Corporate Governance: An International Review, 2016, 24(3): 172–180

Editorial

Advancing the Corporate Governance Research Agenda

Ruth Aguilera, Chris Florackis* and Hicheon Kim

INTRODUCTION

The last few decades have witnessed an explosion of research on corporate governance from a wide array of academic fields including finance, accounting, management, economics, and sociology (Aguilera, Desender, Bednar, & Lee, 2015; Aguilera & Jackson, 2010; Filatotchev & Boyd, 2009). This rising academic interest in corporate governance has been in part triggered by corporate scandals, public outcry on lavish executive compensation (Dorff, 2014), and perceived irresponsibility of some big banks and corporations in recent years. Nonetheless, there are some enduring reasons why corporate governance has attracted substantial interest in diverse academic fields. Corporate governance plays a fundamental role in allocating resources and responsibilities within and across firms, thereby affecting strategic choices as well as value creation and distribution within individual organizations, alliances, and even across countries. As such, understanding the behavioral and strategic choices and the ultimate performance of organizations, alliances, and countries requires an intimate knowledge of the governance dimensions involved.

Moreover, corporate governance is socially constructed in terms of how it is perceived and legitimately accepted, which in turn reflects and influences the institutional logics[1] embedded in corporate goals and controls (Aguilera et al., 2015). As these norms and beliefs of what acceptable corporate behavior is often differ widely across industries, countries, and regions, and they tend to evolve over time, so do the notion and practices of corporate governance. Thus, the study of norms and practices on corporate governance at a given period of time in a country often entails more than addressing questions on corporate governance from purely economic and legal perspectives, and necessitates instead a broader attention to societal norms, cultural attributes, and ethical values.

*Address for correspondence: Chris Florackis, University of Liverpool, Management School, Department of Economics, Finance and Accounting; Tel. +44 (0)1517953807; Email: c.florackis@liv.ac.uk

Despite the complexity of issues around corporate governance, a disproportionate share of prior work has been conceptualized and guided by agency theory (Shleifer & Vishny, 1997). Since the seminal publication by Berle and Means (1932) recognizing the alienation of ownership from control and its concomitant agency conflicts, a great number of studies in the tradition of agency theory have focused on designing governance mechanisms necessary to prevent the manifestation of agency conflicts and to ensure that the firm operates in the best interests of shareholders. However, the validity of some of their findings and subsequent recommendations have been challenged as the assumptions and theoretical foundations underlying agency theory may be too narrow or even invalid (Aguilera & Jackson, 2003; Davis, Schoorman & Donaldson, 1997; Roberts, McNulty, & Stiles, 2005).

More recent work has sought to relax the assumptions behind agency theory in order to enrich our understanding of corporate governance, particularly as we expand outside the premises of the shareholder value maximization governance model which has characterized the Anglo-Saxon world. We discuss three fruitful implications of the relaxation of agency assumptions.

First, early work on agency theory tends to assume away the significance of the identity of owners, relying on ownership concentration as an indicator of agency conflicts or of monitoring effectiveness. However, research on the relationship between ownership concentration and performance fails to produce consistent findings (Dalton, Daily, Certo, & Roengpitya, 2003). Morck, Wolfenzon, and Yeung (2005) emphasize the potential conflicts between controlling shareholders and minority shareholders.

Studies in management also develop this idea of “conflicting voices” and “principal-principal conflicts” to recognize that different owners may have different preferences and time horizons, and that there may even be conflicts of interests among different owners (Connelly, Tihanyi, Certo, & Hitt, 2010; Desender, Aguilera, Crespi, & García-cestona, 2013;

© 2016 John Wiley & Sons Ltd
doi:10.1111/corg.12167

Dharwadkar, George, & Brandes, 2000; Hautz, Mayer, & Stadler, 2013; Hoskisson, Hitt, Johnson, & Grossman, 2002; Young, Peng, Ahlstrom, Bruton, & Jiang, 2008; Zheng, 2010). Different owners may even be attracted to different firms depending upon value orientation such as prosocial orientation (Zeitoun & Pamini, 2015). This tension gets even more pronounced when the owners are from different countries and in turn equipped with distinct shareholder activism practices as Japanese firms experienced during the rise of hedge fund activism following the Asian crises (Buchanan, Chai, & Deakin, 2014). As a consequence, a richer examination of heterogeneity among owners is necessary for designing and implementing effective governance practices.

In this vein, three articles in this special issue provide focused reviews on specific types of owners. First, Grosman, Okhmatovskiy, and Wright (2016) study an idiosyncratic yet not homogeneous type of owner, the state. They show through an implicit comparison of China and Russia that national political and strategic interests are highly embedded in the firms' governance strategies as well as the type of state capitalism that these countries pursue. Second, McNulty and Nordberg (2016) examine different modes of shareholder engagement on what they refer to as "active ownership." Specifically, they develop a process model of institutional investors' engagement and mutual exchange with managers and other owners, taking a longer-term perspective toward investment in the firm and its affairs. These authors show that psychological ownership is an important dimension in capturing who owners are and in defining how owners and managers relate to each other. Finally, the type of owners will certainly determine the type of board as well as these boards' diversity. This is a missing link that the article by Gabaldon, de Anca, Mateos de Cabo, and Gimeno (2016) is seeking to establish when presenting a systematic discussion of the supply-side and demand-side barriers as well as the mechanisms to overcome these barriers in the under-representation of women on boards.

Second, agency theory maintains that shareholders, not other stakeholders, are residual claimants in the firm (Fama & Jensen, 1983). Residual claimants are supposed to bear residual risks and take all the residual profits left over after the firm satisfies its legal obligations to stakeholders (e.g., interest to creditors, wages to employees, taxes to the state). If, indeed, shareholders are the only residual claimants in the firm, the efforts of maximizing shareholder wealth would enhance firm performance and improve social welfare as well. However, a series of scholars examining the breadth of stakeholders in more detail (Blair, 1995; García-Castro & Aguilera, 2014; Stout, 2012; Zeitoun & Pamini, 2015, to cite just a few) argue that stakeholders, like employees, often make substantial firm-specific investments and bear residual risks as well in the case of insolvency or layoffs. In this case, the efforts of maximizing shareholder wealth alone may distort resource allocation within and across firms, generating unintended consequences at the societal level. Zattoni (2011) introduces a contingency model where he proposes an alignment between stakeholder contributions and ownership rights.

For instance, Srivastav and Hagendorff (2016), in this special issue, point out the problems of viewing shareholders of banks as the only residual claimants and taking a shareholder-focused approach in the banking industry. As banks are highly leveraged, and their liabilities are often guaranteed by the state (or taxpayers), shareholder-focused governance may well subordinate the interests of other stakeholders and exacerbate risk-taking concerns in the banking industry (Srivastav & Hagendorff, 2016). Zalewska (2016) shares similar concerns when she states that structuring bankers' remuneration to maximize shareholder value does not necessarily reduce the systemic risk of the banking sector. Thus, designing and implementing governance mechanisms may entail an assessment of incentives and disincentives faced by all the stakeholders that potentially contribute to firm performance. On a broader level, an increasing interest in corporate social responsibility might also reflect the growing recognition of the significance of stakeholder engagement (Bundy, Shropshire, & Buchholtz, 2013). Some firms are more socially responsible than others, and part of it is determined by their ownership incentives and interests (Rees & Rodionova, 2015); whether and how important consideration of social responsibility is in resource allocation and decision making are influenced by corporate governance design, as summarized in the article by Jain and Jamali (2016) in this special issue.

Third, agency theory overlooks the extent to which institutional environments shape the degree and nature of agency conflicts and the effectiveness of corporate governance mechanisms (Aguilera & Jackson, 2003; Tihanyi, Graffin, & George, 2014). As most previous research has focused on US firms, institutional environments might be neglected in published theoretical studies. However, recent work clearly demonstrates that there are substantial variations in institutional environments along dimensions such as investor protection, creditor rights, employee voice, disclosure levels around the globe, to name just a few. It is also shown that these institutional variations accordingly play a critical role in explaining cross-national differences in corporate governance mechanisms (Adams, Licht, & Sagiv, 2011; Hooghiemstra, Hermes, & Emanuels, 2015; La Porta, Lopez-de-Silanes, & Shleifer, 2006; La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 2000). For instance, a recent stream of research has addressed corporate governance in emerging economies such as China and India, whose institutional environments are less developed or quite different from those of advanced economies (Chen, Liu, & Lin, 2015; Huyghebaert & Wang, 2012; Lattemann, Fetscherin, Alon, Li, & Schneider, 2009; Li, 2013; Nagar & Sen, 2016; Singh & Gaur, 2009; Zhang, Chen, & Feng, 2014; Zhang, Gao, Guan, & Jiang, 2014). It is claimed that business groups are an organizational form that can overcome market imperfections prevalent in emerging economies (Colpan, Hikino, & Lincoln, 2010; They exhibit unique governance challenges as well as attributes to overcome broader strategic issues such as institutional voids or competitiveness, as summarized by Colli and Colpan's (2016) article in this special issue. In addition, institutional elements in a country tend to complement each other, giving rise to the varieties of capitalism (Hall & Soskice, 2002), and national business systems (Whitley, 1999).

