How Corporations Make Decisions

I. Legal Requirements

(a) Increase price of shares

The directors and head executives of corporations in Canada are required by law (either the provincial or federal law under which they are set up (e.g. the federal Canada Business Corporations Act (CBCA)) to "act honestly and in good faith in the best interests of the corporation."

This legal requirement has been defined by courts to mean that the directors and head executives should take actions that will give shareholders the best return on their investment in the corporation.

Shareholders buy shares in a corporation and are the owners of the corporation. Buying a share usually give a shareholder the right to vote for the directors, and the right to vote in other major decisions of the corporation. Corporate directors and head executives are required to do what the shareholders (owners) want, but they also have almost complete power over the day-to-day operations of a corporation.

A "share" (also known as "stock") is bought and sold through stock exchanges (e.g. the Toronto Stock Exchange). Corporations sell shares to raise money for the corporation's activities. In some cases, there is only one shareholder. Small corporations often have only one, or just a few, shareholders. Larger corporations usually have many shareholders, but are also often completely owned by another corporation, and that corporation is, as a result, the only shareholder.

Shareholders usually buy shares with the expectation that they will be able to sell them later at a higher price, and keep the profits. As a result, directors and head executives are legally required to try to increase the price of shares in order to satisfy the expectations of shareholders.

Increasing share price for shareholders is therefore usually the primary goal for directors and head executives, and in many cases directors and head executives also personally desire this goal because they also own shares and want to profit from them.

Some shareholders buy shares with the aim of putting forward a proposal to change the decisions of directors and head executives, or to change the actions of the corporation as a whole, even if the change will mean that the corporation will not make as much profit. If other shareholders approve of the proposal, then the directors and head executives are legally required to change their decisions and/or actions.

For example, several shareholders of several corporations put forward proposals in the 1980s that the corporation should stop operating in South Africa because of the apartheid political system in South Africa did not give blacks and other people of colour any rights, and because the South African government was systematically and violently oppressing people of colour in the country (and elsewhere in southern Africa). Other shareholders of these corporations approved the proposal to stop operating in South Africa, and as a result several corporations stopped operating in the country even though these corporations were making profits there.

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(b) Other legal requirements

Because of the basic legal requirement to increase profit and the price of a corporations shares for shareholders, the concerns of stakeholders (workers, customers, communities, governments, the environment) usually come second to the concerns of shareholders.

However, other laws can require corporations to take into account stakeholders. Labour, environmental, consumer protection, tax and other laws define responsibilities for corporations.

II. Other Factors in Corporate Decision-making

The legal requirements set out above are, like many laws, not enforced 100% of the time. However, other factors corporations may consider usually fit with the framework of the legal requirements, especially if the penalties for breaking the law are large.

Other factors may be defined in a corporation's:

- articles of incorporation (the legal document that defines the basis of the corporation);
- mission statement; and/or
- business plan that sets out goals and strategies for reaching goals.

Like any organization, corporations do not always follow every principle in their mission statement or every step in their business plan. Directors, head executives, and employees may not be as aware as they should be of these principles and steps, or they may disagree with some or all of them, or the principles and steps may be set out to convince shareholders to buy shares in the corporation even though the corporation does not really intend to follow the principles or steps.

Also like any organization, a corporation that operates well compares its outputs (results, contributions, evaluative measures) with its goals (stated or unstated) to determine whether it is reaching (and hopefully even exceeding) its goals.

Often results are also compared with competitors to ensure that the corporation is remaining competitive, keeping its customers and not losing them to competitors. This process is usually called "benchmarking".

Other factors considered by corporate directors and head executives in setting goals and designing strategies to achieve the goals include the following, from general to more specific factors:

- strengths of the corporation
- weaknesses of the corporation
- opportunities for the corporation
- threats or risks for the corporation
- ways of lowering costs
- potential short-term profits
- potential growth leading to increased longer-term profits
- difficulties of achieving goal or undertaking strategy
- difficulty of raising money needed to achieve goal or undertake strategy
- customer's needs and wants
- quality control
- collective agreement (if the employees are unionized, the agreement is negotiated by the union to define the corporation's and the workers' rights and responsibilities)
- threat that a government may require the corporation to do something
- threat that a shareholder may get other shareholders to approve a proposal
- citizen group campaign to get the corporation to do something or stop doing something

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