Finding Hard Evidences for the Soft Rhetoric of the Stakeholder Theory

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The hard-science type of rhetoric present in the dominant model in management is put under scrutiny. As a result, the shareholders' profit maximization ideal is understood as just a competing socially constructed rhetoric. We are motivated by: 1. why is it taken for granted that the dominant model of business activity is scientific? and, 2. How the competing stakeholder approach would look like? We present mathematical equations that capture other constructs (e.g. women and employee participation, CSR, CER) and propose a stakeholder index (GOV-Icompr). Results indicate that companies that include other stakeholders have superior market value (measured by Tobin's q).

"In the end, a theory is accepted not because it is confirmed by conventional empirical tests, but because researchers persuade one another that the theory is correct and relevant"
(In Noise, by Fisher Black, 1986)

INTRODUCTION

The paper has both, theoretical and empirical contributions. It is motivated by two questions: 1. why is it taken for granted that the dominant model of business activity is scientific, hard-science like? 2. How the competing stakeholder approach would look like in order to be perceived similarly? and, one application: to build a new framework for our studies on corporate governance sustained by a coherent narrative and mathematical equations. The first part of the paper addresses the dynamic of the narrative construction that supports the supposedly hard-science nature to management sciences. The hard science type of narrative is put under scrutiny and, as a result, the second part of the paper shows the evolving and constructed nature of the social reality and the resultant need for management science to be aware of this social nature and to understand its role in changing this flexible reality. The paper proposes a broader approach to corporate governance (i.e., a comprehensive governance index or a stakeholder approach index) that follows some topics found in contemporary narratives we consider evolutionary for the business world. Finally, we present mathematical equations that allow us to capture the new constructs of the organizational reality and test them empirically.

Part One

Noam Chomsky (2007, p. 4) recognizes with certain cynicism that "Rhetoric is always uplifting, and we are enjoined to admire the sincerity of those who produce it…", nevertheless, it is always appropriate to compare what the narrative promises to its actual consequences. Covert intentions and resultant consequences may be threatening to society. Adam Smith already recognized in the eighteenth century the undisclosed real interest of narratives. “All for ourselves, and nothing for other people, seems, in every age of the world, to have been the vile maxim of the masters of mankind” recognizes Smith (1996(1776), p. 448). The admired “dominant model of business activity”, as its critics like Freeman and Reed (Freeman, 1994; Freeman & Reed, 1983) label it, presents a narrative which sustains that business are to be managed for the benefit of shareholders who will pay taxes and reinvest the profits throughout society. One of the dominant model main proponents, Milton Friedman, pleases a particular audience, the financiers (or shareholders) as the engine of economics and business. Whatever name these “masters of mankind” are called today (e.g. aristocracy, bourgeoisie, ruling class, global oligarchy, plutocrats, elite, the 1%), they seem to find with ease sympathetic speakers who disregard in their narratives the needed analysis of the legitimacy of their power. Gratefully the dominant class recognizes the efforts of those who advocates in their favor paying them back through artifacts of social status, a reciprocal reinforcement. In the case of Friedman, it is hard for one to find arguments that contradicts, for instance, a professor from a prestigious university who advises chiefs of State regarding policies in Economics and who is awarded with, the ultimate reputation builder, a Nobel Prize. The similarity about this scheme goes further in time. Sophists and rhetoricians were hired by kings in ancient Greece to advocate in their favor. Socrates, Plato and Aristotle were, on the other hand, keen in confronting the relativist logic and manipulative effect on people. Aristotle actually establishes criterion for the good use of rhetoric (Reynolds, 1993).

The dominant model’s narrative is elaborated by prestigious people, being it because they were prestigious before elaborating the narrative or because they became prestigious after constructing it. In Aristotle’s definition, the narrator and/or the problem has an ethos, that is, character or prestige. Besides the narrator, the audience addressed must be clear. In the case of the dominant model the audience is, besides the “masters of the humankind”, amplified by the promise made to a larger collective that if they submit to the ideal, they will be rewarded and become a member of this select group. Add this promise to the “love of distinction, so natural to man…” as Smith writes in his “theory of moral sentiments”, or to the propensity for emulation, for invidious comparison, as Thorstein Veblen describes to be a pervading trait of human nature, which leads lower social classes to constantly attempt to achieve the next upper social layer (Kempf, 2008, p. 61), or to Maslow et al.’s explanation about the relationship between group values and what the individual is capable of doing in order to be accept (Maslow, Stephens, Heil, & Bennis, 1998), and one can interpret how broadly convincing the dominant model can be. The path towards these goals (i.e., to accumulate wealth, become prestigious and eventually distribute it) is hidden in the narrative but supposes obedience to the *status quo*. In business environments, one accepts the fact that today the salary of top executives can be hundreds of times the average salary of the company and dreams with the chance to achieve a promised treat. Therefore, few are left behind, the unemployed and the sub-employed labeled as ‘non-hard-workers’, a situation made acceptable by the artificial creation of the dichotomist and inappropriate ‘winners versus losers’ culture. Aristotle would call this the ability to address the pathos, or the aimed audience, in that case the real receiver of the benefits or the eventual receiver, the dreamer of a “better” life. Ethos and pathos are set into a tacit contract of what the audience desires to hear and the narrators deliver. Milton Friedman (1970, p. n/a) pleased the shareholders in several narratives, for example, “…I can express admiration for those individual proprietors or owners of closely held corporations or shareholders of more broadly held corporations who disdain such tactics [i.e., the argument in favor of the corporate social responsibility] as approaching fraud”.

