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Corporate governance and stakeholder conflict

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Abstract The stakeholder management literature is dominated by the 'shareholder value' and 'inclusive stakeholder' views of the corporation. Each views the governance problem in terms of *inter-functional* conflicts between stakeholder groups, such as between investors and managers or managers and employees, and rests on the assumption of an idealized corporate structure characterized by the separation of ownership from management. Our review of corporate governance and stakeholder conflict shows that such functional-based characterization is too simplistic and fails to account for important intra-functional conflict. Through a comparative review that considers managerial, stakeholder and family systems of governance, we demonstrate that, while the modality of conflict varies by system, substantial intra-functional conflict is endemic to each. We integrate the findings of the agency and comparative stakeholder theories of corporate governance to offer an authority-based framework with three different governance structures that offers complementary insights into stakeholder conflicts. Thus, our study highlights the important, but often neglected, intra-stakeholder type of conflict in various organizations and provides a basis for understanding their various manifestations and consequences under the different systems of governance.

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1 Introduction

> Beggars do not envy millionaires, though of course they will envy other beggars who are more successful. (Bertrand Russell)

Russell's observation on the resentment that can attend those sharing the same condition reminds us of a point all but forgotten in the management stakeholder literature- namely that stakeholders who seemingly share a common fate are frequently in conflict with one another. Rather than united in common cause against a more powerful other, like brothers in arms, they can be more like Cain and Abel, the one envious and divided against the other. Contemporary corporate governance is primarily concerned with conflicts *between* stakeholder groups, such as owners, workers, and managers, or what Wolfe and Putler (2002: 298) describe as role-based stakeholder groups. Conversely, we show in this paper that the corporate governance literature identifies settings for numerous conflicts *within* stakeholder groups or *intra*-stakeholder conflicts, such as those among owners (Bergloff and von Thadden 1994; Hoskisson et al. 2002) or creditors. However, while there are several compelling explanations of inter-stakeholder conflicts, such as agency theory (Eisenhardt 1989) or class politics (Roe 1994), there is no comparable account of intra-stakeholder conflict.

We address the issue of intra-stakeholder conflict from the perspective of an authority approach. Through a comparative review that considers managerial, stakeholder, and family systems of governance, we show how patterns of authority inherent in each in system privileges by according salience to distinct classes of stakeholders and increases their capacity to achieve their interests. In this regard, corporations can be understood as venues for distributional contests among stakeholders (Edwards 1979; Fiss and Zajac 2004). The idea that firms are venues for distributional contests will surprise few readers, yet this aspect of governance is rarely investigated. Indeed, Hinings and Greenwood claim that management theory has lost interest in how 'privilege and disadvantage are distributed within organizations' (2002: 411). With a focus on incentive alignment, managerial oversight, and codes of practice, much corporate governance research focuses on mitigating inter-stakeholder conflict with a view of maximizing corporate performance and firm value (Dalton et al. 2003). However, phenomena such as minority shareholder expropriation, executive salary premia, opaque accounting practices, unfunded pension liabilities, and related party transactions indicate that value is often appropriated and redistributed among stakeholders before it appears in bottom line performance measures (Coff 1999). Recurrent corporate scandals highlight the contested nature of stakeholder relationships, as they periodically propel corporate governance practice into the mainstream of political debate. A case in point is the recent public outcry over the bonuses being paid to AIG executives in US, and the demand for capping compensation in the UK.

We propose that intra-stakeholder conflicts are inherent in a firm's functioning, and because stakeholder primacy varies with the governance system, so does the very definition of governance issues—whether as a means of resolving conflicts, or as the very cause of the conflict. The fundamental issue of corporate governance is not simply one of protecting shareholders from managers; rather, the issue is one of determining stakeholder distribution rights, describing inter-stakeholder tensions, and identifying the means through which the primary stakeholders seek to preserve their privileges and to externalize the costs of those privileges onto less powerful secondary stakeholders. Our review suggests that variation in governance systems privileges distinct classes of stakeholders in terms of their capacity to achieve their goals.

Our intended contribution is to advance the idea that 'above the bottom line' value distributions to stakeholders depend decisively upon a firm's corporate governance system. Such contests to capture value can be manifest in either financial or non-financial terms. For example, executives may prefer to take value in the form of perks (Zajac and Westphal 1994) and employees may seek compensation through job security, flexible terms of employment, vacation time or career development opportunities. In this respect, we seek to explain stakeholder salience, which is 'the degree to which managers give priority to competing stakeholder claims'(Mitchell et al. 1997: 854). Whereas Mitchell et al. (1997) propose salience as a function of stakeholder's power, legitimacy and urgency, we argue that stakeholder salience is influenced by attributes of its governance.

In the following sections, we briefly review existing perspectives on inter- and intra-stakeholder conflicts in the governance literature and highlight the shortcomings therein. Subsequently, we develop the notion of authority-based governance systems and demonstrate its utility to assess intra-stakeholder conflicts. Thereafter, we review literature linking stakeholder salience peculiar to each governance system, link each type of governance system to its characteristic stakeholder conflicts, and finally conclude with suggestions for future research.

2 Inter- and intra-stakeholder conflict

2.1 Agency perspective

The prevailing perspective on corporate governance is agency theory, which holds that differences in owner and manager interests constitutes the major stakeholder conflict in the modern corporation (Jensen 1989; Jensen and Meckling 1976). While separation of ownership and managerial control represents an efficient specialization of function (Fama and Jensen 1983), professional managers with little or no ownership stake in the firms they manage make decisions on behalf of shareholders, but have little incentive to manage the firm efficiently or in a manner consistent with the interests of its shareholders. The solution to the conflict is essentially contractual in nature: namely executive compensation through incentive contracts combined with board and stock market oversight (Useem 1993). In this shareholder value maximization conception of the firm, contractual solutions are recommended and extended to other stakeholders. Therefore, each of the firms' constituencies, "labor, capital, suppliers, customers, the community, and management- … are better advised to perfect their relations to the firm at the contracting interface at which the firm and their constituents strike their main bargain" (Williamson 1985: 298). Such a solution conceives of the firm as little more than a nexus of contracts (Williamson et al. 1990) in which inter-stakeholder relations are expected to be inherently adversarial (Roe 1994).

