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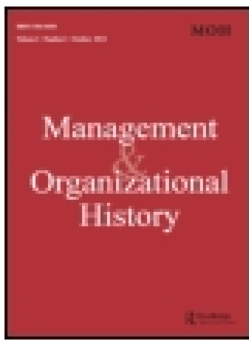

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Captains of industry? Value allocation and the partnering effect of managerial discretion

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ABSTRACT
Can value allocation be left to managerial discretion and does corporate law provide the basis for a balanced stakeholder management and a fair allocation of results? This question is central in an age of inequality. We argue that it can be reappraised by building upon the case of maritime law. Whereas in corporate law, the board is in charge of allocating the results, maritime law stipulates a clear *ex ante* rule according to which it allows a captain to sacrifice some goods to save the ship. This historical 'rule of general averages' emerged in Antiquity. It compels the interested parties to jointly bear costs. This rule makes visible what we call a 'partnering effect' of managerial authority and suggests that corporate law, as it currently stands, lacks a conceptualization of the impacts of managerial discretion and therefore limits the possibility of a fair allocation of results. While management scholars have sought to rethink management theory with a 'view from law', we conclude that law could also be discussed with a view from management history.

KEYWORDS
Stakeholder theory; managerial discretion; value allocation; corporate law; managerial authority; partnering effect; fairness

Today, corporate behavior is implicated in a growth in inequality (Bivens and Mischel 2015). A recent report noted that, in France, for example, the distribution of wealth among the stakeholders of the biggest listed companies has never been so unequal: from 2009 to 2016, the 40 biggest companies redistributed 67.4% of their profits to shareholders in the form of dividends as opposed to only 5.3% to employees (Aubry, Alliot, and Sylvain 2018). Income inequality can have significant effects on organizations (Ni, Qian, and Crilly 2014; Bapuji and Neville 2015), and managerial decisions are recognized as a key factor in income inequality (Cobb 2016) which has reached its highest level ever in the United States (Atkinson, Piketty, and Saez 2011). This situation revives the question of whether value allocation should be normatively ruled by law or left to corporate freedom and managerial discretion.

This is a challenging question for stakeholder theory. Stakeholder theorists emphasize that stakeholders should not be considered in terms of their respective power, but based on the principle of fairness (Buren Van 2001, Phillips 2003). However, they usually refrain from setting clear rules on how to allocate the value created by joint investments in the corporate ventures among the different stakeholders. They argue instead that value allocation is a managerial tool (Scott et al. 2014): managers use value sharing as

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a means of reducing supervision costs, limiting free riding, increasing parties' motivation (Kruse 1996), and retaining their willful participation to foster value creation (Harrison, Bosse, and Phillips 2010). Stakeholder theorists generally consider that it is in the interest of the company to allocate rewards in a neutral and fair way as this determines the possibility of investments from the different constituencies in the company. In this view, the role of corporate law is not to rule on value allocation, but to protect the board, for instance by insulating directors from stakeholder pressure (Blair and Stout 1999; Lan and Heracleous 2010).

Yet, given the increasing level of inequality, a fundamental research question arises: Does corporate law provide the basis for fairness in business? Or could corporate law integrate a more explicit solidarity rule? In this article, we investigate these questions by examining the historical case of maritime law. This historical rule is interesting because, while corporate law leaves value allocation to the discretion of companies' leaders, maritime law adopts the opposite norm: it specifies a clear *ex ante* rule on value sharing. Maritime law vests the captains with great latitude and authority: captains are legally allowed to jettison the goods they are carrying if that will save their vessel from being shipwrecked. Yet, contrary to corporate law, maritime law does not let the captain (or anyone else) decide how the loss is to be shared: it stipulates that the effects of decisions made for the common good should be jointly supported. This rule is called the rule of 'general averages,' as it deals with damages that are general, i.e. decided by the captain and for the collective interest, as opposed to damages that merchants bear privately.

We argue that the historical rule of general averages can enrich the way we theorize fairness in business corporations in important ways. There are clear similarities between the case of the ship and the case of the business corporation: in both cases, there are strong interdependencies between the stakeholders, whose welfare depends on the survival of the ship or the business entity. In both cases, an authority, with important discretion, is entitled to take decisions for the sake of the joint welfare: the captain is responsible for the expedition and his role is to do his best to safeguard the ship and what it conveys. The business leader has also fiduciary duties to run the company for its best interest and long-term success. And for the sake of the common endeavor, both the captain and the business leader have the discretion to make decision that can impact stakeholders' individual wealth. The human capital of employees may also be impacted, either positively or negatively, by managerial decisions. And the latter can also affect shareholder values, as well as other stakeholders' wealth.

While the rule of general averages focuses on the extreme decision of sacrifices, it can shed light on some class of decisions where the managerial decisions impact stakeholders for the common welfare. Typically, when employees are made redundant for economic reasons, their layoffs are meant to enable the firm to survive. Of course, the captain's situation is very different from that of a business manager. But in this article, we would like to show that the analogy can open up the way solidarity is conceptualized in business and suggest new norms for value allocation.