The final test for a good construction of rhetoric is the assessment of its logic, the logos in Aristotelian terms, and, here, is where we find many flaws. The context in which this logic was created is: University of Chicago’s new reading about the Classic Macro-Economic theory. When stepping through the doors of its Social Science building, one can read a sign with its metaphorical orientation established in the 50s that states: “Science Is Measurement”. As Klein (2007, pp. 57, 58) summarizes with precision: “The core of such sacred Chicago teachings was that the economic forces of supply, demand, inflation and unemployment were like forces of nature, fixed and unchanging […] these forces existed in perfect equilibrium, […] according to Friedman's strict theory of monetarism, invariably because misguided policy makers had allowed too much money to enter the system, rather than letting the market finds its balance. Just as eco-systems self-regulate…"

To us, the Chicago school represents one of the best attempts to transform management sciences into hard sciences, however, failing to do so. Free-market capitalism works as a recipe to all deceases and is created and fostered, if not imposed, by those institutions that preach the fundamentalism of the market. The International Monetary Fund, for instance, spreads the formula internationally by refusing to "help" economies that are not liberalized. The liberalization means mainly the suppression of governmental interferences in capital and financial markets (i.e., no regulations), privatization of public owned companies, and pulling down trade barriers (i.e., import tariffs). The rationale of the Fund is simplistic: the free markets are more efficient and the greater efficiency would be translated into more development; more development would attract foreign capital, in special, direct investment (Stiglitz, 2002).

Economics translated into Physics, more specifically Astronomy and Biology, seemed a very convincing ideal. People, through governments, would spoil the perfect system. The resultant political narrative is also catching: "Less taxes and less government" means more money in "your pocket" to spend and thus heat up the economy. The perception is that suddenly the ordinary person becomes a shareholder who allocates resources to the economy. However, galaxies do collide and social systems, different from eco-systems, do not encompass negative feedback mechanisms, as Konrad Lorenz argues (1973). Besides, a moribund government, paraphrasing Thomas Hobbes (2004(1651)), is incapable of stopping the ones with sharp swords to take advantage of the ones without any sword. These metaphors seem to shape the anatomy of the brain of the believers to the point that when facts are presented to these ultra-laissez-faire advocates, like the 2008 financial systems' debacle of deregulated economies such as Iceland, United States or Ireland, they insist that these governments were in fact excessively intrusive. How could one argue against them? Yet, the critics go beyond confronting free-market capitalism's basic assumptions and relating them with unintended consequences. Not only a social inequality is a resultant, but also a environmental constraint. Kempf (2008, p. 62) referring to Veblen's first original insight observes that "the needs are [in fact] not infinite. Above a certain level, it's the social context that stimulates them. In the same way, he [Veblen] did not consider production to be scarce but postulated that it is adequate." The argument thus highlights a contradiction, namely, the attempt to supply unlimited needs (i.e., the Classical economics rationale), speeds the use of limited resources or, in other words, it increases the planet's degradation, a consequence out of the dominant model's equation.

A harmonic laissez-faire system held by self-balanced forces does not need to be regulated by governments. Nevertheless, the social actors most likely to act in favor of such self-balance are the shareholders who by acting on their own interests would help to serve the society. Such idea, is a misinterpretation of the quote by Adam Smith in the "An inquiry into the nature and causes of the wealth of nations", which suggests that it is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own self-interest. The problem is that evidence suggests the opposite. Only five years after Milton Friedman wrote "The social responsibility of business is to increase its profits", an article in which the role of shareholders is inflated, the trend observed between 1945 and 1975 in which a unit gained in productivity would represent a unit increased in purchase power just stagnated. This reversion of an assumed "everybody wins" ideal results in a situation that in the United States by the 2000s the average income of the top 1 percent of the active population was 189 times that of the bottom 20 percent. With few exceptions in the world, the middle class is severely shrinking. Efforts in favor a distributive justice, like John Rawls' theory, are failing in the developed countries, which are facing third world challenges. Conversely, the masters of mankind's fortunes are untouched and growing.

The logical fallacies are several. At first, the free-market theory is not taken as a hypothesis, but as an ideal close to a religious revealed-truth, thus there is no compromise with reality tests. As Klein explains (2007, p. 57), "Frank Knight, one of the founders of the Chicago School of economics, thought professors should 'inculcate' in their students the belief that each economic theory is 'a sacred feature of systems' not a debatable hypothesis", or an experiment to be tested, rejected or advanced. Secondly, in the event of being tested, the theory neglects undesirable outcomes: the externalities. Externality could be understood as an effect of a private purchase or use decision by one set of social actors on others, and on the public space, who did not have a choice and whose interests were not considered. Besides social inequality, pollution, poverty, overpopulation, and the finite characteristic of resources are some externalities that markets do not seem to be able to take care of or worry about. Yet, we would like to focus on a special one: the intentions of the narrators. This third logical flaw consists in the incapacity of the theory to assume the contradictory incorporating it on its implementation and/or development. If interpreted, the intentions behind the actions could in fact explain both the failure of the theory's implementation, and the possibility of its creative improvement. In that sense, the intentions of the narrators must be submitted to the theory, which is incorrectly assumed to be perfect by nature. Divergent narratives with the sacred, like the existence of externalities, should be exposed. As Adam Smith (2010(1759), p. 42) expresses: "The man of system, on the contrary, is apt to be very wise in his own conceit; and is often so enamored with the supposed beauty of his own ideal plan of government, that he cannot suffer the smallest deviation from any part of it[…] He seems to imagine that he can arrange the different members of a great society with as much ease as the hand arranges the different pieces upon a chess-board. He does not consider that the pieces upon the chess-board have no other principle of motion besides that which the hand impresses upon them; but that, in the great chess-board of human society, every single piece has a principle of motion of its own, altogether different from that which the legislature might choose to impress upon it."

The person of system, thus, becomes despotic when he or she is 'forcing' laissez-faire. In the 80s, the neo-liberal doctrine was imposed by Ronald Reagan in the United States and Margaret Thatcher in the United Kingdom. In the 90's and 2000s, Bill Clinton and George W. Bush deregulate even further the USA economy. But, the have-nots were requested to aid the market through stimulus packages and bailouts known as the Emergency Economic Stabilization Act of 2008. The "others" like the have-nots, middle class unions, some public servants, consumer protection institutions did not have a choice and their interests were not taken into account. Besides, the free-market theory did not take into consideration the creative and fraudulent accounting, lobbing industry, the tax evasions that were left unaudited. The democratic debate is reinterpreted as an authorization to the elected government to follow donors' interests like minimize the state bureaucracy instead of supervising a democratically created social contract.