At the heart of the managerial governance model, is the normative acceptance for shareholder value maximization, and the expectation that managers will continue to serve themselves first (Hansmann and Kraakman 2004). The tension between shareholders and managers over value allocation has lately shifted away from the design of incentives toward the intensification of monitoring and accountability. Much formal governance reform is crisis driven (Coffee 2000) and the recent scandals inherent in the financial crisis in the U.S. have created a unprecedented momentum for legislative change. Previous U.S. legislation such the Sarbanes–Oxley Act of 2002, which strengthens disclosure requirements, was enacted in the wake of several earlier corporate scandals in which executives were manifestly manipulating incentive systems in their own favor. However, stronger reporting requirements are not always in the interest of some organizations. For example, information disclosure by high-tech firms might harm their competitive positions, and disclosure can also hinder the restructuring of mature enterprises. Consequently, intensified disclosure requirements may have precipitated a move toward private equity (Engela et al. 2007) with the intent to strengthen equity holders' claim over residual value and does little to improve outcomes for other stakeholders.

Thus, while the focus of agency-driven governance is the conflict between stakeholder groups, there are a few instances of intra-stakeholder conflict assessment. The tension between creditors and equity holders is well-documented (Harris and Raviv 1991; Jensen and Meckling 1976), wherein the debt contract gives equity holders an incentive to invest sub optimally. However, the agency theorists' concern still remains minimizing managerial opportunism, and the recommendations focus on the optimization of debt holding by trading off the "agency cost of debt against the benefit of debt" (Harris and Raviv 1991: 301). Recent literature also points towards the potential of conflict between majority and minority equity holders, commonly known as the Principal-Principal Agency (PPA) or Type 2 agency concerns, especially in the context of emerging economies (Dharwadkar et al. 2000), and dual class shareholding (Jarrell and Poulsen 1988). There are also a few studies looking at the difference in outcome preferences between different types of owners (Thomsen and Pedersen 2000), and long-term (pension fund) and short-term (mutual-fund) investors (Hoskisson et al. 2002). However, the underlying governance concern remains the agency-driven maximization of shareholders' return and/or minimization of managerial self-serving behavior.

While the agency theory of *inter-stakeholder* tensions is insightful, it is partial and oversimplified. Our comparative review of governance systems suggests a more fine-grained perspective that identifies and highlights numerous *intra-stakeholder* tensions, including those between minority and controlling investors, equity investors and creditors, knowledge workers and routine workers, senior and new employees, owner-managers and professional managers, and insider and arm's-length buyer/suppliers. Different governance systems privilege distinct classes of shareholders in terms of their capacity for achieving their investment goals, monitoring performance, and enforcing their claims (Thomsen and Pedersen 2000). Similarly, governance systems also differ in their tendencies to accommodate bargaining and power dynamics that in turn influence stakeholders' abilities to extract firm value.

2.2 Stakeholder theory perspective

Traditional approaches to stakeholder management tend to view distributional contests in terms of gross role-based categories (Wolfe and Putler 2002), such as tensions between investor and employee outcomes or between management and employees (Freeman 1984; Pfeffer 1994). These role-based stakeholder groups are assumed to share similar priorities and interests within the group. Ironically, Freeman (1984), the doyen of stakeholder theory, warned against assuming homogeneity of interests among such groups and has argued that stakeholder theory ought to identify specific points of differentiation within seemingly homogenous groups. However, few studies have gone beyond generic role-based definitions; the majority assume homogeneity of interests and priorities within role-based stakeholder groups (Wolfe and Putler 2002). While the stakeholder management concept promises insight on how managers might balance their responsibilities to shareholders and other interested parties who hold a legitimate stake in the firm (Freeman 1984), the reconciliation of competing claims has proven difficult.

In particular, the logic of shareholder wealth maximization has been inhospitable to the stakeholder view of the firm. One key text declares "mutually beneficial stakeholder relationships can enhance the wealth-creating capacity of the corporation" (Post et al. 2002: 36). However, empirical support for this view is mixed (Berman et al. 1999; Donaldson and Preston 1995; Hillman and Keim 2001; McGuire et al. 1988). In addition, critics of stakeholder theory point out that managers in "such systems have no way to make principled or purposeful decisions" (Jensen 2002). Furthermore, stakeholder theorists, especially proponents of normative and instrumental approaches, often become embroiled in arid debates about the primacy of shareholder wealth maximization versus a broader conception of business ethics (Freeman et al. 2004; Sundaram and Inkpen 2004). In this respect, descriptive stakeholder theory scholars focus almost exclusively on stakeholder outcomes in the publicly-held firm where important corporate decisions are made by professional managers (Jones and Wicks 1999). By focusing on a single corporate type, such research essentially holds corporate governance as a constant. In so doing, significant variation in stakeholder and organizational outcomes in other systems of governance are overlooked.

To summarize, theories of corporate governance typically adopt either an agency/shareholder (Jensen 2000) or a stakeholder/socio-political approach (Fligstein 2001) in addressing issues of performance and efficiency. Table 1 highlights the key findings and major differences between these perspectives.