In recent years, an increasing number of studies have come to take national institutional environments more seriously. A promising yet underdeveloped body of literature takes a

© 2016 John Wiley & Sons Ltd

comparative approach to highlight cross-national institutional differences and their implications for corporate governance and performance (Schiehll, Ahmadjian, & Filatotchev, 2014). Indeed, the review article by Schiehll and Martins (2016) in this special issue compiles the evidence that national institutional environments not only affect the firm-level choice of governance mechanisms, but also interact with firm-level governance mechanisms to influence firm performance. Similarly, one of the most well-researched cross-national governance dimensions has been the rule of law and, in particular, minority shareholder rights. Cuomo, Mallin, and Zattoni's (2016) article in this special issue sheds further light on this research by discussing the co-existence of some very successful soft law "comply or explain" codes of good governance with hard law regulation, as well as the emergence of more normatively effective transnational governance.

SYNOPSES OF ARTICLES INCLUDED IN THIS ISSUE

Drawing upon the 89 empirical studies published in the fields of accounting, finance, and management between 2003 and 2014, Schiehll and Martins (2016) develop a systematic literature review on cross-national comparative studies. In these studies, they find the "substantial variation in the use and measurement of country-level factors as well as a variety of causal forms used to explain the combined effects of country- and firm-level governance mechanisms." To appraise and synthesize these cross-national comparative studies, the authors first classify them into two categories: the ones exploring how country-level governance factors influence firm-level governance mechanisms and the ones exploring how country-level and firm-level governance mechanisms are combined to influence firm performance. They then compile the findings of these studies by causal model forms: additive, intervening variable, independent variable interaction, and moderator variable interaction. In doing so, their article represents an excellent review of the current literature, pointing out future research opportunities.

Grosman et al. (2016) review the extant interdisciplinary literature on state control and corporate governance in transition economies since the fall of the Berlin Wall. They discuss how state control has evolved as countries transition from centrally planned to market-based economies and how in turn firms' corporate governance adjusts to these significant changes in not only ownership but also logics. The article sheds light on the wide range of forms of state control beyond direct majority ownership which has important consequences for governance. Their study focuses mostly on China and Russia and there is an implicit comparison of state-controlled firms across these two transition economics. They conclude with a set of research questions by inviting scholars to explore more deeply the means of state control, their associated corporate governance structures and processes, and of course urge that the institutional context in which these relationships take place not be neglected.

Cuomo et al. (2016) revisit the classic topic of codes of good governance in light of the 2008 global financial crises as well as related corporate governance scandals which question the effectiveness of soft law governance mechanisms such as codes as well as the overall governance regulation. They begin the article with a renewed definition of codes of good governance as well as an assessment of their diffusion around the world. Then, they turn to a systematic review of research on codes of good governance where they distinguish between country-level and firm-level studies on codes. Throughout their article, the question of compliance and enforcement emerges as a driving force for change. Moreover, these authors pay particular attention to the challenges of the co-existence of hard and soft law as well as the increasing salience of transnational codes of good governance such as the OECD code.

Aktas, Croci, and Simsir (2016) focus on the well-developed and growing strand of the literature that links corporate governance with takeover outcomes. By adopting an agency perspective and reviewing both empirical and theoretical research, they provide useful insights for the design of effective governance mechanisms that can improve the efficiency of the takeover market. In particular, the governance mechanisms considered include the board of directors and executive compensation, the takeover market and pressure from financial market participants, product market competition, and the labor market. Their findings demonstrate the important role of both internal and external governance in improving takeover outcomes. They conclude by offering important avenues for future research such as the study of the long-term effects of takeovers on firms' financial performance and the use of quasi-natural experiments to deal with the endogeneity issue.

Taking a broader perspective on corporate governance as the "structure of rights and responsibilities among the parties with a stake in the firm" and focusing on the "organizational processes through which different CG [corporate governance] mechanisms interact and affect corporate financial and social outcomes," Jain and Jamali (2016) provide a systematic overview of work on the relationships between corporate governance and corporate social responsibility. They examine 94 peer-reviewed journal articles published between 2000 and 2015, categorize their findings by the level of corporate governance variables: formal and informal institutions at the institutional level, ownership structure and identities of owners at the firm level, board structure, and director social capital and resource network at the group level, and CEO demographics and socio-psychological characteristics at the individual level. Their article offers an excellent summary of the current literature, concluding by offering future research directions.

Colli and Colpan (2016) engage in an extensive review of a massive yet "siloed" (or segmented) literature on business groups. Their goal is to dissect from this large body of research what have we learned on how business groups design their corporate governance. After a brief discussion on how governance fits within the study of different types of business groups as well as highlighting the main theoretical approaches that have been used to tackle this complex issue, they propose an organizing framework (see their Fig. 1) in which they categorize research addressing governance issues in business groups published in a wide array of disciplines: business, management, finance, as well as business history journals. Their organizing framework allows them to pursue

© 2016 John Wiley & Sons Ltd

an insightful examination of research on: (1) the nature of the ownership in business groups; (2) intra-group mechanisms for control and coordination; (3) the relationship between the two; and (4) a deep exploration of organizational and performance outcomes. Colli and Colpan (2016) conclude their article by proposing "four high priority avenues" of future research, which include specific and fruitful recommendations on where to take future research on business groups next.

John, De Masi, and Paci (2016) review the literature on the governance of banks. They first discuss several unique features of the banking industry, such as restrictive regulation, increased reliance on debt, and complexity of operations, which have important implications for bank governance. A novelty of their survey is that it evaluates bank governance by taking into account the objectives of depositors and society-at-large, in addition to those of bank shareholders. The second part of their study focuses on the effectiveness of several governance mechanisms available to banks (e.g., board structure and quality, ownership structure, incentives) in a cross-country context. Their findings suggest that a multiple stakeholder perspective is required to fully understand what constitutes good governance for banks.

Zalewska (2016) provides a comprehensive review of the literature on the regulation of bankers' remuneration. Similar to John et al. (2016), the first part of her study focuses on the "specialness" of banks, which arises from the riskiness of their assets, their interconnectivity, and their systemic importance to the economy. Such features necessitate a unique regulatory treatment of bankers' remuneration that goes beyond merely resolving the "traditional" principal-agent conflict. The second part of her study discusses the literature on regulation of bankers' remuneration and the current state of regulatory developments in the area. The study concludes that a new theoretical framework is required to address the failure of existing theories of corporate governance for setting goals and performance metrics for the banking industry. A second important conclusion of Zalewska's study is that regulators should be involved in setting remuneration structures. However, it is by no means certain that overzealous regulatory reforms in bankers' remuneration, especially those ignoring the complexity of the banking sector, will be effective in strengthening the banking industry.

Srivastav and Hagendorff (2016) also focus on banks and review the extant literature on corporate governance and bank risk-taking. Their survey provides useful insights into how the effectiveness of bank boards, the structure of CEO compensation, and the risk management systems of banks can mitigate excessive risk-taking. The findings of their study are set against the background of several recent regulatory reforms that are driven by the need to protect the interests of specific groups of stakeholders. They conclude that the design of governance mechanisms and any regulatory reform initiatives should reflect the interests of bank shareholders, but also those of creditors and taxpayers. Their survey points out several opportunities for future research on bank risk-taking.

McNulty and Nordberg (2016) engage in a constructive and provocative discussion of shareholder activism by revisiting the question of who owns the corporation and pushing forward the construct of "active ownership." They define active ownership as a process of long-term investor-firm interactions where the development of relationships is critical. The authors anchor their review in uncovering the interests and motivations of heterogeneous institutional investors in how some of them engage in various forms of "voice." In addition to the more conventional approaches to ownerships such as market and institutions, they discuss how active ownership also encompasses psychological ownership. Their arguments are presented in a comprehensive process framework which takes institutional shareholders through the antecedents, processes, and effects leading to distinct firm outcomes.

Stathopoulos and Voulgaris (2016) focus on Say-on-Pay, a recently developed form of shareholder activism that manifests itself through the expression of voice on the executive pay-setting process. Their study reviews and critically evaluates existing research on Say-on-Pay and its effects on firm value and corporate decision-making. It also provides a general picture of the state of the shareholder activism literature and, in particular, the two main avenues for shareholder intervention in firm governance: "Exit" and "Voice." Their findings clearly demonstrate that there is no consensus within the academic community about the effectiveness of Say-on-Pay as a corporate governance mechanism. Importantly, the authors identify conceptual gaps and empirical discrepancies in prior studies and suggest promising directions for future research.

Gabaldon et al. (2016) develop a well-organized and systematic review of the extensive literature on women on boards. Once they established that despite recent policy and corporate efforts to break the glass ceiling, women are as not as present on boards as men, they discuss the supply- and demand-side barriers. In particular, they argue that the supply-side barriers fall into three categories: gender differences in values and attitudes, identification with gender role expectations, and work–family conflict. Regarding the demand-side barriers accounting for the under-representation of women on boards, they attribute it to gender discrimination, bias perceptions of what women might bring to the board, and the institutional environment. Interestingly, once they have reviewed this literature, they discuss the instruments and means that could overcome or minimize these barriers. They conclude by proposing a set of unanswered research issues that any research on gender and governance should seriously consider.

DISCUSSION AND FUTURE RESEARCH DIRECTIONS

Agency theory has long been the dominant theoretical lens for corporate governance research. However, recent studies have pushed the field beyond the often narrow conceptualization of agency conflicts and corporate governance and have taken seriously the identities of owners, stakeholder engagement, and national institutional environments to address the complexity of corporate governance issues. Theoretical lens have also been expanded to include institutional theory, stakeholder theory, resource dependence theory, cognitive paradoxes, and institutional economics, among others. Overall, our knowledge about corporate governance has been substantially improved in the last decade, some of which is

© 2016 John Wiley & Sons Ltd

well summarized, critiqued, and synthesized by the 12 articles in this special issue.

