International Journal of Business Marketing and Management (IJBMM)
Volume 5 Issue 11 November 2020, P.P. 117-119
ISSN: 2456-4559
www.ijbmm.com

Basic problem of the stakeholder theory from a corporates' social responsibility point of view

Živko Bergant
Živko BergantPhD, College for Accountancy and Finance, Ljubljana, Slovenia.

Abstract: The author states that there are conflicts between profit maximization and value maximization. They are given different attention and also different proposals in professional literature. The author claims that these solutions lead the stakeholder theory more to the philanthropic direction than to the resolution of the problem. He finds the reason in the lack of recognizing the difference between creating and the distributing created value in the companies. The utmost importance of value-based law is emphasized.
Key words: creating value, distribution of value, added-value law, stakeholder theory, shareholder value

I. INTRODUCTION

Quite early, theinevitable conflicts between stakeholders' and shareholders' interests were noticed (e. g. Clarkson, 1995, p. 112).These conflicts evolved to the difference between two notions: the firm *profit* maximization and the firm *value* maximization. It means the question whether shareholders should be held in higher regard than other constituencies, such as employees, customers, creditors, and so on (e. g. Jensen, 2002, p. 239). Different authors answer this question differently, some of them are analyzed by Freeman et al. (Freeman et al., 2010).Almost all of them are seeking a solution within several principles that will be discussed later.

In the following, a critical view of different authors' proposed solutions will be given, together with a new, maybe even revolutionaryaspect.

II. SOME APPROACHES IN PROFESSIONAL LITERATURE

It is probably not necessary to mention Milton Friedman's statement that the main objective of a corporation is its profit (Friedman, 1970). This thesis was criticized enough by several authors, especially regarding the interests of stakeholders and corporates' social responsibility (e. g. Brooks, Dunn, 2018, pp. 17 and 250). One of them was Lynn Stout (2012), which asserted that “U. S. Corporate law does not require corporations to maximize shareholder value” (Brooks, Dunn, 2018, p. 248). At the same time she argued, that putting shareholders first harms investors, corporations and the public (Brooks, Dunn, 2018, p. 247).

Such an approach can be compared by pharisaic or hypocrite behavior, because, according to the same law, the right about the profit uses still rests on the capital ownersand indirectly on the corporates' management boards.In this way, the problem of possible predomination of shareholders' interests, remains not solved. Even more, in practice, the decision-making about profit uses remains on the executives of companies. This allows self-interested managers to pursue their own interests at the expense of society and the firm's financial claimants (Jensen, 2002, p. 242).

Almost all authors' starting point is the fact that the corporation is accountable legally to shareholders and strategically to additional stakeholders. Such a broader accountability of corporations is an object of numerous researches and discussions. With this starting point, stakeholder theory gives an unfettered power to managers to do almost whatever they want (Jensen, 2002, p. 242 and Brooks, Dunn, 2010, p. 227). This is the reason that almost all authors intend to persuade managersto consider long-term strategic objectives.To do so, different argumentsand recommendations are used.

The popular objective is “fairness and balance” in the distribution of the value, created by the firm (e.g. Clarkson, 1995, p. 112). To achieve this goal, different principles are recommended by different authors.The most important is ethics. "Stakeholder theory has become a powerful vehicle for thinking about the way in which ethics becomes central to the core operations of the firm” (Freeman et al., 2010, p. 232). “If business is a social process, then morality is at its center” (Freeman et al., 2010, 282). Ethics principles serve also as the foundation of most corporate codes or business conduct statements (Brooks, Dunn, 2018, p. 272). Still, there are some that take popular joke about “business ethics as an oxymoron” as a serious problem.

Several authors emphasize the role of stakeholder theory in strategic management to ensure the sustainable development. (e.g. Freeman et al., 2010 pp. 83–120). Others talk about innovation and knowledge management strategy (e.g. Mulej et al., 2020) or “corporate citizenship” (Brooks, Dunn, 2018, pp. 254 and 508).

