was starting to include the EVA metric as it measures and evaluates corporate pay-for-performance plans. For 2019, ISS will continue to use TSR and traditional accounting measures plus EVA to evaluate pay-for-performance plans but expects to replace all conventional measures, except TSR, with EVA starting in 2020 if client reactions to EVA are positive (Tully, 2019).

The EVA methodology makes two major adjustments to official GAAP numbers. First, it imposes a capital charge on all debt and equity which is deducted from after-tax operating profits in order to compute the excess or real profit to shareholders. Second, EVA makes several adjustments to GAAP numbers to calculate an adjusted earnings number before the capital charge is deducted. Typical adjustments include capitalizing research and development over a five-year period, increasing the LIFO reserve, increasing the allowance for bad debt, and adding implied interest on operating leases (Chen, 2018). Such adjustments do not include non-GAAP manipulations to make executive pay performance criteria as some current executive pay practices are doing (Jackson & Pozen, 2019). None of these CEO pay-for-performance methods included non-financial metrics.

3. NON-FINANCIAL PERFORMANCE METRICS

Critics have said they will be watching for companies to offer the same level of rigorous data reporting and transparency on non-financial performance metrics, like employee diversity, gender pay data, and greenhouse gas reduction, as they do with financial performance metrics in order to achieve the commitments to stakeholders in the BR Statement on the Purpose of a Corporation. These critics argue for regular external audits on non-financial metrics, just like the public companies' requirement for external audits on their financial statements. Accordingly, some companies have already chosen to have non-financial data monitored by an outside party.

Companies can be certified as a "B Corp", a certification given by the nonprofit B Lab to companies, such as Patagonia, New Belgium Brewing, and Ben & Jerry's. Such certified companies must score a minimum of 80 out of 200 points in an assessment review process. This assessment covers the company's entire operation and measures the positive impact of the company in areas of governance, workers, community, the environment, and the products or services that the company provides. Socially and environmentally focused business model points are accrued in their relevant impact area of governance, workers, community, and environment. Companies must integrate B Lab commitments to stakeholders into their company governance documents and be re-certified every three years. As of June 2019, there were 3,023 certified B Corporations across 150 industries in 64 countries (B Corporation, 2019).

One critic said that the key to assessing a company's commitment to the BR Statement on the Purpose of a Corporation is if the "acid test of firm value" continues to be just shareholder, not stakeholder, value. Decision-making tools and related infrastructure for balancing the needs of different stakeholders are needed to support a real, lasting and positive change. Another critic said the key to company commitment is to look for shifts in how companies think about their overall strategy, i.e., are they getting into businesses that help with climate change, focusing on wages and working conditions for employees, and considering the levels of executive pay? Shareholder value should be a goal, but also a result of a company serving its customers, serving its employees, and serving its communities. If they do these stakeholder things well, shareholders will also do fine (McGregor, 2019b).

In 2015, an alternative for corporate purpose was proposed by the European Parliament's Committee on Legal Affairs: "Shareholders do not own corporations. Contrary to the popular understanding, public companies have legal personhood and are not owned by their investors. The position of shareholders is like that of bondholders, creditors, and employees, all of whom have contractual relationships with companies but do not own them" (Tunjic, 2017). Thus, this alternative is not based upon corporations revolving around the interests of either shareholders or stakeholders, but, conversely, where shareholders and stakeholders move around the corporation which has interests in various capital, specifically human, intellectual, environmental, social, production, and financial. The corporation must then store and convert each of these sources of capital to maintain and enhance itself and focus on long-term intrinsic value creation, not short-term financial engineering to meet the numbers for executive compensation (Nocera, 2017). Theoretically, this cycle of capital creation continues into perpetuity, provided the corporate executives and directors demonstrate wisdom by not exploiting the very sources of capital, i.e., by not doing large share buy backs or excessive dividends, but instead by making effective capital expenditures and investments, especially in artificial intelligence technology (Grove & Lockhart, 2019).

