

The Corporation in Society

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Fundamental Questions:

- As a corporate board member, to whom are you responsible?
- Is the corporation an institution to be developed to serve society?

Or:

- A collection of assets organized to maximize returns to investors?
- If the latter, what is the appropriate time frame over which to measure returns?

The Corporation in Society

- Limited liability corporations are chartered by society, as represented by government officials.
- Corporations have the ultimate obligation to serve society by creating lasting value.
- Violations of that charter result in:
 - Revocation of their charter (e.g., Arthur Anderson, Nationalization in France; Google in China)
 - Regulations and laws limiting its freedom to operate (e.g., Dodd-Frank, Minder Law in CH)

The Evolution of Capitalism

Society is demanding a new form of capitalism that benefits *all* stakeholders

From:

Entrepreneurial Capitalism

Managerial Capitalism


Financial Capitalism

To:

Shared Value Capitalism

When stakeholder interests get out of balance, capitalism is at risk of self-destruction, as in 2002 & 2008 and 201?

Capitalism Is Facing Imperative For Renewal

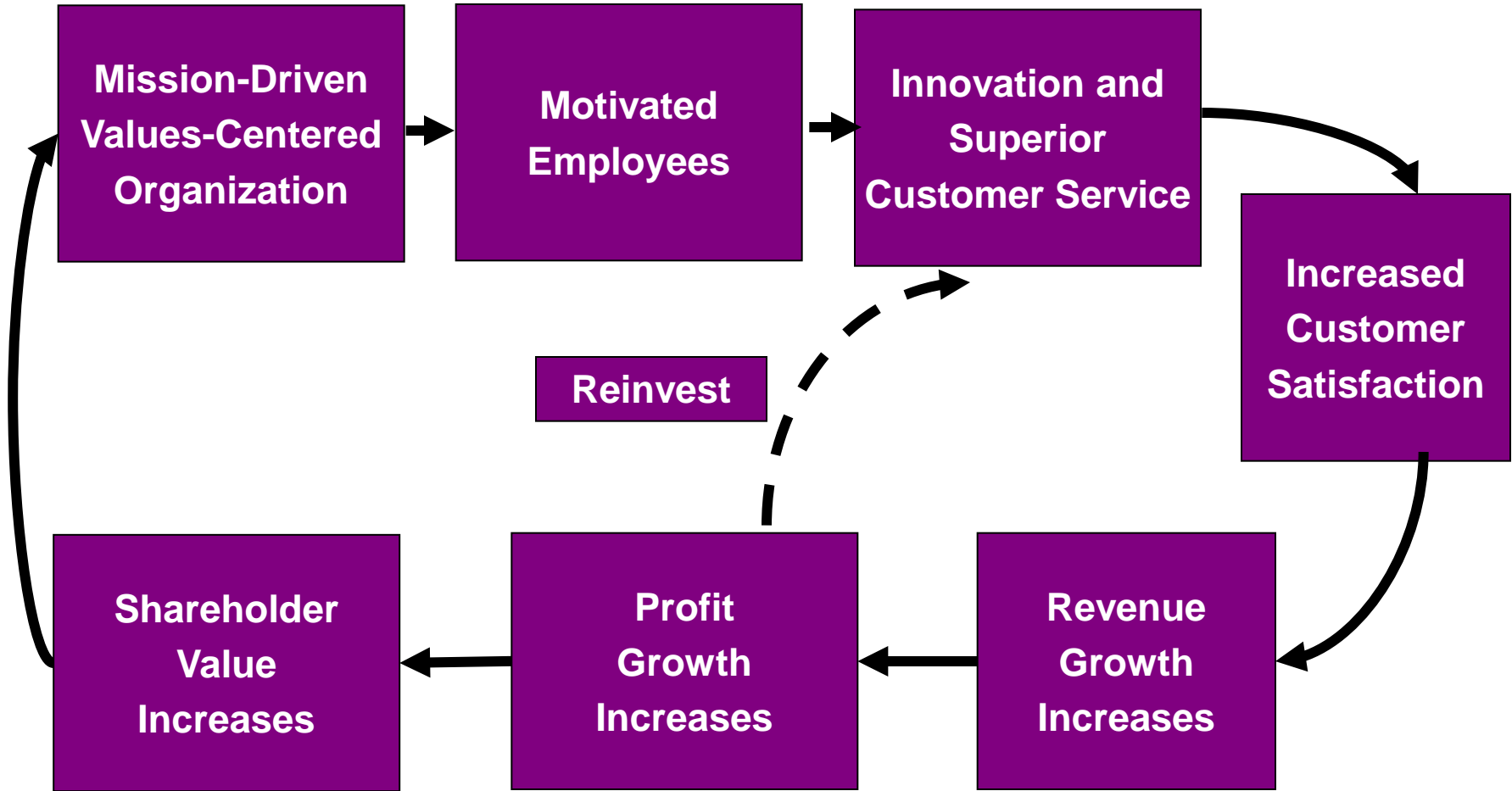
	Entrepreneurial Capitalism	Managerial Capitalism	Financial Capitalism	Shared Value Capitalism
Model Leader	JJ Astor	Alfred Sloan	Carl Icahn	Paul Polman
Failure	<ul style="list-style-type: none"> Doesn't scale No creation of opportunity beyond Founder 	<ul style="list-style-type: none"> Gets too bloated Management complacency 	<ul style="list-style-type: none"> Alienates the 99% Overleverage with Lehman, Bear Stearns 	 <p>New Phase</p>
Drivers	<ul style="list-style-type: none"> Property rights <ul style="list-style-type: none"> US Constitution Land grants 	<ul style="list-style-type: none"> Innovation in corporate organization Business Schools Adoption of technology 	<ul style="list-style-type: none"> Junk bonds Hedge Funds <ul style="list-style-type: none"> Activist Investors Management complacency/ Self-interest 	<ul style="list-style-type: none"> Financial crisis Millennial focus on Mission Globalization
Era	1800 - 1940s	1920s - 1980	1975 - 2014	2009 - present