There is a popular idea about the drift from “creating value for shareholders” to “creating value for stakeholders” (Freeman et al., 2010, p. 23). First notion makes sense because, regarding the corporate law, shareholders decide about the uses of the profit. Second notion doesn't make sense from the same reason. Stakeholders cannot legally decide about the distribution or using of profit.

Some authors see a possibility in creating larger, more intrusive government. The state should resolve the conflicts between stakeholders (Brooks, Dunn, 2010, p. 278). They forgot, that the state is also a stakeholder. Additionally, the state, as a rule, *does not* play a role of stakeholder, especially on two areas:

- Bankruptcy legislation is aimed only to the solvency of companies. The state does not response in the cases of loss in the companies, although losses diminish the result of tax collection.
- The state, as a rule, does not give enough care about the level of social well-being, especially regarding the solidarity issues.

Such and similar statements and/or recommendations have (and will have also in future) a relatively small effect, so they lack decisive arguments for a change in behavior and action. Adizes states that critics (for example World Economic Forum in Davos in 2020) of corporate policy that is directed to shareholder's value are not able to make changes that are needed. Therefore, “new eco-political theories of social responsibility will remain on paper because the power structure—the dynamics of the economic system—has not changed” (Adizes, 2020a). He even named coronavirus pandemic as a missed opportunity to make strategic changes that humanity needs to survive (Adizes, 2020).

As a final result, all above mentioned recommendations have only philanthropic character and do not represent an important progress of the stakeholder theory that is needed in practice.

There is a similar considerationon the discussion about social accounting that is still in the state of hope for “more societally-, organizationally – and environmentally-benign accountability, accounting and accounting education” (Gray, 2002).

This hope can be found also in some conclusions of stakeholder theory discussion: “We can be a generation that remakes business and capitalism, putting ethics at the center of business, and business at the center of ethics, creating a way of understanding business in the world of the twenty-first century” (Brooks, Dunn, 2020, p. 291).In principle, everybody could agree with such a conclusion, but it requires some innovative approaches to overcome theoretical delusions and to be useful in practice.

III. WHERE IS THE PROBLEM?

The best starting point seems to be the syntagm “creating value for stakeholders”, despite its critical evaluation, which was given in the previous section. It expresses “the spirit” of the stakeholder theory and requires a realization.

It is possible only if the important difference between the *creation* of value and the *distribution* of value is understood.This difference is unfortunately, as a rule, neglected by all authors. A shy comment calls this as a problem of the ethics of capitalism, “where individuals are in a constant survival mode with value being distributed rather than created(Brook, Dunn, 2010, p.277).

The creation of value is the main objective of companies. It is based on good management and requires proper information system for decision-making, monitoring and evaluating the outcome. This information system cannot be based on a profit based accounting, because the value for stakeholders is much better expressed by the value added.

The distribution of created value is a matter of recognizing the interests of all stakeholders and of their contributionsin the process of creating value.Itpresents a separated field of decisions and requires proper policy, which is directed to sustainable development according the principles of social responsibility.The decisions about the creation and the distribution of value must consider *value-added law*, which includes two aspects (Bergant, 2017):

1. Value added is the net outcome of the organizational system in managing the risk inherent to the system and belonging to risk holders in proportion to their contribution to the functioning of the organizational system (the aspect of creating value added);
2. The disproportionately high or disproportionately low participation of individual risk carriers in the value added (according to their work contribution) increases the entropy of the organizational system and threatens the realization of its sustainable development (the aspect of value-added guidance and its distribution).

The value-added law is general because of its validation in all socio-economic systems (past, present and future), which are oriented towards sustainable development. The law has various forms of its presence in different economic and political environments and in different types of organization (relations between people) of associations.The value-added law operates regardless of the wishes or activities of the participants and regardless of the normative organization of the organizational system or its environment. It is, therefore, totally independent of the human will that created the organizational system.

The important notion in the dictum of the value added law is entropy, which is originally an otherwise physical category, but in social or organizational systems it is defined as a "general, eternal and natural process that expresses the natural tendency of everything existing to decay" (Mulej *et al*., 2000, 260).