More specifically, the maritime rule leads us to conceptualize what we call the 'partnering effect' of managerial discretion. And this has three main implications. First, our analysis of the rule of general averages illustrates that the impacts of managerial decisions on individual stakeholders could be approached as 'general averages' instead of personal returns. Second, for stakeholder theory, it suggests that a distinction must be made

between those stakeholders who accept managerial authority and others. As the ship captain's decision binds the parties on whose behalf the decision is made, we argue that, in companies, those stakeholders who accept managerial authority (and only them) may be bound together by the partnering effect. Third, our analysis has also normative implications. To date, corporate law has provided directors with the leeway to allocate value. But we suggest that a new view of managerial discretion and its general effects could lead to a more explicit solidarity rule.

The rest of this paper is organized as follows. The first section develops the historical case of maritime law. In order to use the case as the source of our analogy, we map the structural interdependencies of the rule by modeling the 'partnering effect' of the captain's decision. The second section develops the analogy between the ship captain and the corporate leaders, and clarifies both the similarities and dissimilarities of the two domains of maritime and corporate laws. The stakeholder theory views managerial discretion as a central condition both for efficient and fair management. But there are still many debates on the conditions and possibility of fairness in corporations and that is why the analogy with the maritime law can be inspiring. The third section discusses the lessons that can be derived from the analogy. Our study finally opens up new ways to manage value allocation in companies and suggests an agenda for future research on how corporate law could integrate an explicit solidarity rule. It also invites management scholars to reflect on management and management history to rethink corporate law in terms of stakeholder orientation.

Three preliminary remarks are necessary to specify the scope of our research. First, by value allocation, we mean not only the distribution of net corporate income, but also the impacts of management decisions on stakeholders. A company can either issue or buy back shares, and can either provide secure jobs or impose layoffs. Following stakeholder theory, we are thus concerned with all of the potential impacts of management decisions on stakeholders. Second, we do not deal with the general question of fairness or equity in companies, nor do we discuss the various means managers use to allocate value. Instead, we examine how the impacts of managerial discretion need to be apprehended and whether value allocation should be left to managerial discretion or determined by a normative rule. Therefore, our literature review focuses on stakeholder theory, managerial discretion, and value allocation in corporate law. Third, and for the same reasons, we do not make any distinction among corporate leaders. Although there are clear and important distinctions between directors, non-executive directors, and executive officers, we do not distinguish between them because we focus specifically on the corporate freedom to allocate value. Consequently, we refer to 'management' as 'the team of directors and officers who shape board decisions' (Bebchuk, 2005: 842).

1. The case of maritime law: the rule of general averages

To examine how the recognition of an authority affects the principles of fairness, we use the specific example of maritime law. We are particularly interested in one of the rules of maritime law, the so-called 'rule of general averages,' as it concerns the way in which the consequences of the captain's decisions are shared among the various parties involved. This rule explicitly connects the discretionary power of the captain with a specific rule regarding value allocation. The captain's decisions that are taken for the 'common good'

imply rules that contrast with those of corporate law in that they do not leave the allocation of the value to the discretion of the captain.

As we will demonstrate, the historical case is also relevant because it provides a theoretical model of the 'partnering effect' that explains why the rule of general averages is both efficient and fair in relation to the various stakeholders.

1.1 The rule of general averages: historical background

The exact origin of the rule of general averages is unknown, but traces have been found in ancient laws, and it seems to have been applied by most seagoing nations. The rule is apparently an example of *lex maritima*, dating back to the unwritten Rhodian Law of c. 800–900, but actual evidence has only been found from Roman Law onwards.[1] In the late 18th century, the rule was incorporated into the common law of the UK. And in 1801, the definition was clarified in a famous case *Birkley v Presgrave*:

> *"all losses which arise in consequence of extraordinary made or expenses incurred for the preservation of the ship and cargo comes within the general average and must be borne proportionately by all who are interested"* (Jervis 2013, 130)

.

The Glasgow conference in 1860 invited the different maritime societies in all the different European and the USA to discuss the uniformization of the rule and to draw up a code. After important conferences in York (1864) and Antwerp (1877), a code was published with a series of 11 rules dealing with some controversial matters in a conference in Liverpool in 1890.

The York-Antwerp Rules have been revised several times and complemented with different rules of interpretation. But several authors have shown that the rule, which concerns 'general' damages, has been in permanent use from *Lex Rhodia de Jactu* (Rhodian Law of Jettison) to the York-Antwerp Rules of 1994, which are still incorporated into international contracts of carriage today (Frignet 1859; Szramkiewicz 1989; Hatchuel 1997; BIMCO 2002; Tetley 2003; Dusserre 2004).

Under maritime law, the owners of goods are responsible for covering certain maintenance and repair costs, but all those concerned with a maritime shipment must share the costs arising from the damages that are referred to as gross or 'general averages.' General averages correspond to expenditure, investments, or sacrifices made intentionally by the captain in the face of peril at sea or events that endanger the shipment. The York Antwerp Rules state that:

> *"There is a general average act when, and only when, any extraordinary sacrifice or expenditure is intentionally and reasonably made or incurred for the common safety for the purpose of preserving from peril the property involved in a common maritime adventure"* (Rule 2004).

The rules are as follows:

-The captain can make expenditures or sacrifices if they are needed and if they are made in the reasonable interests of ensuring 'the common safety.' In this event, the costs are shared in the common interest of the ship and its cargo.

