



THE PROCESS OF GOVERNANCE FOR SUSTAINABILITY

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ABSTRACT

Recent intensive researches on corporate governance, corporate social responsibility and sustainability tend to subscribe to some simplified theoretical models in describing and explaining the complexity of business reality. The logic problem in here is that the traditional way of theorizing tends to force-fit the complex business practices and concretes into some generalized abstractions. While the fundamental limitations with the static and entitative approach are rooted in the traditional substance philosophy, we suggest that the alternative process thought offers better way of explaining reality. We argue that the processual approach opens up new avenues for understanding the practice of corporate governance, responsibility and sustainability.

Keywords

Corporate governance, shareholding, stakeholding, methodological issues, process thought

INTRODUCTION

Recent intensive researches on corporate governance, corporate social responsibility and sustainability tend to subscribe to some simplified theoretical models in describing and explaining the complexity of business practices. For example, a fierce debate has been surged between shareholding and stakeholding perspectives in corporate governance since the 1990s (Letza, Sun, & Kirkbride, 2004). Whilst researches on corporate social responsibility and sustainability have overwhelmingly rejected Friedman's argument that the only responsibility of a corporation is to make profit (Friedman, 1970), the main stream of CSR have been either grounded on the normative perspective of business ethics and responsibility which is mainly rooted in Kantian philosophy, or based on stakeholder theory. In stakeholder theory, a distinctive line has been drawn between the instrumental and normative perspectives as well. While the former attempts to use stakeholders as tools for



the pursuit of shareholder interests, the later is moral-orientated and seemingly more genuine in stakeholders' intrinsic interests within corporations (Donaldson & Preston, 1995). In all those researches, a similar either-or approach has been prevailing – either shareholding or stakeholding, either instrumental or normative, either obligated, strategic or value-oriented, either market for corporate control, or hierarchical and network governance for sustainability, etc. Such an either-or approach offers polarized alternative perspectives, forms or solutions to governance and its problems.

Behind this either-or approach is the traditional way of theorizing. A general trend in this research area is that we try to generalize some simplified and easily understood rationales out of business practices and theorize them as models, and then in turn apply those abstract models to rich business practices. Thus, we have seen in recent years the mainstream research calling for the application of general principles, norms and codes, universal models/perspectives, and optimal governance structures into the practices of business and sustainability. The logic problem in here is that while business practices are always diverse and multi-orientated, the traditional way of theorizing is much simple, singular and general, which tends to force-fit the complex business practices and concretes into the generalized abstractions. However, empirical evidence and our living experiences suggest that there is no single way of corporate governance and corporate responsibility/sustainability is not an abstract concept, but always resides in rich contexts of societal traditions and conventions, cultures, ideologies, competing perspectives, changing social, economic and political conditions, etc. A simplified way of theorizing is questionable.

This paper aims at exposing the limitations and problems with the current researches on corporate governance, responsibility and sustainability and seeking alternative way of thinking about corporate governance and responsibility issues. We evaluate competing theories of governance and discuss directions for and methodological issues in governance research. We suggest that if we want to push the bounds of our current theories and research we must move beyond the conventional static and poorly contextualized models that have dominated to date, enabling the development of evidence-based and actionable knowledge, grounded in studies of process and focused upon improving practice. We reveal that the fundamental problem with the conventional way of research in this area, however, is the conscious or subconscious core assumption behind the theoretical simplification and generalization, that is, the social reality of corporations and their governance is concrete, entitative, and relatively enduring, in which some generalized laws and regularities can be revealed. The traditional orthodox philosophy of substantialism is underpinning such presuppositions and ways of doing research. However, we show that how a process philosophy (compared with dominant substantialism) offers an alternative world-view and better explains reality. We argue that this approach opens up new avenues for understanding the practice of corporate governance, responsibility and sustainability.

CORPORATE GOVERNANCE MODELS, ASSUMPTIONS AND PROBLEMS

Governance Models

There are four main perspectives in the corporate governance literature: the principal-agent or finance model, the myopic market model, the abuse of executive power model, and the stakeholder model (Blair, 1995; Keasey, Thompson, & Wright, 1997). The former two models belong to a shareholding perspective because they commonly believe that the only purpose of corporations is to maximise shareholders' wealth. Whilst acknowledging that shareholders do not have enough control and influence over managerial action due to their



distance from the day-to-day operations, the principle-agent model argues for the enhancement of the power and control of shareholders (principals) over managers (agents) and corporations (Jensen & Mechling, 1976).

The main goal of agency theory is to determine the most efficient or optimal contract governing the principal-agent relationship. The question is especially related to whether behaviour-oriented governance (e.g. salaries, hierarchical governance) is more efficient than outcome-oriented contractual governance (e.g. commissions, stock options) (Eisenhardt, 1989). For agency theorists, market-oriented governance structures best discipline managers' behaviour. Financial theorists, however, claim that since managerial behaviour could be constrained by the pressures of capital markets, factor markets and the market for corporate control can best address the issue of management underperformance (Manne, 1965). The advocates of this model insist that current corporate governance mechanisms should be allowed to operate freely and that any interference with the market governance mechanisms is irrational and distorts them (Hart, 1995).

The myopic market model argues that the maximisation of shareholders' well-being is not synonymous with share price maximisation because the market systematically undervalues long-term capital investment. It also argues that the Anglo-American style of corporate governance is flawed by an over concern with short-term return on investment, short-term corporate profits, short-term management performance, short-term stock market prices, and short-term expenditures (Charkham, 1994; Hayes & Abernathy, 1980; Moerland, 1995; Sykes, 1994). This model suggests that corporate governance reform should provide an environment in which shareholders and managers are encouraged to share long-term performance horizons. It is thus necessary to increase shareholders' loyalty and voice while reducing the possibility of shareholders' exit, to encourage 'relationship investing' to lock financial institutions into long-term positions, to restrict the takeover process and restrain voting rights for short-term shareholders and to empower other groups such as employees and suppliers who have long-term relationships with the corporation (Keasey et al., 1997).

