EVALUATING THE SHAREHOLDER PRIMACY THEORY: EVIDENCE FROM A SURVEY OF AUSTRALIAN DIRECTORS

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1. Introduction

In recent years, scholars have noted the rise of ‘shareholder primacy’ or ‘shareholder value’ as an aspect of corporate governance.[1] It has also been argued that the rise of shareholder primacy often has an injurious impact upon the interests of corporate employees.[2] The argument suggests that under a certain type of capitalism,[3] and particularly that which characterises ‘market-based’ rather than ‘relational’ styles of production systems,[4] the interests of shareholders are considered paramount by directors, over and above those of other stakeholders, such as employees. At its extreme, this perspective suggests that directors will tend to favour the short-term financial interests of shareholders (shareholder value), being driven in that direction by capital markets fixed on share price and short term returns. But even in a more balanced perspective, the shareholder primacy view would hold that the overriding goal of the corporation is to maximise shareholder wealth.[5] Among nations, the Anglo-American group (the UK, USA, Canada, New Zealand and, perhaps less straight forwardly,[6] Australia) are taken to constitute those most clearly exhibiting the ‘shareholder primacy’ style of corporate governance.

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[1] Some of the extensive literature examining shareholder primacy as an aspect of corporate governance includes S. Deakin, ‘Workers, Finance and Democracy’ in C. Barnard, S. Deakin and G. Morris (eds.), *The Future of Labour Law*, Hart Publishing, Oxford, 2004, 79; P. Davies, ‘Shareholder Value; Company Law and Securities Markets Law – A British View’ in K. Hopt and E. Wymeersch (eds.), *Capital Markets and Company Law*, Oxford University Press, Oxford, 2002, 262; R. Mitchell, A. O’Donnell and I. Ramsay, ‘Shareholder Value and Employee Interests: Intersections Between Corporate Governance, Corporate Law and Labor Law’ (2005) 23 *Wisconsin International Law Journal* 417.

[2] See, for example, W. Lazonick and M. O’Sullivan, ‘Maximising Shareholder Value: A New Ideology for Corporate Governance’ (2000) 29 *Economy and Society* 13.

[3] The Varieties of Capitalism literature suggests that there are different types or families of capitalism; see for example, P. Hall and A. Soskice, *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Oxford University Press, Oxford, 2001; H. Gospel and A. Pendleton, *Corporate Governance and Labour Management*, Oxford University Press, Oxford, 2005.

[4] ‘Liberal Market’ and ‘Coordinated Market’ are the opposing terms used by Hall and Soskice (*ibid*). Gospel and Pendleton, drawing from the financial economics literature use the terms ‘Market/Outsider’ and ‘Relational/Insider’ to maintain the distinction between the two styles (*ibid*, at p. 7). See further nn. 25 and 26 below, and the text associated with those notes.

[5] Mitchell, O’Donnell and Ramsay, above n. 1, p. 424.

[6] See M. Jones and R. Mitchell, ‘Legal Origin, Legal Families and the Regulation of Labour in Australia’ in S. Marshall, R. Mitchell and I. Ramsay (eds.), *Varieties of Capitalism, Corporate Governance and Employment Systems*, Melbourne University Press, forthcoming.

What these scholars argue in more concrete terms is that as business organisations strive for increasing shareholder value, particularly through restructuring or reorganising the business (including mergers, takeovers, vertical disintegration techniques and the privatisation of publicly-owned enterprises),[7] employees usually suffer as a consequence of job losses and, in many cases, poorer working conditions. Much of the literature in this area focuses on the 'job shedding' which is attributable to the rise of 'shareholder value'.[8] In the words of Hamel and Prahalad '(m)asquerading behind terms like refocusing, delayering, decluttering, and right-sizing…, restructuring always results in fewer employees'.[9] However, we should also not ignore the fact that in the restructuring of enterprises and the reorganisation of work and production systems, workers who are not displaced, or who are relocated to other business organisations in the same group, often may be subject to fundamental changes in their working lives through pay cuts, worsening conditions and greater intensity of work effort. Moreover, the legitimacy of employee 'voice' in such restructuring is often completely negated.[10]

Responsibility for corporate restructuring and work reorganisation ultimately lies with company directors, whose task it is to set the strategic direction of the business for profit and growth. The 'shareholder primacy' view of the corporation seems to have emerged from the idea that directors (and the professional managers who give effect to the corporate strategy) are essentially 'agents' for the shareholders, and consequently are under a fundamental obligation to manage the company in the interests of the shareholders.[11]

At the same time, it is clear that directors owe no such legal obligation directly to shareholders in corporate law. Such legal obligations as there are to influence the overall strategic decision making of boards of directors, are owed not to the shareholders as such, but to the company.[12] Directors are legally required to act in the best interests of the

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[7] The best known Australian example of the impact of corporate restructuring upon employees is seen in the events surrounding the Waterfront Dispute; see G. Orr, 'Conspiracy on the Waterfront' (1998) 11 *Australian Journal of Labour Law* 158; D. Noakes, 'Dogs on the Wharves: Corporate Groups and the Waterfront Dispute' (1999) 11 *Australian Journal of Corporate Law* 27.

[8] J. Froud, C. Hazlam, S. Johal and K. Williams, 'Restructuring for Shareholder Value and its Implications for Labour' (2000) 24 *Cambridge Journal of Economics* 771.

[9] G. Hamel and C. Prahalad, 'Competing for the Future' (1994) *Harvard Business Review* (July-August) 122.

[10] See Deakin, above n. 1; Australian Centre for Industrial Relations and Training, *Australia at Work: Just Managing?*, Prentice Hall, Sydney, 1999, Ch. 1 and pp. 147-153; C. Allen *et. al.*, 'More Tasks, Less Secure, Working Harder: Three Dimensions of Labour Utilisation' (1999) 41 *Journal of Industrial Relations* 519; I. Watson *et. al.*, *Fragmented Futures: New Challenges in Working Life*, Federation Press, Sydney, 2003, Ch. 7.

[11] H. Hansmann and R. Kraakman, 'The End of History for Corporate Law' (2001) 89 *Georgetown Law Journal* 439; R. Gordon Smith, 'The Shareholder Primacy Norm' (1998) 23 *Journal of Corporation Law* 277; E. Farmer and N. Jensen, 'Separation of Ownership and Control' (1983) 26 *Journal of Law and Economics* 301.

[12] Section 181(1) of the Australian Corporations Act requires directors and other company officers to exercise their powers and discharge their duties "in good faith in the best interests of the corporation". For analysis of the meaning of the "interests of the corporation" see R.P. Austin, H.A.J. Ford and I.M Ramsay, *Company Directors: Principles of Law and Corporate Governance*, LexisNexis Butterworths, Sydney, 2005, Ch. 7.

company. The interests of the company are usually regarded by courts as those of the company's shareholders.[13] However, recent Australian government inquiries have confirmed the legal competence of directors to adopt a broader set of interests in pursuing corporate strategy.[14] Directors are, under the common law and the Corporations Act, accountable to shareholders in some important respects, but this does not mean that their interests must always be preferred over other stakeholders,[15] and the limited control rights which shareholders enjoy are, in themselves, usually too restricted to enable them to dictate corporate strategy to that end.[16]

This paper is written as part of a larger project on Corporate Governance and Workplace Partnerships[17] which has been designed to test the relationship between corporate ownership structure, corporate governance arrangements and the management of labour. As part of that project, the researchers have undertaken a series of case studies and a survey of corporate directors. In the survey we set out to explore some of the issues raised in this Introduction, particularly the extent to which corporate directors might perceive that their obligations are to give paramount consideration to the interests of shareholders, what the source of any such obligation might be, and whether there is a relationship between company type (i.e. market/outsider models) and a greater propensity to shareholder primacy. We also sought to discover if the prioritisation of shareholders' interests by directors necessarily means that this would be pursued at the expense of labour's interests.