On the basis of the value added law we understand the entropy of organizational systems mainly as a result of the imbalance between participants' contributions and their participation in value added. The imbalance is devastating because it works against cooperation and mutual trust, which is necessary in the context of interdependence (Judt, 2011, 57 and 80).

The value added law in its own way shows the shortcomings of various company theories, including stakeholder theory.

IV. CONCLUSION

It follows from the previous section that adequate sharing of value added does not only mean the enforcement of some ethical norms, but is a fundamental precondition for the sustainable development of companies and society in general. The only alternative is increasing the dissatisfaction and the growth of entropy of all organizational systems.

Ignoring the operation of value-added law leads to the impotent stakeholder theory and to the lower satisfaction of stakeholders in every company. It means that such thinking deteriorates the role of stakeholder theory to the level of philanthropy.

The biggest challenge, without a doubt, lies in the academic sphere and education system.This may seems like a big illusion today, but an important argument is available. Namely, it is a recognition of the operation of the general value-added law, which does not depend on ideological assumptions or individual interests.

It follows from the above that politicians and politics have a great responsibility to take science and the profession into account in moving towards a sustainable society and to protect future generations. Policy change is always (or should be) the result of changes in people's expectations and demands. These changes can only be realized by a changed education system, for which, again, the academic sphere is responsible. Academics need to shake off their possible apologetic roles and expose their independent thinking and suggestions.

REFERENCES

[1]. Adizes Institute:insights@adizes.ccend.com. May, 13th, 2020.

[2]. https://visitor.r20.constantcontact.com/manage/optin?v=001ZaS58ajNOw3HfjIAVUTE0YR37BsyuMFDBaddlwL6OU-r9laI1egz70EksHfQerwkPI2QvjqvFoBkxgkhQV1qVhEFjayI7vFPUhTabRojp0Q%3D

[3]. Adizes, Ichak (2020a). *Why We are NOT Socially Responsible.*Adizes blogs.

[4]. Adizes Institute:insights@adizes.ccend.com. July 3rd, 2020.

[5]. Bergant, Živko (2017). *Appropriate consideration of value added law as a precondition of social responsibility.* Maribor: IRDO. (Retrieved: November 2020). http://www.irdo.si/irdo2017/referati/plenarna-bergant.pdf.

[6]. Brooks, J. Leonard, Dunn, Paul (2018). *Business and professional Efhics for Directors, Executives & Accountants, Eighth Edition.* Boston: Cengage Learning.

[7]. Clarkson, B. E. Max (1995). A Stakeholder Framework for Analysing and Evaluating Corporate Social Performance. *Academy of Management Review,*Vol. 20, No. 1, pp. 92–117.

[8]. Freeman, R. Edward et al. (2010). *Stakeholder Theory* (The State of the Art). Cambridge: Cambridge University Press.

[9]. Friedman, Milton (1970). The social responsibility of business is to increase its profits. *New York Times*, September 13, p.33.

[10]. Gray, Rob (2002). The social accounting project and Accounting Organizations and Society. Privileging engagement, imaginings, new accountings and pragmatism over critique? *Accounting, organization and Society,* No. 27/2002, pp. 687–708.

[11]. Jensen, C. Michael (2002). Value Maximization, Stakeholder Theory, and the Corporate Objective Function. *Business Ethics Quaterly*, Vol. 12, No. 2, pp. 235–256.

[12]. Judt, Tony (2011).*Deželi se slabogodi*. (The country is in a bad shape. In Slovene.). Ljubljana: Mladinskaknjigazaložbad.d.

[13]. Mulej, Matjaž *et al.* (2000). *Dialektična in druge mehkosistemske teorije*. (Dialectical and other soft system theories. In Slovene.). Maribor: Ekonomskaposlovnafakulteta.

[14]. Mulej, Matjaž, O'Sullivan, Grażyna, Štrukelj, Tjaša (2020). *Social responsibility and Corporate Governance, Volume 2: Policy and Practice.* Palgrave, Macmillan. http://www.palgrave.com/gp/series/15192. (Retrieved: November, 2020).