4. SUSTAINABILITY REPORTING

Critics have said that this new BR Statement is so vague that it's unclear what it actually means as companies are supposed to balance the interests of shareholders, workers, customers, suppliers and communities. They argue that there are no specific targets nor ways of meeting, measuring, or enforcing them (Samuelson, 2019). Thus, since "what gets measured gets managed", this BR Statement stakeholders' focus needs to be measured and assessed, such as by well-established sustainability reporting. For example, a Governance and Accountability Institute report also found that one-third (167) of the S&P 500 companies had issued Global Reporting Initiative (GRI) sustainability reports in 2011. These reports contained a GRI Content Index, indicating which of the 36 GRI sustainability reporting standards were applied. Also, many of the Fortune 500 companies are issuing sustainability reports, indicating a strategy to help attract talent, increase brand value, and provide marketing to customers (Stevens, 2012). By 2016, 93% of the world's largest 250 companies reported on their sustainability performances, and 82% reported using GRI Sustainability Reporting Standards (Global Reporting Initiative, 2016). These reporting guidelines may be used by boards of directors to help investigate the sustainability operations of their companies, as well as this emerging focus on stakeholders' interests (Grove & Clouse, 2018).

A Carbon Disclosure Rating (CDR) is a numerical score that indicates the level of reporting of a company's climate change initiatives. It is based on a company's response to the climate control questionnaire of the U.K.-based Climate Disclosure Project (CDP). A high carbon disclosure rating indicates a comprehensive response to this questionnaire with a sound understanding and management of climate-related issues, including greenhouse gas emissions. This CDR rating is based on a methodology developed by the CDP in consultation with its global advisor, PWC (PricewaterhouseCoopers). The carbon disclosure score is not a reflection of the actions taken by a company to mitigate its impact on climate change nor offset its carbon footprint, but the score is simply indicative of a company's disclosure level regarding these issues. Most of the world's largest companies have a CDR score. Google Finance now lists a company's CDR score alongside traditional financial indicators, like revenues and profits, and Bloomberg provides sustainability data on all 310,000 of its in-house terminals (Investopedia, 2017).

Using a matched sample of 180 companies, a recent academic study, Eccles, Ioannou, and Serafeim (2014), found corporations that had voluntarily adopted sustainability policies, called High Sustainability companies, significantly outperformed Low Sustainability companies, which had adopted almost no (or less than 10%) sustainability policies. This superior performance by High Sustainability companies included both stock market and financial accounting results over almost a 20-year period from 1992-2010. A $1 investment beginning in 1993 and ending in 2010 was compared for High and Low Sustainability companies. A $1 stock market investment in the High Sustainability companies grew to $14.30 versus $11.70 for the Low Sustainability companies or a difference of $2.60 (18%). For a cumulative financial accounting performance of $1 based on return on equity, the High Sustainability companies grew to $15.80 versus $9.30 for the Low Sustainability companies or a difference of $6.50 (41%). The 27 sustainability policies analyzed in this study could be used by boards of directors in assessing their companies' sustainability policies and performance.

This research study also found that boards of directors of these High Sustainability companies were more likely to be formally responsible for sustainability policies and top executive compensation incentives were more likely to be a function of sustainability metrics. Moreover, High Sustainability companies were more likely to have established processes for stakeholder engagement, to be more long-term oriented, and to exhibit more complex measurement and disclosure of nonfinancial information. The Low Sustainability companies primarily followed the traditional model of corporate profit maximization in which social and environmental issues are predominantly regarded as externalities. In contrast, the High Sustainability companies not only paid attention to externalities but were characterized by distinct governance mechanisms which directly involved the board of directors in sustainability policies and linked executive compensation to sustainability objectives. These High Sustainability companies exhibited a much higher level and deeper stakeholder engagement; a longer-term time horizon in their external communications matched by a larger proportion of long-term investors; greater attention to nonfinancial measures regarding employees; a greater emphasis on external environmental and social standards for selecting, monitoring, and measuring the performance of their suppliers; and a higher level of transparency in their disclosure of nonfinancial information. Thus, the High Sustainability companies benefited relatively more by being more dependent on their relationships with consumers, communities, and the environment. These High Sustainability companies competed successfully based on brands, human capital, and environmental awareness, even when some of their products depended on extracting large amounts of natural resources (Eccles, Ioannou, & Serafeim, 2014). These comparative results show that High Sustainability companies benefited from essentially following the commitments in the BR Statement on the Purpose of a Corporation.