-A principle of fairness is then applied, obliging all of the people involved in the shipment to share the costs incurred by the captain or the damages suffered by the owner of the sacrificed goods. The owners of the ship and the cargo must share the sacrifice collectively. The contribution of each party is calculated *pro rata* based on the value of their property at the end of the voyage.

The rule and its implementation have raised, of course, a large number of questions, for instance, how to mark out those losses covered by general averages? To clarify the rules, different notions have been introduced, such as the notion of 'direct losses': as only direct losses are accepted as general averages, loss or damages, such as loss of market, sustained by the ship or cargo through delay cannot be admitted as general average. In the case of the *Leitrim* (1902) reported by Jervis (2013, 135), 'the shipowner claimed in general average for the loss of time hire that he had sustained owing to the vessel being off hire while undergoing general average repairs'.

The judge disallowed the claim:

> "*It may be said why on principle should the loss of time not be compensated for where that loss is due to the necessity of repairing damage, itself the subject of general average? I think the answer is that, although there possibly may be cases like the present, the loss of time is common to all the parties interested and all suffer damage by the delay, so that the damage by loss of time may be considered proportionate to the interests and may be left out of consideration.*"

Another question was the methods for dispatching the costs to share among the underwriters: how to assess the values of the cargo and the ship? And how to adjust them? It has become the role of specialized professionals, the average adjusters. But 'average adjustment is a notoriously complicated and time-consuming process'. In 1991, this issue was considered so problematic that a report was commissioned by the Trade and Development Board of the United Nations (UNCTAD 1991).

1.2 General averages: principle of equity

The United Nations report examined the possibility of simplifying general average procedure, but it also investigated '*whether it would be an advantage to abolish the GA altogether and let the loss lie where it falls so that the particular underwriter of the interest concerned bears the burden*' (UNCTAD 1991, 1). Interestingly, the report concluded that those ultimately most concerned recognized the value of leaving the equitable principles of general average undisturbed (UNCTAD 1991, 48).

The main argument in favor of the general averages was clearly equity. The report recalled the conclusion of the former *IUMI committee* in 1948 which 'clearly considered that equity and the historical basis of the institution of GE were the strongest reasons in favour of its retention'. The report referred to equity as being the 'fundamental principle which GE contains'. And it quotes Selmer (1958, 121):

> "*the justice and equity of this idea strikes one immediately. In fact, it is hardly possible to attack general average on point of principle. The distribution appeals so much to the intuitive sense of justice, that everybody must agree that a more fair system cannot be invented.*".

The notion of equity is indeed central in the distribution system underlying the concept of general averages. It was already clear in the Digest, as shown by the Roman jurist Paulus'

quote: "it is perfectly just [authors underlining] that the loss should be partially borne by those who, by the destruction of the property of others, have secured the preservation of their own merchandise' (Digest 14.2.2). As Jervies summarizes: The General averages are '*founded on the principle of equity – in other words, everyone involved in the adventure is in the same boat (both literally and metaphorically) and a sacrifice by one party for the benefit of all should be borne by all (including the one who made the sacrifice or expenditure)*' (Jervis 2013, 130).

1.3 The partnering effect of the captain's discretion

At first sight, the rules seem relatively close to the partnership or corporate framework: the partners or the shareowners embark on a shared enterprise and in the event of losses, these are shared among the participants. However, the rules are quite original. Here, we identify three specificities that will be important in our analogy.

1.3.1. Captains' discretion for the common good

Throughout the voyage, the merchants still own their goods, but they no longer manage them. The captain is entrusted by the different parties (the merchants and the ship owner) to make decision on their goods when necessary. The parties do not transfer their property rights, but transfer control of their goods to the captain, whose mission is to ensure that the goods arrive safe and sound.

The discretion given to the captain is efficient because it ensures unbiased decisions. Thanks to this latitude, the captain can minimize damage. For instance, if one of the merchants issued instructions that influenced the order in which goods were jettisoned, this would be counterproductive, as in practice it would restrict the captain's choices. The captain would be forced to jettison the goods in the prescribed order until the danger was averted. However, the total amount of cargo that was jettisoned would likely not be kept to a minimum, possibly leading to situations in which more goods were jettisoned than was strictly necessary. The captain's discretion means that the safeguarding of the shipment can be maximized in the event of danger, and the collective damages minimized. However, there is a condition necessary for this efficiency to occur: the captain's discretion implies that the parties entrust him with authority on their behalf, and thus abandon their prerogative of control over their goods.

1.3.2. general averages and the "partnering effect"

The merchants are not related to each other *a priori*. Dispatching goods on the same ship is not partnering. However, maritime law views the damages incurred as a result of the decisions of the captain as 'general' instead of personal. This means that the merchants become related in the event that the captain decides to jettison goods. This act brings them together in relation to the goods whose loss saved the ship. The rule of general averages introduces a form of partnership, but *this partnership is generated by the captain's strategic intervention*. Although they did not choose to come together, they are partnered in the sense that *they are jointly liable for the general averages*.