If there is any hope, we place the possibility of deconstructing the supportive narratives behind the dominant model, then, observe the new narratives based on meaningful discrepancies coming from different narrators who might argue differently about the path to the goal but are all coincident with the goal itself.

Part Two

In part one, we concentrated our efforts in deconstructing the assumptions and logic which support the dominant model narrative. The exposition of the procedure of deconstruction is one way to confront the *status quo*. In this part, the paper explains the reasons why management "hard" science narratives can be put under scrutiny, or deconstruction.

We start by discussing the nature of phenomena related to management. The first hint on this matter is the work of Thomas S. Kuhn in the sociology of science presented at book "The structure of scientific revolutions", in which the author states: "…and it remains an open question what parts of social science have yet acquired such paradigms at all" (1996, p. 15). Although the "hard" management scientist might argue the contrary, we believe in a different epistemology: management phenomena should be studied as social phenomena, or subjective reality. One of the reasons for that is similarity of its developmental stage with established social sciences. The present stage of discovery, that is, the premature stage, resembles the same problems faced by social sciences like History or Sociology. In other words, a scientific model in management science, which in order to receive the status of paradigm must include "law, theory, application, and instrumentation together" (Kuhn, 1996, p. 10) is missing. Thus, as Kuhn explains, "[in] the absence of a paradigm or some candidate for paradigm, all of the facts that could possibly pertain to the development of a given science are likely to seem equally relevant" (1996, p. 15).

Another fundamental reason is that theories supposedly constructed to represent realities in Economics and Management can be distorted. Joseph Stiglitz provides a remarkable illustration. The also Nobel Prize in Economics explains that "The French intellectual Pierre Bourdieu has written about the need for politicians to behave more like scholars and to engage in scientific debate, based on hard facts and evidences. Regrettably, the opposite happens too often, when academics involved in making policy recommendations become politicized and start to bend the evidence to fit the ideas of those in charge" (2002, p. x). Our conclusions from that statement are three: the first is the hope that "hard facts and evidences" in Economics exist, we mean by 'hope' the fact that if decisions in Economics involve values, one may argue that although facts may be treated as 'hard' evidence, they were still influenced by contextual beliefs and intentions; accordingly, the second point is that even if they exist, facts would serve to open debates for theory validation instead of establishing laws and courses of actions based only on its face value; and, point three, academics can perceive the reality differently from each other and, thus, apply theory in a different ways.

To apply straightly the Popperian rationale of hypothesis stating and testing and then recommend applications becomes in management, senseless. In fact, according to (Popper, 2014) the complicate debate about values belongs to the territory of Philosophy not science. In that sense, if our claim that Management is social, not natural, it must be opened to the philosophical debate.

The attempt to operate hard-science-like supposes that the hypothesis' statement must be made within a framework, or a paradigm candidate, and the instrumentation to test it is constructed within the framework. As Jurgen Habermas (1972) describes, in the "empirical-analytical sciences" point of view, prognosis is permitted because hypotheses can be interpreted as statements about the correlation of observable magnitudes, starting from initially given conditions. Moreover, for a matter of intellectual honesty, the researcher must highlight that the conditions of the context must be fixed for the hypothesis not to be rejected. Habermas (1972) states these limits by explaining that the "meaning of the prognoses", that is, the possibility of their technical use, is deduced from the rules depending on which theories are applied to reality. Therefore, the act of stating a hypothesis to be tested is already biased by a theory, which is per se biased by the context in which it was formulated. We doubt thus the claim about the agnostic approach to the data (i.e., the kind of assumption: "Let the data tell you the story") because from the begging both the hypothesis and the measurement were constructed within the framework bias. The capacity of the detached social researcher to capture the "reality out there" is much more limited than one may consider.

This rationale brings to our awareness the fact that the narrative present in the hard management science discourse can be, if not misleading, at least imprecise. Fisher Black, discussing a management issue (i.e., the incoherence of a 'certainty': increasing stock value due to increasing dividends payment whereas the present value of future dividends may have gone down) states: "Correlations among economic and financial variables do give us some information of value. Experimental studies in economics and finance have value. Analysis of 'stylized facts' is often useful. Unusual events can provide special insight. In the end, a theory is accepted not because it is confirmed by conventional empirical tests, but because researchers persuade one another that the theory is correct and relevant" (Black, 1986, p. 537); persuasion from the ethos, logos and pathos which delineates the theory. Fisher Black, in fact, builds his conclusion on and gives credit for McCloskey's seminal paper "The rhetoric of Economics" (i.e., McCloskey, 1983), an important epistemological discussion about the social constructed aspect Economics science.

For Popper, the falsification possibility means that we must regard all laws or theories as hypotheses or conjectures or, even, guesses. Nevertheless, for the refinement of such Popperian rationale, Imre Lakatos' proposition (1976) of the methodological falsificationism allows many more theories to qualify as 'scientific'. As this author states: "Furthermore, probabilistic theories may qualify now as 'scientific': although they are not falsifiable they can be easily made 'falsifiable' by an *additional* (third type) *decision* which the scientist can make by specifying certain rejection rules which may render statistically interpreted evidence 'inconsistent' with the probabilistic theory". In other words, the community of practice that focuses on certain phenomena, theories and methods decides about the scientific status of each of them. With this latter point, we however disagree because, in practice, we find positivist quantitative research advocating for a coefficient of explanation as low as 20 per cent, or an r^2 of 0.2, as statistically "significant". After controlling for level of significance and using dummy variables to isolate other influencing factors, a 0.2 r^2 means that the hypothesis can explain 20 per cent of the reality it tries to understand. This level of results that is considered acceptable by consensus on a determined community of practice in social sciences, would unlikely be admitted by hard sciences. In the same way, positivist qualitative research might fall in the same situation claiming through other means to be capturing the truth about a reality.

We understand that good research makes clear its limitations. However, in the end of the day when practitioners (e.g. managers) request orientation for application, the narrative looks like: "Research says…" or, "There is a strong consensus among researchers that says…", and what we highlight here is that these kinds of narratives transform an honest research, clear on its limitations, into "the" truth.