5. CORPORATE GOVERNANCE IMPACTS

Martin Lipton, a founding partner of a corporate law firm, Wachtell, Lipton, Rosen & Katz, summarized the legal position of boards of directors in following the BR Statement on the Purpose of a Corporation as follows: "From a legal standpoint, stakeholder corporate governance recognized that the management and board of directors' primary fiduciary duty is to promote the long-term value of the corporation and is not primarily to maximize shareholder wealth. To fulfill that duty, the board of directors uses its business judgment in reconciling competing interests among the stakeholders: employees, customers, suppliers, the environment, communities, and shareholders. If the directors are not conflicted and use due care in reconciling the competing interests of the stakeholders, and in doing so seek to promote long-term value, they will have the protection of the business judgment rule and the courts will defer to their decisions without second-guessing them. The failure to recognize the existential threats of inequality and climate changes, not only to business corporations, but also to asset managers, institutional investors, and all shareholders, will invariably lead to legislation that will regulate not only corporations but also investors and take from them the ability to use their voting power to influence the corporations in which they invest. Inequality and climate change will not be mitigated without adherence to the BR governance principles not just by members of the BR but by all business corporations" (Lipton, 2019). Similar information was also included in a paper, called the New Paradigm, that Lipton wrote for the International Business Council of the World Economic Forum (Lipton, 2017).

These BR companies have the opportunity to put into action what the BR statement is saying by actually changing their corporate governance. Emphasizing the importance of corporate governance, the CEO of JPMorgan Chase, Jamie Dimon, called the CEO of Berkshire Hathaway, Warren Buffett, and suggested that they get together and come up with general principles for corporate governance that would become a pathway for the future. Thirteen prominent U.S. CEOs from industry, asset management firms, and an activist investment firm secretly worked for one year to develop corporate governance principles and published the Commonsense Principles of Corporate Governance in 2016 (Thakker, 2016). They wanted to provide such guidance at a time when fewer entrepreneurs were deciding to sell shares on U.S. public markets (Mathews, 2016). These CEOs said that the resulting document was detailed and tough-minded with commonsense recommendations and guidelines about the roles and responsibilities of boards, companies, and shareholders (Governanceprinciples.org, 2016).

A financial press commentator said that these principles may set a new standard in American corporate governance and that the stakes couldn't be higher as over 90 million Americans own U.S. public companies through their investments in mutual funds, retirement plans, and pensions (Gara, 2016). A corporate governance expert commented on these principles: "I think it shifts the burden of proof onto any corporation that doesn't comply, and I am delighted the signatories are such influential people" (McGregor, 2016). One research paper applied these eight corporate governance principles, demonstrating their relevance with related examples of weak corporate governance by just 17 public companies who had destroyed more than $1.5 trillion of market capital in the 21st Century. There were memorable corporate governance lessons to be learned from these investment losses, especially for boards of directors and auditors as gatekeepers to help protect investors (Grove & Clouse, 2017).

As an update in October 2018, CEOs of 21 leading public companies, pension funds, and investment firms, including the original 13 sponsors, signed the Commonsense Principles of Corporate Governance 2.0 and committed to using these standards to develop the corporate governance practices within their own organizations. These same eight principles are intended to provide a basic framework for sound, long-term-oriented governance. Given differences among public companies, not every principle will be applied in the same fashion by every company, board of directors, shareholder, or stakeholder (Business Wire, 2018).

There were key endorsements from the Business Roundtable and the Conference Board Governance Center. Joshua Bolten, CEO of Business Roundtable, commented: "Business Roundtable welcomes the Commonsense Principles of Corporate Governance 2.0 and their emphasis on advancing both high ethical standards and long-term economic value creation for the American people. As the operating environment of U.S. public companies continues to evolve, it is more important than ever for corporations, CEOs, and boards of directors to adopt and uphold meaningful corporate governance practices. Business Roundtable supports the leadership and forward thinking that the Commonsense Principles represent." Douglas Chia, Executive Director of The Conference Board Governance Center, said: "We commend and support the persistent leadership of this group to give actionable direction to boards and investors on governing corporations for the long-term benefit of their key stakeholders" (Business Wire, 2018).