Table 1 Comparative table of the differing governance perspectives

	Shareholder perspective	Stakeholder perspective
Stakeholder outcome	Singular: specific Shareholder returns[i]	Multiple: holistic Distribution to all stakeholders[ii]
Purpose of firm	An instrument for shareholder wealth maximization[iii]	A locus in relation to wider external stakeholders' interests[iv]
Theoretical underpinnings	Transaction cost economics[v]; Agency theory: managerial agency (type 1)[vi]; principal–principal agency (type 2)[vii]	System theory[viii] Stakeholder theory[ix]
Key assumption	Dispersed shareholders as rightful owners[vi]	All stakeholders have equitable rights[ix]
Interaction	Antagonistic[x]; Arm's length[xi]	Relational[xii]
Nature of stakeholder conflict	Dyadic: Owner–manager (type 1)[xiii] Owner–owner (type 2)[xiv]	Inter-related[xv]
Examples of intra-stakeholder conflicts	Owners vs. managers (type 1)[xvi] Voting rights vs. cashflow rights (type 2)[xvii] Debt vs. equity holders (type 1 & 2)[xviii] Intra-ownership type conflicts (type 2)[xix] Long-term vs. short-term investors (type 2)[xx]	Differing perspectives of multiple stakeholders[xxi] Unmonitored and unaccountable managers[xxii]
Primary Stakeholder	Shareholder[xxiii]	No specific stakeholder group(s)
Secondary stakeholder	Managers[xiii]	No specific stakeholder group(s)
Authority	Managers for dispersed shareholder[xvi]	Network[xxiv]
Contracting mode	Formal, arm's length[xxv]	Relational contracting[xviii]
Governance focus	Mitigating agency cost[i] Minimizing transaction cost[iv]	Identifying & resolving stakeholder concerns[xxii]
Governance mechanism	Managerial monitoring Alignment of incentives[xxvi]	Network; control embedded in lasting relationships[xxvii]
Contributions	Ease of modeling[xxviii] Clear quantifiable outcome[xiii]	Realistic Includes all possible factors
Limitations	Ignores most external factors[xxii]	Complexity in modeling[xxix]; Unclear, emergent outcome[xxx]

[i] Jensen (2002)

[ii] Kochan and Rubinstein (2000)

[iii] Friedman (1970)

[iv] Letza et al. (2004)

[v] Williamson (1985)

[vi] Jensen and Meckling (1976)

[vii] Dharwadkar et al. (2000)

[viii] Trist (1981)

[ix] Freeman (1984)

[x] Galbraith (1977)

[xi] Jacoby and Mitchell (1990)

Table 1 continued

	Shareholder perspective	Stakeholder perspective

[xii] Post et al. (2002)

[xiii] Shleifer and Vishny (1997)

[xiv] Faccio et al. (2001)

[xv] Ring and Van De Ven (1992)

[xvi] Becht et al. (2003)

[xvii] Jarrell and Poulsen (1988), Gompers et al. (2004)

[xviii] Harris and Raviv (1991)

[xix] Thomsen and Pedersen (2000)

[xx] Hoskisson et al. (2002)

[xxi] Schwarzkopf (2006)

[xxii] Agle et al. (2008)

[xxiii] Fligstein (2001)

[xxiv] Charkham (1994)

[xxv] Biggart and Delbridge (2004)

[xxvi] Himmelberg et al. (1999), Jensen and Murphy (1990)

[xxvii] Sabel (2004)

[xxviii] Daily et al. (2003)

[xxix] Phillips and Reichart (2000)

[xxx] Sundaram and Inkpen (2004)

The agency or shareholder-centric approaches focus on questions relating to the incentives and allocation of decision rights among managers and providers of capital (Jensen 1998) and are preoccupied with addressing a narrow range of agency problems that stem from that relationship. On the other hand, socio-political approaches adopt a wider perspective invoking society (Fligstein 2001), politics (Gourevitch and Shinn 2005), class (Roe 2003), and history (Bebchuk and Roe 1999) to explain continuing differences in national systems of corporate governance. Although they possess great face validity, socio-political approaches to governance generally say very little about the practice of administration (Aguilera and Jackson 2003). We reason that as agency theories reduce concerns with dyadic relations in the absence of context, while socio-political theories reify host society, both streams flow away from a concern with organizations, their primary activities and purposes, and the distribution of outcomes for the stakeholders.

To address the issue of stakeholder conflict, we adopt an organization-centric and comparative governance approach that puts the firm at the center of its analysis (Aguilera et al. 2008). We describe our perspective as an authority approach that incorporates elements of both agency and socio-political theories of corporate governance. Whereas Aguilera et al.'s (2008) approach focuses on the costs and contingencies of particular corporate governance practice, we focus instead on the effects of stakeholders of the authoritative hierarchical order inherent in any governance system. In the following section, we elaborate on our authority-based governance model, ground it in existing literature, and highlight how this approach might be better positioned to explain intra-stakeholder conflicts.

3 An authority-based approach to governance

Our authority-based approach addresses a long-standing debate in the stakeholder management literature. This literature has reached an impasse between advocates of 'shareholder value' and 'inclusive stakeholder' supporters of the corporation (Jensen 2002; Kochan and Rubinstein 2000). The academic stalemate rests on the assumption of a singular, idealized corporate structure characterized by separation ownership and management, which ignores the diversity of corporate governance systems found around the world. On the other hand, the varieties of capitalism literature (e.g. Hall and Soskice 2001; Lazonick and O'Sullivan 2002; Whitley 1999) shed light on important institutional-level issues such as the incidence and prevalence of governance types, particularly societies and their implications for national competitiveness. However, there are limits to the extent to which institutions can explain patterns of corporate governance (Roe 2003). This is because, de jure, formal institutions often have little de facto impact on administrative practice (Khanna et al. 2003). Moreover, comparative approaches to corporate governance typically assume that each variety of capitalism will produce an 'emblematic firm' (Boyer 2005), such as the widely-held managerial enterprise, that will predominate in liberal market economies.

Our authority approach to corporate governance recognizes the heterogeneity of corporate governance systems within any particular institutional context. For example, while the widely-held managerial enterprise is prevalent in liberal market economies, there is also a significant presence of private equity-held managerial enterprise and a long tradition of family-controlled firms (Anderson and Reeb 2003). In practice, within any institutional architecture there will typically exist a plurality of 'pure' and 'hybridized' governance systems that consist of combinations of formal, rationally designed or selected instruments and informal, socially structured elements that 'bundle' together in various ways (Young et al. 2008). Some governance bundles are socially or economically infeasible and rarely found, whereas other governance bundles become prevalent and diffuse across societies. Our comparative review focuses on stakeholder salience under three systems: managerial, stakeholder, and family governance. Other systems of governance such as not-for-profit or co-operative ownership certainly do exist, but the three systems reviewed here appear to be the most prevalent in capitalist economies (La Porta et al. 1999). In addition, government or state-controlled enterprises, though commonly found, are not considered in this review, as governance in such entities is more a function of geo-political and national agendas, rather than fundamental business principles.