In short, we agree that in management science, theories cannot be proved but can be falsified and understand that the standards which allow for the non-rejection of a hypothesis is generously inclusive. However, we argue that the guarantee of scientific status passes through the criterion of appropriateness of the ethos, pathos and logos considered into the theory building's narrative.

In order to make a hypothesis accept as scientific these beliefs must be made aware and conveyed to all interested stakeholders. For example, it is harder today to convince about the scientificity of the Political Economics of Karl Marx in the mainstream thinking in the United States or, on the other hand, to suggest the decentralization of power and lessening of the government in China or Russia. Therefore, how can one assume that the scientificity of theory in management has to do with the law found from the methodology applied to a research? To use a common expression: there are theories more 'politically correct' than other theories despite their level of falsification. The beliefs present in a certain context allow for certain kinds of narratives and avoid others.

A second, but as important, argument is brought by Bitektine and Miller who, from the perspective of sociology of science, enables us to argue about the existence of a management research life-cycle which starts from the decision of what to research about. This decision is taken under administrative (e.g. university's performance appraisal or resources availability) and social (e.g. recognition by peers) pressures, leading to "an unintended effect: researchers begin to prefer easy, quick-turnaround projects to more fundamental research that would require more time and effort. This production pressure induces researchers to maximize publication output and minimize the risk associated with their investment of time and effort" (Bitektine & Miller, 2015, pp. 118, 119). In other words, as soon as the research topic becomes less attractive or the efforts to refine the methods testing the theory become overwhelming (i.e., as expected by the nature of social sciences), the research interest is dropped without achieving the initially intended axiomatic status.

Finally, the third point seems to be very revealing. As we mentioned above, the r^2 of 0.2 accepted by the community of practice in a given topic, in effect, helps to hide the changing nature of social reality, which has hopefully, but not necessarily, an evolving nature. Konrad Lorenz calls "pseudo-knowledge" (1973) the assumption that human and social sciences have achieved the same level of development of physical science. The claim assumes that natural sciences start by the observation and description of the phenomenon (descriptive phase), then to its classification (systematic phase) and finally to the abstraction of the set of laws which govern them. The empirical test serves to verify the claimed laws and thus occupies the last stage of a series of methods (nomothetic phase). The author suggests, nevertheless, that to human and social sciences it would be more desirable to use the simple method of observation and description because the more complex and organic the system is and the higher its level of integration the more difficult it is to establish laws of functioning.

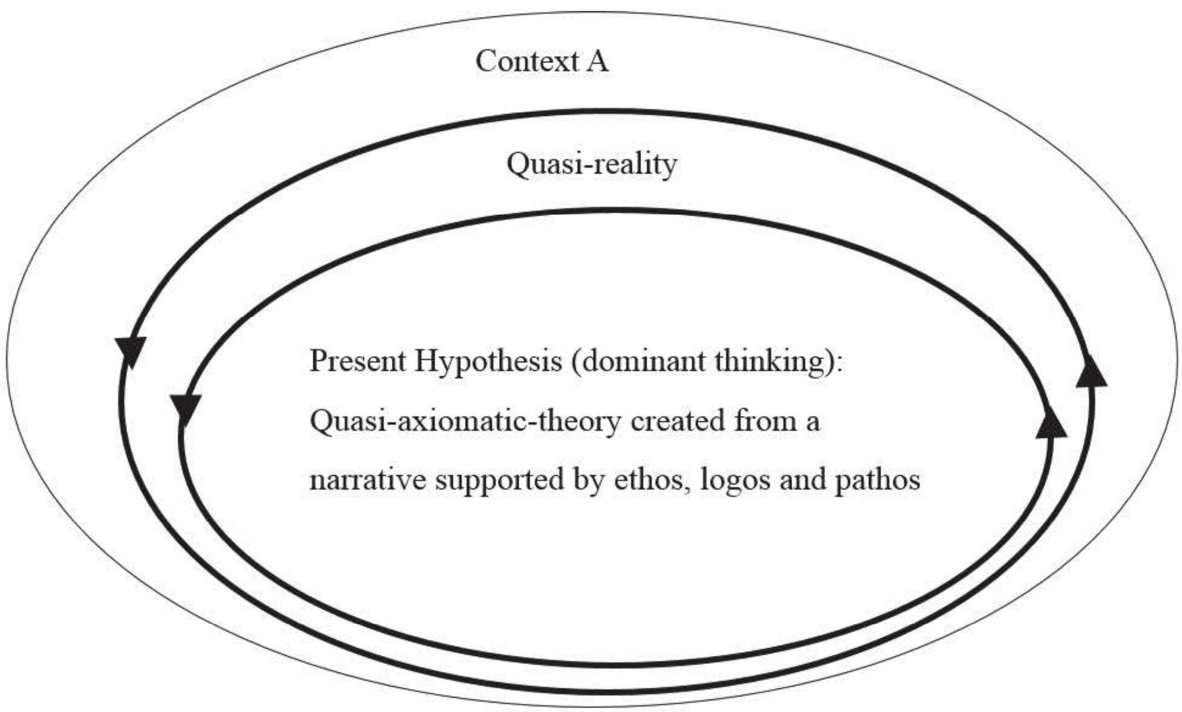
Therefore, if one still intends to consider human and social realities as objective phenomena, nomothetic instead of idiographic, he/she must at least recognize that their theories just did not achieve the maturity status of natural sciences.

Part Three

We come then to the problem of paradigm-shift, which must be understood differently from the Kuhnian term. In our case, we are considering the quasi-paradigm, or laws, theories, methods and applications about a particular social reality grounded on contextual beliefs and interests supported by circumstantial ethos, pathos and logos. A constructed social reality is our assumption about the nature of management reality. Although we observe some limitations to that statement, like the universal need to respect people and contracts for relationships and deals to become fruitful, our beliefs are similar of the work of John Searle on "The construction of social reality" (1995).