To some extent the findings outlined here are incidentally informed by our case study research, but we are by and large reporting on the relevant outcomes from the survey data. Two previous studies have also informed our work. The first of these is the 1993 study of company directors carried out by Tomasic and Bottomley.[18] That study reported on, among other things, the impact of law and legal rules on directors in the performance of their obligations. The second study, conducted for the Australian Institute of Company Directors in 1997 by Francis,[19] sought to examine the role of company directors and to determine the appropriate combination of directorial functions for optimal company performance. From time to time in our text we refer to relevant parts of these studies insofar as they tend to confirm or disaffirm our own findings.

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[13] Ibid.

[14] See Corporations and Markets Advisory Committee, *The Social Responsibility of Corporations*, Report, December 2006, Ch. 3; Parliamentary Joint Committee on Corporations and Financial Services, *Corporate Responsibility: Managing Risk and Creating Value*, June 2006, Senate Printing Unit, Canberra.

[15] See Deakin above n. 1 at pp.81-82.

[16] See Mitchell, O'Donnell and Ramsay, above n. 1, pp. 431-439; Deakin, above n. 1, pp. 81-89; M. Blair and L. Stout, 'Specific Investment and Corporate Law' (2006) 7 *European Business Organisation Law Review* 473.

[17] This is a joint project of the Centre for Employment and Labour Relations Law and the Centre for Corporate Law and Securities Regulation at the University of Melbourne. For more information about the project, visit <http://cclsr.law.unimelb.edu.au/go/centre-activities/research/corporate-governance-and-workplace-partnerships-project/index.cfm>

[18] R. Tomasic and S. Bottomley, *Directing the Top 500: Corporate Governance and Accountability in Australian Companies*, Allen and Unwin, Sydney, 1993.

[19] I. Francis, *Future Direction: The Power of the Competitive Board*, Pitman, Melbourne, 1997.

2. Methodology

Our survey targeted company directors as those responsible for the corporate strategy within companies. The survey was undertaken through a self-completion mail-out form which was posted to 4,000 company directors in June 2006. The survey asked a total of 52 questions, testing not only the attitudes and opinions of directors but also seeking factual information about the relevant company.[20] The initial survey sample was obtained from Dun and Bradstreet,[21] according to various criteria, including a roughly equal distribution in company size,[22] a random mix of companies from all Australian States, and a random mix of all industries. Prior to the mail-out, the survey was piloted with six directors selected through our networks. We obtained useable completed responses from 367 directors. Whilst this is a low level of response,[23] such a rate of return is not unusual in surveys of senior personnel.[24]

In approaching some aspects of this exercise, we have attempted to build typologies of companies based on the categories 'market/outsider' and 'relational/insider', derived from the work of Howard Gospel and Andrew Pendleton.[25] Based on their analysis of broad company characteristics in market/outsider and relational/insider national systems, we established a set of criteria which would allow us to categorise the companies represented in our sample as belonging either to the market/outsider or relational/insider group.[26] The selected criteria related to particular characteristics such as whether there

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[20] The detailed research report, from which parts of this paper are drawn, is available on the website address in note 17. The research report includes the survey.

[21] Dun and Bradstreet conducted the random sampling from their database. This database can be accessed in book form as a yearly volume: *The Business Who's Who of Australia*, Sydney, R.G. Riddell, or at the website http://bww.dnb.com.au/advancedsearch.asp

[22] The three size groupings used were those employing between 50-100 employees, those employing between 101-250 employees, and those employing 250+ employees.

[23] The results in this paper are based on analysis of 351 responses as the final 16 completed surveys were delivered after analysis had commenced. Around 200 surveys were returned due to incomplete or incorrect mailing details, and a further 50 were returned with apologies for lack of ability or capacity to complete the survey.

[24] See S. Jacoby, E. Nason and K. Saguchi, 'The Role of the Senior HR Executive in Japan and the United States: Employment Relations, Corporate Governance and Values' (2005) 44 *Industrial Relations* 207 at p. 216; B. Agle, R. Mitchell and J. Sonnenfeld, 'Who Matters to CEOs? An Investigation of Stakeholder Attributes and Salience, Corporate Performance and CEO Values' (1999) 42 *Academy of Management Journal* 507 at p. 513.

[25] See above n. 3; see also H. Gospel and A. Pendleton, *Financial Structure, Corporate Governance and the Management of Labour*, Research Paper No 6, Kings College London, The University of London, October 2001.

[26] The model comprises six criteria which are characteristics we would expect to find in a market/outsider company. These are: listed company; largest shareholder not represented on the board; no other shareholders represented on the board; higher level of holding by institutional investors; short term debt financing; and creditors not represented on the board. For a relational/insider company the criteria are: unlisted; largest shareholder is on the board; other shareholders on the board; lower level of institutional holding; long term debt financing; and creditors on the board. Each item was given a score 1=present, 0=not and two indexes developed Index.I6 and Index.O6. Those which scored 4 or more on the Index.I6 were categorised as HighIns6 and those that scored 3 or more on the Index.O6 were categorised as HighOut6.

was shareholder representation on the board, the level of shareholding by institutional investors and whether the company was listed or not, among others. This was done to enable us to compare the responses of directors from these different types of company and thereby ‘test’ aspects of the theoretical framework offered by these authors. Our modelling is, however, experimental at this stage and it is necessary to bear this in mind when considering the findings.

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In this paper we present the survey findings on four questions:

- whether directors prioritise the interests of shareholders over and above the interests of employees and other stakeholders (shareholder primacy);
- whether, if that is the case, the source of that prioritisation lies in legal obligation or duty;
- whether directors in types of companies corresponding to the market/outsider model are more inclined to prioritise shareholder interests; and
- whether the prioritisation of shareholder interests tends to come at the expense of employees (shareholder primacy equals poor outcomes for labour).

These four questions are addressed in section 3 of the paper. Section 4 of the paper contains our analysis of the data. Section 5 concludes.

3. The Questions and the Survey Data

Do Directors Prioritise the Interests of Shareholders?

The literature would suggest a tendency for directors to acknowledge a primary obligation to the interests of shareholders (and perhaps even to the short term interests of shareholders). We tested this assumption in a number of ways. First, using a ranking exercise adapted from the Francis study[27] we asked directors to rank stakeholders in the order in which those stakeholders’ interests were prioritised. Second, we utilised a scale to assess the relative influence of key stakeholders over the decision making of directors. Third, we asked directors about the priority they assigned to certain specific shareholder-oriented matters such as dividend policy and share price. These three tests enabled us to form an assessment of the shareholder orientation of the surveyed group.

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[27] See above n. 19.

Table 1: Stakeholders in Order of Priority#

Stakeholder	Average Ranking	Percentage Ranked 1	Percentage included in Top 3
1. Shareholders	2.23	44.0	78.2
2. The Company	2.25	40.4	71.1
3. Employees	2.87	6.7	72.8
4. Customers	3.53	8.2	44.8
5. Suppliers	5.99	1.2	3.9
6. Lenders/Creditors	5.83	0.6	10.6
7. The Community	6.43	0.3	3.4
8. The Environment	7.07	0.6	2.0
9. The Country	8.41	0.3	1.1

Directors were asked to rank the list of stakeholders in order of priority between 1 and 9 with 1 being highest priority. The smaller the average rank, the higher the priority.

Table 1 sets out the results for the priority ranking exercise. It shows the average ranking given to each stakeholder group, the percentage of directors who ranked each group as their number one priority, and the percentage of directors who included that stakeholder group as one of their top three priorities. It is clear that shareholders constitute the stakeholder group accorded the highest priority by the directors in our sample. Forty-four percent of directors ranked shareholders as their highest priority, followed by 40.4 per cent who ranked the interests of the company as their number one priority. Only 6.7 per cent ranked employees as their number one priority. These outcomes bear comparison with the earlier Francis study. In that survey, 74 per cent of directors ranked shareholders as their number one priority.[28]

We also sought to test the ‘shareholder primacy’ norm in a more nuanced way according to a scale adapted from research conducted in the US by Agle, Mitchell and Sonnenfeld.[29] This research sought to move beyond the assumption that stakeholders have a fixed position of influence in relation to the company and to apply a more flexible model of stakeholder salience (or importance) based on the idea that relative stakeholder importance will depend upon the perception by CEOs of the power held by stakeholders, and the relative urgency and legitimacy of their claims in differing contexts.