Note that the partnering effect only covers damages resulting from the captain's decisions. If the merchants and the captain had formed a company, they would pool the total proceeds of the sales made at the destination and, after deducting any losses and 'general averages,' would share the profits in proportion to the initial shares of the goods

sold. The rule of general averages does not work in quite the same way. Only the damages caused by the captain's decision to jettison are pooled, and are shared by the merchants in proportion to the *final* value of the goods, not the *initial* value of the goods embarked.

1.3.3. A Solidarity rule

Any damages are to be shared when they result from decisions that are made by the management (captain) for the collective interests. The rule is fair because, in practice, damages are shared between the merchants and because the losses are not borne by the merchants in proportion to the value of the goods on board at the port of embarkation, but in proportion to the *value of the goods at destination*, i.e. to the value of the *goods which have been saved* by the sacrifice. The lost value is not the value of the goods at the outset of the journey, but the value they would have had if they had reached their destination. Note that the rule of general averages does not apply to cases when goods are no longer fit for use or consumption on arrival at their destination. This is considered a 'private' rather than a general average, and there are no grounds for compensating the owner.

In addition, if the merchants had to share the losses in proportion to the initial value of the goods, this would rapidly give rise to unfair situations. Merchants whose goods have been saved and increased in value during the voyage would be favored, while a merchant whose cargo had no value on arrival (e.g. food no longer fit for consumption) could not compensate others. The rule is therefore preferable for each of the merchants, since the sharing of losses helps to limit their individual risk. In terms of probabilities, the expectations of gains are the same, but the shared risk is preferable in terms of risk aversion. The rule whereby losses are shared makes the sacrifice acceptable because of the understanding that it is a collective rather than an arbitrary sacrifice. Hence, it also makes the captain's discretion acceptable.

To summarize, maritime law provides the captain with great discretion: this discretion must be used for common safety and for joint welfare. But maritime law does not provide the captain with excessive leeway. It defines an *ex ante* rule to ensure that strategic discretion is exercised in a fair way. The discretionary power of the captain is legitimate only to the extent that the effects of his/her decisions are shared.

2. An analogy with managerial discretion in business corporations

The captain's situation is very different from that of a business manager, but the analogy is interesting, from a methodological point of view, in terms of thinking about the implications of discretion in relation to value allocation.

Scholars have acknowledged that analogies can effectively support theory building (Oswick, Keenoy, and Grant 2002; Tsoukas 1991). The key idea of analogies is to "compare what is being researched to something else; and in doing so, open up the topic to new perspectives." (Swedberg 2012, 23). Building upon cognitive science, scholars have shown that analogies do not work as simple comparison. Instead they foster the generation and creation of new meaning beyond previously existing similarities:

> "*rather than selecting a particular profile of features or senses from a given set, the metaphoric conjunction of concepts (and their associated domains) creates new features and senses*" (Cornelissen 2005, 757).

In this approach, Ketokivi *et al*. (2017: p.640) suggest that the analogy is not merely a heuristic 'scaffold' to be discarded after it has served its purpose. Just the opposite, the analogy provides the very justification for the hypothesis by supplying an underlying structure for the explanation. An analogy opens up new ways of seeing a phenomenon proceeds with three steps (Cornelissen 2005):

-First, the structure of the source and the target to be seen as parallel are found and the correspondences between the two structures are mapped.

-Second, the elements from the target and source concepts are composed.

-And third, the emergent meaning is formulated, that invites to see the target subject in a new light.

And at the end, Ketokivi *et al*. (2017) propose a methodology to evaluate an analogy. An analogy must meet three criteria: 1) relevance ('Does the analogy offer potential for insight? Is the analogy familiar enough to be understood by the audience?'), 2) structural soundness ('Does the analogy lend itself to multiple related research questions?'), and 3) factual validity ('Does the analogy lend itself to empirical research?').

Following this framework, we want to use the analogy with the ship captain to open up new perspectives on the impacts of corporate leaders. The correspondences with the case of maritime law are important: first, managers in business corporations are expected to decide can be promoted the joint welfare of the corporation as a whole team. Second, managers are given legally and in practice important leeway to make decisions for the sake of the long-term success of the corporation. Third, these decisions can however impact the individual wealth and welfare of stakeholders. We will detail here the generic structure of this domain of managerial discretion to highlight the correspondences with the maritime case.

2.1 The need for equity: a central issue for stakeholder management

The term 'stakeholder' was popularized by Freeman (1984), but the impetus toward stakeholder theory emerged earlier. Freeman defined the stakeholder as '*any group or individual who can affect or is affected by the achievement of the organization's objectives*' (Freeman 1984: 46). It arose from the conviction that management's role goes beyond a profit maximization function and that the responsibilities of managers are far broader in scope than merely maximizing shareholder value (Friedman 1970), extending to the interests and claims of non-stockholding groups (Mitchell, Agle, and Wood 1997). Fundamentally, stakeholder theory views the firm as a 'wealth-creating team' (Kaufman and Englander 2005) and as a nexus of team-specific assets provided by shareholders, managers, employees, and others who hope to profit from team production (Gabrielsson, Huse, and Minichilli 2007).

Management scholars have characterized the various sources of stakeholders' rights. Beyond the legal claims of the first stakeholders ('internal or primary' stakeholders), some stakeholders have no contractual relationships, but nonetheless are critical to the firm's operations (Clarkson 1995). They can claim some rights to the firm's value (Asher, Mahoney, and Mahoney 2005) as they contribute to the wealth-creation process, either through specific investments (Hill and Jones 1992) or because the value of their assets is affected by the fate of the enterprise (Kochan and Rubinstein 2000).