Figure 1 shows the self-reinforced (e.g. narrator and audience reciprocity) quasi-axiomatic-theory (meaning a law, theory and application supposedly scientific due to a flexible falsification requirement created within a "quasi-reality", meaning the transitory character of a constructed reality), originated from a logos and ethos capable of persuading an audience, the pathos.

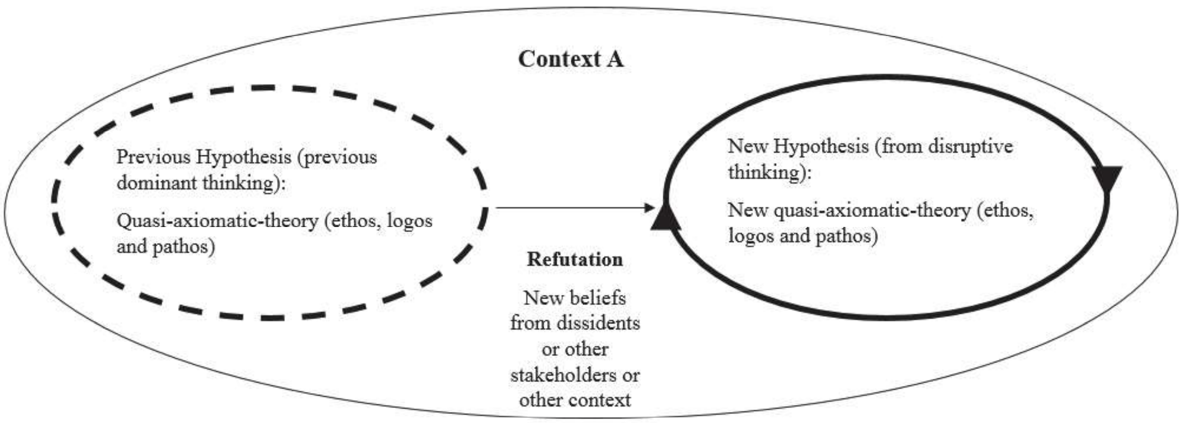
FIGURE 1
THE STRUCTURE OF THE QUASI-AXIOMATIC-THEORY



Consequently, we also review the idea of anomaly, discovery and invention. Kuhn (1996, p. 52) states that "We must now ask how changes of this sort [in normal science] can come about, considering first discoveries, or novelties of fact, and then inventions, or novelties of theories… Discovery commences with the awareness of anomaly, i.e., with the recognition that nature has somehow violated the paradigm-induced expectations that govern normal science." If our assumption is correct, discovery commences with the establishment of conflicting beliefs which causes disruption in the present *status quo* and which in order to prevail must have at least similar strength regarding the narrator prestige, the narrative internal logic, and the capacity of persuading an active audience towards new beliefs. In the same context A, new beliefs may be driven from within a group (e.g. dissidents who changed a position or innovate their thinking); or from outside of the group as external pressure made from different stakeholders, or also, from the beliefs of another context. The institutionalization of the new belief is expected to follow.

The criterion thus to refute a hypothesis changing the quasi-paradigm, differently from the scientific falsificationism although we might use it as an argument, relies on the logos of the argument and the ethos of the narrator and their capacity to persuade individuals towards an innovative thinking (figure 2).

FIGURE 2
THE REFUTATION OF THE QUASI-AXIOMATIC-HYPOTHESES



The just mentioned considerations allow us to address the third objective of this paper, which is to apply the rationale developed to our own studies in corporate governance.

As a side effect of the dominant model thinking, corporate governance theory assumes that there is a conflict between the principal and the agent due to asymmetries of information. Shareholders want to maximize their investments while managers seek long-term security. Corporate governance aims to minimize this conflict by providing some control mechanisms (e.g. the board of directors, ownership concentration) and transparency as the agency theory postulates (Jensen & Meckling, 1976). As a resultant of the dominant model, the bias in this conflict commonly bends towards the shareholders as management has the fiduciary obligation to maximize their profits.

Our model follows the general assumption of the influence of governance in enhancing firm performance and ultimately firm value. The model also assumes that firm performance and good governance are simultaneously determined which means that governance influences firm performance (Equation 1.1), but firm performance also influences governance (Equation 1.2). The endogeneity of governance and performance is well described in the literature, governance structures are not exogenously determined but rather simultaneously determined with other firm decisions. For this reason, the statistical method we used to assess the relationship between governance and performance is the simultaneous equations applying three-stage least squares. We thus simultaneously estimate the following equations:

EQUATION 1.1

$$Q_i = \alpha + \beta_1 GOVI_i + \beta_2 LEVER_i + \beta_3\ ROA_i + \beta_4\ SIZE_i + \beta_5 GROWTH_i + \beta_6 TANG_i + \beta_7 BETA_i + \\ + \sum_{j=1}^{20} \delta_j IND_{ji} + \sum_{l=1}^{5} \gamma_l IDENT_{li} + \varepsilon_I$$

Where: Firm value proxy by Tobin's q (*Q*), capital structure (*LEVER*), future growth opportunities (*GROWTH*), firm profitability (ROA), the tangibility of firm's assets (*TANG*), firm size (*SIZE*) and firm risk (*BETA*).

The variables *IND* and *IDENT* are dummy variables that control for industry and identity of the main shareholder.

EQUATION 1.2

$$GOV\text{-}I_i = \alpha + \beta_1 Q_i + \beta_2 LEVER_i + \beta_3 INTANG_i + \beta_4 GROWTH_i + \beta_5 SIZE_i + \beta_6 ROA_i + \\ + \sum_{j=1}^{20} \delta_j IND_{ji} + \sum_{l=1}^{5} \gamma_l IDENT_{li} + \varepsilon_l$$

Where: GOV-I is the governance index, *Q* is the proxy for firm value (measure through Tobin's *q*) *LEVER* is the capital structure, future growth opportunities (*GROWTH*), firm profitability (*ROA*), the level of intangible assets (*INTANG*), and firm size (*SIZE*).

