An introduction to:
Stakeholders and Shareholders

Corporations interact with and affect many "stakeholders," both internally and externally – employees, customers, regulators, etc. Among these stakeholders, owners or "shareholders" are often seen to be the "primary" stakeholder, whose needs for financial returns ultimately outweigh the needs of any others. While attractive in its simplicity, this perspective has been challenged by the idea that companies must consider other stakeholders' needs too.

What is at stake in this debate, and how does it relate to corporate sustainability or responsibility?

What is a "stakeholder"?

Stakeholders are people or groups that are directly or indirectly affected by an organization's policies and actions. They include internal stakeholders (such as employees, customers and shareholders) or external stakeholders (such as the general public, activist groups and communities).

From Freeman, R. E. (1984). *Strategic Management: A Stakeholder Approach*. Boston: Pitman.

What is a "shareholder"?

Shareholders (also called "stockholders") are a corporations' owners who invest in a company in the expectation that their investments will grow in value over time. Shareholders have a range of rights, including rights to transparency, the right to vote on major decisions, and the right to receive dividends, or proceeds from any sale. Although there are a number of variations (stage of ownership, type or class of stock, etc.), typically, the more stock owned by a shareholder, the greater is their ability to influence the policies, programs and business investments of the company they're invested in.

What is the "Friedman Doctrine"?

In 1970, American economist Milton Friedman famously argued that companies' only real stakeholders are its shareholders. To Friedman (and many economists), corporation owners hire executives to act and operate the company. Thus, owners are the "principals" and executives their "agents." As agents, executives' first and only objective is to increase the value of the principal's shares. According to Friedman: "there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game."

This conception of business remains widely held among economists and business people alike.

What are the limitations of this "doctrine"?

Critics of the Friedman Doctrine claim that this approach causes businesses to deprioritize (or even ignore) its responsibilities to other stakeholders, in effect, achieving the shareholders' main objective (the growth of their investments) at the expense of others. For example, a company might run a healthy profit but pay employees relatively poorly, or pollute in the communities in which it operates, or pay low prices to suppliers. While these effects are bound to some degree by laws and regulations, in general, the more a company tries to generate returns for shareholders without sufficient attention to the needs of other stakeholders, the more likely it is to be criticized, subjected to negative media or government attention, face public backlash, and other challenges to its "licence to operate."

What is "stakeholder theory"?

Stakeholder theory is a framework that describes a business's obligation to create value for a range of stakeholders, not simply its shareholders. It promotes the idea that businesses must look beyond the "bottom line" and examine how their decisions may impact their stakeholders. This may mean trade-offs in its returns to investors, but ultimately can lead to a more sustainable business with fewer risks and more satisfied group of stakeholders.

In order to create this value, the business must work to ensure that a business interests are aligned with its key stakeholders. While the salience and influence of stakeholders may differ from company to company, each must optimize the value it creates for its most important stakeholders, such as its customers, employees, shareholders, suppliers, and the communities it operates in.

Stakeholder theory has become one of the foundations of corporate social responsibility and sustainability. It is most often associated with the work of business professor R. Edward Freedman, although others have written parallel ideas or developed the concept further. In Canada, business professor Max Clarkson developed *The Principles of Stakeholder Management* to guide Canada's largest companies.

Critics of this theory point out that it is much more complex than the Friedman Doctrine because simultaneous optimization against several objectives is hard to achieve in practice. It can also takes far more time and validate some stakeholders whose claims may be less salient than others.

About this series

This series presents brief introductions to new and ongoing issues in sustainability for business audiences. It is not intended to be used as business or investment advice.

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