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NEW AVENUES IN STAKEHOLDER GOVERNANCE

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A COMMENTARY ON Flore Bridoux and J. W. Stoelhorst (2022), "Stakeholder Governance: Solving the Collective Action Problems in Joint Value Creation," ***Acad Mgmt Rev*** 47(2): 214–236,
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ABSTRACT

Bridoux and Stoelhorst (2022) employ Nobel laureate Elinor Ostrom's institutional design principles to develop two models of stakeholder governance. They argue that these "community governance" models will help achieve a fairer distribution of stakeholder value compared with approaches that centralize governance in the hands of management. We identify four characteristics, however, that thwart any straightforward application of these community governance models to business firms: ease of exit; lack of legacy social capital; heterogeneity of interests; and power imbalances. We then conclude, following Ostrom herself, that governance often requires external institutional arrangements that stakeholder theorists have not fully appreciated.

NOTICING THAT BUSINESS managers increasingly face challenges in reconciling the interests of multiple stakeholders, leading management scholars have called for development of a theory of stakeholder governance (Amis et al 2020). "Stakeholder governance" refers to the set of firm-level rules that regulate decisions about the creation, appropriation, and distribution of value to the firm's various stakeholders. These rules help address collective action problems, notably situations where some stakeholders withhold their resources for fear that other

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stakeholders will contribute less – or appropriate more – than their fair share, thereby undermining the collective enterprise. Administering the rules of stakeholder governance requires monitoring the firm's and stakeholders' activities, sanctioning those who take unfair actions, and resolving conflicts among stakeholders.

In a well-received contribution to this discussion in the *Academy of Management Review*, Bridoux and Stoelhorst (2022) present two new "community governance" models of stakeholder governance. In these models, stakeholders *participate in*, and are not merely *subjects of*, stakeholder governance. As such, these models challenge the dominant "hub-and-spoke" model, which centralizes stakeholder governance in the hands of managers. Bridoux and Stoelhorst explicitly root their contribution in the insights of the Nobel prize-winning institutional economist Elinor Ostrom (1990; also see Ostrom 2005), who showed that by following principles of democracy and transparency, the users of common pool resources (CPRs) can overcome the above-mentioned collective action problems and sustainably manage their resources. According to Bridoux and Stoelhorst, the advantage of community governance models over the hub-and-spoke model is that they enable stakeholders to develop the interpersonal trust (trust in each other) and system trust (trust in institutional arrangements) that, in turn, stimulate the cooperation and learning needed to accomplish collective action in complex, dynamic environments.

Challenges to Effective Community Governance

We share the concerns that motivate Bridoux and Stoelhorst's work and see the promise of thinking about more democratic approaches to stakeholder governance. Because business contexts differ from Ostrom's CPR settings in important ways, however, we are skeptical that community governance models based on her principles will be effective in building trust, overcoming collective action problems, and producing fairer distributions of value. There are four characteristics of business settings that Bridoux and Stoelhorst's analysis does not consider which thwart any quick application of Ostrom's community models of stakeholder governance to business firms in a competitive marketplace.

First, stakeholders in business settings enjoy *ease of exit*. The resource users in the communities studied by Ostrom largely could not and would not sell their allotments because there was no market in them and because their histories, identities, and cultures tied them to the resource. By contrast, within business settings, stakeholders often can cease transacting with firms. This changes their calculus of whether to invest in community governance arrangements by introducing consideration of opportunity cost; stakeholders must determine whether investing time and resources into participating in community governance will produce more value for them than would other options, which may require fewer resources and effort. Ease of exit is an important part of the conceptual apparatus of stakeholder theory because it is the ability of stakeholders to exit that disciplines managers to create value for them (Phillips 2003). But while the potential for exit may be an important driver of stakeholder value creation, it also undermines deeper commitments to shared governance.

Ease of exit amplifies other impediments to building trust and achieving collective action through community governance in business settings. One of these impediments, related to the first, is *lack of legacy social capital*. Many of the communities studied by Ostrom stably existed for long periods of time, in some cases hundreds or even thousands of years. These were composed of relatively small numbers of ethnically homogeneous people who engaged in largely the same activities and saw themselves as living in the community in perpetuity. Further, they were characterized by "extensive norms regarding proper behavior" (Ostrom 1990: 88) that facilitated stability among their membership. In contrast, many, if not most relationships in business settings, are established to undertake market transactions, and not necessarily with cooperative motives. These relationships may be impersonal, change with changing business conditions, and are not deeply embedded in shared social histories, traditions, and networks. Under such conditions, and especially when other options are available due to ease of exit, building and maintaining shared governance arrangements becomes less likely.

Establishing and maintaining community governance also may be more difficult in business settings than in CPR management because of *heterogeneity of interests*. In Ostrom's studies, the resource users who effectively managed their CPRs largely engaged in the same activities, possessed similar knowledge and skill sets, and believed that they would suffer significant harm if they did not develop workable institutions. These factors increased their motivation and commitment to establishing and implementing mutually agreeable institutional arrangements.