The abuse of executive power model and the stakeholder model share the same proposition that a corporation should not merely serve its shareholders' value, but work for the corporation as a whole and for the wider stakeholders' interests. The abuse of power model believes that Anglo-American companies suffer from a widespread abuse of executive power and corporate irresponsibility. The current corporate governance arrangements leave excessive power in the hands of management who may abuse it to serve their own interest at the expense of shareholders and society as a whole (Hutton, 1995). This model assumes that managers are trustees of the corporation as a whole rather than agents of shareholders. Therefore, a new proposal for corporate governance reform is advocated, in which the statutory duties of directors should be to promote the business of the company as a whole and to balance it with shareholders' claims, more power should be given to the independent directors for nominating and selecting senior managers, and the appointment of a CEO should be for a fixed four-year term with only one renewal of contract.

The stakeholder model in corporate governance has been regarded as the most fundamental challenge to the principal-agent model. The central proposition of this model is that the objective and purpose of the corporation should be defined more widely than the maximisation of shareholder wealth alone. The corporation should recognise the well-being of other groups such as employees, suppliers, customers and managers who have a long-term association with the firm and thus some 'stakes' in its long-term success. A wider objective function of the corporation is not only economic equitability, but also social accountability and efficiency (Keasey et al., 1997).



Instrumental stakeholder theory sets up a framework for examining the connections between the practice of stakeholder management and the achievement of corporate performance goals (Freeman, 1984). The assumption is that if corporations practise stakeholder management, their performance such as profitability, stability and growth will be relatively successful. Thus, stakeholder management becomes a significant strategy for managers who would be sensitive to future change. However, there is no clear guideline in the stakeholder model to ensure managers perform stakeholders' benefits and social obligation. Some suggestions for stakeholder management include trust relationships and long-term contractual associations, interlocking shareholdings and inter-firm co-operations, ethical behaviour, employees' participation in decision-making and ownership-sharing scheme.

Common Assumptions

Despite their competing and conflicting diagnoses of and solutions to corporate governance ills, these perspectives share some common assumptions in terms of the nature of corporation, the governance structures, and the reason for governance. It is these assumptions and their underlying presuppositions that suggest some fundamental and irresolvable problems with current governance theory.

The current debate on corporate governance is traceable to a nineteenth century argument on the nature of the corporation in corporate law theory, between the 'aggregate theory' and the 'nature-entity theory'. The aggregate theory claims that the corporation as a legal person is not a real person, but an artificial person created by law or the state as a matter of convenience. The corporation is only a collective name for its members and the aggregate rights of its members. By contrast, the nature-entity theory argues that the reality of the corporation is a real person with its own enduring personality, distinctive mind and will, and a capacity to act through its organs. The corporate personality is rightly recognised, and not simply created, through the process of incorporation (Arthur, 1987; Barker, 1958; Mayson, French, & Ryan, 1994). This aggregate-entity debate eventually suggests an 'individualistic' view versus a 'holistic' view of the nature of the corporation, which largely influences the current debate in corporate governance between shareholder and stakeholder perspectives. Generally, economists are interested in the organisation of economic actors regardless of their legal form (Loasby, 1998). In this context, a firm is no more than a 'nexus of contracts' joining inputs to produce outputs among actors and between principals and agents in order to maximise behaviour of all individuals. Whilst shareholder perspectives share the individualistic view of the corporation, stakeholder perspectives tend to view the corporation more or less as a broader collective unity, as an enduring entity and more than just the totality of the shareholdings. Both perspectives attempt to claim a solid, clear-cut, self-contained, enduring, and describable characteristic of either an individual atomic entity as the foundation of the corporation or corporate-as-a-whole entity beyond individuals. Those entities are regarded as neutral objects waiting for our discovery and analysis, and seem to be pre-given and already existent 'out there' independently of our minds. In either case, these entities are extant, socially and legally constructed systems, which we as individuals discover and analyse, and to which we add our own constructs and interpretations. Furthermore, the corporation as a social system either bound by contracts or by laws is normally rational with maximum goals, reasonable actions and optimal solutions for the sake of economic efficiency. In both shareholder and stakeholder perspectives, the corporation is viewed as a social tool for the purpose of governance and control in order to maximise the economic interests of shareholders or certain stakeholders.



Following these assumptions, both perspectives try to discover an optimal governance structure that can effectively solve the agency problem or the problem of abuse of executive power. Thus, the market governance mechanisms advocated by the principal-agent model and the hierarchical forms of governance by the other three models are regarded as competing alternatives for rational selection and appropriate design. Both sides of the debate assert that only one optimal and universal governance structure is effective in disciplining management performance, which could be repetitively tested and objectively chosen. The criterion of selecting the optimal governance structure for all the perspectives accords to the principle of economic efficiency since, it is argued, institutional change has its root cause in efficiency. There exists a rational process of ensuring more efficient economic forms and governance structures prevail over less efficient ones (Williamson, 1975). Economic rationality or efficiency is seen as a common reason for both shareholder perspectives and stakeholder perspectives to search for an elegance, purity, certainty and universality of governance form – ‘the ultimate demonstration of rationality at its best’ (Solomon & Higgins, 1996). In agency theory rationality is embodied in the optimisation of contracts. The myopic market model suggests curbing irrational short-termism by forcing actors to take a more considered (rational) long-term view. The abuse of executive power model seeks a similar route to rationality, insisting that irrational (in the eyes of the corporate whole) directors’ powers be curtailed, with independent scrutineers seeking the optimum path. Stakeholder theory seeks a collective rationality, in which the demands of one group cannot disproportionately outweigh the requirements of others.