However, we believe that there is still a lot to learn by further challenging and relaxing the core assumptions of agency theory. Here we introduce several new directions and issues to consider. First, new types of investors such as hedge funds, private equity funds, sovereign wealth funds, socially responsible investors, and crowdfunding have emerged and added to the heterogeneity of shareholders. Not only do these new types of investors constitute different sources of capital coupled with distinct interests, but they also provide different challenges on corporate governance. For instance, hedge funds in the US have increasingly engaged in shareholder activism (Brav, Jiang, Partnoy, & Thomas, 2008). Some argue for hedge fund activism as benefiting shareholders; others criticize it as distracting executives from important projects. Deeper knowledge of hedge funds is necessary to understand whether and how hedge fund activism differs from activism by other institutional investors such as mutual funds and pension funds. The in-depth research about these heterogeneous owners, how they cope as co-owners, their organizational form, incentive structure, and monitoring capabilities should offer a fruitful avenue for future research.

Second, future research should further disentangle the antecedents to and consequences of stakeholder engagement in corporate governance. The diversity in stakeholders seeking to influence the firm and their mechanisms has expanded in recent years, making it more complex and difficult to accommodate their differing interests in the design of corporate governance (Bundy et al., 2013). Sometimes, different stakeholders uphold different yet competing preferences toward the firm. For instance, non-family shareholders of family firms are primarily interested in obtaining financial gains, but family members' interests often go beyond obtaining financial gains to include socio-emotional wealth or emotional and social benefits accruing from controlling the firm (Gomez-Mejia, Cruz, Berrone, & De Castro, 2011). Thus, the challenge that large family firms may face in designing corporate governance is how to balance or synthesize these somewhat competing demands from multiple stakeholders. It awaits future research on how firms recognize and address differing preferences of multiple stakeholders.

Blair (1995: 274) defines stakeholders as all the "participants who have substantial firm-specific investments at risk" and recognizes employees as an important stakeholder. She states that "fewer and fewer publicly traded corporations actually look like the factory model. Much of the wealth-generating capacity of most modern firms is based on the skills and knowledge of the employees and the ability of the organization as a whole to put those skills to work for customers and clients" (pp. 233–234). As the economy becomes more knowledge-based, recruiting and retaining human talent presents a key challenge to the firm, generating a lot of academic research in the area of human resource management. However, addressing the issues surrounding firm-specific human capital may require going beyond a functional view of human resource management to adopt the corporate governance perspective. How can the firm motivate employees to make a high level of firm-specific human capital? How should property rights be allocated between capital providers and employees? How should the firm-specific human capital be protected ex post? Future research on these questions may generate new insights about the design of corporate governance of the firm where human talent is a more important resource than financial capital.

Third, despite a recent increase in cross-national comparative research such as the cross-national study of internal control disclosures (Hooghiemstra et al., 2015), there is still a lot to learn from it. In addition, multinational firms provide an excellent setting to address corporate governance issues in the globalized world (Starbuck, 2014; Tihanyi et al., 2014), as shown by Driffield, Mickiewicz, and Temouri's (2014) study of how the strength of institutions influences the division of equity shares between the home country and the foreign affiliates for firms from 16 eastern and central European countries. Given their presence in multiple countries, multinational firms interact with local customers, states, and stakeholder groups that may have different preferences and expectations across countries. They may have incentives to change governance mechanisms in some countries; however, such changes may create conflicts with governance mechanisms of the parent company or other national subsidiaries. Alternatively, because of their economic power, multinational firms may influence the preferences and perceptions of local customers, shareholders, and stakeholder groups, thereby transplanting their own notion of corporate governance in foreign countries. Future research on corporate governance issues of multinational firms would enhance our knowledge of how the national corporate governance systems interact with the firm-level corporate governance and certainly move beyond agency debates into more institutional and resource-oriented concerns.

Fourth, agency theory and corporate governance research in general have not paid much attention to understanding how corporate governance affects the process of value creation. While addressing the "ways in which suppliers of finance to corporations assure themselves of getting a return on their investment," theorizing in the tradition of agency theory has focused on how to ensure returning a fair share of profits to shareholders (Shleifer & Vishny, 1997: 737). However, generation of value and distribution of the generated value fall into interrelated yet distinctive domains. For instance, Kim and Ozdemir (2014) classify fiduciary roles of boards into "wealth protectors" and "wealth creators" and show how national institutional environments drive the choice of these two different roles of boards. The corporate governance designed with an emphasis on protecting shareholders' rights as residual claimants may not promote risk-taking and firm-specific investments by other shareholders, thereby failing to realize the value-creating potential of firm resources. Realizing value-creating potential in the first place might be as important as fairly distributing subsequent profits to involved stakeholders. However, agency theory alone might be quite limited in addressing how the firm generates value, knowledge, and sources of competitive advantage because it neglects the importance of firm-specific investments made by stakeholders other than shareholders (García-Castro & Aguilera, 2014; Lazonick, 2003). Entrepreneurial firms might present appropriate settings to explore the link between corporate governance and value creation; combining agency

© 2016 John Wiley & Sons Ltd

theory with stakeholder theory, resource-based view, and dynamic capability theory might offer a fruitful lens.

Fifth, the governance of banks, and financial institutions more generally, should also be analyzed within a framework that goes beyond the "traditional" principal-agent conflict. In particular, the "specialness" of banks, as analytically discussed by John et al. (2016), Zalewska (2016), and Srivastav and Hagendorff (2016) in this special issue, requires an analytical framework that does not focus exclusively on protecting the interests of equity claimants but also expands to incorporating non-shareholder constituencies' interests such as depositors and the society-at-large. In the presence of potentially conflicting interests among heterogeneous constituents, the effectiveness of traditional governance mechanisms is also limited for the case of banks (see Grove, Patelli, Victoravich, & Xu, 2011; Leventis, Dimitropoulos, & Owusu-Ansah, 2013). More research is therefore warranted on the corporate governance of banks and, more specifically, on determining what constitutes good governance for financial entities. Of particular importance is to address the question of whether (and to what extent) bank governance contributed to the 2007–2009 financial crisis. One view is that the poor governance of banks was among the major causes of the crisis (see Bebchuk & Spamann, 2010; Kirkpatrick, 2009). This view is challenged, however, by recent research showing that banks with more independent boards, shareholder-friendly boards, and with CEOs whose incentives were better aligned with the interests of shareholders performed worse during the crisis than other banks (see Adams, 2012; Beltratti & Stulz, 2012; Fahlenbrach & Stulz, 2011). A related avenue of research is to examine whether the post-crisis calls of regulators and policy-makers for governance reforms (see European Commission, 2010; Kirkpatrick, 2009; Walker, 2009) have influenced the quality of bank governance. For example, there is no consensus in the literature on whether human capital resources at a board level (e.g., financial experience and skills) are significant predictors of bank risk-taking and performance. The results of recent research by Guner, Malmendier, and Tate (2008) and Minton, Taillard, and Williamson (2014) challenge the view that more financial expertise on banks' boards reduces risk-taking and improves specific corporate policies, such as financing, investment, and compensation. Last but not least, there is scope for more research on the complementarity between bank-level governance and regulation. Survey evidence (see Laeven, 2013) and evidence from the market of corporate control (see Hagendorff, Collins, & Keasey, 2010) support the view that governance and regulation should be developed in synchrony. Yet, more systematic research is needed on whether (and to what extent) financial regulation can compensate for weaknesses in the internal governance of banks.

Sixth, more research is warranted on the resource dependence role of corporate directors (see, e.g., Haynes & Hillman, 2010; Hillman, Cannella, & Paetzold, 2000; Hillman & Dalziel, 2003). A significant strand of the corporate governance literature focuses on the impact of board capital on corporate outcomes (see, e.g., Barroso, Villegas, & Pérez-Calero, 2011; Chen, 2014; De Maere, Jorissen, & Uhlaner, 2014; Kroll, Walters, & Wright, 2008). However, the vast majority of these studies either consider the board as a collective unit or restrict their attention to the CEO and the Chair of the board. An interesting avenue for future enquiry is to look beyond the CEO and the Chair by studying how "top management teams" (TMTs) affect corporate governance and how boards provide resources to organizations. Extant research usually emphasizes the importance of the CEO and board chair in the governance process, yet it fails to systematically account for their interaction with the TMT. This is an important oversight because the role of several members of the so-called "C-suite" has been extended to make more strategic contributions. The role of the Chief Financial Officer (CFO), for example, has evolved from a financial controller to a key strategic partner to the CEO. The role of the Chief Risk Officer (CRO) has also grown over the years with most CROs currently working closely with their CEO, Chief Operations Officer (COO) and other top executives, while shaping key strategic decisions that involve risk (e.g., mergers and acquisitions). In addition to their influence on corporate strategy, a promising area of future research is to investigate whether the incentives, actions, behaviors, skills, and other personal attributes of CFOs, CROs, COOs, and other members of the TMT promote effective corporate governance.