Our measure of GOV-I includes four constructs: access to information (AIn); board structure (BStr); ownership structure and control (Own); and, transparency (Tr) assessed through a questionnaire developed based on the OECD Governance Principles. Thus the complete assumptions are: $GOV\text{-}I_i = [(AIn) + (BStr) + (Own) + (Tr)]_i$

Then, it came the financial meltdown in 2008 affecting the financial sector in virtually all the bigger economies. We were astonished. How the thought "lawful" corporate governance mechanisms failed to, if not avoid the meltdown, at least to deliver a prognostic in advance? Discussions that started in the 2010 European Academy of Management Conference in Rome and the 2010 Academy of International Business Conference in Rio de Janeiro among academic colleagues from corporate governance and social and environmental responsibility tracks ended up into a mutual demonstration of frustration as we concluded that if any school of thought was signalizing the hazard that was about to come, it would not be the dominant thinking in governance. Among the tons of explanations provided after the fact, of course, we reflected about two which are intertwined: first, the group thinking phenomenon which affected a group of people with shared interests regarding the maximization of profits within a context; and, second, the thesis of Coffee Jr (2003, p. n/a) about the 2001 crisis which we extend as the same reason for the 2008's: "Now we get to the heart of the matter. Something did change dramatically during the 1990s. It was executive compensation. The executive compensation package of the typical chief executive officer went from being 92 percent cash (and 8 percent equity) in 1990 to 34 percent cash (and 66 percent equity) in 2001. […] With this transition from cash-based to equity-based compensation also came a basic change in managerial incentives."

In Aristotle terms, ethos and pathos in place within these groups and contexts needed logos, the corporate governance theory and mechanisms, to justify actions. For example, level of leverage or risk taken by the companies would be overseen by the board of directors which would make "logical" recommendations to managers and shareholders. Such narrative has if any, little hard hypotheses vested in it. From this fact comes our suggestion for a new framework to corporate governance. We advance that it has not the objective to forecast the next crisis but it does include views neglected by the dominant model, namely wealth distribution and externalities like corporate social and environmental responsibility. It is more inclusive because it is based, besides Freeman's stakeholder's approach, on the principal of democracy in which equals have voice and deserves the same attention. In that sense, Freeman et al. gives, besides the shareholders, voice to employees, customers, suppliers, communities, government, among others, confronting the "separation thesis" by assuming that maximization of output or creation of value may be done to all the interested stakeholders (Freeman, Harrison, & Wicks, 2007).

The construction of the model takes advantage of different and contemporary narratives delivered by different sources but with similar objectives. We integrate them coherently and derivate an equation on governance, which, we must highlight, is always transitory. The model may include other sources but in this paper, we analyse: gender issues, putting people first, corporate social and environmental responsibilities, and consumer satisfaction. The justifications of their inclusion are in the following.

CONTEMPORARY NARRATIVES

Gender Studies in Management

From the equations derived from the dominant model, we add the presence of women in the board of directors and argue in its favour with the following examples. In 1990, Judy B. Rosener writes, "Ways women lead", an article we consider seminal in the consideration of women leadership style's benefits. "The command-and-control leadership style associated with men is not the only way to succeed," argues Rosener (1990, p. 119) politely. She does not condemn male style but invites one to think that they can co-exist. From this more argumentative article, descriptive studies followed. Helping to legitimate the narrative, in 2000, Business Week magazine put together five articles regarding performance appraisal of managers. The studies were not addressing gender issues. Nevertheless, they accidently found that women leadership was better rated on the skills of motivating others, fostering communication, producing high-quality work and listening to others and, equally rated on strategic planning and analysing issues in comparison with their counterpart men (Sharpe, 2000). From these kinds of studies, institutionalization followed. Scandinavian countries seem to be dictating the trend on the matter and becoming a context, which influences others. According to *Leena Linnainmaa, Director, The Central Chamber of Commerce of Finland,* Finland and Sweden have the highest number of women on the boards of listed companies in the European Union. A situation strengthened by the change of the Finnish Corporate Governance Code for listed companies made in 2010, which requests both genders to be equally represented on the board of directors (Linnainmaa, 2010).

The enhanced equation built from the dominant model presented above includes thus the presence of women in the board (Wom). GOV-Ienhanced is equal:

GOV-Ienhanced1 = [(AIn) + (BStr) + (Own) + (Tr) + ***(Wom)]***

Putting People First

In the dominant model, we deduce, employees are important if, and only if, they are productive because employees are the means to profit maximization for shareholders. A great part of the knowledge in Management and Psychology is devoted to preparing and satisfy employees in order to perform well. It does not matter if one uses a stick or offers a carrot because we still would find a donkey in the middle. At present, we believe we are not close enough to the second formulation of the categorical imperatives of Kant, namely: "Always treat the humanity in a person as an end, and never as a means merely." We, however, do recognize societies' effort in providing minimum welfare and as well companies which at least try to put people first (e.g. Levering, 1988; Ferris, et al., 1999). Jeffrey Pfeffer (1998, p. 292) sustains that as differently from people, "almost every other source of organizational success – technology, financial structure, competitive strategy – can be imitated in an amazing short period of time", therefore, organizational success is primarily a result of the quality of employees.

We evolve, thus, our model considering proxies, which we perceive as signs of putting people first attitude. The enhanced equation by this source includes employee presence in the board, presence of discrimination policies and whistleblowing protection (Empl). GOV-Ienhanced is:

GOV-Ienhanced2 = [(AIn) + (BStr) + (Own) + (Tr) + (Wom) + ***(Empl)]***

Corporate Social Responsibility

The distinction among social responsible, environmental responsible and ethical policies adopted by firms is becoming more and more integrated. In the words of the founder of The Body Shop cosmetics, Anita Roddick (2000, p. 56): "One of our greatest frustrations at the Body Shop is that we're still judged by the media and the City by our profits, by the amount of product we sell, whereas we want and have always wanted to be judged by our actions in the larger world, by the positive difference we make". This criterion refers to the company's involvement in the community and as well its respect to fair trade, respect to human rights and labour rights, and application of anti-corruption initiatives.