Each governance system differs with respect to efficiency and performance characteristics but we do not enter into the debate about the causes of diffusion and prevalence of governance systems, in particular societies. Instead, our purpose is to describe the organizational link between governance and stakeholder salience. Our authority approach is inductive and recognizes that '*particular configurations of hierarchy-market relations'* (Whitley 1992) constitute systems of governance that have become prevalent and institutionalized in capitalist economies. Systems of governance determine how authority is shared and allocated within organizations. Authority sharing is the extent to which *'owners and top managers delegate considerable discretion over task performance to skilled employees (and) with suppliers, customers and competitors in varied inter-firm networks* (Whitley 2007: 149). In this regard, authority may be widely shared among the firm's internal and external stakeholders or centralized in the hands of a single individual.

Authority is also implied in the relationship between owners and managers, and pertains to the decision rights accorded the management. In managerial governance, ownership and management control is separated but professional managers' discretionary authority is bounded by a series of checks and balances; managers must justify their actions on the basis of shareholder welfare (Charkham 1994). Authority most widely shared under stakeholder governance, ownership and management control is separated, however, executives of a focal firm share authority with external stakeholders, such as buyer/suppliers and capital providers. These groups make mutual commitments to one another, thereby embedding control in a network of enduring relationships. Stakeholder governance also delegates significant discretion over task organization to skilled employees and typically invites their participation in decision-making processes (Whitley 2007). Stakeholder governance is often referred to as "insider", or "network" governance (Charkham 1994) and is sometimes equated with either the Japanese or Germanic systems in which complex and durable inter-corporate networks feature prominently. Due to its decoupling from stock-market oversight and long-term relational linkages with bank and employee groups in the form of employment and co-determination, stakeholder governance most approximates what scholars identify as the stakeholder model of the firm (Sabel 2004).

In family governance, managerial authority and capital provision are concentrated and in the hands of the same individuals. The exercise of authority is largely unchecked since owner-managers are making decisions with their own money (i.e. exercising their property rights). The concentration of authority enables the firm to serve as an instrument that reflects the personal value systems of the entrepreneur and family members (Gedajlovic et al. 2005; Schulze et al. 2001). Owner-managers' decisions do not need to be justified to outsiders and as they view the firm as 'our business' (Demsetz and Lehn 1985), they may project their own idiosyncratic vision onto the business (Chua et al. 1999).

The structure of authority also dictates the *contracting mode,* which refers to prescribed norms about the way business transactions are conducted. A contracting mode varies in terms of whether transactions between the firm and resource providers are regulated by arm's length formal rules, or by more tacit agreements and relational norms (Macneil 1978; Poppo and Zenger 2002). The former reflects a highly calculative rationality, wherein actors 'attempt to consider all possible means to an end and weigh the alternative means in a decision making calculus' (Biggart and Delbridge 2004: 11). Managerial governance tends towards the arm's length side of this dimension; it emphasizes making transactions publicly transparent and establishing formal mechanisms for enforcing contracts and settling disputes (Biggart and Delbridge 2004). Stakeholder governance relies more extensively on relational contracting among its resource providers, and transactions are governed by tacit agreements and socially embedded practices with unspecified time horizons (Hamilton and Biggart 1988; Ring and Van De Ven 1992). Under family governance, owner-managers have greater freedom to exercise their discretion in utilizing either contracting mode. They can also use their social capital to transact in their social networks for financial and managerial resources, and for business opportunities (Carney 2005). Alternatively, owner-managers may adopt a highly instrumental and arm's length approach to contracting (Uzzi 1997). In the following sections, we elaborate further on each governance system and the stakeholder salience specific to it.

4 Governance systems and stakeholder salience

The salience of stakeholder claims on management attention has been viewed as a stakeholder attribute (Mitchell et al. 1997). In contrast, our authority approach proposes that firm corporate governance will determine an enduring, legally prescribed, and/or socially sanctioned *stakeholder hierarchy* regarding the rights and claims to the value created. Stakeholder salience specifies primacy or 'who really benefits' from the firm's activities through rewards and incentives that can be legally and legitimately attained. In the following sections we distinguish between primary and secondary stakeholders and show how stakeholder hierarchy engenders an array of both inter- and intra-stakeholder conflicts endemic to a specific governance system.

4.1 Stakeholder outcomes under managerial governance

The great virtue of managerial governance is its capacity to simultaneously provide equity investors with the liquidity of their capital and participation in returns from long-term investment. It is this dual shareholder benefit that lies behind large liquid capital markets that allow for the emergence and persistence of managerial governance (Rappaport 1990). Firms characterized by managerial governance make greater use of public equity markets than other types of firms. Thus, the majority of capital is supplied by diversified arm's length suppliers who are more concerned with returns on their portfolios than the performance of any one investment (Shleifer and Vishny 1997). The primary role-based stakeholder conflict is between equity investors and executives. The authority structure arising from separated ownership and management vests strategic decision rights with professional managers who serve as agents for widely dispersed and diversified shareholders and to whom they hold a fiduciary duty. However, arm's length investors are vulnerable insofar as they have neither the ability nor, by virtue of their small holdings in any one firm, the incentive to monitor managers (Kester 1992). Agency theory recognizes that the interests of managers and shareholders diverge and that salaried executives tend to pursue expansion strategies and/or consume a variety of perquisites that benefit them at the expense of shareholders (Jensen and Meckling 1976). Due to their delegated authority, structure professional managers possess access to critical information and tacit knowledge of the firms' operations and have significant opportunity to capture value.