Finally, there is need for methodological advances in corporate governance research. For example, there is scope for more research using a mixed-methods approach. Most studies in corporate governance have so far focused on archival data for their empirical analyses. Despite their obvious attractiveness, data that are in the public domain are not well suited for analyzing governance attributes such as board processes, dynamics, and culture. Future studies combining archival data and data from surveys and interviews with key players (e.g., board members) will help to better understand the inner workings of a boardroom and draw inferences about how board members make their decisions.[2] We also expect to see future research using more appropriate methods for dealing with the endogenous nature of the relationship between corporate governance and firm outcomes (e.g., takeover outcomes, dividend policy, capital structure, firm valuation). Endogeneity arises when firm- and/or management-specific characteristics that affect an outcome variable are also correlated with corporate governance measures, leading to a spurious correlation between the former and the latter. There are several econometric methods aimed at addressing endogeneity concerns including instrumental variables, difference-in-differences estimators, matching methods, and higher order moments estimators (for a detailed discussion, see Roberts & Whited, 2013). A more extensive use of these methods in corporate governance research would enable a better understanding of the impact of corporate governance on firm outcomes.

To conclude, there is no doubt that the field of corporate governance has been prolific, but there is much more to learn and to draw on to better understand how the rights and responsibilities of different stakeholders are distributed within and outside the firm.

ACKNOWLEDGEMENTS

We would like to thank the Editors-in-Chief Praveen Kumar and Alessandro Zattoni for insightful comments and suggestions. The third author acknowledges the partial support of the Korea Business School Research Grant.

© 2016 John Wiley & Sons Ltd

REFERENCES

Adams, R. B. 2012. Governance and the financial crisis, ***International Review of Finance***, 12: 7–38.

Adams, R. B., Licht, A. N., & Sagiv, L. 2011. Shareholders and stakeholders: How do directors decide? ***Strategic Management Journal***, 32: 1331–55.

Aguilera, R. V., Desender, K., Bednar, M. K., & Lee, J. H. 2015. Connecting the dots: Bringing external corporate governance into the corporate governance puzzle, ***Academy of Management Annals***, 9: 483–573.

Aguilera, R. V. & Jackson, G. 2003. The cross-national diversity of corporate governance: Dimensions and determinants, ***Academy of Management Review***, 28: 447–65.

Aguilera, R. V. & Jackson, G. 2010. Comparative and international corporate governance, ***Academy of Management Annals***, 4: 485–556.

Aktas, N., Croci, E., & Simsir, S. A. 2016. Corporate governance and takeover outcomes, ***Corporate Governance: An International Review***, 24: 242–252.

Barroso, C., Villegas, M. M., & Pérez-Calero, L. 2011. Board influence on a firm's internationalization, ***Corporate Governance: An International Review***, 19: 351–67.

Bebchuk, L. & Spamann, H. 2010. Regulating bankers' pay, ***Georgetown Law Review***, 98: 247–87.

Beltratti, A. & Stulz, R. M. 2012. The credit crisis around the globe: Why did some banks perform better? ***Journal of Financial Economics***, 105: 1–17.

Berle, A. A., Jr. & Means, G. C. 1932. ***The modern corporation and private property***. New York: Commerce Clearing House.

Binacci, M., Peruffo, E., Oriani, R., & Minichilli, A. 2016. Are all non-family managers (NFMs) equal? The impact of NFM characteristics and diversity on family firm performance, ***Corporate Governance: An International Review*** , DOI: 10.1111/corg.12130.

Blair, M. M. 1995. ***Ownership and control***. Washington, DC: The Brookings Institution.

Brav, A., Jiang, W., Partnoy, F., & Thomas, R. 2008. Hedge fund activism, corporate governance, and firm performance, ***The Journal of Finance***, 63: 1729–75.

Buchanan, J., Chai, D. H., & Deakin, S. 2014. Agency theory in practice: A qualitative study of hedge fund activism in Japan, ***Corporate Governance: An International Review***, 22: 296–311.

Bundy, J., Shropshire, C., & Buchholtz, A. K. 2013. Strategic cognition and issue salience: Toward an explanation of firm responsiveness to stakeholder concerns, ***Academy of Management Review***, 38: 352–76.

Chen, H.-L. 2014. Board capital, CEO power and R&D investment in electronics firms, ***Corporate Governance: An International Review***, 22: 422–36.

Chen, Y., Liu, W., & Lin, J. K. 2015. Cumulative voting: Investor protection or antitakeover? Evidence from family firms in China, ***Corporate Governance: An International Review***, 23: 234–48.

Colli, A. & Colpan, A. M. 2016. Business groups and corporate governance: Review, synthesis, and extension, ***Corporate Governance: An International Review*** , 24: 274–302.

Colpan, A., Hikino, T., & Lincoln, J. 2010. ***Oxford handbook on business groups***. New York: Oxford University Press.

Connelly, B. L., Tihanyi, L., Certo, S. T., & Hitt, M. A. 2010. Marching to the beat of different drummers: The influence of institutional owners on competitive actions, ***Academy of Management Journal***, 53: 723–42.

Cuomo, F., Mallin, C., & Zattoni, A. 2016. Corporate governance codes: A review and research agenda, ***Corporate Governance: An International Review***, 24: 222–241.

Dalton, D. R., Daily, C. M., Certo, S. T., & Roengpitya, R. 2003. Meta-analyses of financial performance and equity: Fusion or confusion? ***Academy of Management Journal***, 46: 13–26.

Davis, J. H., Schoorman, F. D., & Donaldson, L. 1997. Toward a stewardship theory of management, ***Academy of Management Review***, 22: 20–47.

De Maere, J., Jorissen, A., & Uhlaner, L. M. 2014. Board capital and the downward spiral: Antecedents of bankruptcy in a sample of unlisted firms, ***Corporate Governance: An International Review***, 22: 387–407.

Desender, K. A., Aguilera, R. V., Crespi, R., & García-cestona, M. 2013. When does ownership matter? Board characteristics and behavior, ***Strategic Management Journal***, 34: 823–42.

Dharwadkar, R., George, G., & Brandes, P. 2000. Privatization in emerging economies: an agency theory perspective, ***Academy of Management Review***, 25: 650–69.

Dorff, M. B. 2014. ***Indispensable and other myths***. Berkeley, CA: University of California Press.

Driffield, N., Mickiewicz, T., & Temouri, Y. 2014. Institutions and equity structure of foreign affiliates, ***Corporate Governance: An International Review***, 22: 216–29.

Du, Y., Deloof, M., & Jorissen, A. 2011. Active boards of directors in foreign subsidiaries, ***Corporate Governance: An International Review***, 19: 153–68.

European Commission, 2010. Corporate governance in financial institutions and remuneration policies. Green paper. Brussels: European Commission. Available at: http://ec.europa.eu/internal_market/company/docs/modern/com2010_284_en.pdf (accessed March 21, 2016).

Fahlenbrach, R. & Stulz, R. 2011. Bank CEO incentives and the credit crisis, ***Journal of Financial Economics***, 99: 11–26.

Fama, E. F. & Jensen, M. C. 1983. Agency problems and residual claims, ***Journal of Law and Economics***, 26: 327–49.

Filatotchev, I. & Boyd, B. K. 2009. Taking stock of corporate governance research while looking to the future, ***Corporate Governance: An International Review***, 17: 257–65.

Gabaldon, P., de Anca, C., Mateos de Cabo, R., & Gimeno, R. 2016. Searching for women on boards: An analysis from the supply and demand perspective, ***Corporate Governance: An International Review***, 24: 371–385.

García-Castro, R. & Aguilera, R. V. 2014. Incremental value creation and appropriation in a world with multiple stakeholders, ***Strategic Management Journal***, 36: 137–47.

Gomez-Mejia, L. R., Cruz, C., Berrone, P., & De Castro, J. 2011. The bind that ties: Socioemotional wealth preservation in family firms, ***Academy of Management Annals***, 5: 653–707.

Grosman, A., Okhmatovskiy, I., & Wright, M. 2016. State control and corporate governance in transition economies: 25 years on from 1989, ***Corporate Governance: An International Review***, 24: 200–221.

Grove, H., Patelli, L., Victoravich, L., & Xu, P. 2011. Corporate governance and performance in the wake of the financial crisis: Evidence from US commercial banks, ***Corporate Governance: An International Review***, 19: 418–36.

Guner, A. B., Malmendier, U., & Tate, G. 2008. Financial expertise of directors, ***Journal of Financial Economics***, 88: 323–54.

Hagendorff, J., Collins, M., & Keasey, K. 2010. Board monitoring, regulation, and performance in the banking industry: Evidence from the market for corporate control, ***Corporate Governance: An International Review***, 18: 381–95.

Hall, P. A. & Soskice, D. (Eds.). 2002. ***Varieties of capitalism***. Oxford: Oxford University Press.

Hautz, J., Mayer, M. C., & Stadler, C. 2013. Ownership identity and concentration: A study of their joint impact on corporate diversification, ***British Journal of Management***, 24: 102–26.

Haynes, K. T. & Hillman, A. 2010. The effect of board capital and CEO power on strategic change, ***Strategic Management Journal***, 31: 1145–63.

© 2016 John Wiley & Sons Ltd

Hillman, A. J., Cannella, A. A., & Paetzold, R. L. 2000. The resource dependence role of corporate directors: Strategic adaptation of board composition in response to environmental change, ***Journal of Management Studies***, 37: 235–56.

Hillman, A. J. & Dalziel, T. 2003. Boards of directors and firm performance: Integrating agency and resource dependence perspectives, ***Academy of Management Review***, 28: 383–96.

Hooghiemstra, R., Hermes, N., & Emanuels, J. 2015. National culture and internal control disclosures: A cross-country analysis, ***Corporate Governance: An International Review***, 23: 357–77.