[28] Francis, above n. 19, p. 354.
[29] See above n. 24. We made minor modifications to their scale – some of the items were removed because of duplication and the language was changed to make it more suitable for Australian directors.

Table 2: Shareholders' Salience Scale

Thinking about the relationship between the company and its shareholders over past year…	% of Directors Agree*	Mean score#
Had the power to influence management	81.2	4.03
Were active in pursuing demands or wishes which they felt were important	66.5	3.61
Actively sought the attention of our management team	64.6	3.54
Urgently communicated their demands or wishes to our company	48.8	3.20
Demands or wishes were viewed by our management team as legitimate	78.7	3.88
Received a high degree of time and attention from our management team	65.0	3.61
Satisfying the demands or wishes of shareholders was important to our management team	83.3	4.02

* includes responses 'strongly agree' and 'agree'
# Directors were asked to rate the extent to which they agreed or disagreed with each statement on a scale of one (strongly agree) to five (strongly disagree)

In order to address these issues, a series of propositions was presented to the surveyed group concerning the relative influence of shareholders, employees and creditors. The scale was comprised of several propositions and directors were asked to rate the extent to which they agreed or disagreed with certain statements on a scale of one (strongly agree) to five (strongly disagree). Table 2 sets out both the proportion of directors who agreed with each proposition (in relation to shareholders) and the mean score for that proposition. The table demonstrates that both the power of shareholders and the legitimacy of their interests remain a high priority in the perception of directors' interests. The items 'shareholders had the power to influence management' and 'satisfying the demands or wishes of shareholders was important to our management team' achieved the highest scores and had the largest proportion of directors who agreed. The item 'shareholders demands or wishes were viewed by our management team as legitimate' also scored highly. On the other hand these high levels of legitimacy and power do not seem to be associated with similarly high levels of activity on behalf of shareholders as measured by the items 'shareholders were active in pursuing demands or wishes', 'shareholders actively sought the attention of our management team' and 'shareholders urgently communicated their demands or wishes to our company'. This suggests that shareholder power and the legitimacy of shareholder interests for directors arise, at least in part, independently of any direct pressure exercised by shareholders over directors in terms of governance strategy. In other words, shareholders have a level of power that is partly independent of their specific demand activity. This distinction between different types of shareholder salience, as we shall see later in this paper, becomes more important when companies are disaggregated according to certain company characteristics.

Taken as a whole, these outcomes establish that 'shareholder primacy' is prominent in the attitudes of our respondent company directors. This is confirmed when we compare the relative importance of shareholder interests and employee interests. Table 3 shows the breakdown between the high and low ranges of the scale for both shareholders and employees and the mean scores for each. Shareholders have a high level of salience with 73.7 per cent of directors in the high range of the scale, and an overall average score of 3.70 (the highest of any of the stakeholders we tested). There was a slightly lower percentage (71.7 per cent) of directors in the high range of the 'employees active' scale and the overall score for employees was lower in both employee scales.[30]

Table 3: Proportion of High and Low Ratings on Salience Scale#

Stakeholder	% High 3+	% Low <3	Mean score
Shareholders	73.7	17.9	3.70
Employees –Active	71.7	19.3	3.49
Employees – Legitimate#	68.6	31.0	3.49

for the employees' legitimate scale, 'high' is a score of 4 or more due to very high overall scores

We can gain further insight into the extent of shareholder primacy by analysing the results of our question on the matters that are important to directors. However, we get a less distinct picture from this analysis. We had hypothesised that the matters which are relevant to the interests of shareholders (dividend policy, increasing share price, reducing costs and special dividends) would be valued by a greater proportion of directors than those matters relating to employees or other stakeholders. This hypothesis was based on the results of a previous study from which this question was drawn. In that study, a comparative study of US and Japanese management,[31] the shareholder value model of governance in operation in the US was evident in the fact that share price was ranked most important to CFOs and second in importance to HR executives. In Japan, by

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[30] The items in the scale measuring shareholder salience were all highly correlated and averaged for a scale that runs from high (average score of 3 or higher) which represents the strong influence of shareholders to low (average score of less than 3) for weak influence of shareholders in the company. For the employee salience scale all the items were not highly correlated and so the scale has been arranged as two scales: employees active and employees legitimate. The 'employees active' scale contains the items: (a) power to influence management; (b) active in pursuing demands; (c) actively sought the attention of management team and (d) employees urgently communicated their demands or wishes to our company, which were all correlated. The scale runs from high (scores 3 or over) representing strong active influence of employees to low (scores under 3) representing weak active influence of employees. The 'employees legitimate' scale contains the items: (e) demands or wishes of our employees were viewed as legitimate by our management team; (f) employees received a high degree of time and attention from our management team; and (g) satisfying the demands or wishes of employees was important to our management team. These items were all correlated. Scores are averaged and run from high (scores 4 and higher) representing strong legitimate influence of employees in the company to low (scores under 4) representing weak legitimacy and influence of employees. In this scale only, the scores must be 4 or 5 to be classified as high because the overall scale scores were high and there were too few under a score of three.

[31] S. Jacoby, E. Nason and K. Saguchi, 'The Role of the Senior HR Executive in Japan and the United States: Employment Relations, Corporate Governance and Values' (2005) 44 *Industrial Relations* 207 at p. 232.

comparison, with a more stakeholder-oriented governance model, share price was much less important. On the basis that Australia sits closer to the US model of governance, we predicted that Australian directors would be similarly concerned with shareholder related matters.

The results, however, were not as predicted. Table 4 indicates that ‘ensuring that customers and clients are satisfied’ was the item that was most important to the directors surveyed (97.4 per cent of directors). ‘Growing the business’ was also very important (95.4 per cent) as was ‘ensuring employees are fairly treated’ (94.2 per cent), with ‘improving productivity’ highly valued as well (92.8 per cent of directors believing it was important). ‘Reducing costs’ was considered to be important by 80 per cent of directors. Contrary to the shareholder primacy/shareholder value theory, the results show that some of those items relating specifically to shareholders’ interests (dividend policy, increasing share price, special dividends) were rated as important by relatively few directors. ‘Increasing share price’ was rated as important by 45 per cent of directors, ‘dividend policy’ by 41 per cent and ‘special dividends’ by only 6.6 per cent.

Table 4: Importance to You as a Director

Item	% of directors who rated item Important#
Ensuring Customers/Clients are Satisfied	97.4
Growing the Business	95.4
Ensuring Employees are Fairly Treated	94.2
Improving Productivity	92.8
Improving Employee Morale	87.3
Reducing Costs	80.1
Ensuring Other Stakeholders are Satisfied	67.2
Safeguarding Existing Employee Jobs	66.2
Diversifying and Expanding into New Markets	48.8
Creating Job Opportunities Within the Company	46.3
Increasing Share Price	45.0
Dividend Policy	41.0
Making a Contribution to Society	32.1
Special Dividends	6.6

Where rated either most, or very, important

Do Directors Perceive they are under a Legal Obligation or Duty to Prioritise the Interests of Shareholders?

In this section, we narrow our focus from a broad investigation of the existence of a shareholder primacy norm among the directors surveyed, to whether the priority accorded to shareholders’ interests, to the extent that it exists, has a basis in perceived legal obligation. As we noted in the Introduction to this paper, directors must act in the best

interests of the company which is typically defined by courts as the interests of the company's shareholders yet they have the power to consider the interests of a broad range of stakeholders of the company. But the question remains whether directors perceive this to be the case, or whether they act under a degree of mistaken apprehension as to their legal duties.

To test this question, we pursued two lines of enquiry. First, we asked respondent directors to indicate which of a number of statements best described their understanding of their obligation to act in the 'best interests of the company' as required by the law. Second, we asked them to indicate whether they believed that the current law on directors' duties was broad enough to allow them to consider interests of stakeholders other than shareholders, or whether it required them to consider the interests of shareholders only.