To contain potential agency problems in managerial-controlled firms, an array of capital market instruments and agencies have emerged to redress the power of managers. Fligstein (2001) describes the ideology behind these developments as the rise of the shareholder value conception of control and its principal mechanism is an active market for corporate control to constrain managers. Factors such as the rise of institutional investors, the growth of blockholding, and the existence of active-private equity firms are designed to mitigate the free-rider tendencies of dispersed ownership. Acting collectively, these institutional agents are unencumbered by any loyalty to a specific family or company and are able to extract greater value than they had been receiving under the 'unchallenged rule of managerial capitalism' (Useem 1993: 237). Nevertheless, institutional investors also have the potential for agency issues, wherein fund managers make suboptimal decisions for shareholders (Woidtke 2002).

In the past few decades there were attempts to align investor-manager incentives through stock options or similar mechanisms that make a portion of top executive pay contingent upon stock market performance (Hall and Liebman 1998). However, many factors outside of executives' control can influence corporate financial performance (Finkelstein 1992). Thus, a potential cost to executives of being remunerated largely based on performance incentives is that they must assume some downside risk in compensation that is not attributable to their ability or effort levels. These executives also face a serious threat of dismissal if market returns are viewed as unsatisfactory (Walsh and Seward 1990). Attempts to minimize employment risk suggest managers will seek control over their firms' compensation processes and negotiate the structure of their compensation so that vesting and capitalization occur in the near term (Combs and Skill 2003). Executives may also capture value in the form of selectively designed incentive compensation (Porac et al. 1999), or by back-dated grants of stock options (Arya and Sun 2004; Lie 2005). In the U.S. the vast majority of stock-options are cashed on vesting (Blasi et al. 2003). Thus, equity linked executive compensation can also be part of the agency problem itself. For example, managers may divert value to themselves through a variety of mechanisms, such as self-dealing and insider trading (Bebchuk and Jolls 1999), or managers may adopt but not implement the substance of long-term incentive plans by symbolically managing shareholder perceptions and decoupling external and internal processes (Westphal and Zajac 1998). While shareholders possess a legal claim on firm value (they are primary stakeholders), senior executives also achieve primacy due to an authority structure that accords them sufficient power to pursue their interests.

4.1.1 Secondary stakeholders

Because executives wish to access capital on public markets on the most favorable terms, they might find it necessary to accommodate suppliers of financial capital;

the exercise of this imperative often comes at the expense of suppliers and employees. Under managerial governance, secondary stakeholders' outcomes are attained through calculative arm's length contracts' contractual means. Managerially governed firms tend to utilize instrumental pay-for performance systems for employees that heavily weight rewards toward specific behaviors or measurable outcomes, such as hourly pay, piece rates or sales commissions. As a consequence of their arm's length and instrumental orientation, these firms often hire and fire workers with a calculative rationality in response to changes in technology or market conditions (Jacoby and Mitchell 1990). Consequently, they present their employees with significant employment risk without the corresponding upside accorded senior executives (Hoskisson and Turk 1990). Employees are likely to reciprocate their employer's calculative rationality with respect to firm tenure, maintaining employment alternatives and developing generic, occupational and professional skills that increase their value on external labor markets (Waterman et al. 1994).

Intra-stakeholder conflicts between employees are evident under managerial governance where the principle of seniority mitigates some effects of labor market flexibility for employees with long tenure. Seniority is prevalent in the U.K., U.S.A. and Canada, where it is applied in practices related to lay-off, recall and promotions (Post et al. 2002). Seniority backloads rewards for employees who commit themselves to idiosyncratic firm-specific learning. However, seniority effects are most prevalent in declining and hypercompetitive industries such as airlines, where two-tier wage systems are common (Heetderks and Martin 1991). Intra-stakeholder conflicts are also evident between knowledge workers and routine employees. In these circumstances highly skilled and 'star' employees may be offered 'pieces of the action' (Rousseau and Shperling 2004) in the form of stock options as a means of securing their continuing contribution. However, a contractual approach to employees provides managerially governed firms with skilled workers whom they may readily hire and fire. On the other hand, because employees may sell their services to the highest bidder, the prevailing wage for high performers and those offering scarce resources can be significantly higher than in systems where job security and firm tenure is valued more. Hence, employee stakeholder outcomes may rise and fall depending upon the urgency of the demand for their services, but the variability of their outcomes stems from a secondary status in the stakeholder hierarchy (Mitchell et al. 1997).

Equally, the firm-supplier relationship has been the subject of much transaction cost analysis and the competitive advantages of long-term cooperation is a virtue often extolled (Dyer and Singh 1998). Still, managerially governed firms are constrained in their capacity to privilege their supplier relationships. Consequently, the default position in such relations is that suppliers tend to be selected upon considerations of value, price, and functional efficacy at the expense of other considerations (Dyer 1996). Professional managers are accountable to shareholders and it is difficult for them to justify tacit and extra-contractual commitments or partner selection upon relational or intuitive criteria (Mintzberg 1994). Contracts with suppliers, distributors and other partners tend to be formalized, precise and complex to account for foreseeable contingencies (Williamson 1985). Contracts also tend to be discrete and pertain to clearly defined activities over a specified period (Ring and Van de Ven 1992). The precise terms will tend to reflect the relative bargaining power of the parties at a given point in time. The risk of shifting power and the potential for opportunism it creates manifests in a preference for joint ventures structured as autonomous third parties that are governed by clearly designed partnership agreements, carefully allocated property rights, value appropriation rules and clear exit options (Kogut 1988). Indeed, business partners may be considered as tradeable options (Folta and Miller 2002). The potential for opportunism limits firms' commitments to one another and pushes each to seek new buyer/suppliers and to transfer their business if better contractual returns are offered or if partners begin to falter in their performance. Managerial firms have sought to incorporate elements of the relational model into their supply chain management practices, yet a highly calculative rationality prevails (Gereffi 2001).