Issues with Current Corporate Governance Analysis

Both anecdotal evidence from the news media and public inquiries into major corporate failure, as well as the authors’ experience as practitioners demonstrates that the claim of universal principles and optimal governance structures explicitly made by the four models is not supported in corporate governance practice. This raises the question of whether there is any solid and objective foundation such as individual entity or corporate entity for building an optimal and universal structure. As all of the four models suggest that the validity of the competing analyses on corporate governance relies on supporting empirical evidence (Keasey et al., 1997), therefore, either market governance or hierarchical governance, as alternative solutions, should be demonstrated in practice to be optimal or superior. However, this is not the case, as the evidence available does not simply support any single governance structure claimed to be most effective. Counter-evidence from both sides of the corporate governance debate denies both market governance optimal and hierarchical governance effectiveness. Indeed, corporate governance has experienced perhaps too much of both ‘hierarchical dysfunction’ and ‘market failure’ in Anglo-American business history. Whilst hierarchical governance failure is largely due to reluctant shareholders and defective boards of directors (Bishop, 1994; Hart, 1995; Hawley & Williams, 1996; Jensen, 1993; Latham, 1999; Sternberg, 1998), market governance failure is primarily due to short-termism and unreliable market forces (Bishop, 1994; Hart, 1995; Herman & Lowenstein, 1988; Parkinson, 1995; Pound, 1993). For example, the designed function of hierarchical governance relies on shareholders’ effective monitoring such as vote, voice and proxy fight. However, since the increasing separation of ownership from control in the early twentieth century (Berle & Means, 1932), individual shareholders are less inclined and have less incentive to participate in the monitoring system due to the free-rider problem, lack of information, useless proposals, managers’ manipulation and legal restrictions. It is arguable that this incentive problem might be offset by the gravitas of large institutional directors,



and there are signs that pension funds and their 'City'-based managers are not atomised, but aggregated in global 'investment villages'. Further, there is some evidence that major fund holders are using their 'muscle' to leverage the behaviour of boards in search of improvements in effectiveness (Bhojraj & Sengupta, 2003), but this same evidence also suggests problems with other performance measures. Chief amongst several issues, institutional shareholders suffer from a corporate form of disassociated multiple personality disorder, since their small shareholders require them to monitor corporates on their behalf, whilst at the same time they must act as investors whose duty is to maximise the returns for their beneficiaries. Whilst they may be able to strike a balance, conflict and dissociation will occur where they take a long-term view of their positions and incur expense in intervening in management under-performance, whilst simultaneously as investors enjoying the freedom to incur the least expense in intervening in management to secure the best return for their beneficiaries. These roles are not easily reconcilable and fail by dint of a compound agency problem (Short & Keasey, 1997). Thus, shareholders in practice fail to monitor both directors and managers who should act on behalf of shareholders under the current governance arrangements.

As an alternative to hierarchical governance, market discipline is highly valued by the principal-agent theorists. The hostile takeover movement, the so called market for corporate control, reached a peak in the US and the UK in the 1980s, but was quickly ended at the end of the 1980s due to the collapse of the junk bond market, resistance by managers, political pressure and an economic downturn. Market governance has been seriously criticised as less effective and too costly in improving corporate performance and promoting long-run wealth (Bishop, 1994; Latham, 1999; Parkinson, 1995; Pound, 1993). Stock market and share price are in fact less unbiased and useful indicators of the 'fundamentals' of corporate performance, rather it often reflects shareholders' psychology, guessing, changing moods and prejudices, and thus routinely misprices assets (Keynes, 1936; Shiller, 1989).

Furthermore, the conception of economic rationality and efficiency has been criticised as too narrow and too static. Economic logic is the prevailing core assumption in current corporate governance analysis. The principal-agent or finance model is deeply rooted in market efficiency theory originated in both classical and neo-classical economics. The other three corporate governance models, as described above, challenge the 'market-optimum' assumption and propose hierarchical-like governance structures based on various internal monitoring mechanisms. Nevertheless, underpinning all these models is the notion of economic rationality as well. The only difference is that those three models prefer long-term, rather than short-term, corporate performance horizons shared together by shareholders or stakeholders with managers. Although some aspects of the stakeholder theory emphasise corporate ethical behaviour and social responsibility, the main purpose of this model is instrumentalist, based on the principles of economic rationality and efficiency such as managerial strategies and long-term business success.

The main criticism of the economic logic as an explanation of social phenomena is that it presupposes pure economic conditions and a level playing field in considering rational selections in a corporation, under which the selections are simplified and isolated from other social processes such as social (non-economic) relationships, structural power and institutional contexts (Roy, 1997). It is also arguable that economic rationality and efficiency is an overly narrow conception which loses insight of the complexity and many-sides of rationality as well as inevitable irrationality in human life (Rescher, 1988). Further, empirical evidence in corporate governance has shown that there is no rationality of action or some absolute standard of efficiency at all, nor one most efficient mode of organisation and optimal governance structure in the world, nor only one way to pursue organisational goals.



The rules by which realities are constructed can be negotiated and changed as the outcome of the social interactions between key players/actors such as managers, their corporations and government agencies (Fligstein, 1990).

The essential problem with the dominant economic logic in governance is that 'a static conception of governance ... ignores the continuous and ongoing interaction between choices made, and the context into which choices are embedded' (Mueller, 1995). Obviously, the static approach in corporate governance analysis presupposes and inherits *a priori* principles, ready-made concepts and taken-for-granted notions, such as principal-agent relationships, market efficiency, and hierarchical structure, and then identifies, classifies and simplifies the complex practices of corporate governance with these conceptual templates for analysis and explanation. In so doing, the dynamic practice and lived experiences of corporate governance are forced to fit theoretical models, which become increasingly abstracted, isolated, fixed, endured, and finally static and dogmatic.

The theoretical foundation of representationalism to which current corporate governance analyses implicitly commit has been seriously challenged in recent years. There are two basic theoretical obsessions intrinsically embedded in the static approach to corporate governance. The first is the presupposition of a concrete, enduring and permanent corporate reality which is 'out there' beyond human cognition, perceptions, beliefs and biases. It is this relatively static entity that enables our concepts and theories to genuinely represent it. The second assertion is that our minds can accurately or approximately copy and 'mirror' the external reality. Our knowledge is true or nearly true because it corresponds to the outside world through our 'scientific' minds and appropriately designed methodology. Therefore, the static approach in corporate governance is firmly underpinned by epistemological representationalism.