Table 5: Directors' Understanding of the Scope of Directors' Duties

Primary Obligation: I must act in the best interests of the company and this means acting in the….	% Yes
Short term interests of shareholders only	0.0
Long term interests of shareholders only	6.6
Interests of all stakeholders to achieve short term interests of shareholders	0.3
Interests of all stakeholders to achieve long term interests of shareholders	38.2
Balancing the interests of all stakeholders	55
Parameters of Law on Directors' Duties	
I must only be concerned with shareholders' interests	5.7
Allows me to take account of interests other than shareholders'	94.3

Again, working from the 'shareholder primacy' theory, we had predicted that directors might understand that their primary legal obligation was to act in the best interests of the company and that they might tend to define this as acting in the interests of shareholders in the short or long term.[32] However, as Table 5 indicates, this was not the case. None of our survey group equated the 'best interests of the company' with the short term interests of shareholders alone, and only a very small proportion of directors (6.6 per cent) equated the 'best interests of the company' with the best interests of shareholders in the long term. A significant proportion (38.2 per cent) equated the 'best interests of the company' with the interests of all stakeholders as a means to achieving the long term interests of shareholders. Perhaps surprisingly, the majority of directors (55 per cent) understood acting in the 'best interests of the company' as requiring them to balance all stakeholder interests as an end in itself.

[32] This seems to be the general conclusion reached in the Tomasic and Bottomley study, see above n. 18, at pp. 70-71.

Similarly, an overwhelming majority (94.3 per cent) of directors believed that the law of directors' duties was broad enough to allow them to take into account the interests of stakeholders other than shareholders. The answer to our question posed at the start of this section then is clearly in the negative. Consequently, it would seem to be the case that where the 'shareholder primacy' norm is influential, its influence does not stem from an understanding by directors that they are under a legal obligation to pursue shareholder-oriented strategies.

Are Directors of Companies Corresponding to the Market/Outsider Model more Inclined to Prioritise Shareholder Interests?

Here we are testing aspects of the theoretical framework developed by Gospel and Pendleton in their work *Corporate Governance and Labour Management*.[33] In that work, the authors argue that managerial strategic choice is largely determined according to differences in corporate finance and governance arrangements. Specifically, the 'market/outsider' systems are characterised by dispersed share ownership and strong capital markets, in which an 'outsider' system of governance is supported by relatively strong legal protections for investors and/or an active market (through takeovers and mergers) for corporate control. This in turn is said to produce outcomes which are favourable to the short term interests of shareholders over those of other stakeholders in the enterprise.[34] The 'relational/insider' model of corporate governance on the other hand is characterised by forms of ownership and control which are much more concentrated through block-holdings of shares and finance through banks and other sources of relational investing.[35] This concentration allows for a more direct form of monitoring and observation of management performance and decision-making, and minority, or dispersed, investors are correspondingly less well protected than in the 'outsider' model.

Adopting this general argument we have, in turn, hypothesised that 'shareholder value/shareholder primacy' governance norms will be evident to a greater extent in companies with characteristics that best match the market/outsider model as compared with companies which would appear to more closely fit the relational/insider model. In order to test this, our survey sought information about relevant company characteristics, such as whether the company was listed on a stock exchange, whether major shareholders were represented on the board and the level of holding by institutional investors. From this information we were able to construct an approximate model of company type and then to explore the relationship between that company type and our indicators of 'shareholder primacy'.[36]

As we noted in our earlier argument, a degree of 'shareholder primacy' is indicated among company directors according to a priority ranking order and the analysis of the

[33] See above nn. 25 and 26 and the text associated with those notes.
[34] Gospel and Pendleton, above n. 25, pp. 14-17.
[35] See K. Hopt and E. Wymeersch (eds.), *Comparative Corporate Governance: Essays and Materials*, Walter de Gruyter, Berlin, 1997, pp.151-164.
[36] See above n. 26 and associated text for a description of the methodology for the development of these typologies and criteria on which they are based.

salience scales (see above, Tables 1 and 2). What does our data tell us about the relationship between the existence of a shareholder primacy norm and company type? As can be seen in Table 6, both the average rankings and the proportion of directors who ranked shareholders number one among stakeholders are very similar for both company types. There were no statistically significant differences, except for the difference between the ranking for lenders/creditors.[37] Directors from market/outsider companies were more likely to have ranked lenders and creditors lower than those from relational/outsider companies. This is in accordance with the Gospel and Pendleton predictions.

However, when we compare the mean scores of shareholder influence on the salience scales we do see a significant difference between company types. As shown in Table 7, the mean scores on 'the influence of shareholders scales' for companies which were highly correlated with the relational/insider model (3.82) and those which were highly correlated with the market/outsider model (3.46) differ significantly. In other words, contrary to our supposition, shareholder influence and importance appears to be *greater* in relational/insider companies rather than those of the market/outsider type.

Table 6: Priority Ranking of Stakeholders by Company Type#

Stakeholder	Average Ranking		Percentage Ranked 1	
	Insider	Outsider	Insider	Outsider
Shareholders	2.21	1.96	43.3	47.4
The Company	2.60	2.34	40.3	43.6
Employees	2.93	2.91	5.1	5.3
Customers	3.39	3.67	8.1	4.2
Suppliers	2.60	2.34	40.3	43.6
Lenders/Creditors	5.55	6.09*	1.5	0.0
The Community	6.58	6.45	0.0	0.0
The Environment	7.21	7.02	5.1	5.3
The Country	8.36	8.47	0.7	0.0

Directors were asked to rank the list of stakeholders in order of priority between 1 and 9 with 1 being highest priority. The smaller the average rank, the higher the priority.
* significant at the 5% level

Table 7: Influence of Shareholder Salience Scale by Company Type

Influence of Shareholder Scale	High Insider Mean Score	High Outsider Mean Score
High	3.82	3.46**

** significant at the 1% level

[37] In this section, we use the term significant where we have found a statistically significant difference between the groups being compared.

If we break down the 'influence of shareholders scale' into its composite items as we have in Table 8, we see further statistically significant differences between the mean scores for individual items and between the proportion of directors who agree with individual scale items according to company type.

Table 8: Influence of Shareholders by Company Type[38]

Thinking about the relationship between the company and its shareholders over past year…	% of Directors Agree#		Mean Score	
	Insider	**Outsider**	**Insider**	**Outsider**
Satisfying the demands or wishes of shareholders was important to our management team	87.6	81.5	4.12	3.91
Had the power to influence management	86.9	75.0*	4.17	3.77**
Demands or wishes were viewed by our management team as legitimate	81.8	71.4	3.96	3.67*
Were active in pursuing demands or wishes which they felt were important	75.0	53.3**	3.82	3.18**
Received a high degree of time and attention from our management team	72.1	59.8	3.76	3.43*
Actively sought the attention of our management team	70.1	56.5*	3.66	3.30*
Urgently communicated their demands or wishes to our company	50.4	42.4	3.26	2.98

includes responses 'strongly agree' and 'agree'
* significant at the 5% level,
** significant at the 1% level

Shareholders are perceived as having a *significantly* greater power to influence management in insider-type companies than in outsider-type companies. Similarly, shareholders are perceived by directors in the insider-type companies as being more active in pursuing demands and, based on the mean scores, as both receiving a higher degree of time and attention from management and higher degrees of legitimacy. This is contrary to our hypothesis based on the presumed dominance of the shareholder primacy norm in market/outsider companies.[39]

Our final 'test' of the relationship between company type and 'shareholder primacy' was to compare the responses of directors in market/outsider companies with those in relational/insider companies on the matters of importance to them in their roles as directors. These results are set out in Table 9.

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[38] The tests between proportions are chi square tests of independence, while the means are t-tests.
[39] Our hypothesis is based on the literature, observing that the 'shareholder value' or 'shareholder primacy' model of corporate governance tends to be dominant in 'market/outsider' systems such as the US, UK and Australia (see above n. 6).

