How large companies can make shareholders happy

The Age.com
By James McConvill
December 22, 2005

Next year can be the year of the happy shareholder, with or without a dividend cheque, argues James McConvill.

The annual reporting season of publicly held companies is just about at an end. This, combined with the impending close of business for the holiday season, provides an excellent opportunity to think about the corporate governance practices of Australia's public companies.

Corporate governance is not just of academic interest. It is a topic that more and more Australians are considering. According to the Australian Stock Exchange's Share Ownership Survey 2004, 55 per cent of adult Australians now own shares either directly or indirectly (through a managed fund or self-managed superannuation fund).

A major corporate governance issue at present concerns the allocation of power between shareholders and company officers in large public companies, and whether the power of shareholders should be increased. Traditionally, officers have assumed the bulk of power, and are responsible for almost all the decisions affecting the company. Given that these companies have a large number of shareholders, it is considered rational for shareholders to remain passive-collecting the dividend cheques and occasionally signing off on decisions (via the annual general meeting) already made.

A very interesting point regarding the specific issue of shareholder empowerment is that both the proponents and opponents of empowerment are approaching the issue in the same way. Somewhat counter-intuitively, their harmony in approach could be the primary cause of conflicting views. Both opponents and proponents of shareholder empowerment view shareholder governance rights as being a means to an end, rather than an end in itself. The "end" which connects both proponents and opponents in their analysis is maximising company performance — making the company as healthy as possible in governance terms to achieve more profits.

Indeed, the chief proponent of shareholder empowerment, Harvard law professor Lucian Bebchuk, has conceded as much. In an article published in the *Harvard Law Review* earlier this year, Bebchuk commented that: "I do not view increasing shareholder power as an end in and of itself. Rather, effective corporate governance, which enhances shareholder and firm value, is the objective underlying my analysis."
In my view, shareholder empowerment could generate consensus, rather than what seems at present to be inevitable conflict, if we did consider increasing shareholder power to be an end in and of itself.

The annual reporting season of publicly held companies is just about at an end. This, combined with the impending close of business for the holiday season, provides an excellent opportunity to think about the corporate governance practices of Australia's public companies.
Corporate governance is not just of academic interest. It is a topic that more and more Australians are considering. According to the Australian Stock Exchange's Share Ownership Survey 2004, 55 per cent of adult Australians now own shares either directly or indirectly (through a managed fund or self-managed superannuation fund).

A major corporate governance issue at present concerns the allocation of power between shareholders and company officers in large public companies, and whether the power of shareholders should be increased. Traditionally, officers have assumed the bulk of power, and are responsible for almost all the decisions affecting the company. Given that these companies have a large number of shareholders, it is considered rational for shareholders to remain passive-collecting the dividend cheques and occasionally signing off on decisions (via the annual general meeting) already made.

A very interesting point regarding the specific issue of shareholder empowerment is that both the proponents and opponents of empowerment are approaching the issue in the same way. Somewhat counter-intuitively, their harmony in approach could be the primary cause of conflicting views. Both opponents and proponents of shareholder empowerment view shareholder governance rights as being a means to an end, rather than an end in itself. The "end" which connects both proponents and opponents in their analysis is maximizing company performance — making the company as healthy as possible in governance terms to achieve more profits.

Indeed, the chief proponent of shareholder empowerment, Harvard law professor Lucian Bebchuk, has conceded as much. In an article published in the *Harvard Law Review* earlier this year, Bebchuk commented that: "I do not view increasing shareholder power as an end in and of itself. Rather, effective corporate governance, which enhances shareholder and firm value, is the objective underlying my analysis."

In my view, shareholder empowerment could generate consensus, rather than what seems at present to be inevitable conflict, if we did consider increasing shareholder power to be an end in and of itself.

The end game would be shareholder empowerment because the recipients of this power, shareholders, would be inherently happier for the very reason of having the power, not because of any consequential benefits to the corporation.

Since the days of Aristotle, it has been recognized that happiness is the ultimate objective of human beings, and the underlying reason for our actions. But happiness as a concept has been considered too vague and indeterminate to shape the way we live and are governed. This, however, is changing. Empirical studies now tell us with a fair degree of precision what does and does not contribute to happiness.

One of the common ingredients to happiness is participation. For example, a study by psychologist Judith Rodin found that by encouraging nursing home patients to contribute more to the policies determining their environment in the home, 93 per cent of patients became more active, alert and happy.

Another important study by psychologists Leaf Van Boven and Thomas Gilovich, *To Do or to Have? That is the Question?*, found that (1) those interviewed experienced more positive feelings after pondering an "experiential" purchase (purchases that involve some kind of active component which people engage in to generate a life experience) than after pondering a "material" purchase (those that involve buying tangible objects such as television, cars and jewellery) and (2) the interviewees indicated that they were more likely to anticipate that experiences would make them happier than material purchases after adopting a temporally distant, versus a temporally proximate, perspective.

Applying these studies to shareholder empowerment, it is misguided not to respect increasing shareholder power as an end in itself. Greater empowerment, beyond the formality of the annual general meeting, could be achieved through having a separate board with shareholder representatives (as occurs in Germany), regular meetings between company management and shareholders (as occurs in Japan), or through company shareholder committees designed to improve communication channels between officers and shareholders (as in the US).
If participation is a key factor contributing to individual happiness, and the pursuit of happiness is the natural underlying objective of all human beings, then participation rather passivity becomes the rational choice. Even if active involvement in the company seems less desirable at the time than kicking back and collecting the dividend cheque, the study of Van Boven and Gilovich highlights that when looking back on the decision we made we are likely to be happier by following the participation path.

Participation will, of course, not appeal to all shareholders. Many shareholders may simply not have the time or the inclination to get involved. But this should not form the basis for preventing other shareholders who want, or are encouraged, to get involved, doing so.
James McConvill is principal of the Corporate Research Group, and a senior lecturer at La Trobe Law School, Melbourne.