There were also quotes from the two original motivators of Commonsense Principles, Jamie Dimon and Warren Buffett. Dimon said: "We're pleased that some of America's greatest institutions have signed on to the Commonsense Principles – formally joining a dozen others in our efforts to promote best-in-class corporate governance. With the commitment of these additional signatories, the endorsement from the Business Roundtable and The Conference Board Governance Center, and support from the Millstein Center for Global Markets and Corporate Ownership at Columbia Law School, we are working hard to promote principles that help drive the long-term strategy, healthy growth, and sustainability of America's companies". Buffett said: "Good corporate governance is critical to the success of American companies and to the American economy overall. This document takes it to another level of sound, commonsense principles that have been endorsed by multiple prominent business leaders and investors. It is a living document to help spur a larger conversation among boards, investors and companies for the benefit of all Americans" (Business Wire, 2018).

6. KEY POINTS IN BOTH VERSIONS OF COMMONSENSE PRINCIPLES

Both versions aimed to understand where there was broad consensus that could establish a baseline for ongoing discussion among constituencies with different points of view. They reframed the conversation from advancing individual perspectives to collectively advancing the interest of all stakeholders over the long term which is also the major goal of the BR Statement on the Purpose of a Corporation. Key points in both versions are as follows (Bresnahan, 2019; McGregor, 2016):

- Truly independent corporate boards are vital to effective governance, so no board should be beholder to the CEO or management. Every board should meet regularly without the CEO present, and every board should have active and direct engagement with executives below the CEO level.
- Board diversity is encouraged. Diverse boards make better decisions, so every board should have members with complementary and diverse skills, backgrounds, and experiences. It's also important to balance the wisdom and judgment that accompany experience and tenure with the need for fresh thinking and perspectives of new board members.
- Every board member needs a strong leader who is independent of management. The board's independent directors usually are in the best position to evaluate whether the roles of chairman and CEO should be separate or combined, and if the board decides on a combined role, it is essential that the board has a strong lead independent director with clearly defined authorities and responsibilities.
- Our financial markets have become too obsessed with quarterly earnings forecasts. Companies should not feel obligated to provide earnings guidance and should do so only if they believe that providing such guidance is beneficial to shareholders. Making short-term decisions to beat earnings guidance (or any performance benchmark) is likely to be value destructive in the long run.
- A common accounting standard is critical for corporate transparency, so while companies may use non-Generally Accepted Accounting Principles (GAAP) to explain and clarify their results, they should never do so in a way that obscures GAAP-reported results. In particular, since stock or options-based compensation is plainly a cost of doing business, equity compensation should always be reflected in non-GAAP measurements of earnings.
- Effective governance requires constructive engagement between a company and its shareholders. The company's institutional investors who are making decisions on proxy issues important to long-term value creation should have access to the company, its management, and in some circumstances, the board; similarly, a company, its management, and board should have access to institutional investors' ultimate decision-makers on those issues.
- Dual class share structures, which are often found in founder-led companies and give select stockholder outsize voting power, are not a best practice, i.e. Mark Zuckerberg owns 60% of the voting shares in Facebook.
- Director compensation should be made up of a substantial portion of equity-based compensation, i.e. company stock/stock option, suggesting 50% or more, to keep goals of directors in line with those of investors.
- Companies should maintain "clawback provisions" which allow them to recoup compensation given to executives in the event of earnings restatements.

7. KEY CHANGES IN COMMONSENSE PRINCIPLES 2.0

Version 2.0 built on the strong foundation of the 2016 Principles and strives to drive forward a more developed understanding of, and agreement on, the key tenants of corporate governance that support long-term value creation for all stakeholders. It also calls for enhanced transparency on the part of both companies and asset managers to ensure greater understanding between shareholders and the companies in which they invest. Key additions to version 2.0 are as follows (Bresnahan, 2019):

- Board members should be prepared to serve a minimum of three years.
- If board elections are not annual, companies should explain why.
- Companies and shareholders are encouraged to engage early on important proxy proposals.
- Companies should allow some form of proxy access.

• Poison pills and other anti-takeover defenses should be put to a shareholder vote and re-evaluated by the board on a periodic basis.

• Asset managers should disclose if they rely on proxy advisors to assist their decision-making.

• Asset managers should disclose their conflict of interest policies in their proxy voting and shareholder engagement activities.

• Portfolio managers should be compensated based on performance over an appropriate term, given the strategy and investment time horizon for the portfolio.

• Asset owners should promote sound, long-term oriented governance in their direct interactions with both companies and asset managers.

• Asset owners should use benchmarks and performance reports consistent with their investment time horizon to affect governance outcomes with asset managers and evaluate the asset managers' performance on both investment returns and governance.