Creditors, too, possess only a secondary status in managerial governance since they are limited to a contractual stake in the firm. They are exposed to the risk of opportunism, for example through accelerated dividend payment schedules (Williamson 1985). For instance, banks will typically establish long-term contracts that are secured against specific, earmarked assets holding a predictable residual market value (Copeland 1986). Creditors have few rights of participation in managerial corporate governance; indeed, U.S. legal doctrines impose costs on banks for participating in governance through board membership (Krosznera and Strahan 2001). Since creditors are confined to structuring debt contracts, they have little capacity to influence value allocation. Creditors may participate in corporate governance only in circumstances of distress, such as Chapter 11-style reorganizations, where creditors are granted rights to renegotiate contracts with several other stakeholders and where the risk of opportunism is intensified. Generally, shareholder-creditor conflicts are more pronounced under managerial governance than in other corporate governance systems (Renneboog and Szilagyi 2008).

4.2 Stakeholder outcomes under stakeholder governance

Stakeholder governance, like its managerial counterpart, is characterized by the separation of ownership and control, and an extensive use of professional, salaried executives with little or no ownership stake in the firms they manage. However, the agency problem of managerial discretion is constrained by the embedding of executives in the network of relational contracts with a wider constituency of interests. The enduring nature of relational contracting often manifests itself in the cross ownership of patient, non-liquid equity (Dyer 1996). Consequently, executives are less accountable to and somewhat insulated from capital market pressures and their primary focus is on promoting stable and growing business relations between the organization and its key partners (Walsh and Seward 1990). As buyer/suppliers often own each other's shares and have recurring commercial ties, there are multiple means of monitoring and sanctioning top executives who perform their job poorly or who violate relational norms.

Under stakeholder governance, capital and buyer/suppliers contributions are frequently bundled, as partners may supply financial resources to a firm in the form of equity holdings, trade credit, loans and guarantees. In such circumstances, the economic significance of their equity ownership might be less significant than other linkages (Gerlach 1992). A great strength of stakeholder governance is that it facilitates forging enduring ties between suppliers of capital and focal organizations. Central to these ties is the mitigation of oversight from financial markets in exchange for "insider" status within the firm (Berglöf and Perotti 1994). As relations are conditioned by norms and incentives favoring long-term reciprocity, mutual support in the form of inter-temporal smoothing often takes place (Gerlach 1992). For instance, stronger partners may exercise forbearance in leveraging their superior bargaining power and may even prop up faltering buyer/suppliers through loans or favorable contractual provisions because of the credible expectation that these actions will be reciprocated should the need arise (Allen and Gale 2000). In Japan, financial institutions tend to bail-out firms that are part of their keiretsu and there is also an ongoing transfer of profitability from high to low performing firms in these networks (Gedajlovic and Shapiro 1998). Thus, contracting between firms operating under stakeholder governance tends to be much less discrete, formalized, and specific with respect to returns and performance expectations than those found under managerial governance. The underlying labor and managerial contract, at least for core employees, is similarly relational based upon enduring mutual commitment. The emphasis on growth and stability enhances job security, inducing in employees a willingness to invest in companies' specific skills (Hall and Soskice 2001). In return, stakeholder firms are less likely to use individual high-powered incentives, and more likely to use system rewards such as seniority, profit sharing and annual cash bonuses. To the extent that employees view the firm as an institution, they may evoke a normative orientation that encourages identification with the firm. Perceived labor-management goal congruence facilitates commitment to continuous improvement processes and self-directed team designs (Barker 1993). In such a context, incentives rewarding loyalty and dependability are offered in the form of salaries tied to seniority and firm performance, and there is less reliance on pay for performance incentive systems.

4.2.1 Secondary stakeholders

Relational contracting with insider stakeholders promotes goals of growth and stability. However, insider influence attenuates pressures to maximize market value to the detriment of equity investors who are relegated to secondary status. This occurs because the interests of equity investors can significantly diverge from suppliers of finance who are also buyer/suppliers. Contributors of finance, either through credit, equity or loan guarantees who are buyer/suppliers have multiple ways of benefiting from their association with the firm. Arm's length suppliers of capital, on the other hand, have only one (Gedajlovic and Shapiro 2002).

For instance, shareholders-buyer/suppliers may take their benefits in the form of favorable trade arrangements and externalize the cost of those benefits onto arm's length investors. Insiders and buyer/suppliers may redistribute profit by transferring financial resources from more to less profitable firms, thereby depriving arm's length shareholders in high profit firms from maximal return on their investment.

To the extent that arm's length investors perceive this risk, it will be priced into the financial instrument and make raising capital on public markets more costly.

Moreover, commitment to insiders, however, also creates a set of incentives that favors organizational persistence over financial performance and risk aversion over risk taking (Meyer and Zucker 1989). If managers and employees develop firm specific assets, their alternative employment opportunities are reduced and they are likely to prefer organizational survival to high-risk ventures that might threaten the firm's existence. A similar rationale applies to dedicated suppliers or customers who intermesh their value chain with a focal organization. Thus 'the interests of elite owners may be subordinated to the interests of non-elite dependent actors (Meyer and Zucker 1989: 100) and are often sufficiently powerful to offset owners' preference for improved financial performance. In the absence of shareholder incentives, stakeholders tend to rely upon bank financing. However, banks too tend to favor a conservative business stance. As the suppliers of credit to a firm, banks have little incentive to fund high-risk projects. The nature of debt contracts limits their upside to the repayment of the principal and an agreed upon interest payment. On the other hand, if the project fails, they lose their investment. Since banks cannot profit from the upside return of highly successful projects, but bear the full costs of failed projects, bank debt is structurally unsuited to the high-risk uncertainties of lending to start-up firms at the initial stages of a product life cycle (Prowse 1996).

Stakeholder governance provides core employees with incentives to invest in developing deep firm specific skills (Hall and Soskice 2001). In return, core employees are provided with internal rights, such as employment security, career mobility and due process with an internal labor market. However, the establishment of stable internal and labor markets for core employees creates segmenting tendencies for non-core workers. The latter face much poorer working conditions and bear the burden of product market uncertainty. Core employees have little incentive to share the stability they enjoy with non-core employees (Doeringer and Piore 1994). Instead, core employees tend to rationalize and legitimize their positions in terms of superior skill and effort, and institutionalize internal labor markets through collective action (Whittaker 1998). Similarly, while stakeholder governance clearly privileges a core group of first-tier buyer/suppliers, research shows that firms operating under stakeholder governance may also establish a second tier of dependent non-core firms (Kim et al. 2004).