Creating “Shared Value”*

- The ultimate goal for global companies is to sustain success by creating value for *all* its stakeholders
- This includes:
 - Clients, customers & beneficiaries
 - Employees
 - Owners and investors
 - Local government & communities
 - NGOs with stake in organizations

*The idea of “Creating Shared Value” was first proposed by HBS Professor Michael Porter in [HBR](#), January 2011.

Sustaining Growth and Performance



Stakeholders in Society

With societal expectations for companies rising and trust declining, should companies shift from considering local governments and communities as *their* stakeholders to becoming:

“Stakeholders in Society”*

This notion dovetails with Prof. Porter’s ideas on “Creating shared value,” i.e., companies should look at their mainstream business as contributing to societies all over the world.

*This idea was proposed by Prof. Klaus Schwab of the World Economic Forum at Harvard Kennedy School on March 27, 2014.

Challenges to Board Governance

Are external challenges to board governance strengthening or weakening the board's ability to govern the corporation and provide effective oversight of management?

Examples for discussion:

- Elimination of staggered boards
- Direct nomination of directors
- Majority and cumulative voting
- Say on pay
- ISS and Glass –Lewis

Board Leadership

Which leadership model is preferable?

- Independent board chair; CEO not on board
- Independent board chair; CEO on board
- Chair & CEO, with independent lead director

Board Time Management

How should boards allocate their time?

- Financial results and projections
- Updates on current events
- Strategy and long-range planning
- Succession planning and organization changes
- Risk management
- Audit reviews
- Legal and regulatory reviews
- Public responsibility and serving society
- Open discussions with management

Activist Challenges

- What is the appropriate role of activist investors demanding changes in strategy or financial structure to produce near-term value accretion?
- Examples:
 - PepsiCo
 - eBay
 - P&G
 - Target
 - Allergan
 - JC Penney
 - DuPont
 - Kraft

“I believe in running the company for shareholders that are going to stay, rather than ones that are going to leave.”

- Warren Buffett, Oct 16, 2013

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Case Study: Battle for Allergan

Valeant making hostile bid for Allergan, cutting R&D from 17% to 3% and tax rate from 34% to 3%. Has raised its offer five times from \$150/share to \$200.

AGN increased shareholder value 10X in 15 years, and performing well. (+187% in 1 yr. vs. +18% for Valeant)

Proxy vote scheduled for Dec. 2014.

<u>Allergan P&L:</u>		<u>Stand-alone</u>		<u>Merge w/ Valeant</u>
Revenues		\$10.0 B		\$10.0B
R&D	17%	1.7	3%	0.3
Other X	53%	5.3	53%	5.3
Oper Profit	30%	3.0	44%	4.4
Tax	34%	<u>1.0</u>	3%	<u>0.1</u>
Net Income	20%	2.0	43%	4.3

Dealing with Activist Shareholders

1. Have clear strategic focus and stick to it
2. Analyze your business as an activist would
3. Have your external advisors lined up in advance
4. Build board chemistry by being transparent with board about challenges and vulnerabilities
5. Perform near-term against stated goals
6. Don't dismiss activist's ideas out of hand

Nobel Peace Prize Albert Schweitzer

“I don't know what your destiny will be, but one thing I do know:

The only ones among you who will be really happy are those who have sought and found how to serve”