Table 9: Importance to Director by Company Type

Item	Insider % Important#	Outsider % Important#
Ensuring Customers/Clients are Satisfied	97.9	97.8
Growing the Business	95.0	93.5
Ensuring Employees are Fairly Treated	93.6	93.3
Improving Productivity	93.5	91.3
Improving Employee Morale	89.3	83.3
Reducing Costs	79.1	80.9
Safeguarding Existing Employee Jobs	67.1	57.8
Ensuring Other Stakeholders are Satisfied	63.0	71.9
Diversifying and Expanding into New Markets	51.1	46.7
Increasing Share Price	46.1	50.0
Dividend Policy	46.0	38.5
Creating Job Opportunities within the Company	44.2	40.0
Making a Contribution to Society	31.7	24.7
Special Dividends	6.5	4.5

Where rated either most, or very, important

Here though, we do not find any statistically significant differences between the matters that are important to directors according to company type.

Consistent with our findings on shareholder salience in relational/insider companies, we see slightly higher proportions of directors in insider-type companies emphasising the matters prima facie consistent with a 'shareholder primacy' corporate strategy, such as 'dividend policy', and 'special dividends'. However, these are not statistically significant differences. As with the results for the sample overall, these items tend to be much less important to directors than items such as 'growing the business', 'ensuring customers are satisfied' and 'ensuring employees are fairly treated'.

We further explored whether there was a relationship between individual company characteristics and shareholder primacy. The characteristics explored were: first, whether the company was listed or unlisted; second, whether it was a public or proprietary company; [40] and third, company size measured by annual turnover. We explored the relationship between individual company characteristics and shareholder primacy through two methods. The first was by looking for statistical correlations through cross-

[40] A proprietary company, according to the Australian Corporations Act, is one that (1) has no more than 50 non-employee shareholders; (2) does not do anything that would require disclosure to investors under the capital raising provisions contained in Chapter 6D of the Corporations Act; and (3) is limited by shares or is an unlimited company with a share capital: s 45A(1) of the Corporations Act.

tabulations and chi square tests to explore the significance of any differences between the compared groups. The second was through regression analysis. Here, we present some of our general findings (not set out in table form) from the cross tabulations first, before going on to explore the results of our regression analysis.

The cross tabulations revealed that there were statistically significant differences between listed and unlisted companies, and between proprietary and public companies in the ranking given by directors to shareholders and the company, but no statistically significant differences in the rankings given to employees. Among directors of listed companies, shareholders had a higher average ranking (1.78 compared with 2.39 in unlisted companies) and were ranked first by a greater proportion of directors (55.4 per cent of listed and 39.7 per cent of unlisted). Both these differences were significant at the 5 per cent level. Directors in unlisted companies were more likely than their counterparts in listed companies to rank 'the company' as their first priority (42.3 per cent of directors in unlisted companies did so, compared with 35.1 per cent of directors in listed companies). When we compared the average rank given to shareholders by directors in public and proprietary companies, we found a significant difference: the average rank of shareholders in public companies was 1.89 compared with 2.34 in proprietary companies. Despite this difference, however, shareholders in public and proprietary companies were still ranked as first priority by the largest proportion of directors within each company type (42.5 per cent in proprietary companies and 48.1 per cent in public companies). Company size, as measured by turnover, did not make a difference to the priority ranking of shareholders by directors.

Turning next to the shareholder salience scales set out in Table 10, we find again that listing makes a significant difference. Contrary to expectations, 'shareholder salience' is higher in *unlisted* companies, both in terms of the overall scale score and in some of the individual scale items. This finding is, however, consistent with our earlier finding on the higher level of shareholder salience in insider-type companies. Similarly, 'shareholder salience' appears to be stronger in proprietary companies than it does in public companies and also appears stronger in smaller companies (measured by turnover) than it does in larger companies.

Table 10: Effect of Company Characteristics on Shareholder Salience

Thinking about the relationship between the company and its shareholders over past year…	Listed /Unlisted % Agrees#		Proprietary / Public % Agrees#		Size by Turnover % Agrees#	
	Listed	**Unlisted**	**Prop.**	**Public**	**Small (less than $50M)**	**Large (more than $50M)**
Had the power to influence management	68.5	85.9**	84.9	68.4**	84.7	75.9*
Were active in pursuing demands or wishes which	47.8	73.3**	72.4	48.1**	72.0	60.1*

they felt were important						
Actively sought the attention of our management team	56.0	67.7**	68	57	67.2	62.1
Urgently communicated their demands or wishes to our company	33.7	54.4**	55.4	27.8**	53.7	42.8*
Demands or wishes were viewed by our management team as legitimate	74.7	80.2	79.4	74.4	78.4	79.0
Received a high degree of time and attention from our management team	58.1	67.6	67.2	58.8	65.8	64.1
Satisfying the demands or wishes of shareholders was important to our management team	82.8	83.5	83.7	82.5	83.7	83.6
Average score for shareholder salience scale	3.42	3.80**	3.79	3.40**	3.73	3.66

includes responses ‘strongly agree’ and ‘agree’
* significant at the 5% level
** significant at the 1% level

We noted in our earlier discussion of directors’ perceptions of shareholder influence that high levels of shareholder power and legitimacy were not necessarily matched by similarly high levels of activity or urgency of demand by shareholders (suggesting that the ‘shareholder salience’ test should be split into two scales according to the categories ‘shareholders legitimate’ and ‘shareholders active’.) This distinction between types of shareholder salience becomes more important when companies are disaggregated based on certain company characteristics. What Table 10 reveals is that there are significant differences in directors’ perceptions of the level of activity or urgency with which demands are conveyed by shareholders that appear related to company size and character. In unlisted companies for example, shareholders are perceived as being more active in seeking the attention of management, having greater urgency in communicating demands and being more active in pursuing demands than they are in listed companies. It appears to be the case that the higher levels of activity and urgency of shareholder demands in unlisted and proprietary companies increase the level of shareholder salience overall.

In addition to looking for correlations between individual company characteristics and salience rankings, we also employed multiple regression analysis to identify those individual characteristics which best explained (or predicted) a ‘shareholder primacy’ corporate strategy (once the effects of all other characteristics have been factored out). Multiple regression can be used to explore the relationship between one dependent variable and a number of independent variables or predictors.

In the case of Table 11, the dependent variable is the ranking given to shareholders out of a list of ten possible stakeholders. Among the explanatory (or 'right-hand side') variables, we included a dichotomous variable which identified a company as being consistent with a relational/insider type (namely, one which scored high on the presence of those

characteristics which define it as relational/insider). We also tested (in a separate regression) the explanatory variable (again, dichotomous), which identified a company as being consistent with a market/outsider type. Relational/insider and market/outsider companies are mutually exclusive; a number of companies scored toward the 'middle' on both scales and were coded zero.

In the case of the relational/insider model, these characteristics are:

- unlisted;
- largest shareholder on the board;
- any other large shareholders represented on the board; and
- proportion of shares held by institutional investors <10%.

In the case of the market/outsider model, these characteristics are:

- listed;
- largest shareholder not represented on the board;
- any other large shareholders not represented on the board; and
- proportion of shares held by institutional investors >10%.

We chose to include these characteristics in the models because, after much experimenting, these variables held together the best.[41]

Table 11 indicates that only the variable for 'high market/outsider' was significant (t-value –2.1840, significant at the 0.05 level). The coefficient for the 'market/outsider' dummy was negative (and significant) indicating that the presence of this characteristic in a company strongly favours the first-choice ranking of shareholders as the number one stakeholder.

Table 11: Regression Analysis on Stakeholder Ranking Exercise

Dependent (A.SHARE): Influence on Ranking Shareholders First on Order of Priorities Ranking Variable (two separate regressions)[42]						
Variable	*B*	*SE B*	*Beta*	*T*	*Sig T*	*Sg*
Insider/Relational	0.1128	0.2417	0.0317	0.4660	0.6412	
Market/Outsider	-0.5736	0.2627	-0.1543	-2.1840	0.0297	*

[41] We originally included long term debt finance arrangements and creditors represented on the board as part of the relational/insider model, as is outlined in our methodology, however, a ‘First Rotated Principal Components Analysis’ showed that these elements did not align with the others.