Although there have been numerous debates on whether and how these rights should be recognized contractually and enforced normatively, scholars have mainly considered that it was the duty of management to run the business for the best interest of the corporation. According to the Team Production Theory (Blair and Stout 1999), this is precisely why the corporation was designed in law as a special entity. A firm is created when a series of individual efforts are combined, with a cooperative spirit for a joint output. Specific investments (meaning that they are difficult to recover once committed to the project) must be made by the different gains are inseparable (meaning that it is difficult to attribute any particular portion of the gains to any particular stakeholder). Under these conditions, it is difficult to draft explicit contracts regarding value allocation because it is difficult to decide on the allocation of profits beforehand, as it would reduce incentive, but if the rules for sharing are not decided in advance, there is the risk of very expensive *ex post* bargaining.

To agree on a procedure that all consider fair, what do team members do? 'They form a public corporation' they voluntarily transfer 'authority over the division of production rents and surpluses to an independent body – a mediating hierarchy in the form of the board of directors – that will monitor their efforts and determine how each can best be rewarded for past contributions, as well as be incentivized for future contributions, in the process also guarding against mutual opportunism among the parties' (Lan and Heracleous 2010, 300).

In law, this is consistent with the fiduciary duties directors and executive officers have: they are entrusted with the power to act on behalf and for the benefit not of one particular stakeholder, but for the benefit of the corporation itself. In the UK for instance, the Company Act 2006 says: '*A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole*'. It means that directors and managers can be made accountable to the company if it can be shown that their decisions resulted in a loss for the company. In these conditions, managerial discretion is a key condition for stakeholder management and fair value allocation.

2.2 Managerial discretion: a key condition for stakeholder management

In Team Production Theory, the board is conceived as a third party capable of arbitration between the stakeholders to solve potential conflicts of interest (Hillman and Dalziel 2003; Lan and Heracleous 2010). Its role is to encourage firm-specific investments by making sure that value is allocated in a fair way. To give it the necessary leeway to do that, corporate law aims at protecting directors' discretion in a number of ways. For instance, the business judgment rule grants that directors' decisions cannot be challenged by stakeholders in normal situations, i.e. if they were made in good faith, on an informed basis, and 'in the honest belief that the action taken was in the best interest of the company' (Blair and Stout 1999, 787).

'Managerial discretion can be defined as the latitude of managerial action available to a decision-maker' (Wangrow, Schepker, and Barker 2015), 100), be it latitude in terms of objectives or in terms of actions (Shen and Cho 2005). Although stakeholder theory is not framed explicitly in terms of managerial discretion, its central premise is that managers have the leeway to pay attention to different constituencies and to promote the general

welfare. For instance, stewardship is facilitated when a CEO chairs the board of directors because he/she is then given greater authority and discretionary powers (Donaldson and Davis 1991, Charreaux and Desbrières, 2001).

The literature on managerial discretion has addressed both the antecedents for and the effects of managerial discretion (Hambrick and Finkesltein 1987; Hambrick and Abrahamson 1995). Regarding its antecedents, managerial discretion appears to be constrained not only by the task environment, internal organization, managerial characteristics, and activities (Finkelstein and Peteraf 2007), but also by the broader environment. Industry regulation and state legislation play a noticeable role in managerial discretion (Crossland and Hambrick 2007, 2011). The impacts of managerial discretion have also been studied, especially in relation to executive compensation and firm performance (Wangrow, Schepker, and Barker 2015). However, the dynamics of managerial discretion are rarely analyzed (Phillips et al. 2010).

2.3 The impact of managers' discretion upon stakeholders

Managerial discretion refers to the options available to managers to manage the business in the best interests of the corporation (for the common good). It does not imply the transfer of property rights but, rather, control rights: the parties, while maintaining ownership of their assets, transfer their control rights so that management can use them for a collective strategy. For instance, shareholders own their share but entrust business leaders with the management of their capital. Similarly, workers own their competencies but their employment contract makes them subordinate. They are required to follow managerial prescriptions even when the strategy may impact them either positively (e.g. increase in human capital through learning processes) or negatively (e.g. limited employability).

How does corporate law deal with the heterogeneous impacts of managerial decisions upon stakeholders? *A priori*, corporate law does not prescribe either the way benefits are allocated or the way losses are distributed. We usually see the corporate setting as a solidarity system as stockholders share benefits and losses. But in practice, even among shareholders, there is no complete solidarity rule. The value of the company's shares can vary significantly as a result of managerial decisions, but if one shareholder realizes a significant gain by selling his/her shares, he/she does not share his/her gain with the other shareholders (who do not sell), or with the other stakeholders. There are some important *ex ante* rules however. Some of them, like economic lay-offs and bankruptcy law, concern precisely decisions for the collective interest of the corporation.