Representationalism has been criticised as 'God's eye view of the world' (Putnam, 1981) as a black-boxing idea and self-evident truth. If representation must be taken as a given, what does the representation actually represent? How can we prove the claimed 'objective' representation beyond our human representation, the 'subjective'? In other words, how can we verify the correspondence between the world and our minds if they must be separated? This is an age-old untestable question (von Glasersfeld, 1991), an insoluble ontological issue, which undermines the creditability of representationalist claims. More fundamentally, the presupposed fixed 'being' (entity) as an ontological foundation on which the ideology of representation completely relies is questionable. It has been revealed in the modern scientific revolution, particularly the new physics, that there is not firm foundation of substance (being), and that matter and energy are interchangeable (Jungerman, 2000; Rescher, 1996). There are also some logical problems with a 'being' ontology (substantialism). For example, if substance is fixed, how can substance act or destabilise itself and bring new states of affair into itself? If substance exists permanently, the future must be the same as the past. However, this is counter-intuitive: future things do not yet exist (Rescher, 1996), and the future is uncertain and unpredictable rather than the reverse. Since substance philosophy cannot overcome those inherent difficulties and problems, an alternative process metaphysics based on 'becoming' ontology offers us a better understand of social reality in general and corporate governance in particular.

A PROCESS PHILOSOPHY APPROACH TO CORPORATE GOVERNANCE

The Western intellectual tradition is underpinned by two competing pre-Socratic cosmologies that continue to shape intellectual priorities and orientations. Heraclitus emphasised the primacy of a fluxing, changeable and emergent world, whilst Parmenides,



Heraclitus's successor, insisted upon the permanent and unchangeable nature of reality. Heraclitus emphasised reality as inclusively processual while Parmenides privileged a homeostatic and entitative conception of reality. Although there is clear evidence that there has been a resurgence of interest in Heraclitean-type thinking in recent years, it is the Parmenidean-inspired mindset ('substantialism' in stead of 'processism' - (Rescher, 1996) that has emphatically prevailed over the past five hundred years.

This privileging of a homeostatic and entitative conception of reality generates an attitude that assumes the possibility and desirability of symbolically representing the diverse aspects of our phenomenal experiences using an established and atemporal repository of terms and conceptual categories for the purposes of classification and description. For it is only when portions of reality are assumed to be stable and hence fixable in space-time that they can be adequately represented by symbols, words and concepts. A representationalist epistemology thus orients our thinking towards *outcomes* and *end-states* rather than on the processes of change themselves. It is this basic epistemological assumption which provides the inspiration for the scientific obsession with precision, accuracy and parsimony in representing and explaining social and material phenomena, including the practices of corporate governance. These social phenomena are regarded as relatively enduring, concrete and observable entities which can straightforwardly be subjected to factor analysis. The consequences of this on the direction which research and theorising in the field of corporate governance has taken must not be underestimated. Indeed, it has instilled a set of instinctive 'readinesses' (Vickers, 1984) amongst management academics to construe theories as being straightforwardly 'about' an externally existing and pre-ordered reality. This predisposition explains the intellectual orientation of the orthodox approach to analyses of corporate governance. It justifies prevalent notions such as 'the marvel of the market', 'the finance notion of control', 'the principal-agent relationship', 'nexus of contracts', 'self-regulation', and 'internal monitoring' as relatively enduring and universally valid conceptual entities which are taken for granted and seemingly theoretically unproblematic.

With the awareness of the fallacy of representationalism, all the justifications of the theoretical entities about corporate governance, including the preoccupied concepts of market governance and hierarchical governance and their related assumptions, must consequently be questionable. If the corporate governance issues cannot simply be interpreted by an economic logic founded upon a static and entitative conception of reality, then, an alternative processual approach, we believe, can better describe and explain corporate governance practice.

A process approach must not be equated with the commonsensical idea of the process that an individual or a system as a separate and solid entity undergoes in transition from one place to another caused linearly by external forces or power. Rather, it is a metaphysical orientation that emphasises an ontological primacy in the '*becoming*' of thing; that sees things as always momentarily stabilised outcomes: 'stability waves in a sea of process' (Rescher, 1996). This process ontology promotes a dispersive view of reality as a heterogeneous concatenation of atomic event-occurrences that cannot be comprehensively captured by static symbols and representations. For process philosophers (Bergson, 1903; James, 1909, 1911; Whitehead, 1929/1978, 1933/1961), the principle of process such as movement, change, indeterminacy and probability is the fundamental feature of reality. Process and modes of change rather than things and fixed stabilities best represent our encounters with and in the natural and social world. The immediate and dynamic intuition of living experience is more faithful to reality than the conceptual work of thought, for thought can only deal with stable things. The symbolic system of representation (e.g. language) is always inadequate in capturing the real world, since much of what we experience remains tacit and



unspeakable. Thus, processes cannot be described or explained in terms of non-processual elements.

What the processual approach offers is an opportunity to view the corporation in its original sense as a human association and social construct, a social world that is fully constituent of human minds and direct experiences in addition to physical materials, which are fundamentally processual in nature. This worldview has no pre-given, neutral and fixed essence and meaning unless it is individually experienced and understood and collectively perceived and constructed. It has its own logic and intrinsic value embedded in its social processes characterised by inter-relatedness, systemic-wholeness and periodic-historicity. What the processual approach offers is the option to turn our attention away from the theoretical abstraction of governance models to the fundamental human experience and practice of governing processes. It affords us the means to develop keen sensitivity and awareness of the subtle and complex governing relationships and forces, the tacit and explicit knowledge generated in direct and indirect experiences, the firm-specific and contextual-dependent governing problems and their pragmatic solutions. It fully accommodates the rational and irrational, conscious and intuitive sides of social attitudes and behaviours, and the ceaseless and endless search for the reflective and renewable understanding of governance practices for continuous improvements.