[42] Overall regression for the Insider/Relational model: F-stat=1.4188 with 4 degrees of freedom (regression) and 336 degrees of freedom (residual) was *not* significant on the F test. Adjusted r-squared was negligible. In any case, the Insider/Relational variable was not significant. Overall regression for the Market/Outsider model: F-stat=2.5751 with 4 degrees of freedom (regression) and 336 degrees of freedom (residual) was significant on the F test at p=0.0376. Adjusted r-squared figure is 0.0182. Market/Outsider variable was significant at 0.05 level. Other variables (relating to selected company characteristics) are not shown (and none of which were statistically significant).

The relational/insider and market/outsider models did not have a significant influence on any other indicators of a high shareholder primacy corporate governance strategy, such as the shareholder salience scales.

Further results are reported in Tables 12 and 13. In the case of Table 12, the dependent variable is the overall 'shareholder primacy corporate strategy': a scale that averages the seven questionnaire items which reflect the relationship between the individual respondent companies and its shareholders. The five explanatory (or 'right-hand side' variables) are all dummy variables (that is dichotomous) which test the influence of the presence of the following factors:

- whether the company is a proprietary company (otherwise, it is a public company);
- whether the company is stock exchange listed (otherwise, unlisted);
- whether the largest shareholder has a seat on the company board (otherwise, not);
- whether the largest shareholder holds less than 30 percent of the shares (otherwise, 30 percent or more); and
- whether the company has a turnover in excess of $50 million per annum (otherwise, a small company with less turnover).

Table 12 indicates that only the dummy variable for 'Proprietary Limited' was significant (t-value 2.1650, significant at the 0.05 level); the significance is positive implying that the company being a proprietary company would raise (positively influence) the belief that the company has a shareholder primacy corporate strategy. No other item in the regression returned a suggestively high t-stat. (The 'Large Company' t-stat was 1.475, while the 'Listed Company' t-stat was –1.3, results which would need more research to substantiate a possible influence).

Table 12: Regression Results for the Seven-Item Shareholder Primacy Corporate Strategy Scale

Dependent (INFSHA$): Influence of Shareholders Scale (Average of seven items)						
Variable	*B*	*SE B*	*Beta*	*T*	*Sig T*	*Sg*
Proprietary Limited	**0.3314**	**0.1530**	**0.1703**	**2.1650**	**0.0311**	**
Listed Company	-0.2006	0.1543	-0.1095	-1.3000	0.1945	
Largest Shareholder on Board	0.0179	0.1388	0.0081	0.1290	0.8977	
Largest Shareholder holds < 30%	-0.0708	0.1169	-0.0390	-0.6050	0.5454	
Large Company (Turnover > $50m)	0.1445	0.0980	0.0865	1.4750	0.1412	
(Constant)	3.4442	0.2163		15.9220	0.0000	

Notes: Overall regression F-stat=4.9702 with 5 degrees of freedom (regression) and 336 degrees of freedom (residual) was significant on the F test at p=0.000. Adjusted r-squared figure is 0.055.

We also separately tested each of the two sub-scales which could be derived from the seven items. The first tested the 'shareholder legitimate' scale, a factor composed of the average of three items relating to legitimacy, but the overall regression was not significant. Secondly, we tested the 'shareholder active' sub-scale, composed from the

averaging of four questionnaire items. The results are reported in Table 13 below. Again, it shows that only the 'Proprietary Limited' dummy was significant (t-stat=2.734, and statistically significant at the 0.01 level) with a positive significance, giving some confirmation to the overall regression reported in Table 12 above. Again, the negative sign attached to the 'Listed Company' dummy is of interest, but note that, again, it was not statistically significant (t-stat= -1.434).

Table 13: Regression Results for the Four-Item Shareholder Primacy Corporate Strategy Scale

Dependent (INFSHA1$): Influence of Shareholders Scale (Average of four items)						
Variable	*B*	*SE B*	*Beta*	*T*	*Sig T*	*Sg*
Proprietary Limited	**0.4863**	**0.1779**	**0.2113**	**2.7340**	**0.0066**	**
Listed Company	-0.2570	0.1792	-0.1188	-1.4340	0.1524	
Largest Shareholder on Board	-0.0783	0.1611	-0.0302	-0.4860	0.6273	
Largest Shareholder holds < 30%	-0.1420	0.1360	-0.0664	-1.0440	0.2973	
Large Company (Turnover > $50m)	0.1249	0.1137	0.0634	1.0980	0.2730	
(Constant)	3.3492	0.2510		13.3460	0.0000	

Notes: Overall regression F-stat=7.2791 with 5 degrees of freedom (regression) and 335 degrees of freedom (residual) was significant on the F test at p=0.000. Adjusted r-squared figure is 0.0845.

What does this regression analysis tell us about the difference between proprietary limited companies, as compared with other companies? When we factor out the influence of all other dummies in these regressions, precisely what is the contribution of a company being proprietary (as opposed to being public) to a 'shareholder primacy corporate strategy'? The scale in each regression ranges from 1 (low shareholder primacy) to 5 (high). To aid interpretability we may take as an example the first item which made up both scales (in Tables 12 and 13), namely, agreement with the proposition that 'Shareholders had the power to influence management'. We note that the coefficients for 'proprietary company' in the regressions were, respectively, 0.3314 (the seven-item scale in the second column of Table 12); and 0.4863 (the four-item scale in Table 13). This means that the impact of being a proprietary company would move the response on the item about one third to one-half between any two adjoining options on a Likert Scale. So, for example, if absence of proprietary company was 'agree' to the proposition that 'shareholders had the power to influence management', then the presence of a company being proprietary limited would move the response to the right of the 'Agree' option toward the 'Strongly Agree' option, but only one third to one half of the way. In other words, it is has some significance, but is not highly influential.

We turn finally to the relationship which exists between those issues of significance to directors and company characteristics. Here, we can note (not shown in table form) that share price appeared to be important to a significantly larger proportion of directors of listed companies than those of unlisted companies (60.4 per cent compared with 38.9 per

cent). Similarly, and not surprisingly given the fact that listed companies must be public companies, directors in public companies were more likely to rate the share price as important than were directors of proprietary companies (64.5 per cent compared with 38.7 per cent of directors of proprietary companies). Neither of these outcomes was unexpected.

To sum up, we can say that, with one exception our modelling of the market/outsider, relational/insider typologies did not reveal the predicted emphasis on 'shareholder primacy' we expected to find in the market/outsider group. For reasons which we have set out earlier (see Part 2), this finding should be treated with some caution because of the experimental nature of our modelling. However, we do find significant differences in the extent of 'shareholder primacy' between listed and unlisted companies, and between proprietary and public companies. Shareholders were more likely to be ranked as first preferred stakeholder in listed and public companies, and share price was more important to directors in listed and public companies. Surprisingly though, given these findings, overall 'shareholder salience' was higher in unlisted and proprietary companies.

Does Shareholder Primacy come at the Expense of Employees' Interests?

As we noted at the outset, the rise of the 'shareholder value' norm is argued by some commentators to have had particularly harmful consequences for employees in the form of lower levels of employment security, poorer working conditions and the decline of legitimate voice or representation within business organisations.[43] The information gathered in our survey was not designed to enable us to determine objectively whether employees had suffered loss or harm in their employment as a result of directorial strategies in 'shareholder-oriented' companies. We were, however, able to secure information which to a limited degree enabled us to examine how directors in 'shareholder-oriented' companies perceived their priorities in relation to employee interests. We explore this question first by examining the evidence on the relative positions of shareholders and employees as revealed by our analysis of the 'salience' scales, and second, by comparing aspects of company practice, such as the human resources matters raised at board level in companies that have a high level of shareholder orientation with those that have a lower level of shareholder orientation. Finally, we examine the intentions of directors regarding their priority actions as they affect shareholders and employees, in the event of an improvement or decline in the financial performance of the company.