In the case of economic lay-offs, labor law proposes a justice principle: severance packages are planned in employment contracts to compensate wage-earners in case of lay-offs. However, if the economic lay-offs are successful, i.e. if they allow the business to prosper, then the future benefits of the company are not considered in the calculation of the compensations. Similarly, in a case of bankruptcy, the law sets some priority rules: secured investors are given clear priorities over the assets compared to unsecured ones (Jackson and Scott 1989). Bankruptcy law however looks more like a general averages system when debt restructuration is decided for the sake of the business survival. This analogy has already been outlined by some authors (Jackson and Scott 1989; Iwicki 1990), but it is limited. In particular, the law allows debt restructuring for the collective interest

even if it causes important losses for some stakeholders. But the law does not explicitly determine those losses should be balanced or shared among them.

Apart from these cases of decisions taken to 'save' the company, we can note that some legislation requires companies to negotiate agreements in relation to profit sharing. In France, when profits allow for an increase in equity, big companies must allocate a portion of the newly created shares to their employees who have made this increase in equity possible (Baghdadi, Bellakhal, and Diaye 2016). However, these are exceptions. There are few rules about how to deal with the possibility of unbalanced distributional outcomes among the parties. And this may be all the more problematic when managers can be influenced to promote the interests of some stakeholder, at the expense of others.

In practice, shareholders are given great power to influence directors, as directors are appointed exclusively by the shareholders (Greenwood 2005; Greenfield 2008; Mayer 2013). Directors are legally accountable to the firm's shareholders (Kaufman and Englander 2005), and thus corporate law does not really 'insulate' the board from shareholder pressure (Millon 2000). More generally, some stakeholders, even if they do not have explicit legal rights, can influence the firm's behavior (Mitchell, Agle, and Wood 1997). Previous studies have described how the value that is created can be appropriated by stakeholders in accordance with their respective bargaining power (Coff 1999; Garcia-Castro and Aguilera 2015).

Given the risks of unbalanced impacts of managerial decisions, different options have been considered in addressing inequality. The first consists of reinforcing managerial discretion against external pressure. Various corporate laws have been amended, such as the constituency statutes that strengthen managers' leeway and allow them to pay attention to interests other than those of the shareholders (Bainbridge 2004). New legal forms of corporations, such as benefit corporations in the US or 'société à mission' in France, have also been introduced in a number of states to provide a 'safe harbor' to allow managers of companies to pursue social or environmental objectives (Bromberger 2011; Cormac, Susan, and Haney 2012a, 2012a; Segrestin, Hatchuel, and Levillain 2020). The alternative is to make managers accountable to various stakeholders (Wells 2002) by extending measures of performance beyond mere shareholder value, broadening fiduciary duties, or broadening the control rights of various parties by allowing them to sit on the board (Asher, Mahoney, and Mahoney 2005).

These proposals have been implemented locally, but have given rise to a number of criticisms. For instance, it has been argued that managers can hardly be asked to pursue all stakeholders' interests, as this could lead to significant control issues (Boatright 1994; Jensen 2001). The need to attend to multiple stakeholders would likely diminish managers' accountability. Any attempt to challenge directors would become illusory, as any decision could be justified in terms of its potential impact on at least one stakeholder (Sternberg 2009).

While managerial discretion has been seen as a fundamental condition for fair value allocation, it is necessary to re-examine how corporate law should handle the impacts of managerial discretion in a fair way.

3. Discussion: the partnering effect in a corporate setting

Maritime law helps us to explore the effects of a ship captain's discretion, as ship captains historically enjoy exceptional powers when at sea (Tarrade 1999). More specifically,

maritime law makes visible a class of decisions that are at the same time critical from an efficiency point of view and problematic in terms of fairness. These decisions are the expenditures or sacrifices managers can be required to make for the commonwealth. This kind of decision has a more general relevance in companies, where managers not only make decisions to 'sacrifice' assets (for instance, through layoffs or restructuring plans), but can also proceed with beneficial actions (for instance, investing in research that develops employees' competencies or making decisions that increase shareholder value). Finally, maritime law has adopted rules that differ fundamentally from those of corporate law regarding value allocation. In the case of companies, there is no norm on how the impacts of managerial decisions on different parties are shared collectively. Corporate law leaves the question of allocation up to the board of directors. On the contrary, maritime law defines *ex ante* rules.

The rule of general averages thus provides important insights into the way in which value is allocated in companies and helps us to analyze the relationship between managerial discretion and fair value allocation. To discuss the 'structural soundness' of the analogy, we develop its theoretical and normative implications for companies along three lines. First, the analogy enriches our view of managerial discretion and makes visible the 'general' impacts of managerial decisions upon stakeholders. Second, we argue that managerial discretion has a 'partnering effect', which leads to discriminate, among the stakeholders, those who are effectively partnered. Third, the analogy challenges both the team production theory of the corporation and corporate law by calling for a solidarity rule.

3.1 Qualifying impact of managerial decisions as general averages

The rule of general averages first invites to see in a new light the impact of managerial decisions upon stakeholders.

Managers, by their hierarchical function and by contract, are entitled to make decisions that may impact the potential (assets or capabilities) of some stakeholders. For instance, managers' decisions can strengthen the human capital of some employees but it can also lead sometimes to a decrease in the employability of employees. They can also increase or decrease the value of the company's shares. As the consequences of their decisions are uncertain, managerial authority is a source of risk, at least for those who submit to their authority.