Hoskisson, R. E., Hitt, M. A., Johnson, R. A., & Grossman, W. 2002. Conflicting voices: The effects of institutional ownership heterogeneity and internal governance on corporate innovation strategies, ***Academy of Management Journal***, 45: 697–716.

Huyghebaert, N. & Wang, L. 2012. Expropriation of minority investors in Chinese listed firms: The role of internal and external corporate governance mechanisms, ***Corporate Governance: An International Review***, 20: 308–32.

Jain, T. & Jamali, D. 2016. Looking inside the black-box: The effect of corporate governance on corporate social responsibility, ***Corporate Governance: An International Review***, 253–273.

John, K., De Masi, S., & Paci, A. 2016. Corporate governance in banks, ***Corporate Governance: An International Review***, 24: 000–0.

Kim, Y. U. & Ozdemir, S. Z. 2014. Structuring corporate boards for wealth protection and/or wealth creation: The effects of national institutional characteristics, ***Corporate Governance: An International Review***, 22: 266–89.

Kirkpatrick, G. 2009. The corporate governance lessons from the financial crisis. *Financial Markets Trends*, 2009/1.

Kroll, M., Walters, B. A., & Wright, P. 2008. Board vigilance, director experience, and corporate outcomes, ***Strategic Management Journal***, 29: 363–82.

Laeven, L. 2013. Corporate governance: What's special about banks? ***Annual Review of Financial Economics***, 5: 63–92.

La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. 2006. What works in securities laws? ***The Journal of Finance***, 61: 1–32.

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. 2000. Investor protection and corporate governance, ***Journal of Financial Economics***, 58: 3–27.

Lattemann, C., Fetscherin, M., Alon, I., Li, S., & Schneider, A.-M. 2009. CSR communication intensity in Chinese and Indian multinational companies, ***Corporate Governance: An International Review***, 17: 426–42.

Lazonick, W. 2003. The theory of the market economy and the social foundations of innovative enterprise, ***Economic and Industrial Democracy***, 24: 9–44.

Leventis, S., Dimitropoulos, P., & Owusu-Ansah, S. 2013. Corporate governance and accounting conservatism: Evidence from the banking industry, ***Corporate Governance: An International Review***, 21: 264–86.

Li, S. 2013. China's (painful) transition from relation-based to rule-based governance: When and how, not if and why, ***Corporate Governance: An International Review***, 21: 567–76.

McNulty, T., Florackis, C., & Ormrod, P. 2013. Boards of directors and financial risk during the credit crisis, ***Corporate Governance: An International Review***, 21: 58–78.

McNulty, T. & Nordberg, D. 2016. Ownership, activism and engagement: Institutional investors as active owners, ***Corporate Governance: An International Review***, 24: 000–0.

Minton, B. A., Taillard, J. P. A., & Williamson, R. 2014. Financial expertise of the board, risk taking, and performance: Evidence from bank holding companies, ***Journal of Financial and Quantitative Analysis***, 49: 351–80.

Morck R., Wolfenzon, D. & Yeung, B. 2005. Corporate governance, economic entrenchment and growth, ***Journal of Economic Literature***, 43: 655–720.

Nagar, N. & Sen, K. 2016. How does regulation affect the relation between family control and reported cash flows? Comparative evidence from India and the United States, ***Corporate Governance: An International Review***. DOI:10.1111/corg.12157.

Rees, W. & Rodionova, T. 2015. The influence of family ownership on corporate social responsibility: An international analysis of publicly listed companies, ***Corporate Governance: An International Review***, 23: 184–202.

Roberts, J., McNulty, T., & Stiles, P. 2005. Beyond agency conceptions of the work of the non-executive director: Creating accountability in the boardroom, ***British Journal of Management***, 16: S5–S26.

Roberts, M. R. & Whited, T. 2013. Endogeneity in empirical corporate finance. In G. M. Constantinides, M. Harris, & R. M. Stulz (Eds.), ***Handbook of the economics of finance, Volume 2, Part A***: 493–572. Amsterdam: Elsevier.

Schiehll, E., Ahmadjian, C., & Filatotchev, I. 2014. National governance bundles perspective: Understanding the diversity of corporate governance practices at the firm and country levels, ***Corporate Governance: An International Review***, 22: 179–84.

Schiehll, E. & Martins, H. C. 2016. Cross-national governance research: A systematic review and assessment, ***Corporate Governance: An International Review***, 24: 000–0.

Shleifer, A. & Vishny, R. W. 1997. A survey of corporate governance, ***The Journal of Finance***, 52: 737–83.

Singh, D. A. & Gaur, A. S. 2009. Business group affiliation, firm governance, and firm performance: Evidence from China and India, ***Corporate Governance: An International Review***, 17: 411–25.

Srivastav, A. & Hagendorff, J. 2016. Corporate governance and bank risk-taking, ***Corporate Governance: An International Review***, 24: 334–345.

Starbuck, W. H. 2014. Why corporate governance deserves serious and creative thought, ***Academy of Management Perspectives***, 28: 15–21.

Stathopoulos, K. & Voulgaris, G. 2016. The importance of shareholder activism: The case of Say-on-Pay, ***Corporate Governance: An International Review***, 24: 359–370.

Stout, L. 2012. ***The shareholder value myth***. San Francisco, CA: Berrett-Koehler.

Tihanyi, L., Graffin, S., & George, G. 2014. Rethinking governance in management research, ***Academy of Management Journal***, 57: 1535–43.

Thornton, P. H. & Ocasio, W. 2008. Institutional logics. In R. Greenwood, C. Oliver, R. Suddaby, & K. Sahlin (Eds.), ***The Sage handbook of organizational institutionalism***: 99–129. Los Angeles, CA: Sage Publications.

Walker, S. D. 2009. A review of corporate governance in UK banks and other financial industry entities: Final recommendations. Available at http://webarchive.nationalarchives.gov.uk/+/http:/www.hm-treasury.gov.uk/d/walker_review_261109.pdf, retrieved on 10 March 2016

Whitley, R. 1999. ***Divergent capitalisms***. Oxford: Oxford University Press.

Young, M. N., Peng, M. W., Ahlstrom, D., Bruton, G. D., & Jiang, Y. 2008. Corporate governance in emerging economies: A review of the principal–principal perspective, ***Journal of Management Studies***, 45: 196–220.

Zalewska, A. 2016. A new look at regulating bankers' remuneration, ***Corporate Governance: An International Review***, 24: 322–333.

Zattoni, A. 2011. Who should control a corporation? Toward a contingency stakeholder model for allocating ownership rights, ***Journal of Business Ethics***, 103: 255–74.

Zeitoun, H. & Pamini, P. 2015. Corporate ownership structure and top executives' prosocial preferences: The role of relational and external blockholders, ***Corporate Governance: An International Review***, 23: 489–503.

© 2016 John Wiley & Sons Ltd

Zhang, Q., Chen, L., & Feng, T. 2014. Mediation or moderation? The role of R&D investment in the relationship between corporate governance and firm performance: Empirical evidence from the Chinese IT industry, ***Corporate Governance: An International Review***, 22: 501–17.

Zhang, M., Gao, S., Guan, X., & Jiang, F. 2014. Controlling shareholder-manager collusion and tunneling: Evidence from China, ***Corporate Governance: An International Review***, 22: 440–59.

Zheng, Y. 2010. Heterogeneous institutional investors and CEO compensation, ***Review of Quantitative Finance and Accounting***, 35: 21–46.

ENDNOTES

1. The institutional logics research claims that there exists a dominant logic defined as "socially constructed, historical patterns of material practices, assumptions, values, beliefs, and rules by which [organizations] produce and reproduce their material subsistence, organize time and space, and provide meaning to their social reality" (Thornton & Ocasio, 2008).
2. Recent studies that opted for a mixed-methods approach include Binacci, Peruffo, Oriani, and Minichilli (2016), McNulty, Florackis, and Ormrod (2013), and Du, Deloof, and Jorissen (2011).

Ruth V. Aguilera is a Full Professor at the D'Amore-McKim School of Business at Northeastern University. She received her PhD in Sociology from Harvard University. Ruth's research interests lie at the intersection of strategic organization and global strategy, specializing in international corporate governance, corporate social responsibility, and internationalization. Her research has been published in various journals, including *Academy of Management Journal*, *Academy of Management Review*, *Global Strategy Journal*, *Journal of International Business Studies*, *Organization Science*, and *Strategic Management Journal*, among others.

Chris Florackis is a Professor of Finance at the Management School of the University of Liverpool. He holds a PhD in Economics from the University of York (UK). His research interests range from corporate finance and governance to various aspects of asset pricing and risk management. He currently serves as an Associate Editor for the journals "Corporate Governance: An International Review" and "Journal of Multinational Financial Management". His research work has been published in a series of international academic journals, such as the Journal of Empirical Finance, Journal of International Money and Finance and the Journal of Banking and Finance.

Hicheon Kim is currently a Professor of Strategy and Organization and a former Associate Dean at the Korea University Business School (KUBS). He received his Ph.D. at Texas A&M University. Prior to joining the KUBS, he was a faculty member at George Washington University in the United States and at Hanyang University in Korea. His research interests include business groups, corporate strategy and governance, and corporate innovation. His work has appeared in the leading journals such as *Academy of Management Journal*, *Strategic Management Journal*, *Organization Science*, and *Journal of International Business Studies*.