APPLICATIONS: CORPORATE GOVERNANCE AS SELF-GENERATING ORDER

The 'true' and 'objective' representation of a fixed corporate reality in current corporate governance theory is misleading, since, 'truth' and 'objectivity' are in of themselves relative constructs around which scientific and pseudo-scientific debate frequently rages (e.g. there are several different 'truths' about global warming, constructed by different groups of scientists, and exploited differentially by different governments). This is particularly so in social realities such as corporate governance for even the standing of a 'fixed' legal entity is may be subject to change as a result of a political process. The distinctiveness of the social reality from the natural world is that it is fully composed of human minds (conscious and unconscious) and ideas (practical and theoretical), which are the most basic elements of the social world, and from which our attitudes, behaviours, actions, social relations and social conventions derive and are generated. Since mental activities are always in flux (Rescher, 1996): 105-118) and social reality as mind-composed and mind-mediated is, fundamentally, processual rather than substantial. Any perceived enduring pattern or social stability in practice are, relative in themselves (i.e. temporary in history and during a period), and subject to manipulation and collective maintenance.

Hence, in a truly processual sense, corporate governance is a process of governing which varies continuously and emerges from social interaction. The current crop of governance models are evidently unsupported because they are simplified abstractions filtering out the concrete experiences and complex dynamics of governing practice, based upon historical 'snapshots' taken from the continually moving and flowing processes of governance that is moving towards an uncertain future). Rather than searching for general, universal and timeless principles (Porter, 1991), corporate governance theorists would do better to become aware of the sensitivity of time, process and history (Tsoukas, 2001), that is, the actual workings of reality where ambiguous perceptions, individualistic understandings, local contingencies, pragmatic actions and solutions, rational and irrational behaviours prevail.

The concepts of 'spontaneous order' (von Hayek, 1982) and 'emergent pattern' (Morgan, 1997) better than any fixed notions describe the fluid character of corporate governance practice. Social systems are intrinsically open to diversities of individual actions, since



individual actions depend on individual perceptions and understandings, which are inextricably bounded with individual properties of experiences (Sayer, 1984; Tsoukas, 1992, 1994) ('subject-referring properties' (Taylor, 1985)). Individual experiences cannot be exactly repeated over time and across contexts, and individuals are in the process of continuous learning, developing and interacting with others. Hence, self-understandings and self-interpretations as both responses to local contingencies and 'enactment' of environments (i.e. interpreting whatever they think their environments are or consist of - (Weick, 1977, 1979) are necessarily implicated in defining individual actions. This eventually means that under close scrutiny, individual actions and behaviours are self-governed patterns that emerge from a combination of their own historical experiences, current understandings, local conditions and multiple possibilities. This corresponds to the process philosophy's metaphor of 'organism' that has its own self-determined driving forces, which constitutes an organic realm as essentially a process intrinsically driven by the organic life itself (Bergson, 1903, 1911). Humans experience our life-processes in our own activities and in our own acts of free will, rather than being driven and determined by external forces. This means that the emergent patterns of self-governance are not directly imposed from outside such as through hierarchical orders or through predetermined logic (Morgan, 1997): 266), but through self-determination (Frankl, 1959). Thus, power (essentially, governance) is not a possessed, fixed and abstracted thing, a sense of imposed domination and centralisation (Foucault, 1979). Rather, it must be exercised, existent in relationships and expressed in actions. Power as exercised is not simply an obligation or a prohibition on those who 'do not have power'; it is manifest in the reaction to and reflection of the given pressure, in their attitudes, willing and intent. The outcome of power and governance is transmitted by them and through them in the process of obeying, disobeying, negotiating, debating, and compromising. This suggests that patterns of governance are only dynamically emergent and in a continuous process of 'becoming'. External forces and pressures are only possibly influential on individual perceptions and reactions, as one of the elements of individual 'enactment' in their environments. However, it is important to recognise that when self-governance is defined as spontaneously emergent and individually distinctive, it does not mean that it is isolated from social processes. On the contrary, as social beings, individuals' understandings and interpretations are the results of social interactions through communications, observations, learning and thinking. Hence, self-generating pattern and spontaneous order in a society and in the corporation are largely characterised (or coloured) by collectively constructed pattern and order through more or less shared values, beliefs, cultures, conventions, habits, negotiated meanings, compromised actions, *inter alia* (Berger & Luckmann, 1966).

Given the subjectivity of meaning-generations and mind-dependence of social actions, corporate governance should not be understood as pre-defined in the context of pre-designed structures, fixed and unchangeable entities, imposed and externalised order; rather it should be generated from daily experiences and dynamic practices. Thus, belief in corporate governance framework that can be clearly prescribed and specified in rules, regulations or agreements such as corporate laws, company articles and private contracts and then effectively implemented in practice is too simplistic and unnatural. Governance that relies on maintaining a fixed definition by the provision of rules is impossible to practice and sustain in the long-term. No doubt that governance is often embedded within contextual rules for guiding behaviours and actions. However, in the process of application in practice, the interpretation of governing rules is dependent upon the understandings of the individual actors and complex social interactions, for rules can never 'provide for their own interpretation independently of those agencies whose interpretations instantiate, signify or imply them' (Clegg, 1989). Hence, power or governance is a nexus not of contracts,



but of contested meanings and interpretations within multiple possibilities and a socially negotiated order and collectively constructed reality. Governance is not rule-reification and rule-implementation in general, but in the process of rule adapting to local conditions within specific contexts.