The enhanced equation includes corporate social responsibility (CSR) then GOV-Ienhanced is:

GOV-Ienhanced3 = [(AIn) + (BStr) + (Own) + (Tr) + (Wom) + (Empl) + ***(CSR)]***

Corporate Environmental Responsibility

In the same way that Popper believed in the lawfulness of Newton's gravity theory until he was presented to Einstein's new hypothesis. We took for granted that green energy was more expensive than fossil fuels and, thus, unlikely to utilized expressively. In reality, that might not be the case, at least according to the International Energy Agency, which in a report issued in November 2010 argues that abolishing fossil fuel subsidies would boost the world's economy, environment and energy security (Burniaux & Chateau, 2014). Fossil fuels receive close to six times more subsidies than greener sources every year, or an extra US$255 billion just in 2009. This important part of the discussion on sustainability shows how a narrative may be transformed into a sacred belief in the mind of the ordinary people (i.e., costly green energy). It took a movie, called "The inconvenient truth" and promoted by a former vice-president who receives subsequently a Nobel Prize along with a team of scientists organized by the United Nations, for a sense of awakening to the matter occur.

Corporate environmental responsibility (CER) is included in the enhanced equation which becomes:
GOV-Ienhanced4 = [(AIn) + (BStr) + (Own) + (Tr) + (Wom) + (Empl) + (CSR) + ***(CER)]***

Customer Satisfaction

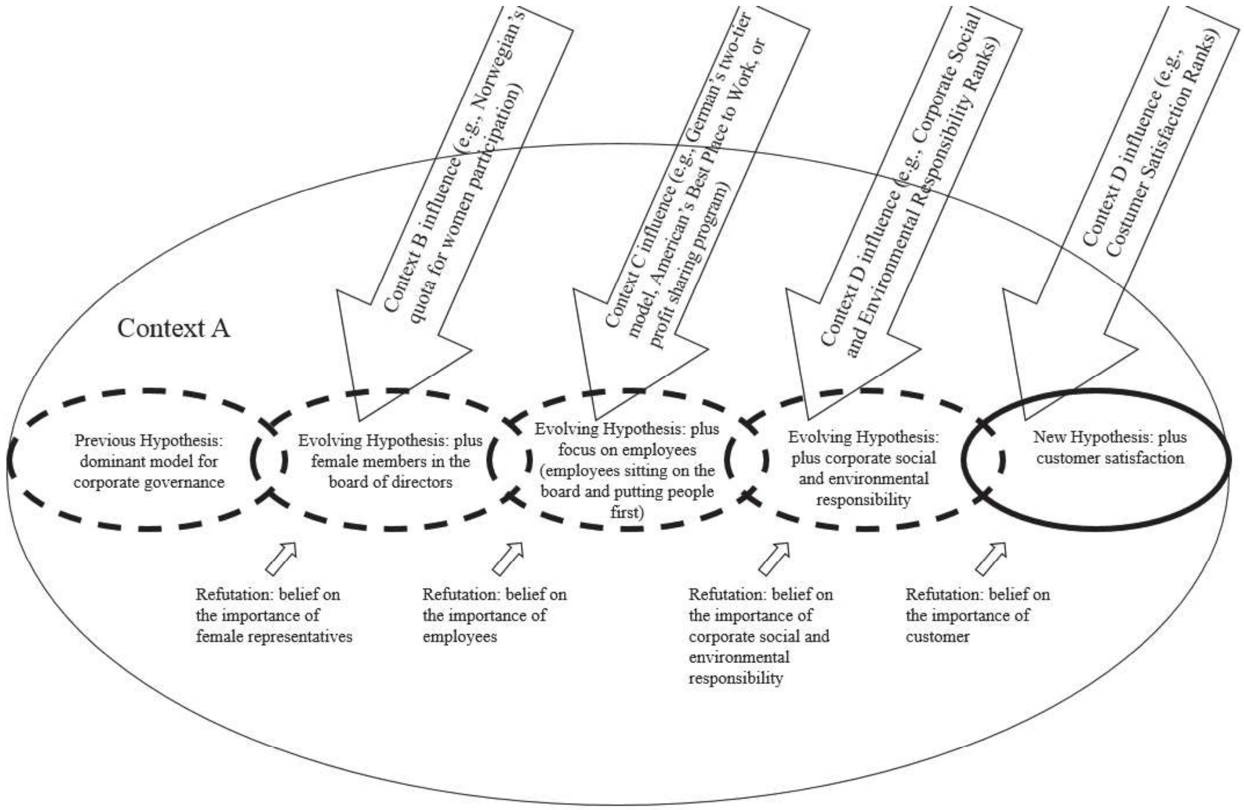
The need to satisfy consumers should be a shared belief among managers. Our original governance index includes measures of firm profitability (*ROA*) and the level of intangible assets (*INTANG*), for instance. One could argue that these are indirect measures of customer satisfaction. To us, they are not as several cases of customer lack of satisfaction are found in companies which still present profits or valuable brands. Such fact is, however, counter intuitive. Some monopolies and oligopolies are traditional examples in which customer have no other purchase choices. Green-washing and even social-washing (i.e., fake corporate social responsibilities practices) are contemporary ones in which customers are misled by businesses. We call this last, but not least, criterion: consumer assessments (Consu) which brings the enhanced index to:
GOV-Ienhanced5 = [(AIn) + (BStr) + (Own) + (Tr) + (Wom) + (Empl) + (CSR) + (CER) + ***(Consu)]***

Therefore, the final comprehensive meaning for governance (GOV-Icompr) is:

GOV-Icompr = [(AIn) + (BStr) + (Own) + (Tr) + ***(Wom) + (Empl) + (CSR) + (CER) + (Consu)]***

Figure 3 demonstrates and summarizes the evolving narrative. Hypotheses are systematically refuted and replaced by new, more comprehensive ones. The previous quasi-paradigms are included in the new hypothesis and the enhanced equations follow.

FIGURE 3
THE DYNAMICS OF HYPOTHESIS AND REFUTATION OF THE QUASI-AXIOMATIC-HYPOTHESES ON CORPORATE GOVERNANCE



In case these new narratives are accepted by audiences who are discontent with the *status* quo, the present quasi-reality will change being replaced by another which seems to incorporate wishes from a broader society. The quasi-axiomatic-theory will follow.