© 2016 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 181–199

Cross-National Governance Research: A Systematic Review and Assessment

Eduardo Schiehll* and Henrique Castro Martins

ABSTRACT

Manuscript Type: Review
Research Question/Issue: Using a systematic literature review approach, we survey 192 cross-national comparative studies published in 23 scholarly journals in the fields of accounting, economics, finance, and management for the period 2003 to 2014. The purpose is to synthesize and appraise the extant empirical research on the interplay between country- and firm-level governance mechanisms and the effects on firm outcomes. Particular focus is placed on studies that examine firm economic performance.
Research Findings/Results: We identify and distinguish between two groups of cross-national governance studies. The first type compares macro, country-level outcomes and the second compares three different firm-level outcomes: economic performance, governance mechanisms, and strategic decisions. We compare the theoretical frameworks used and further analyze the country-level factors and firm-level governance attributes that have been combined to investigate their interplay and the effects on firm outcomes. We find substantial variation in the use and measurement of country-level factors as well as a variety of causal forms used to explain the combined effects of country- and firm-level governance mechanisms. This wide variability precludes comparison, and consequently prevents identifying consistent patterns of influence between country-level governance factors and firm-level governance mechanisms and/or performance. We identify research gaps and provide fruitful directions for future research on this topic.
Theoretical Implications: The cross-national governance research has been guided mainly by an economic perspective focusing on international differences in the effectiveness of specific governance mechanisms. Few comparative studies have integrated an institutional perspective or examined the external forces that drive the diffusion and use of specific governance mechanisms. Such integrative framework would improve the understanding of cross-national differences in the salient dimensions of country-level governance factors and how they mediate the effectiveness of firm-level governance mechanisms.
Practitioner Implications: Our results reveal that firm- and country-level governance mechanisms have been interacted and combined, either to address various agency problems or to compensate for a weak national environment. This calls for regulators and investors to consider national governance factors when assessing firm-level governance practices.

Keywords: Corporate Governance, Cross-National Corporate Governance, Systematic Review, Firm-Level Governance Mechanisms, Country-Level Governance Factors

INTRODUCTION

The corporate governance literature provides extensive insight into the associations between firm-level governance mechanisms and a number of firm outcomes. Nevertheless, the reviews by Brown, Beekes, and Verhoeven (2011), Denis and McConnell (2003), and Durisin and Puzone (2009) indicate that national governance characteristics and how they impact the effectiveness of firm-level governance mechanisms have received little attention. Another research stream views corporate governance as primarily the means by which a nation channels corporate power for the good of society, so that wealth is created efficiently and distributed fairly within a national economy (e.g., Jackson & Deeg, 2008; Judge, Douglas, & Kutan, 2009). This perspective has motivated cross-national governance research, which attempts to explain firm outcomes mainly as under the influence of economic development and national-level governance forces external to the firm (e.g., Millar, Eldomiaty, Choi, & Hilton, 2005; Weimer & Pape, 1999). At the same time, the interplay between country- and firm-level governance mechanisms tends to be disregarded.

Some governance scholars argue that these two promising research streams would gain by converging and informing each other, thereby advancing our understanding of the effectiveness of corporate governance practices (e.g., Aguilera, Desender, Bednar, & Lee, 2015; Filatotchev, Jackson, & Nakajima, 2013; Judge, 2009; Judge, Filatotchev, & Aguilera, 2010). This argument finds support in North's (1990)

*Address for correspondence: Eduardo Schiehll, HEC-Montréal, 3000, Chemin de la Côte-Sainte-Catherine, Bureau 5369, Montréal, QC H3T 2A7, Canada. E-mail: eduardo.schiehll@hec.ca

© 2016 John Wiley & Sons Ltd
doi:10.1111/corg.12158

institutional theory, whereby a country's informal and formal institutions provide guidelines for individuals and organizations to deal with uncertainty, decode the environment, and take appropriate actions. Accordingly, Aoki and Jackson (2008: 2) suggest that "There are various patterns of linkage between corporate governance (CG) mechanisms (institutions) and organizational architecture (OA) as a non-market information system, the workings and implications of which cannot be adequately understood only in terms of the standard framework."[1] The main motivation for this systematic literature review is the need to identify cross-national variations in the salient dimensions of country-level governance forces, and how these forces impact the effectiveness of governance solutions at the firm level.

Our aim is to contribute to the discussion by synthesizing the extant empirical cross-national corporate governance research on the interplay between country- and firm-level governance mechanisms and the effects on firm outcomes. Our study departs from previous comprehensive reviews on international governance research (Brown et al., 2011; Denis & McConnell, 2003; Durisin & Puzone, 2009) in two respects. First, we review only studies that compare governance mechanisms across several countries. Second, we focus on empirical evidence of the interactive or combinatory effects of firm- and country-level governance mechanisms. Thus, using a systematic literature review methodology, we examine 192 studies published in 23 scholarly journals in the fields of accounting, economics, finance, and management for the period 2003 to 2014. Our overall objective is to synthesize and organize the cross-national governance research to date. We present our review under five general headings: (1) What are the predominant theoretical frameworks? (2) What outcomes have been investigated? (3) What country-level factors have been investigated as independent variables? (4) What country- and firm-level governance mechanisms have been combined to explain firm performance? (5) What country-level governance factors have been used to explain firm-level governance mechanisms?

We identify and distinguish between two groups of cross-national governance studies. The first compares macro, country-level outcomes and the second compares three types of firm-level outcomes: governance mechanisms, strategic decisions, and performance. We compare the theoretical frameworks adopted and the country-level factors used to proxy for external governance forces. We demonstrate that the cross-national governance research has been largely informed by La Porta, Lopez-de-Silanes, Shleifer, and Vishny's (1998) (hereafter LLSV) classification of a country's degree of investor protection. Although there is consistent evidence that investor protection has a fundamental effect on financial market development and firm ownership structure, its effect on the use of other firm-level governance mechanisms or their effectiveness is less convincing. Our results also reveal that, up to now, the cross-national governance research has examined only a small number of informal institutions. We further analyze the country-level factors and firm-level governance attributes that have been combined to investigate their interplay and the effects on firm outcomes. We find substantial variations in the use and measurement of country-level factors, as well as differences in the causal forms used to explain the combined effects of country- and firm-level governance mechanisms. This wide variability precludes comparison, and consequently prevents the identification of consistent patterns in how country-level governance factors influence firm governance structure and/or performance. We identify several research gaps and provide fruitful directions for future research.

This article is structured as follows. The next section summarizes the ongoing debate in the cross-national governance research. We highlight the theoretical underpinnings and point out certain challenges in integrating an institutional perspective to examine the interplay between firm- and country-level governance mechanisms and the effects on firm outcomes. We then describe the systematic literature review methodology, including journal selection, article selection, and content analysis. In the third section we present and discuss our findings on the dependent variables and national governance factors that have been examined as well as the main firm- and country-level mechanisms that have been combined to explain firm economic performance. We end with a conclusion and directions for future research.

THE ONGOING DEBATE IN THE CROSS-NATIONAL GOVERNANCE RESEARCH

Corporate governance can be viewed as bundles of interrelated or intertwined country- and firm-level forces that underlie the structures and processes involved in the relationships between a firm's management and its stakeholders, who are most commonly shareholders (Schiehll, Ahmadjian, & Filatotchev, 2014). The historical path dependence among country- and firm-level mechanisms has produced a variety of country- and organization-specific governance systems that tend to work well within the institutional environments in which they have evolved. Although internal and external governance mechanisms are assumed to complement and substitute for each other (Aguilera et al., 2015; Roe, 2005), our understanding of the relationship between national governance systems and the internal governance and economic performance of firms remains limited.

The principles of complementarity and substitutability among governance mechanisms have provided the theoretical basis for the configurational approach in comparative governance research (Aguilera, Filatotchev, Gospel, & Jackson, 2008; Aguilera & Jackson, 2010; Aoki & Jackson, 2008). Accordingly, similar firm outcomes may result from multiple pathways and functionally similar effects, a principle known as equifinality (Fiss, 2007). This principle has motivated studies on firm-level governance bundles, which have in turn produced valuable insights into why different configurations of firm-level governance mechanisms result in similar firm outcomes (Garcia-Castro, Aguilera, & Ariño, 2013 [M081]; Hoskisson, Castleton, & Withers, 2009; Misangyi & Acharya, 2014; Rediker & Seth, 1995; Ward, Brown, & Rodriguez, 2009).[2] However, these studies examine complementarities and substitutions among firm-level (internal) governance mechanisms, with limited consideration of the national (external) governance factors of the country in which the firm operates. As suggested by Filatotchev et al. (2013), national

© 2016 John Wiley & Sons Ltd

institutions also affect the degree of complementarity and/or substitutability among different firm-level governance mechanisms, producing patterned variations in firm-level governance mechanisms.

The cross-national corporate governance research has also examined country-level configurations to some extent. Nevertheless, in this research stream, firm behavior tends to be explained by the country's social norms, economic and financial development, and legal system – mainly investor protection and its enforcement (e.g., Judge et al., 2009; Millar et al., 2005; Weimer & Pape, 1999) – with limited consideration of their interactions with firm-level governance mechanisms. As Aguilera and Jackson (2010: 532) suggest, "comparative studies of corporate governance must go beyond broad typologies of institutions, and look in a 'contextualized' way at the underlying identities and constellations of actors." These authors also suggest that a better understanding of how corporate governance practices differ around the world requires a "more comprehensive comparative" view of national institutions. The nature of firm-level governance conflicts and the effectiveness of well-known corporate governance mechanisms differ among countries due to several sets of complementarities among firm-level governance mechanisms and formal and informal national institutions (e.g., Bell, Filatotchev, & Aguilera, 2014; Filatotchev et al., 2013; Judge, 2012; Judge et al., 2010).