In contrast, business stakeholders often have heterogeneous and sometimes conflicting interests, and are likely to make different assessments of the value of overcoming conflict and investing in community governance arrangements. Some stakeholders and stakeholder groups often have more to lose than others, or perceive that they do. Further, the members of some stakeholder groups may not even be aware of the interdependence of their interests with those of other stakeholder groups or that their ability to appropriate fair value depends upon the ability of other stakeholder groups to do the same. These factors decrease the likelihood of key stakeholders investing in community governance, particularly when these stakeholders are free to consider other possibilities.

Power imbalances are a final factor that undermines community governance in business settings. Ostrom (1990) found that power symmetry was important to the establishment and sustained implementation of community governance arrangements for CPRs. Consistent with this assumption, stakeholder scholars tend to assume that value will be distributed fairly among stakeholders because markets are efficient, i.e., that firms and stakeholders pay market prices for the factors they purchase from each other because all lack the power to command lower prices (Harrison et al 2010). In markets characterized by low competition, however, this clearly is not the case. In such markets, some stakeholders will have the power to set prices and extract rents, to the detriment of less powerful stakeholders. Meanwhile, the less powerful might accept less than adequate (but still positive) returns because of their inability to exit. (While some stakeholders may enjoy ease of exit as just discussed, not all do and not all the time.) In short, the temptation of powerful stakeholders to extract rents rather than investing in cooperation will be greater in business settings than in most CPR settings.

In a chapter on “institutional failures and fragilities,” Ostrom (1990: 143) provides examples that support these arguments. In one of these, in the Bay of Izmir in Turkey, fishers were unable to develop cooperative institutional arrangements to manage their CPR due to numerous factors, including “the opportunities for quick economic gain, the large number of fishers, [and] the internal division of fishers into distinct sub-groups with conflicting interests” (1990: 145). In another, Sri Lankan farmers were unable to “achieve self-governance” due to internal factors including the fact that the farmers had “recently been recruited to the project and [had] little attachment to the land or one another,” “the extreme diversity of ethnic and cultural backgrounds,” and “the opportunity for wealthier farmers to control water . . .” (1990: 166). In sum, Ostrom found that when CPR conditions approximate those of many business settings, establishing and implementing effective community governance arrangements was difficult.

Addressing the Challenges

Ostrom identified a final, important design principle for addressing such problems. This is the principle of polycentricity, which Bridoux and Stoelhorst (2022: 218) acknowledge but do not employ. Polycentricity involves the nesting of governance arrangements at multiple levels. While Ostrom (1990) focused on the value of nesting in managing complex CPRs (1990: 101, as captured in Bridoux and Stoelhorst 2022: 218), she and her colleagues demonstrated the benefits of polycentricity even in managing simpler CPRs. One major benefit is redundancy. Ostrom and colleagues found that adding layers of governance becomes necessary even under relatively favorable conditions for organizing to address collective action, because resource users often fail to adhere to voluntary governance arrangements, or even to establish them in the first place (Andersson and Ostrom 2008; Ostrom 2005). Andersson and Ostrom (2008: 73) con-clude that:

> All governance institutions are imperfect responses to the challenge of collective-action problems. Because . . . imperfections may exist at any level of governance, we argue that analysts should consider the extent to which complementary back-up institutions exist at higher or lower levels of governance that can help offset some of the imperfections at any one level.

The clear implication of Ostrom’s principle of polycentricity is that while community governance arrangements may be more effective in preventing shirking and rent extraction than the hub-and-spoke model, they will still suffer from these problems unless complemented by external institutional arrangements. The presence of external incentives and accountability mechanisms for a fair distribution of stakeholder-generated value would increase stakeholders' system trust, especially among less powerful stakeholders; and this system trust, in turn, would lead stakeholders to be more willing to invest in relationship-building, thereby producing greater interpersonal trust.

Ostrom's principle of nested enterprises suggests a systems approach to the study of stakeholder governance, one in which the degree of stakeholder fairness is understood not as the product of firm-level governance arrangements alone, but, rather, as the product of the interplay of these arrangements with the many other types of institutional requirements. These could include, for example, statutes regarding the terms of incorporation and board composition, economic and social regulations, and norms developed by industry and professional associations. From this systems perspective, the degree to which community governance arrangements are applicable to business firms depends on things like: whose interests are represented on the board of directors; laws regarding minimum wages, benefits, and conditions for workers; antitrust arrangements that shape the prices and terms offered to customers; and the perceived coherence of different stakeholder interests by stakeholder groups themselves. One can imagine a comparative approach to the study of stakeholder governance that examines how firms in different institutional contexts tailor their governance arrangements to achieve fairer terms for cooperation. This stands in contrast both to the standard hub-and-spoke model, that presumes managers, not institutional systems, can find those terms creatively on their own, and to the community governance approach of Bridoux and Stoelhorst that does not fully integrate the lessons from Ostrom's work.

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