Given the emergent and self-generating nature of corporate governance, what theorists and practitioners need to deal with corporate governance issues effectively is not to presuppose a mechanic and machine-like notion of corporate entity that can be governed externally and objectively through the traditionally designed three-tier hierarchical structure of governance or through the market for corporate control. They need to evaluate specific contexts, historical backgrounds, temporary circumstances and contingent factors that condition the process of governing practices and must be sensitive to the processual character of direct experiences, particular interpretations, meaning-generating and sense-making in both collective sense and individual manner. In a processual view, self-governance itself is not a fixed notion either; it is a continuously renewing and innovative pattern. What is needed for theorists and practitioners is not to attempt to stop and freeze or ignore change, but to flow with and facilitate it (Morgan, 1997), leaving room for individual interactions, innovations, judgement and adjustment so as to enable effective actions. Looking inward both intuitively and thoughtfully to address the contingencies and temporary issues at hand and generating order out of chaos from 'inside' is a more effective route to understanding and facilitating corporate governance.

IMPLICATIONS: GOVERNING PROCESS AND THE 'RATIONALITY OF PRACTICE'

One common and underlying assumption of current corporate governance theorising rests on the principle of economic rationality and efficiency. It is implicitly committed to the belief that the optimal selection between shareholder interest maximisation and stakeholder wealth maximisation, between market-disciplinary governance (external control) and hierarchical-shaped governance (internal monitoring), will ultimately depend on cost-benefit calculations and comparisons, the root cause of efficiency. In the conventional analysis, economic rationality is pre-assumed with a sense of universality, permanence, absoluteness and 'taken-for-grantedness'. However, if we look over the history we may immediately find that economy as the dominant principle of governance is due to the rise of capitalism as a social, economic and political system. In protecting capitalist interests, the economic principle is claimed as primary, true and objective, which subsumes all other principles and values such as religion, justice, equality, and humanity. As a self-evident truth, it justifies and legitimates its rationality and emasculates dissent (Foucault, 1974, 1979). It is arguable that the term 'rationality' should not be pre-occupied with an invariant, absolute, objective and perfect value, but should be understood in its *instrumental* and *relative* meaning (Foucault, 1991). "Practices" do not exist without a certain regime of rationality (Foucault, 1991): 79) and forms of rationality are intrinsically inscribed in a regime of practices or systems of practices. Hence, the rationality of practices may involve new ways of envisaging, reviewing, calculating, justifying, graduating, effecting, etc. It is however the local and conditional that makes the practices acceptable at a given moment, and thus, the practices

'... are not just governed by institutions, prescribed by ideologies, guided by pragmatic circumstances—whatever role these elements may actually play—but possess up to a point their own specific regularities, logic, strategy, self-evidence and 'reason'.' (Foucault, 1991: 75)



What this essentially means is that the nature of rationality is individualistic, specific, periodic and thus processual in character. In process philosophy, any process in a period has its own pattern, own function, and own lawful regularity. The fundamental 'reason' of a process is its intrinsic value and inner reality for itself, that is, a certain 'intensity of experience', or 'satisfaction' (Jungerman, 2000): 9-15). Hence, an occasion of experience is 'the self-enjoyment of being one among many, and being one arising out of the composition of many' (Whitehead, 1929/1978): 145). Thus, any eventual experience occurred has its own logic, as a result of interaction of many influential factors incorporated and integrated together. Since experience is one out of many and increasingly becoming many, 'rationality' cannot be a unitary and static one, but multiple, diverse and momentary. As such, the interest of human life, arguably, is neither necessarily rational in theory, nor necessary as one's best pursuit. Our wants and desires are such a kind of satisfaction 'that very much depends on exactly what it is that one happens to want' (Rescher, 1988): 5).

Therefore, when we turn attention from abstracted theories to concrete practices, we find that there are any number of conditional and contingent rationalities, rather than only one universal rationality of economy and efficiency, in corporate governance. Even within the 'pure' economic and business domain, rationality is not as unitary as supposed. For example, the current dominant theory of corporate governance asserts that the shareholder model best represent the reality of corporate governance because by definition, shareholder interest is superior to other stakeholders and the purpose of a corporation is to maximise the wealth of shareholders. However, recent studies have shown that as shareholders' ownership has been separated from managerial control the shareholder model is not realistic because managers have totally dominated the corporations and shareholders' monitoring is less successful (evidenced in both board failure and market failure). More significantly, shareholders are actually reluctant to monitor the corporation since they are much more interested in speculation in stock markets than in genuine participation in corporations. This indicates strongly that the shareholder model is not a representation of the reality of corporate governance practices. The issue is one of control. If we agree (for the sake of debate) that the normative purpose of corporations is to maximise shareholder wealth, whilst staying within the law, then in principle there is nothing wrong with principal-agent theory, since principals expect agents to fulfil their 'normative' duty. Provided agents stay within the law and bring in returns approximating to principals' expectations, then the shareholder model is legitimate. It is, however, generally not efficient – agents satisfice principals utilities to accommodate their own – and it is increasingly irrelevant since the reality is that

'the financial vitality of the corporation and the value of the company shares is in the hands of the directors and managers of the firm', and 'directors, not shareholders, are charged with the duty to manage the firm.' (Sullivan & Conlon, 1997)

This is to say that in practice management has autonomy and judgment in corporate business operation independently of shareholders and shareholders have no rights to interfere with business affairs. Indeed, this was a general trend of the twentieth century in the Anglo-American corporate system, particularly in the USA, what is popularly termed 'managerialism' (Chandler, 1977). In this case, the theoretical rationality of shareholder interest has given way to the practical rationality of managerialism, and all within the bounds of law and tradition!