As part of our earlier discussion on shareholder primacy, we briefly noted the position of employees relative to shareholders on the salience scales and saw that while shareholders had slightly higher salience ratings than other stakeholders, employees were ranked a close second. We now turn to a closer examination of this issue.

[43] See Froud *et. al*., above n. 8; Lazonick and O'Sullivan, above n. 2; and the works cited in n. 10.

Table 14: Comparison of Shareholder and Employee Salience

Statement	**Shareholders** % of Directors Agree	**Shareholders** Mean score	**Employees** % of Directors Agree	**Employees** Mean score
Had the power to influence management	81.2	4.03	78.0	3.74
Were active in pursuing demands or wishes which they felt were important	66.5	3.61	65.4	3.48
Actively sought the attention of our management team	64.6	3.54	70.5	3.60
Urgently communicated their demands or wishes to our company	48.8	3.20	47.0	3.14
Demands or wishes were viewed by our management team as legitimate	78.7	3.88	76.7	3.83
Received a high degree of time and attention from our management team	65.0	3.61	85.9	4.03
Satisfying the demands or wishes of this stakeholder group was important to our management team	83.3	4.02	87.9	4.04

As Table 14 indicates there were very similar patterns of response regarding both shareholders and employees for the individual scale items. While we noted earlier that shareholder salience was higher overall than employee salience, there are some scale items on which employees were more highly rated. In particular, we can see that directors were more inclined to agree that employees received a high degree of time and attention

from management (85.9 per cent) than shareholders (65 per cent). A slightly larger proportion of directors felt that employees had actively sought the attention of management (70.5 per cent regarding employees compared with 64.6 per cent regarding shareholders). Thus, while we have seen that shareholder power and legitimacy seem to exist to some degree separately of the level of demand by shareholders, employee power and legitimacy may be more closely related to the level of demand that they exhibit.

Moving beyond the relative position of shareholders and employees, we examine the effect of a high level of 'shareholder primacy' on the interests of employees. We do this by comparing the responses of directors in companies where shareholder primacy was highly rated (those in which shareholder salience was at the high end of the scale) with those of directors in companies where shareholder primacy was lower (those in the low range of the shareholder salience scale). We compare organisational matters such as the frequency of human resources issues raised at board level, the priorities of directors in the event of a change in company financial performance, and attitudes to partnership relations with employees.

Table 15: HR Issues Raised at the Board

HR Issues Raised at Board	% of Whole Sample raised 3 or more times	% of High Shareholder raised 3 or more times	% of Low Shareholder raised 3 or more times
Remuneration	37.1	37.9	35.5
Productivity	66.3	65.4	68.3
Performance Management	64.2	63.0	71.4
Industrial Disputes	10	10.2	6.5
Enterprise Bargaining	15.4	15.9	14.5
Restructuring or Retrenchments	16.1	18.9	4.8**
Employee Share Schemes	15.8	17.2	14.5
Work Organisation	56.9	57.6	61.3
Training	65.0	65.0	63.9
Occupational Health and Safety	73.3	71.6	74.2

** significant at 1% level, significant difference is between high and low shareholder groups

The most striking finding is that directors in companies in the high range of the shareholder salience scale were significantly more likely to report that restructuring or retrenchments concerning employees below executive level had been considered by the board during the previous twelve months (18.9 per cent) than directors in companies in the low range of the shareholder salience scale (4.8 per cent). A similarly significant, and related, finding (not shown in Table 15) is that directors in companies where 'shareholder primacy' was emphasised were more likely to report that staff numbers had decreased in the past year (20.4 per cent) than those in companies in the low range of the shareholder

salience scale (7.9 per cent). This is a significant finding, providing some support for the view that a strong emphasis on shareholder primacy may lead to an emphasis on costs and job reductions, detrimental to the interests of employees.

In terms of other matters raised, there were no significant differences. The results show that the four most commonly raised issues concerning employees below executive level were: occupational health and safety (73.3 per cent of whole sample); productivity (66.3 per cent); training (65.0 per cent); and performance management (64.2 per cent).

To gauge further the extent to which a 'shareholder primacy' conception of the company was likely to result in a lower priority being given to the interests of employees, we asked directors to identify their priorities in the event of an upturn or downturn in the financial performance of the company.[44] Given the demonstrated relationship between high levels of shareholder salience and discussion about retrenchments, we expected to find that there would be differences between the priorities of directors in high shareholder salience companies and those in low shareholder salience companies in the face of change in the financial performance of the company.

Table 16: Priority in the Event of Upturn or Downturn in Financial Performance

Priority	Improvement % Ranked No. 1#		Downturn % Ranked No. 1#	
	High Shareholder	Low Shareholder	High Shareholder	Low Shareholder
Increase/Decrease Number of Employees	11.1	10.7	14.7	11.9
Increase/Decrease Executive Compensation or Bonuses	6.3	7.1	24.0	33.9
Increase/Decrease Shareholders Dividend	62.6	57.9	59.9	54.1
Increase/Decrease Employees Salaries or Bonuses	23.3	25.9	3.2	1.7

Directors were asked to rank in order of priority from 1 to 4 with 1 being highest priority

However Table 16 does not support this expectation. There are no significant differences between the priorities of directors based on the level of shareholder salience. What is interesting is that while it is clear that shareholders' dividends are considered to be the

[44] This question was drawn from responses in a 1999 Japanese Ministry of Labour survey of executives at large firms, cited in I. Takeshi, 'From Industrial Relations to Investor Relations? Persistence and Change in Japanese Corporate Governance, Employment Practices and Industrial Relations' (2001) 4 *Social Science Japan Journal* 225. In this study, the interests of shareholders and employees appeared to be treated fairly equally.

first priority in the event of an improvement in the financial performance of the company (62.6 per cent of high shareholder salience directors and 57.9 per cent of low shareholder salience directors), shareholders' dividends are also the first to 'suffer' in the event of a downturn. Some 59.9 per cent of directors in high shareholder salience companies, and 54.1 per cent of directors in low shareholder salience companies reported that they would prioritise smaller dividends to shareholders in the event of a downturn in the financial performance of the company in preference to decreasing the number of employees or decreasing employee salaries. While nearly one quarter of directors reported that they would increase employees' salaries or bonuses in the event of an improvement in financial performance, only a very small proportion reported that they would decrease them in the event of a downturn.

Finally, we asked directors about partnership relations with employees. Here we had hypothesised that a strong emphasis on the interests of shareholders would be antithetical to 'partnership style' relations between the company and its employees and therefore we anticipated that directors in companies in which shareholder primacy was high would be less likely to indicate that the company worked in partnership with employees. We asked directors to indicate whether they conceived of the relationship with employees in their companies as being one of partnership. We also asked them to indicate whether, if they did conceive of a partnership, it was founded on the alignment of interests between employees and the company or whether it allowed for difference. This distinction was based on our case study findings and also a previous survey conducted by Guest and Peccei.[45] In the course of our case studies, the views of respondents concerning the nature of the partnership differed widely. In semi-structured interviews conducted during the course of our case studies respondents sometimes described a direct and unitary conception of the relationship between the company and its employees, or, at other times, an indirect and separate relation with the employees or unions. In their study, Guest and Peccei revive the terms 'pluralist' and 'unitarist' to explain approaches based on 'a clear acknowledgement of differences of interest between capital and labour'[46] on the one hand, compared with those which 'explicitly seek to integrate employer and employee interests',[47] on the other. (They added to these two categories a hybrid approach which 'combines elements of the two previous perspectives'.[48])

Following these distinctions, the survey questions were divided between views that reflected a 'single-interest' (unitarist) conception of relations with employees and a 'separate-interests' (pluralist) conception. If respondents did not think that a partnership style relationship was present, we asked them to identify the reason for this based on closed options which were also based on this 'unitarist'/'pluralist' distinction. The responses are shown in Table 17.