This source of risk is usually underestimated. It is generally acknowledged that stakeholders can make risky firm-specific investments. For instance, employees might invest in specialized learning processes whose outcomes only have value in their particular team (Rajan and Zingales 1998). In this view, investment decisions are made by individuals and the risks they take derive directly from their investment decisions or from the opportunism of the other team members. However, this view overlooks the fact that the investments of the stakeholders are often not decided by the parties themselves: risks can result from the decisions made by the managers instead of stakeholders themselves.

Our analogy thus suggests that these impacts, either positive or negative, could be considered as 'general averages' since there are made for the benefit of the joint welfare. This is very different from the classical view in business corporation, where neither the negative nor positive impacts of management decisions are usually seen as 'general'

averages. On the contrary, stakeholders generally appropriate the various assets that are (collectively) accumulated by a firm in accordance with their respective bargaining power (Coff 1999).

Should we consider that the approach from maritime law should apply to all impacts of managerial decisions? This would be excessive, especially because the rule for general average is conceived only for exceptional situations of emergency. In practice however, it is important to note that the scope of the rule has been expanded far beyond imminent peril (Tetley 2003, 23): the peril does not need to be imminent, nor is the peril necessary to apply the rule of general averages: "If 'peril' was an essential ingredient of general average, it was reduced in importance in 1890 and 1950 by new dispositions. Peril did not have to be 'immediate', provided that it was 'real and not imaginary'. A potential danger is enough. Since 1994, '*claims may be made for general average expenses at the port of discharge, even when there is no peril*.' In the spirit of this observation, it is perhaps legitimate to consider a range of impacts of managerial decisions on stakeholders as general averages.

And more generally, the role of our analogy is not to make only strict correspondences between our source and target domains. Its role is instead to challenge our way of conceptualizing equity in business decisions. And here, the rule of general averages makes us realize that some stakeholders can be affected by decisions taken for collective purposes, without being considered as general averages. It thus questions whether these impacts are treated in a fair way.

3.2 The 'partnering effect' and a new delimitation of team members

If we consider that positive and negative consequences of managerial decisions could be considered as 'general' rather than 'personal,' then they should be viewed as collective, and shared among the team members. Under these conditions, the partnering effect could also apply in the case of companies. But while the merchants are concerned by sacrifice in maritime law, who are the corporate stakeholders actually concerned by this collective interest?

Here we need to explore further the consequences of the rule to characterize among the stakeholders, who is effectively partnered. Conceptually, the *partnering effect* characterizes the interdependencies generated by the strategic discretion among the stakeholders that submit to hierarchy of managers. While all stakeholders can be impacted by management decisions, not all stakeholders transfer their control rights over their capital to management. Not all of them submit to hierarchy or consent to managerial discretion. We need to distinguish the parties which entitle managers to make decisions on their behalf, from those which keep their control rights and can sue management if they are negatively affected by a management decision.

The partnering effect leads us to suggest that managerial discretion introduces differentiation among stakeholders. Stakeholder theorists have a broader view that includes all parties affected by management. Many typologies seek to account for managerial priorities (or to prioritize parties). For instance, internal/external or primary/secondary stakeholders are often distinguished. Kochan and Rubinstein (2000) come closer to the notion of team production by focusing on the stakeholders 'who put something at risk' and speaking about 'genuine stakeholders.' Other authors suggest different categories, such

as stakewatchers and stakekeepers, and further outline the reciprocal obligations that some stakeholders can have toward the firm (Fassin 2012).

When Blair and Stout (1999) talk of a 'production team,' they are referring to those who contribute, by their specific investment, to the production process. However, to the best of our knowledge, no distinction has been suggested that differentiates stakeholders based on their level of commitment to managerial authority. A distinction must then be made between those stakeholders who transfer their control rights to management and others. In other words, parties who formally accept managerial authority and allow managerial discretion, i.e. give their consent (Phillips 1997), entrust managers, and accept that their resources and capabilities are used in the common interest, are partnered. The other stakeholders can still be affected by the collective action but they continue to manage their resources on their own: they are not concerned by the partnering effect.

This analysis invites to reconsider the perimeter of the team:

-Typically, workers and stockholders will *a priori* be the most partnered stakeholders. Workers, as subordinates, permit management to define the actions that must be performed in doing their jobs. They are clearly subject to managerial discretion. Stockholders formally permit the board to make decisions to develop their capital on their behalf, although here, the legal status is less clear, and we can question whether all shareholders are partnered. Do those shareholders who remain anonymous and whose shareholding is only for a very short period really grant the board strategic discretion?

-Similarly, we could consider some suppliers, subcontractors or service providers, even though they are *a priori* external to the company, as partnered parties if they agree to follow the company's strategic orientations.

3.3 The need for a solidarity rule

Corporate law does not stipulate any general *ex ante* rule regarding the individual impact of managerial decisions. There are some cases of ex ante rules, as we have mentioned, for instance for economic lay-off or bankruptcy. But can we consider these rules as fair in the light of the maritime law?

For instance, some employees can be laid off for economic reasons, that is, their sacrifice is considered necessary for the firm to survive. By law, they receive severance pay, but neither the loss they bear through being laid off nor the future profits of the company are shared. Take the case of an engineer who contributes to the design of a new plant. If he is laid off for economic reasons, and if the plant becomes afterward very profitable, the engineer will be compensated for the lost job, but not for the future value his job could have had.