The problem of unitary rationality in corporate governance can also be found from the claims of the stakeholder theory. There are two strong propositions upholding the challenging stakeholder model. One is that the number, range and influence of stakeholder groups have increased significantly over past few decades and thus management strategy must take account of stakeholders' interest to ensure a company's profitability and long-term success (Freeman, 1984). The other proposition is that if management take care of stakeholders the corporation can have more success in financial performance, efficiency and competition (Cadbury, 1992; Campbell, 1997; Plender, 1997). Based on these arguments instrumental stakeholder theory claims to represent the corporate reality and the stakeholding rationality. However, empirical studies so far do not support those assumptions without question. For example, one study from 50 industrial Fortune 500 firms found no evidence (Molz, 1995) linking pluralistic control to improvements in the firms' 'social performance'; i.e. the number of stakeholder groups doesn't matter. Furthermore, the range and number of stakeholder groups so easily vilified by critics (Coelho, McClure, & Spry, 2003a), is limited by the theory's more moderate advocates (Post, 2003b), suggesting strongly a narrowing of the original conception. With respect to the second proposition stated above, a number of investigations on the relationship between corporate social performance (CSP) and corporate financial performance (CFP) find inconclusive evidence and very limited positive relationship: only about a half of all studies from the 1970s to the 1990s show a positive relationship and nearly a half show no effect or negative (Griffin & Mahon, 1997). Based on the above counter-evidence, it is reasonable to question the reliability of universal stakeholding rationality and the creditability of the instrumental stakeholder theory. Hence, the justification for stakeholding theory may not simply rely on economic rationality, it may come from our belief and emotion (Stoney & Winstanley, 2001). The current fierce debate over the justification for stakeholding (Coelho et al., 2003a; Coelho, McClure, & Spry, 2003b; Post, 2003a, b) indicates that 'there is no rational way of securing a consensus for it in our culture', since

'... all these premises are ultimately expressions of preference, attitude or feeling. Clearly many of the rationales provided for stakeholding are post hoc rationalisations of our fundamental principles and premises to which we are emotionally attached (for reasons such as our upbringing, life experiences, etc.) but for which we have no rational basis.'
(Stoney & Winstanley, 2001): 698

The rationality of practice has significant implications for corporate governance theorising and practice. Corporate governance is not simply a fixed legitimate thing vested in specific agency or position in accordance with an economic rationality to justify its power, domination and subordination, nor with a pre-designed and a universally claimed governance structure, form or mechanism working ideally for economic efficiency. Rather, it is an activity and practice inherently indeterminate and unstable in line with the multiplicity, contingency and 'momentariness' of practical reasons. For example, either hierarchical forms or market disciplines of corporate governance is not pre-supposed theoretically rational and intrinsically ideal; rather it is historically developed in specific conditions and backgrounds. Hierarchical control and other structural patterns 'are likely to develop as different team members, functions, or activities take a leading role, or as different priorities create a focus of attention'. They are 'temporary conditions or outcomes', 'no more than "snapshot points" on a self-organising journey' (Morgan, 1997): 267). Similarly, the development of shareholding or stakeholding is not purely dependent on the assumed rationality of economic efficiency as mentioned above, it has been conditioned by or in some



ideologies, faith, emotion, social movement and social concern in a particular time. What is needed in corporate governance practice is not to work with an abstracted universal rationality, but to sensitise and care about individual differences, their specific situations, their understandings ('rational' and 'irrational'), their collective culture, values, beliefs, and habits, so as to fashion out fluid models and temporary patterns of rationality workable and acceptable in the practice. Thus, in practice there are many governing forms and practical models workable (or not workable) in line with many specific rationalities. It is notable that many hybrid or innovative forms distinctive from the traditional ones are continually emerging. It is unrealistic and naïve to subscribe to and insist on some universal one, to forced-fit the practices into theoretical models.

CONCLUDING REMARKS: FROM GOVERNANCE TO GOVERNING PROCESS

Currently dominant theories of corporate governance, despite their contrasting and competing perspectives, remain trapped in the same mode of thinking which assumes that the reality of governance practice should be force-fitted to idealised models. However, such an approach is not likely to be applied in practice and would not improve corporate governance if it did, and

'The alternative approach - of adapting the model to reality rather than reality to the model - deserves equal consideration' (Kay & Silberston, 1995) 86).

The fundamental problem with the current analyses of corporate governance is that their perspectives are constructed through a purely homeostatic approach (Kirkbride & Letza, 2004) that ignores the continuous interaction between choices made and their specific contexts, and the continuous flow of corporate governance practices including especially issues of precedence, personal incentives, individual perceptions, and societal approval. Although the competing models may claim that their perspectives are based on corporate governance practice and drawn from observations and investigations, there is, in fact, little evidence of their theoretical viability. The main reason for this is quite simply that such research and analyses rely upon a static and entitative view of reality which presupposes that situations, definitions and contexts remain stable and are hence not subjected to the necessary vagaries of change and interpretation.

Thus, they tend to deal only with abstract conceptual frameworks and pre-given assumptions as well as *a priori* principles rather than on discrete empirical factuality, continuity and radical experiences. The preoccupation is thus on consistency rather than on relevance. Taking their hypothetical and theoretically established 'entities' and 'generative mechanisms' as ontologically unproblematic, they justify their theses by insisting that their perspectives are truthful in so far as they accurately represent the 'objective' realities of corporate governance practice. By so doing, they commit to 'the fallacy of misplaced concreteness': mistaking theories for reality itself (Whitehead, 1929/1978, 1933/1961).

We argue that corporate governance cannot be viewed as a pre-designed, universalised and fixed model, rather, it is a process of governing, an emergent pattern continuously generated from complex social interactions in historical and contextual specifications. It is an ongoing reality-constituting and reality-maintaining activity in which all participants both inside and outside corporations actively participate in shaping and reshaping perceptions and priorities. In this sense, principles, assumptions, issues, problems and solutions cannot be interpreted as pre-given, objective and taken-for-granted. They are always in the process of constructing, reconstructing, changing and renewing. We thus suggest that to



comprehend corporate governance practice should not attempt to subscribe to theoretical linearity, extremity and absoluteness, and ignore the dynamics and flexibility of human minds, character, behaviours and social interactions. What is needed is to draw attention to and understand the 'rationality of practice', the diverse responses to localised requirements and the continually emerged governing pattern, having its own logic and intrinsic value and acceptable at a given moment. A significant inspiration for 'governors' in practice is an 'art of governance' (Foucault, 1974), an art 'which concerns all and which touches each' and 'which presupposes thought' (Burchell, Gordon, & Miller, 1991). Human minds, thought and ideas enjoy real power in the construction and change of social reality and governance. An art of governance is, in contrast to the 'science' of governance, to work with the invented and changeable ideas, appreciate different viewpoints, respect distinctive ways of doing things, set fluid targets, take flexible measures and solutions, adjust and readjust strategies and techniques. Governance is a non-linear and unstable equilibrium. It is to prepare for change, flow with change, and forward to change.