Although the Commonsense Principles 2.0 reflect the status quo of late 2018, they will continue to stimulate conversation about how to best serve the long-term interests of public companies, shareholders and other stakeholders. Because of the complex global landscape of corporate governance, the Commonsense Principles 2.0 focus on U.S. companies. However, its ideas and policies are applicable around the world and should benefit from international learnings, like employees and other stakeholders being on international boards of directors and minimum board quotas for women (Bresnahan, 2019).

8. DISCUSSION

Following the corporate governance guidance and recommendations above does not guarantee that a company will meet the commitments in the Business Roundtable Statement. Conversely, a company can meet the commitments without implementing the Commonsense Principles. However, we postulate that companies buying into both of these documents will create a corporate governance and strategic management environment that will create long-term value for all stakeholders.

This long-term stakeholder focus has been long emphasized internationally. Professor Klaus Schwab, who founded the World Economic Forum, drafted the Davos Manifesto in 1973: "The purpose of professional management is to serve clients, shareholders, workers and employees, as well as societies, and to harmonize the different interests of the stakeholders" (Sorkin, 2019a). However, there will be the ever-present reality of whose ox is gored, with CEOs embracing a stakeholder approach when it suits their purposes and rejecting it when it does not. Hence, some of the cynical reaction to the Business Roundtable statement is well justified.

This corporate panic about capitalism could be a turning point for a future U.S. President to begin fixing the problems of stagnant wages and inequality that are at the core of America's disarray today. When America's capitalist system was broken in the past, President Franklin D. Roosevelt fixed it with the New Deal as did President Theodore Roosevelt with the Progressive Era. Thus, America's historical experience teaches us that economic reform succeeds when it goes mainstream and that is what is happening now (Ignatius, 2019). Although sceptics say that the BR Statement is a public relations gimmick that will do little to change the way American corporations are managed, its significance is not so much that it will change corporate behavior, but rather that it confirms a shift in attitude that has already occurred. By disavowing shareholder primacy and embracing a broader vision of corporate purpose, the BR Statement has now enhanced the political legitimacy of such efforts (Pearlstein, 2019).

To further enhance this new BR Statement perspective, Jamie Gamble, a partner at a corporate law firm which counts virtually every major U.S. company among its clients, has proposed that every company devise a set of ethical rules to be part of their bylaws, a move that would potentially open them up to shareholder lawsuits should they fail to stick to those rules. He suggests that companies should adopt a binding set of ethical rules, approved by shareholders and addressing the key ethical dimensions of corporate life (Sorkin, 2019b):

• relationships with employees;

• relationships with the communities in which they produce and sell;

• relationships with customers;

• effects on the environment; and

• effects on future generations.

Such ethical rules also emphasize the stakeholder focus of the BR Statement.

9. CONCLUSION

The major purpose of this paper is to analyze the Business Roundtable Statement on the Purpose of a Corporation and to link it to corporate governance, especially by following the guidelines and recommendations in the Commonsense Corporate Governance Principles. Jensen and Meckling (1976) started the investigation on the purpose of a corporation. It was followed by Jensen and Murphy (1990), which promoted stock options as the way to compensate CEOs. The law and economics movement also gained prominence in the mid to late 1970s, with the formation of the Law and Economics Center in 1973. CEOs and the Business Roundtable bought into those financial theories around the same time but pushed back somewhat against the activities of corporate raiders, since they threatened CEO jobs. Ever since, the Roundtable has steadily evolved back to managerialism, though it will never return to compensating CEOs by cash/salary only. Thus, this latest BR Statement on the Purpose of a Corporation is not such a dramatic break from the past, but rather the next step in a steady retreat from a purely financial approach and an evolution to embrace a stakeholder approach, which is now gaining more and more lip service.

The original Commonsense Corporate Governance Principles were published in 2016 and updated with Version 2.0 in 2018. They provide significant guidance for corporations, boards of directors, shareholders, and other stakeholders to follow in analyzing and applying the BR Statement on the Purpose of a Corporation. The future implementation and application of the BR Statement should be facilitated if the corporation has a corporate governance friendly environment created through the guidelines and recommendations from the Commonsense Corporate Governance Principles.

Future empirical research could focus on what corporations are doing to meet the commitments from the BR Statement on the Purpose of a Corporation in the context of the Commonsense Principles.

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