



# Industrial Structures and Corporate Governance

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# Development of Corporate Governance

# The United States

- > Traditionally seen to represent a model of dispersed ownership
  - But consider recent tech-firms (google, facebook, etc.)
- > Corporate system developed in era of infra-investments
  - Funding requirements were beyond the capability of single shareholders
- > Banking was restricted
  - Political issues (Roe)
  - State banking licenses
  - Glass-Steagall

# US CG Phenomena

- > CEO and board position strong
  - Takeover defences emerged in 1980's
- > Shareholder influence relatively low
  - Shareholder cooperation discouraged
- > Litigation risk real
  - Precedents formed by Delaware law
  - Regulatory capture relevant

# Germany

- > Industrial development post WWI and WWII
- > Labour had strong influence in these efforts
- > Industrial focus was on advanced industries and fine mechanics
- > Labour influence reflected in codetermination efforts

# France

- > In France, corporations have traditionally been financed through operational cash flow and by their shareholders.
  - Traditionally high level of family ownership and control in even large listed corporations
  - See Antoin E. Murphy, Corporate Ownership in France - The Importance of History, ECGI, 2004. Murphy mentioned Michelin, L'Oreal and Peugeot as examples of large corporations with concentrated ownership by families.
- > Long history of government involvement in the economy.
  - Several “national champions” focusing on industries requiring significant research and investment costs.
- > Significant privatization programme
  - Starting in the mid 1980's leading to the government giving up control of over 1000 companies within a decade.

# The United Kingdom

- > Dispersed Ownership model usual
  - Companies were driven to consolidation already in the early 20th century leading to a decrease in family ownership.
  - Liquid capital market and equity financing was usual in connection with corporate acquisitions.
  - Studies have found ownership in listed companies to have remained dispersed largely throughout the 20th century.
  
- > The United Kingdom underwent a significant privatization program in the 1980's
  - Government retaining no shareholdings in the largest 100 companies in the country.  
See Franks, Mayer, Rossi (2006)



# Sweden

- > Concentrated ownership
  - Ownership in the largest listed companies in Sweden remains concentrated. Typically controlling shareholders are families who have held control over a longer period.
  - Control enhancing structures, mainly dual-class shares and pyramid structures, are in use in a large portion of these companies.
- > The industrial development starting with industrialization in the late 19th century, together with the extensive role of bank financing, supported the development of concentrated ownership.
- > Influence of the dominance of social democratic policies during the main part of the 20th century.
  - It has been argued that in Sweden the social democratic agenda in the first part of the 20th century supported the development of corporatist style large companies.

# Finland

- > Concentrated Ownership
  - Government has significant role in corporate ownership
  - Family ownership also important (lesser role than in Sweden)
- > Traditionally bank-focused financial system
  - Bank based industrial groupings
- > Foreign ownership
  - Ownership structures changed with 1) deregulation late 1980's and 2) bank crisis in early 1990's
  - Foreign ownership and governance models introduced



# Institutional Environment

# Factors Affecting Stakeholder Dynamics

- > Industrial Structures
  - Raw material processing / Machinery
  - Precision mechanics / International trade
  - Type of labour requirements
  - Financing requirements
- > Structure of the Economy and Finance
  - Open / closed economy
  - Export reliant economy
  - Sources of financing (cash flow, banks, equity)
- > Political Environment
  - Stability
  - Quality of institutions
  - The political background of US ownership structures (Mark Roe)
  - Social democratic systems → CO (Mark Roe)
  - Political coalitions (Gourevitch & Shinn)
- > Abrupt changes in the economy
  - Economic structures
  - Financial Crisis
  - Effect on bargaining position
  - Effect on vested interests
  - Change in focus