Here, the rule of general averages provides a compelling reason for challenging the fairness of corporate law. Blair and Stout (1999) assume that corporate law was designed to give directors the leeway to allocate the results in a fair way. The board, as a 'mediating hierarch,' has the duty of promoting the interest of the corporation and of protecting it from various private demands and interests. Yet, as noted earlier, the neutrality of the board is somewhat hypothetical, and rarely verified, as only the shareholders can appoint directors. Theoretically, our analysis shows that team production theory does not conceptualize the impacts of managerial discretion: Corporate law allows for managerial

discretion without requiring any solidarity between those who are affected by the related 'general impacts' of managerial decisions.

Under these conditions, we argue that managerial discretion has a 'partnering effect' and that it normally binds together those stakeholders who actually recognize and accept managerial strategic discretion. Thus, our analogy calls for a solidarity rule to share the impacts of managerial decisions on 'partnered stakeholders.' In practice, this rule would require *ex ante* that any strategy designed by corporate leaders must achieve a balance between employees and shareholders. Management should also be required to report on how they integrate fairness into their strategic thinking. *Ex post*, corporate officers should also be asked to account for the general impacts of their decisions and to organize some form of redistribution when these impacts are not balanced. Some form of redistributive mechanism could be set up.

For instance, when employees are made redundant for economic reasons, their layoffs are meant to enable the firm to survive. The solidarity principle suggests that they should benefit at a later date from the profits that are made possible by their sacrifice. In practice, this could be achieved by a distribution of free shares to enable them to share in future dividends. However, one could also imagine the creation of a 'solidarity fund.' All partnered stakeholders could contribute to this fund when their assets increased. For example, shareholders could be required to contribute a percentage to the fund when they sold their shares if the performance of the firm had increased the value of their shares. This fund could then be used to compensate the partnered parties when they suffered 'general damages.' Such mechanisms need to be further examined and tested. Our intention is not to formulate detailed mechanisms, but to suggest a general duty of fairness on the part of corporate leaders and to suggest that such a duty should be mandated by law.

4. Conclusion

Stakeholder theory suggests that multiple groups have a stake in the activities of the firm and merit consideration in managerial decision-making. It emphasizes the importance of non-stockholder groups to the success of companies. However, not all stakeholders who have legitimate claims receive the consideration they merit. To date, the freedom that managers have to allocate value among stakeholders has remained relatively unchallenged. However, given the inequalities that can be generated by corporate behavior, as scholars, we need to question this freedom and its foundations.

In this paper, we have built upon a historical case to discuss how stakeholder theory and corporate law connect value allocation and managerial discretion. Our aim in using this analogy was to introduce a new way of considering the impacts of managerial discretion. When stakeholders allow managerial discretion by recognizing managerial authority, they are made interdependent by a 'partnering effect' of managerial discretion. Should they not, therefore, jointly support the impacts of managerial decisions made for collective purposes?

Obviously, managerial authority differs from a ship captain's authority, and its legal framework is, of course, highly specific (including rules such as the business judgment rule). The analogy does not build a case for transposing the rule of general averages from maritime law to the corporate setting. Rather, it offers creative theoretical insights

through its contribution to the theorization of the partnering effect of managerial discretion. It also makes visible the implications of managerial discretion that to date have been ignored by both stakeholder theory and corporate law, and it helps us to discuss multiple related research questions such as managerial discretion, stakeholder theory, and solidarity in corporate law. Thus, it provides new insights into how we should conceptualize managerial discretion, and how to differentiate among the stakeholders partnered by strategic managerial discretion and the possible normative implications of this effect.

Our study clearly calls for further research, especially empirical research (the third criterion of factual validity, according to Ketokivi *et al*., (2017)). The rule of general averages suggests a research agenda aimed at identifying the general impacts of managerial decisions that need to be considered and shared. Beyond financial profits, a variety of assets (e.g. cognitive, financial, and relational) would need to be taken into consideration. Here, both evaluation methods and management techniques need to be elaborated, as do the criteria for assessing what is meant by fair (Barney 2020). For instance, the rewards do not need to be allocated equally among stakeholders. They can vary according to the level, length, and importance of the investments made by the various constituencies. New ways to design balanced strategies, to define fairness, and to organize solidarity also need to be explored.

More generally, our study opens up new avenues for research at the crossroads between management and law. By modeling the partnering effect of strategic discretion, our study questions how corporate law conceptualizes management and managerial discretion. The role of law is not to impose new duties or restrictions on the latitude of managers, but it has to build upon a comprehensive view of management to make sure managerial discretion can be exercised in an efficient and legitimate way. It is therefore possible that research in management can help in reframing corporate law. While management scholars have sought to rethink management theory with a 'view from law' (Lan and Heracleous, 2010), they could also question corporate law with a view from management and management history.

Note

1. Justinian's *Digest of Roman Law*: one section relates to general average. The first paragraphs says: '*The Rhodian Law decrees that, if goods are thrown overboard to lighten a ship, all shall make good by contribution that which has been given for all*.' Quoted by (Jervis 2013).

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No potential conflict of interest was reported by the authors.

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