The theoretical grounds for this interplay among firm- and country-level governance mechanisms and the combined effects on firm-level governance practices and performance are based on the studies by Aguilera and Jackson (2010), Crossland and Hambrick (2007) [M099], and Hambrick and Finkelstein (1987), among others. Hambrick and Finkelstein (1987) demonstrate that a manager's degree of discretion – or managerial latitude – is determined by the interaction of three sources: the individual (e.g., political acumen), the organization (e.g., board of directors), and the environment (e.g., industry regulations). The conceptual study by Crossland and Hambrick (2007) [M099] builds on this idea to demonstrate that managerial discretion also differs among countries due to the disciplinary powers of formal and informal national institutions. Firms operate within a system of social norms, practices, and relationships – the national governance system – that both enables and imposes constraints on the discretion of managers and large shareholders. Hence, the effectiveness of specific governance mechanisms needs to be examined with respect to the constraints on managerial discretion imposed by firms and/or national authorities. Similarly, Aguilera and Jackson (2010) provide a comprehensive discussion of the four main theoretical paradigms (economics and management, culture and sociology, legal, and political) that have been used to examine corporate governance issues and that contribute to explain similarities and differences among countries, which they call cross-national diversity. More importantly, they suggest that corporate governance scholars should pay closer attention to "how private economic actors (e.g., firms, networks, associations) are socially organized and interact with one another" (Aguilera & Jackson, 2010: 532).

It is challenging to theorize about specific interactions among firm- and country-level governance attributes, a task made even more difficult by problems in conceptualizing and measuring the monitoring power of national institutions (Schiehll et al., 2014). The monitoring benefits of country-level governance factors depend on other national attributes that influence firms' investment opportunities and access to financial markets. As Doidge, Karolyi, and Stulz (2007) [F040] suggest, the extent to which firms choose to improve upon the monitoring forces afforded by the state depends on the costs and benefits of doing so. Their results indicate that the effect of external governance mechanisms on firms' internal governance configurations is weaker in countries with poor financial development, where firms are less dependent on funding from capital markets and hence benefit less from any governance-related reductions in capital costs. Therefore, reviews of the literature on this issue are occasionally needed in order to organize and assess the current empirical evidence on the influence of country- and firm-level corporate governance mechanisms on firm outcomes. Our aim is to identify the salient dimensions of country-level governance forces and how these forces affect the nature and extent of conflicts of interest. The hope is that our review will guide research towards governance configurations that can operate at both the firm and country level so as to govern firms within an overall economy or collection of economies (Schiehll et al., 2014). Nevertheless, this type of research can be challenging due to (1) the wide range of firm- and country-level governance attributes that must be considered, and (2) the theoretical difficulty of specifying the mechanisms whereby country- and firm-level governance mechanisms interact and affect firm outcomes, such as internal governance, managerial decisions, and economic performance (Schiehll et al., 2014). These challenges are the main motivation for this systematic literature review. In the next section we describe the methodology.

METHODS

We applied a systematic literature review methodology (Tranfield, Denyer, & Smart, 2003) consisting of a comprehensive search for relevant studies on a specific topic that were then synthesized and appraised according to predetermined methods.[3] Systematic reviews take stock of the body of literature to date using precise filtering techniques to screen the articles and evaluate each related study in a critical, justified way. Unlike the traditional narrative review, the systematic review follows a rigorous, replicable, scientific, and transparent process (Tranfield et al., 2003). Our aim is to provide a comprehensive coverage of the empirical evidence in the cross-national governance research on the interplay among country- and firm-level governance mechanisms. Given the interdisciplinary nature of corporate governance research, (Brown et al., 2011; Durisin & Puzone, 2009) we consider empirical studies of cross-national governance published in journals covering four business disciplines: accounting, economics, finance, and management. We describe the steps in this process below.

Journal and Article Selection

The first step was to sample a set of representative journals in the four aforementioned business disciplines. We began by identifying the five leading journals for each discipline

© 2016 John Wiley & Sons Ltd

according to the ISI impact factors reported in the 2011 Journal Citation Report (JCR) Social Sciences Edition. Although they do not meet our selection criteria, we included five additional journals – four in management and one in economics – for their strong international and cross-disciplinary focus: *Journal of International Business Studies* (*JIBS*), *Corporate Governance*: *An International Review* (*CGIR*), *Strategic Management Journal* (*SMJ*), *Administrative Science Quarterly* (*ASQ*), and *Journal of Political Economy* (*JPE*). Two of the selected journals (*Journal of Financial Studies* and *Journal of Finance*) cover the fields of both finance and economics, but were considered for finance only due to their higher ISI ranking in this discipline. Table 1 presents the final list of 23 scholarly journals, with impact factors ranging from 1.897 to 9.243.

The next step was to set the parameters for an advanced electronic keyword search in the selected journals using the ABI/INFORM[4] database. In order to identify relevant keywords, we first performed a content analysis of the following influential articles on cross-national corporate governance research: Aguilera and Jackson (2010), Aoki and Jackson (2008), and Filatotchev et al. (2013). The result was a set of 11 keywords: "cross

TABLE 1
Distribution of Sample Articles

Journal	Abbrev.	Impact factor	Total no. of studies	Non-empirical studies	Non- cross-national studies	Studies analyzed
Accounting						
Journal of Accounting & Economics	JAE	3.281	5	0	3	2
Accounting, Organizations and Society	AOS	2.878	4	4	0	0
Accounting Review	AR	2.418	2	0	0	2
Journal of Accounting Research	JAR	2.378	5	0	1	4
Review of Accounting Studies	RAS	2.022	1	0	0	1
Subtotal			**17**	**4**	**4**	**9**
Finance						
Review of Financial Studies	RFS	4.748	9	1	1	7
The Journal of Finance	JF	4.218	7	1	2	4
Journal of Financial Economics	JFE	3.725	20	1	3	16
Journal of Banking and & Finance	JBF	2.6	29	1	5	23
IMF Economic Review	IER	2.1	0	0	0	0
Subtotal			**65**	**4**	**11**	**50**
Management						
Academy of Management Review	AMR	6.169	1	1	0	0
Academy of Management Journal	AMJ	5.608	4	0	4	0
Journal of Management	JofM	4.595	1	0	0	1
Organization Science	OS	4.338	5	2	3	0
Journal of Management Studies	JMS	4.255	9	2	4	3
Journal of International Business Studies	JIBS	3.406	13	6	4	3
Corporate Governance: An International Review	CGIR	1.897	57	24	15	18
Strategic Management Journal	SMJ	3.783	10	2	5	3
Administrative Science Quarterly	ASQ	4.212	4	1	1	2
Subtotal			**104**	**38**	**36**	**30**
Economic						
Journal of Economic Literature	JEL	9.243	2	2	0	0
Quarterly Journal of Economics	QJE	5.92	1	1	0	0
Journal of Economic Perspectives	JEP	4.211	2	2	0	0
Journal of Political Economy	JPE	2.902	1	1	0	0
Subtotal			**6**	**6**	**0**	**0**
Total			**192**	**52**	**51**	**89**

© 2016 John Wiley & Sons Ltd

country," "cross-national," "comparative," "bundles," "national governance bundles," "multi-country," "external mechanisms," "national institutions," "institutional environment," "institutions of governance," and "international." These keywords were then combined with the word "governance" to perform an advanced search within the abstracts of all the selected journals. Table 1 presents the 192 scholarly articles that were originally identified. In line with our objectives, we focused on empirical[5] cross-national studies. Hence, based on a preliminary content analysis of the abstracts of the 192 original articles, we excluded meta-analyses, conceptual articles, book reviews, editorials, perspectives, and single-country empirical studies (i.e, noncomparative). The final sample includes 89 cross-national empirical studies published in 23 high-impact journals from 2003 to 2014.

Content Analysis

In order to synthesize and appraise the final sample of 89 studies, the two authors independently identified and coded for each article the following elements: (1) the main research questions or topics examined, (2) the dependent variables investigated and their measures, (3) the theoretical frameworks used, (4) the country-level governance factors examined and how they were measured, (5) the firm-level governance mechanisms examined, and (6) the main findings. For each of these elements, a coding scheme was developed and pre-tested in a subsample of 20 studies, which the two authors then refined jointly to finalize a common coding scheme for the independent content analysis. After analyzing all the studies independently, the two authors compared their results, which revealed high agreement. Only 14 of the 89 studies required a second look due to inconsistent (disagreement) coding of some elements, and these were revised jointly to resolve the inconsistencies. Agreement was reached and some elements were re-coded.

DISCUSSION AND DIRECTIONS FOR FUTURE RESEARCH

Going back and forth between the sample studies and our coding scheme, we summarized the key elements of the content analysis. Below, we present the categorization results and the main observations. We begin with an overview of the main theoretical frameworks used to predict the interplay between country- and firm-level governance mechanisms (Table 2). This is followed by reporting on the dependent variables examined and the units of analysis (Table 3). We then describe which salient country-level factors have been either combined with firm-level governance mechanisms to explain firms' economic performance (Table 4) or have been used to explain cross-country variations in the use of firm-level governance mechanisms (Table 5). We conclude by summarizing the lessons provided by this systematic literature review and presenting the implications, limitations and directions for future research.