# Factors Affecting Stakeholder Dynamics: Mechanisms

- > Pension System
    - Funded vs. pay-as-you-go
    - Labour interest vs. minority interest
  - > Tax System
    - Treatment of debt vs. equity financing?
    - Treatment of dividends
    - Favouring minority / majority shareholders?
  - > Legal System
    - Ability to Control
- CO system: "Large block necessary / gives satisfactory ROI" (Roe)
  - DO system: "Large block does not give additional control" (Cools)
  - Monitoring Private Benefits of Control
    - CO: Related party transactions
    - DO: Management monitoring systems

# Who owns / controls?

- > Life cycle
  - Founder-entrepreneur
  - Growth phase
  - Stock Exchange traded company
- > Types of Owners
  - Entrepreneurs
  - Families
  - Financial institutions
  - State
  - (Passive) investors
- > Types of Ownership/Control Structures
  - > 1) Dispersed Ownership
    - > Exit enhancing:
      - Disclosure requirements
      - Takeover mechanisms
  - > 2) Concentrated Ownership
    - > Control Enhancing:
      - Share classes
      - Pyramids
      - Cross-shareholdings
      - Foundations (Parked ownership)
      - Regulatory protections

# Political coalitions

<b>Political Coalitions and Governance Outcomes*</b>			
<i>Coalitional Lineup</i>	<i>Winner</i>	<i>Political Coalition Label</i>	<i>Predicted Outcome</i>
<b>“Class Conflict”</b> Owners+managers vs. workers Owners+managers vs. workers	Owners+managers  workers	“Investor”  “Labor”	Diffusion of shareholdings  Blockholding
<b>“Sectoral”</b> Owners vs. managers+workers Owners vs. managers+workers	Managers+workers  Owners	“Corporatist Compromise”  “Oligarchy”	Blockholding  Blockholding
<b>“Property and Voice”</b> Owners+workers vs. managers Owners+workers vs. managers	Owners+workers  Managers	“Transparency”  “Managerism”	Diffusion  Diffusion
*Gourevitch & Shinn (2005), p.23			

# Development of Regulation

- > Corporate governance structures depend on the environment
  - Structures are path dependent
- > Regulation responds to the demands of the environment
  - Different regulatory solutions in different environments
  - Regulation is also subject to path dependence



# Development of Regulation - Mechanisms

- > Concentrated Ownership
  - Strong voice rights
  - Weak management
- > Control Enhancing:
  - Share classes
  - Pyramids
  - Cross-shareholdings
  - Foundations (Parked ownership)
  - Regulatory protections
- > Dispersed Ownership
  - Disclosure regimes
  - Cash flow / Exit rights
  - Takeover mechanisms
  - Weak voice rights
  - Strong management control



# Functional Approach

# A Functional Perspective to CG

*“[F]ive main ways to mitigate shareholders’ collective action problems:*

- 1) Election of a board of directors representing shareholders’ interests, to which the CEO is accountable.*
- 2) When the need arises, a takeover or proxy fight launched by a corporate raider who temporarily concentrates voting power (and/or ownership) in his hands to resolve a crisis, reach an important decision or remove an inefficient manager.*
- 3) Active and continuous monitoring by a large blockholder, who could be a wealthy investor or a financial intermediary, such as a bank, a holding company or a pension fund.*
- 4) Alignment of managerial interests with investors through executive compensation contracts.*
- 5) Clearly defined fiduciary duties for CEOs and the threat of class-action suits that either block corporate decisions that go against investors’ interests, or seek compensation for past actions that have harmed their interests.”*

*Source: CORPORATE GOVERNANCE AND CONTROL; Marco Becht, Patrick Bolton & Alisa Röell (Working Paper 9371; <http://www.nber.org/papers/w9371>)*



# Observations

# Observations

- > CG must be analyzed in the broader institutional context
  - What are the issues in the relevant environment
  - Consider broader set of factors
  - Recognize path dependence and complementary institutions
  - Comparative Institutional Analysis (Masahiko Aoki, Ruth Aguilera & Gregory Jackson, Elinor Ostrom)
  
- > Comparative CG
  - Remains relevant and important
  - Indices can and need to be developed

Thank you for your interest

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