4.3 Stakeholder outcomes under family governance

The global prevalence of concentrated ownership in large, diversified conglomerates and business groups, especially in emerging markets, has produced a 'principal-principal' literature (Young et al. 2008) that highlights the tension between majority and minority investors. On the one hand, because owner-managers exercise both managerial control and a direct claim on the firm's profits, they have a 'high powered' incentive to use resources efficiently (Alchian and Demsetz 1972). There is accumulating evidence to suggest that ownership by a founding entrepreneur who is also the firm CEO is strongly related to firm performance (Amit and Villalonga 2004; Anderson and Reeb 2003). On the other hand, high-powered owner incentives are effective only within a relatively limited range of ownership. Morck and Yeung (2003) suggest that family ownership below 10% provides inadequate incentives for efficiency, and ownership above 20% appears to generate negative performance effects. Negative effects arise from the probability that majority owners may use their control rights to extract private benefits at the expense of minority shareholders. Shleifer and Vishny (1997) argue that the large premiums are associated with superior voting shares and other control rights, and provide evidence that controlling shareholders seek to extract private benefits. Research from emerging markets suggests that the probability of expropriation is particularly high in the absence of enforceable property rights for minority shareholders. There is now substantial evidence that closely held family firms pay an equity premium to compensate arm's-length minority investors for the risk of owner-managers using their control rights to expropriate private benefits at their expense (Claessens et al. 2000; La Porta et al. 1999; Lins and Servaes 2002). To mitigate the equity capital constraint, family firms frequently engage in relational contracting with banks to assure access to growth capital. Long-term relationships with a main bank were instrumental in the emergence of diversified family owned business groups in Asia (Carney and Gedajlovic 2002).

The primary beneficiaries of family governance are the entrepreneur, his/her kin, and a network of selected insiders. The accumulation of private wealth and its transmission to succeeding generations of the family is a primary value in capitalist societies. The primacy of family is reflected in the view that the firm is an instrument of the entrepreneur and his or her family. This is evident in what Chandler (1990) calls personally managed firms that demonstrate a preoccupation with wealth preservation. The focus on wealth preservation tends to be reinforced in succeeding generations wherein heirs to large family fortunes are less likely to fund innovative ventures, entrench their management, and seek to preserve their wealth through political lobbying (Morck et al. 1998).

Kinship is one of several axes of social solidarity (Granovetter 2005) and owner-managers may choose to favor those in their social networks—based on religious, linguistic, political or geographical solidarity—or others with whom they have a sense of affiliation or obligation. The concentration of authority in the hands of family business owners, and their exemption from the checks and balances that are applied to professional managers in stakeholder and managerial governance, provide owner-managers with discretion to decide the social basis of transactions. The consequence is that stakeholder outcomes are likely to be highly particularistic, reflecting the personal and idiosyncratic preferences of the owner-manager (Carney 2005).

In this manner, the radius of trust (Fukuyama 1995) often extends beyond the family into a personal network of close partners who may become an associated category of beneficial stakeholders. Though owner-managers of family firms have a strong incentive to manage costs very tightly, they commonly form preferential business relations with specific customers and suppliers. In this regard, Uzzi (1997) notes that arm's-length transactions are most frequently used by entrepreneurs, but they maintain close or special relations with a narrow range of partners. The comportment of owner-managers with respect to 'ordinary' and 'favored' customers and suppliers varies greatly. For instance, favored suppliers and customers may be offered preferential trade credit and access to goods in short supply (Uzzi 1997). Research on ethnic Chinese family entrepreneurship finds a preference for relational contracting in transactions related to ‘big deals’, extending credit or transferring a business, but most routine transactions are conducted through calculative and arm’s length contracts (Redding 1990).

4.3.1 Secondary stakeholders

Senior-executives, employees, and minority shareholders are a distant second behind family and buyer/suppliers in terms of outcomes. Senior executives in owner-managed firms typically have less discretion relative to managers in firms where there is a separation of ownership and control. Owner-managers have strong incentives to monitor their managerial agents closely, making it difficult for them to divert resources into value destroying activities or by consuming organizational perquisites (Anderson and Reeb 2003). The personalized character of the owner-managed firm constrains its ability to offer high-powered incentives such as stock options to non-family members over concerns related to diluting family control and wealth. Third, non-family executives might face a glass ceiling since top positions are reserved for the children of the founders. Such practices can inject discord and a sense of inequity among the management team and can militate against recruiting and retaining highly qualified external management. In fact, the inability to reward extremely high performance creates self-selection dynamics that may impede a firm’s ability to attract and retain high quality executives. Entrepreneur-controlled firms must compensate professional managers for these deficiencies through increased cash compensation packages. Gomez-Mejia et al. (2003) find that non-family professional CEOs in U.S. family-controlled public firms receive on average four times more income than CEOs who are family members.

Similarly, employees are rarely accorded special standing because parsimony and particularism condition the rewards provided employees in systems of entrepreneurial governance. Since owners-managers appropriate residual returns, they can be exceedingly parsimonious in offering inducements to employees. In this regard, owner-managers can bring an ownership mentality to human resource decisions and often view compensation and benefits as expenses rather than investments. In general, labor costs in family businesses tend to be significantly lower than their non-family counterparts and they report spending less on training and career development programs than other firms do. In sum, relative to other governance systems, family governance privileges owners’ personal wealth and subordinates external capital in a way that creates a characteristic capital constraint. However, released from the constraints of the accountability to arm’s length investors and buyer/suppliers under managerial and stakeholder governance, owner-managers are free to exhibit particular and idiosyncratic tendencies that produce a variety of organizational outcomes. Thus, family firms have simultaneously the highest mortality rates and are among the longest lived organizations spanning several generations (Miller and Breton-Miller 2005).