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[45] D. Guest and R. Peccei, 'Partnership at Work: Mutuality and the Balance of Advantage' (2001) 39 *British Journal of Industrial Relations* 207, 209.
[46] Ibid, 208-9.
[47] Ibid, 209.
[48] Ibid, 210.

Table 17: Yes to Partnership between Company and Employees

Partnership with Employees?	% of Whole Sample - Yes	% of High Shareholder -Yes	% of Low Shareholder -Yes
Is the relationship between the company and its employees best described as one of partnership?	76.9	75.8	76.2
Company and employees are parties with separate interests	29.2	30.2	25.5
Company and employees are parties with same interests	70.8	69.8	74.5

We can observe that a large majority of directors perceived that the relationship between their company and its employees was one of partnership. This did not vary between companies with either a high or low 'shareholder orientation'. In terms of the nature of such partnerships, a large majority of directors, around 70 per cent, saw the company and its employees as being parties with the same interests. Again, the importance of shareholders within the company did not have a significant effect on this response.

There is some evidence, however, that there may be a negative relationship between partnership and a strong 'shareholder primacy' view. A comparison of the responses of directors who indicated that they believed that the relationship between their company and its employees was one of partnership with the responses of those who did not, revealed that directors who indicated the relationship was not one of partnership were more likely to characterise their understanding of their legal obligations as 'I must act in the best interests of the company and this means acting in the long term interests of shareholders only' than directors who believed that the relationship was one of partnership. Directors who believed the relationship with employees was not one of partnership were also statistically more likely to have ranked shareholders as their number one stakeholder.

To conclude on the question of the effect of an emphasis on shareholder primacy on the interests of employees in our surveyed companies, we have seen that a high level of shareholder primacy is associated with a reduction in employee numbers over the past year and a higher incidence of board level discussion of restructuring or retrenchment. This provides some support for the argument that 'shareholder primacy' may induce directors to act negatively toward employees. This relationship was, however, not evident when it came to directors' priorities in the event of a downturn in company performance. Here a majority of directors, regardless of the level of shareholder salience, indicated that they would prioritise decreasing dividends to shareholders, rather than decreasing the number of employees. In addition, as indicated in Table 14, in which directors' responses

to shareholder and employee salience are compared, there is a similar pattern of response regarding both shareholders and employees and for some specific items employees' interests are more highly ranked by directors. Similarly, it did not appear to be the case that a high level of shareholder salience would stand in the way of partnership relations with employees as we had hypothesised it would. Nonetheless, given the evidence of a relationship between directors' attitudes to partnership and their understanding of their obligations to shareholders, it may still be the case that 'shareholder primacy' is in certain respects antithetical to the idea of partnership.

4. Conclusion

It is clear that the shareholder primacy view of directors' priorities has considerable cogency, but at the same time the results of our survey indicate that this cannot be reduced to a simple proposition that directors will necessarily pursue shareholders' interests at the expense of other stakeholders. There is very little evidence, for example, that directors see short term returns to shareholders through share price or other short term gains as a priority at all. Clearly, though, shareholders are seen as important and, probably, the most important, of stakeholders. Shareholders and the company have first priority over others, with very few directors ranking employees as their number one concern, though they appear generally equal with shareholders when other measures are compared. Shareholder primacy is also seen in the results of the salience scale insofar as the scale clearly indicates that a large majority of directors regard satisfying shareholder demands as important (80 per cent plus), regard their demands as legitimate (around 78 per cent) and view them as having the power to influence management (80 per cent plus).

How this prioritisation plays out in directors' minds, however, is far from clear cut. It evidently does not follow that other stakeholders are not prioritised or that their interests are not attended to or seen as legitimate. Other evidence derived from the survey results indicates that employees, for example, are also ranked highly in these respects and sometimes ranked more highly than shareholders (see Table 14). We might conclude, therefore, that shareholder primacy appears more of a general outlook than a specific policy based around certain strategies aimed exclusively at maximising profits for shareholders. For instance dividend policy and increased share price ranked relatively poorly as against job security and employee morale in the list of specific corporate agenda items put to directors. Having said that, there were some outcomes which indicate that shareholder primacy may have a harder edge than this general portrayal would suggest. For example, there is evidence that among directors who were at the higher end of the shareholder primacy scale, job reductions appeared to be more likely to have been considered as part of corporate strategy. However, we doubt that too much can be read into this finding. First, directors who reported having discussed job reductions still only constituted about one fifth of those who were at the high end of the shareholder primacy oriented group. Second, the finding does not consistently arise when other characteristics are taken into account such as when comparisons are made between listed and unlisted companies or between market/outsider and relational/insider companies.

One major disparity between the literature and our survey findings concerns the hypothesised relationship between the shareholder primacy conception and the market/outsider type of company. In general terms, we might expect to find Australia situated as a member of the market/outsider group of countries and accordingly to find that Australian corporations generally fit the pattern suggested by the theorised link between shareholder primacy and the market/outsider type of company. These reasons are explained elsewhere;[49] however, it is sufficient for our purposes here to note that it is assumed that companies with market/outsider characteristics will be more shareholder oriented because a liquid capital market which allows for high rates of share trading results in strong pressure on companies to attract and maintain shareholders by appearing shareholder focussed. However, in our research we attempted to distinguish *within* Australia between companies more approximating the market/outsider model and those more approximating the relational/insider model. Our results on several (but not all) related indicators revealed a stronger link between the shareholder primacy conception and the relational/insider type than between shareholder primacy and the market/outsider model. The one exception to this was when we conducted regression analysis. The regression analysis suggested that presence of the market/outsider characteristics in a company strongly favours the first-choice ranking of shareholders as the number one stakeholder (see Table 11). However, these characteristics did not have a significant influence on any other indicators of a high shareholder primacy corporate governance strategy.

This finding leads us to a number of possible conclusions. The first is that it may not be valid to try to generalise about the form of governance on such a broad national basis. The second is that the model we built for statistical testing may be flawed. That is, that the model is statistically, but not theoretically flawed. A third possible conclusion is that the theory itself is flawed. Our findings seem to indicate that the third of these options is most plausible. We constructed a number of different statistical models in order to put together a relational/insider model and a market/outsider model which held together statistically, and although a coherent model was achieved, it did not have great explanatory strength when used in regressions.[50] With regards to the theory itself, it seems logical that where companies have 'insider-relational' characteristics, such as being a proprietary company rather than a public company, being unlisted rather than listed, having a major shareholder represented on the board, and so on, the relationship with equity investors would be more direct and thus the likelihood that there may be a shareholder orientation may be higher than in market/outsider companies in which shareholders are more distant. In a proprietary company, for instance, it may often be the case that the manager is also a director and a shareholder. In such a setting, it is easy to imagine that shareholders might be perceived to be both 'active' and 'legitimate'.

Finally, whatever the normative strength of the shareholder primacy view, it is clear that shareholder primacy is not derived from a legal obligation on the part of directors, nor is it derived from a misconceived view by directors that they are under an obligation to pursue such a policy. Directors seem clearly to understand that they are legally free to

[49] See Jones and Mitchell, above n. 6.
[50] See the discussion in the text explaining Table 11.

pursue any strategy which they feel will benefit all stakeholders. If anything, this more rounded perspective of the goals of corporate governance has become more developed over the past decade, probably as a result of numerous failures of corporate governance and regulation which have plagued Australia along with the USA and UK,[51] and the consequent extensive debate over corporate responsibility to society at large. Earlier studies of directors' attitudes suggest that Australian directors were previously more inclined to equate the best interests of the company with those of shareholders, and to prioritise the interests of shareholders over those of other stakeholders.[52] The obvious disparities between key outcomes in those earlier studies and the results in our survey may indicate a substantial shift by directors away from a simplistic shareholder primacy view towards a more balanced approach.[53]

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[51] J. Hill, 'Regulatory Responses to Global Corporate Scandals' (2005) 23 *Wisconsin International Law Journal* 417.
[52] See Tomasic and Bottomley, above n. 18 and n. 32; Francis, n. 19 and n. 28 and associated text.
[53] See S. Deakin, above n.1 at pp. 99-100.