From this more comprehensive governance measure, our stakeholder approach index, we will estimate the effect of governance on firm performance simultaneously as follows:

COMPREHENSIVE EQUATION 1.1

$$Q_i = \alpha + \beta_1 \boldsymbol{GOVIcompr}_i + \beta_2 LEVER_i + \beta_3 \ ROA_i + \beta_4 \ SIZE_i + \beta_5 GROWTH_i + \beta_6 TANG_i + \beta_7 BETA_i + + \sum_{j=1}^{20} \delta_j IND_{ji} + \sum_{l=1}^{5} \gamma_l IDENT_{li} + \varepsilon_I$$

COMPREHENSIVE EQUATION 1.2

$$\boldsymbol{GOV\text{-}Icompr}_i = \alpha + \beta_1 Q_i + \beta_2 LEVER_i + + \beta_3 INTANG_i + \beta_4 \ GROWTH_i + \beta_5 SIZE_i + \beta_6 ROA_i + \sum_{j=1}^{20} \delta_j IND_{ji} + \sum_{l=1}^{5} \gamma_l IDENT_{li} + \varepsilon_I$$

EMPIRICAL RESULTS

Next, we test our comprehensive model by using the Environmental, Social and Governance (ESG) scores provided by the Sustainalytics responsible investment research firm as proxies to our constructs. Each score is calculated by weighting different dimensions (women on board, employee satisfaction, ethical issues, consumer satisfaction, anti-discrimination and anti-corruption policies, diversity programs, whistle-blower protection, board independence, among others) into the scores. Our sample is composed by 251 non-financial Canadian firms listed on the Toronto Stock Exchange from 2004 to 2011.

Table 1 reports the estimated coefficients for each score. Column [1] shows the results of the regressions for the ESG score (which includes all three categories: environmental, social, and governance). The results show a positive impact of the adoption of best ESG practices on firm value creation as measured by Tobin's *q* (Q), our measure of firm value. In columns [2-4] we analyze the effect of each category in isolation and once more, we find evidence of a positive impact in firm value.

Our results corroborate our hypothesis that a stakeholder approach in the present context brings better results to organizations.

TABLE 1
REGRESSION RESULTS

	Dependent variable = Tobin's *q* (Q)			
	[1]	[2]	[3]	[4]
ESG score$_t$	0.020** (0.039)			
Environmental$_t$		0.020* (0.057)		
Social$_t$			0.021** (0.034)	
Governance$_t$				0.017** (0.032)
ROA	0.036** (0.031)	0.036** (0.031)	0.036** (0.031)	0.036** (0.031)
FirmSize	11.956*** (0.000)	11.959*** (0.000)	11.976*** (0.000)	11.948*** (0.000)
Intercept	9.935*** (0.000)	9.955*** (0.000)	9.931*** (0.000)	9.928*** (0.000)
Control variables	included	included	included	included
Observations	2008	2008	2008	2008
R-squared	0.0185	0.0183	0.0188	0.0184

This table presents the return regressions for the proposed models. The dependent variable is Tobin's q (Q). We used panel data fixed effects regressions on a panel of 251 non-financial Canadian firms listed on the Toronto Stock Exchange from 2004 to 2011. The dependent variables are the environmental, social and governance indices measured by Sustainalytics investment research firm. P-values based on robust standard errors are in brackets. *, **, and *** means significance at 10%, 5% and 1% levels respectively.

CONCLUSION

Our main conclusion is that it is plausible that an elaborated mathematical equation which supports a theory in management can be originated from a narrative accepted by an interest group in a given context. Thus, instead of originating from a law based on the observation of the objective reality, these managerial theories are socially created and reinforced within a limited context and timeframe. The theory, along with the equation, seems to work quite well during a period but then it suddenly expires. Laws in the physical world instead, are unlikely to expire and, if they do, we face a paradigm shift. Mistakenly, factors like a flexible falsification criterion or even the duration of the not rejected hypothesis seem to work as criteria of validity. However, the episodes in which hypotheses do not function do not serve to drop them because what was holding these hypotheses as true were in fact the ethos, pathos and logos attached to their supportive narratives. In other words, what keeps the theory alive are the beliefs attached to it, which must be supported by a group. "In the end, a theory is accepted not because it is confirmed by conventional empirical tests, but because researchers persuade one another that the theory is correct and relevant", as Fisher Black reveals.

Beyond the sociology of science, the paper insights might bring to awareness the politics of science, at least for social sciences, meaning the recognition of biased ethos, pathos and logos of narratives, which can create, capture, or modify both the reality and its resultant quasi-paradigmatic theory towards the wishes of an interest group. Like in the case of subsidies for fossil fuels, the hard management scientist might be researching and finding hard data regarding prices, productivity, demand, distribution about an industry that seems to exist only because of the decision of a group of people, which will benefit from it, and which provides a convincing rhetoric to the general public, e.g., "It costs less", and to the politician, who is the decision-maker on the matter and a more suitable to be persuaded by the lobbing activity.

Thus, there is no other way to go back to reality and invite, metaphorically, the child to leave fantasyland, to mature and to become humanized, focusing our human virtues and capacities, including the democratic inclusion of all the voices at stake. Yet, recognizing meta-mechanisms, like rhetorical devices which shape our reality, and questioning them. Our approach to hard management science consists of considering the not-rejected hypotheses as analogies of realities. It is fine if an audience aware of its great limitations wants to take advantage of it. However, these 'proved' hypotheses are not more important than any other innovative interpretation of the reality. The point is how any approach to the actual state-of-affairs can reinforce a reality that seems to be working well or change it in case of been neglecting individuals with a stake into relevant issues. That is what we were able to appreciate in our empirical results, which indicate that companies that take into considerations the interests of a broader scope of stakeholders in their decision-making process create more firm value (as measured by Tobin's *q*).

Finally, to the practitioners, our proposed index serves to reinforce individuals who intend to be inclusive by understanding the evolving nature of social issues, their impact in business' decisions and performance and, therefore, who are willing to consider inputs from the ones we suggest and other relevant stakeholders.

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