5 Discussion

Governance systems weigh heavily and systematically in the manner through which stakeholder distributional outcomes are made and sustained. Because governance systems vary in terms of authority and contracting mode, they affect the legitimacy, power, and kinds of tensions stakeholders can expect to meet. Our comparative review of governance systems summarized in Table 2 summarizes some of the intra-stakeholder tensions inherent in each governance system.

While managerial governance highlights shareholder-manager conflicts, other conflicts are also evident under this system. Under stakeholder governance, creditors, suppliers, and employees enjoy a primary stake while arm's length equity investors endure a subordinate position. The expropriation of minority shareholder wealth under family governance has attracted the lion's share of attention; however, its concentration of authority tends to generate idiosyncratic stakeholder tensions. In this respect, and without entering into normative debates, governance viewed from an authority perspective might shed light upon the efficacy of mechanisms available to agents to reorder stakeholder outcomes.

Two mechanisms suggest solutions to this problem: the first approach is to utilize 'market' strategies that either increase the bargaining power of a group or undertake action to reduce dependence on a focal firm by developing alternatives. In many contexts it is given that stakeholders will leverage their relative power to improve their outcomes (Porter 1980). Yet the exercise of bargaining power must be seen as legitimate in the context within which it is wielded. Sustained and illegitimate uses of power, such as attempts to hold-up an organization, will tend to generate countervailing powers (Gelpi 2003). Consequently, norms and conventions tend to develop among frequently transacting parties that form part of the bargaining context (McNeil 1978), which tend to moderate and mediate the exercise of power. Indeed, institutional theorists take it as axiomatic that structures of power and authority are socially constructed and power relations will be context dependent.

Table 2 Comparative corporate governance systems and stakeholder conflict

	Managerial	Stakeholder	Family
Authority structure	Separated ownership Executive control	Separated ownership Insider control	Concentrated ownership Insider control
Contracting mode	Arm's length	Relational	Arm's length & relational
Inter-stakeholder conflict	Equity investors vs. professional executives Equity investors vs. employees	Equity investors vs. insider stakeholders	Family vs. outsiders
Intra-stakeholder conflict	Knowledge vs. routine employees Senior vs. junior employees Creditors vs. equity investors	Creditors vs. equity investors Core vs. noncore employees Core vs. noncore buyer/suppliers	Majority vs. minority equity investors Family vs. professional executives Arm's length vs. relational buyer/suppliers

A second approach is to advance stakeholder interests collectively by seeking to influence the policy and legislative agenda and to encourage the state to develop legal protection for the rights of unprotected groups. This approach implies sustained processes of institutional entrepreneurship (Granovetter 2005) that require advocacy and legitimization of alternative models of firm governance and managerial practice.

In this paper, we have not been particularly concerned with the wealth-generating effects of different governance systems. Advocates of the stakeholder model of corporate governance claim that zero sum contests can be converted into positive sum games due to the competitive advantages of more inclusive and egalitarian stakeholder management. Because it mitigates the demands of capital and labor markets, stakeholder governance has attracted much attention. What is often advocated is the adoption of a stewardship approach in which managers are charged with a fiduciary responsibility to serve as a neutral coordinator of the contributions and returns of all stakeholders in the firm, while promoting its overall wellbeing. Such advocacy is well meaning, but overlooks the primacy and hierarchical nature of stakeholder claims in managerial governance. For example, Kochan and Rubenstein (2000) lament the failure of General Motors management to transfer high productivity cooperative labor management practices that were pioneered in a joint venture with Toyota and refined in the Saturn division into other divisions. This was due to multiple organizational conflicts and the absence of a strong legal foundation for stakeholder management. Pfeffer (1991) too vents frustration at American managers for their resistance to employee incentives, such as profit sharing, employee stock ownership and knowledge-based pay, despite accumulating evidence of their positive contribution to firm performance.

Successful management practices that thrive in stakeholder governance systems are not easily accommodated without substantial modification in managerially-governed firms (Gooderham et al. 1999). Advocates of the stakeholder management model underestimate the historical origins of this governance system and the requirements for a complex institutional and legal architecture needed to support the model. The courts too have found it difficult to formulate and enforce 'fiduciary duties of sufficient refinement to assure that managers behave more efficiently and fairly' (Hansmann and Kraakman 2004). Stakeholder models in favor of better employee outcomes seem to flounder on the diversity of employee interests, and the development of a unitary bargaining position seems elusive.

6 Conclusion

We propose that firms are arenas for conflict among rival stakeholders. While much literature has focused upon the conflict between executives and the owners and stewards of capital and between executives and employees, we have assembled and reviewed a disparate literature that directly and indirectly identifies numerous intra-stakeholder conflicts. Our intended contribution is to review governance conflicts from an authority perspective in a manner that reveals many intra-stakeholder conflicts as inherent within particular governance systems. Governance viewed in this way sheds light on a divergent shareholder value and stakeholder management literature, which have largely ceased to inform one another. The implications of our view suggest no easy solutions for the myriad of conflicts found in various systems of governance, but we believe that stakeholder conflict viewed from this perspective may put future research on a firmer footing.

While some scholars argue for a corporate governance convergence thesis that suggests that "the triumph of the shareholder-oriented model of the corporation over its principal competitors is now assured" (Hansmann and Kraakman 2004: 67), we are unconvinced and point to a growing literature suggesting continuing divergence in systems of governance around the world (Guillen 2001; Hollingsworth 1997; Khanna et al. 2003; Whitley 1999). Consequently, understanding cross-national differences in distributional outcomes among and between stakeholder groups is likely to remain a continuing focus for governance research. Moreover, as the varieties of capitalism literature has established (Boyer 2005; Carney et al. 2009), there is, within any particular nation state, a plurality of institutional architectures that will support a diverse array of governance and organizational forms. We hope and suggest that stakeholder differences can be better appreciated through the authority-based perspective outlined this paper.

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