The term 'governing' as a descriptive action verb is better than the static noun 'governance' as the intended description of governing activities in continuing processes, 'here and now', rather than the abstracted description of any end-state and outcome of activities, 'there and then'. 'Governing' directs our attention to what is emerging and happening in practice, what is being done and relating to people involved in specific governing processes, and what people are directly experiencing, ideally perceiving, and socially communicating and interacting. It avoids directing interest to abstracted theorising and modelling. Above all else, governance suggests the past, whereas governing is firmly in the 'here and now', albeit with one eye on a multiplicity of uncertain futures.

FUTURE RESEARCH DIRECTIONS

Perhaps the major issue in corporate governance research stems from our limited understanding of what really goes on in directors' minds and inside boardrooms – the *fields*, *symbolic capital* and *habitus* that comprise the *practice* (Bourdieu, 1984) of corporate governance. Current theories focus upon external impacts based around a static view of the corporate entity. Conventional models do not look at the process of governing as the evolving sum of experiences of those who govern. Related to this is a research issue that focuses upon developing a deeper understanding of directors' knowledge, experience and skills, and the effects of these upon behavior, particularly in decision making processes. Some of this type of research has occurred (Leblanc & Gillies, 2005; McNulty, Roberts, & Stiles, 2005), but its findings whilst valuable are often limited by methodology focused on variance analysis, and as such are far from definitive or significant. Such research is also important if we are to build a picture of the state and nature of the 'talent pool'. Also we must recognise in all of this that governance does not take place in a vacuum; context is critical, and our accounts of governing must in turn account for the influence of politics, polity, culture, economics and the natural environment.

These related issues reflect a renewed interest in the 'practice turn' in organisation and management studies (Schatzki, Knorr-Cetina, & von Savigny, 2001), particularly in what key organisation members do to realise strategy. An approach that focuses upon process will allow the research community to fully and properly understand the complexities of governing, and to assess the implementation of best practice or deep causation in decision making.



METHODOLOGICAL ISSUES

At the heart of this research agenda is process, which presents to us a methodological issue, since much of extant governance theory is derived from the traditional 'variance approach' to social science (Mohr, 1982). This approach focuses on studying fixed entities with varying attributes (which have a single meaning over time), and which only 'synopsizes' reality (Tsoukas & Chia, 2002). Explanations are based upon necessary and sufficient causality, and upon efficient causality. The generality of theory derived from this approach depends upon uniformity across contexts. Time ordering among independent variables is not relevant and the emphasis of such work is on immediate causation. This approach to theory development does not accommodate all types of forces that influence the process of governance, and the research strategies used focus upon deterministic causation (Van de Ven & Poole, 2005). This approach cannot explain phenomena that

'encompass continuous and discontinuous causation, critical incidents, contextual effects, and the effects of formative patterns' (Poole, Van de Ven, Dooley, & Holmes, 2000): 4).

Research in corporate governance requires an approach that will clarify similarities and differences among theories, in order to facilitate theoretical integration, and to generate a comprehensive understanding of governance. This requires a rigorous epistemological base, built upon an ontology that is more in keeping with understanding governing processes. We argue that the requirement is for an approach that accommodates a 'fluxful', changeable and emergent post-modern world, emphasizing reality as inclusively processual. A processual approach acknowledges that corporate governance practice around the world developed and continues to develop in a variety of unique cultural, historical and social circumstances.

In this approach, explanations of events would be based on necessary causality, as well as final (goal), formal (structure) and efficient causality, which means that explanations would be layered and incorporate both proximal and distal causation. This is because such explanations recognize that change and interconnectedness are predominant characteristics of nature. Generality depends on versatility across cases and time, and time ordering is paramount. What emerges from such an approach is a process study narrating the emergence of the social construction of governance (Van de Ven & Poole, 2005).

Well specified though they may be, many of the 'variance theoretical' papers are based upon an analysis of corporate financial data. Consequently, we need more evidence from acts of governing rather than the output from such acts. If we are to develop a deeper understanding of governance, then we need to understand directors as well as the artifacts that they produce. In other words our research designs must capture data about the process of corporate direction over time (Ancona, Okhuysen, & Perlow, 2001). Capturing time-oriented action leads to a focus on events, which represent a temporarily stable picture of individual and collective actions or experience, and which inevitably change the context in which processes occur. Developing process studies of governance requires researchers to intimately observe the actions and interactions of organisation members in the real-time instantiation of governing processes, through deploying ethnographic and participant observer methods in order to access and generate data (Boden, 1990). Such methods enable the researcher to identify events; characterize process sequences and their properties over time; test for temporal dependencies in process sequences; evaluate hypotheses of formal and final causality; recognize coherent patterns that integrate narratives; and evaluate development models (Poole et al., 2000: 92). However, the data produced by such approaches is more complex than the norm, requiring that we employ different approaches



to its analysis, if we are to discover patterns in governing processes, and to develop grounded explanations of these processes (Poole et al., 2000: 5).

FINAL NOTES

Our current *knowledge* of corporate governance and responsibility is limited, mainly because of ideological posturing in favour of shareholder or stakeholder primacy that goes back to the 1930s and beyond. As a consequence, *action* in pursuit of improved governance in response to public concern is similarly often ideologically limited. Carter & Lorsch (2004) call for a return to the 'drawing board' for corporate governance in order that practice reflects the complex world. Reflecting complexity requires that we understand the practice (Leblanc & Gillies, 2005) of governance and the processes that comprise this practice. This in turn requires that we researchers too should return to the drawing board seeking deeper and more meaningful evidence from which to inform and improve practice.

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