TABLE 2
Theoretical Frameworks Used in the Studies Analyzed

Theoretical framework	Firm-level outcome	Country-level outcome	Total
Agency	46	6	52
Institutional	7	8	15
Agency & Institutional	10	1	11
Agency & Portfolio theory	2	1	3
Agency & Institutional & Transaction cost	0	1	1
Agency & Managerial hegemony	1	0	1
Agency & Resource-based view	1	0	1
Agency & Resource-based view & Transaction cost	1	0	1
Institutional & Managerial hegemony	1	0	1
Institutional & Transaction cost	1	0	1
Transaction cost	1	0	1
Portfolio theory	0	1	1
Total	**71**	**18**	**89**

What are the Predominant Theoretical Frameworks?

Although this topic has previously been covered in international governance reviews (e.g., Aguilera et al., 2015; Denis & McConnell, 2003), we believed it would be useful to analyze the theoretical backgrounds used in our sample. We therefore present an overview of the predominant theoretical bases for predicting the interplay between country- and firm-level governance mechanisms, as summarized in Table 2. As could be expected, agency theory is the most frequently used theoretical perspective for investigating cross-national differences in firm-level governance configurations and their performance effects. The second most frequently used perspective is institutional theory or a combination of agency and institutional theory. A detailed examination of the various theoretical premises and differences is not within the scope of this review, and a discussion of the different theoretical frameworks used in international and comparative governance research is provided by Aguilera et al. (2015).

The studies that adopt an agency perspective tend to consider country-level governance factors as macro-level attributes that influence the effectiveness of firm-level governance mechanisms. Consistent with the premises of agency theory, such as managerial self-interest and bounded rationality (Eisenhardt, 1989), these studies assume that firms trade off the costs and benefits of improving firm-level governance mechanisms while taking into account the national institutional environment in which the firm operates. In other words, firms adopt and/or improve firm-level governance mechanisms when the country-level governance is too weak to reassure investors (e.g., Dahya, Dimitrov, & McConnell, 2008 [F042]). These studies generally focus on the effects of firm ownership

© 2016 John Wiley & Sons Ltd

TABLE 3
Outcomes Examined in the Studies Analyzed

Outcomes	Accounting	Finance	Management	Total
Firm-level				
Firm performance				
Market-based	0	14	3	17
Accounting-based	0	5	3	8
Market & accounting-based	1	2	2	5
Corporate social responsibility	0	0	1	1
Firm governance practices				
Capital structure[a]	0	5	5	10
Board of directors	0	1	3	4
Financial information	3	0	0	3
Governance quality	0	1	0	1
Strategic decisions				
Merger and acquisitions	0	4	5	9
Risk taking	0	4	0	4
Trading volume	1	2	0	3
Cost of capital	1	0	1	2
CEO turnover	1	0	1	2
Top management team	0	0	1	1
Taxation	0	1	0	1
Country-level				
Financial market development	0	4	0	4
Foreign investment	1	2	1	4
Investor protection	0	3	0	3
Governance legitimacy	0	0	2	2
Governance codes	0	0	2	2
Market vs. bank financing	0	1	0	1
Financial disclosure regime	1	0	0	1
Globalization	0	1	0	1
Total	**9**	**50**	**30**	**89**

[a]Capital structure is a broad item. It includes financing decisions, dividend policies, securities listing decisions, bond issue costs, stock repurchases, and minority share incentives for partners.

structures on agency costs, measured by either firm economic performance or capital cost (see Tables 4, 5). Overall, their results indicate that country-level governance factors such as legal origin, investor protection, and/or contract enforcement reduce the cost of diversion when large shareholders are present. This in turn defines the nature of the agency conflict within the firm (e.g., Peng & Jiang, 2010 [M05]), and can explain national differences in the firms' governance–outcomes relationship. Given the focus on agency costs, there are surprisingly few studies that explore how country-level attributes interfere with the monitoring role of financial information (Bushman & Smith, 2001), or with the incentives provided by contingent compensation schemes for executives (Boyd, Santos, & Shen, 2012; Schiehll & Bellavance, 2009). Although these are important governance mechanisms that have been widely investigated in governance research in individual countries,[6] data availability problems due to differing national financial and compensation disclosure rules can make cross-national comparisons difficult.

In contrast, the studies that adopt an institutional framework (e.g., Filatotchev et al., 2013; Peng, 2004; van Essen, Heugens, Otten, & van Oosterhout, 2012) generally view national governance factors and/or individual perceptions about governance practices as determinants of firms' internal configuration choices, and not necessarily as intervening factors for the effectiveness of governance mechanisms. Accordingly, firm-level governance attributes are viewed as the result of social systems, in the sense that the firm is subject to external forces that drive the diffusion and use of specific governance best practices. A common theme emerges from this group of studies: a firm's quest for legitimacy or mimetic behavior tends to explain its internal governance mechanisms (e.g., Honig, 2008; Judge et al., 2009).

Given the topics examined and the multi-country samples, it is remarkable that only a few studies explicitly combine

© 2016 John Wiley & Sons Ltd

TABLE 4
Country- and Firm-Level Governance Mechanisms that Were Combined to Explain Firm Economic Performance (*N* = 30)[a]

Panel A	Legal origin (LSSV)	Investor protection (LLSV)	WGI (Kaufmann, Kraay, and Mastruzzi)	National governance system	Disclosure regime
Ownership structure	[F010][F014][F015] [F016][b][F021][F023] [F030][F038][F041] [F042]	[F06][F08][F016][b] [F021][F037][F038] [F042][F055][b][M064] [M085][M099]	[F06][F014][F025][M085]	[M051] [M099]	[F08][F041]
Board of directors	[F015][M068][F042]	[F06][F042][M085] [M099]	[F06][M085]	[M099]	
Financial information	[F014]	[F062]	[F062][F014]		[A017][F032]
CEO compensation		[M085]	[M085]		
Governance quality		[F037]			
Panel B	Enforcement	ICRG[c]	Industry	National culture	Market forcorporate control
Ownership structure	[F010][F015][F023] [F041][F042][F055][b] [M05]	[F010][F015]	[F06][F023][F030]		[F045]
Board of directors	[F015][F042]	[F015]	[F06][M087]	[M099] [F063]	[M081]
Financial information	[A017][F032][F062]	[F062]	[A017]		[M081]
CEO compensation					[M081]
Governance quality					

[a]Biggs and Shah (2006) [F031] analyze alternative social arrangements to formal institutions, such as business relationships and networks, while Cope, Piche, and Walter (2012) [F050] analyze several macro-environmental factors and the effects on bank operational losses. Because these studies use a very particular approach, we did not include them in Table 4.
[b]Beck, Demirgüç-Kunt, and Maksimovic (2006) [F055] do not provide a source for their control of corruption measure (available upon request). Chua, Eun, and Lai (2007) [F016] use data from the *Global Competitiveness Report*.
[c]*International Country Risk Guide* (ICRG): Boubakri, Dionne, and Triki (2008) [F015] use the following ICRG indexes: Law & Order, Corruption, and Enforcement of Contracts. Boubakri, Cosset, and Guedhami (2005) [F010] use Law & Order. Enikolopov, Petrova, and Stepanov (2014) [F062] use Law & Order, Corruption, and Bureaucratic Quality.

agency and institutional theory (e.g., Desai, Dyck, & Zingales, 2007; Driffield, Mickiewicz & Temouri, 2014 [M088]; Kim & Ozdemir, 2014 [M080]). These studies respond to recent calls for a more holistic view of firm-level governance configurations as an attempt to gain either economic benefits or legitimacy. Rather than focusing on firm economic performance or strategic outcomes, these studies instead attempt to explain firms' voluntary adoption of governance-related mechanisms such as greater transparency (e.g., financial disclosure, IFRS accounting standards, quality of independent auditor) and board composition attributes (e.g., board diversity, proportion of female directors or outsiders).

What Outcomes have been Investigated?

Our content analysis of each article also aimed to identify which outcome was investigated in each article. To do so, we coded the dependent variable in each study and how it was measured. Based on the results, we classified the studies into two groups. The first group (71 studies) includes comparative cross-national studies with the firm as the unit of analysis. They investigate whether country-level factors explain internal governance mechanisms, strategic decisions (e.g., CEO turnover, mergers and acquisitions), or the effectiveness of internal governance mechanisms – generally captured by the effects on firm economic performance. The second group (18 studies) includes cross-national studies with a macro-level outcome as the unit of analysis, and with the dependent variable measured at the country level. In general, these studies attempt to explain cross-national differences in economic and financial development and the quality of national governance systems.

What ultimately matters to firms, regulators, and economists is whether or not corporate governance affects the bottom line. Unsurprisingly, therefore, Table 3 shows that firm economic performance is the most frequently investigated dependent variable at the firm level (30 studies). Corporate social responsibility (CSR) is compared cross-nationally in only one study (Prior, Surroca, & Tribó, 2008). The other firm-level outcomes are classified into two subgroups: (1) cross-national studies that examine cross-national differences in the use of

© 2016 John Wiley & Sons Ltd

TABLE 5
Country-Level Factors Used to Explain Firm-Level Governance Mechanisms (N = 18)

Panel A	Legal origin (LSSV)	Investor protection (LLSV)	WGI (Kaufmann, Kraay, and Mastruzzi)	National governance system	Disclosure regime
Capital structure	[M026][M088] [F051][F052][F056]	[M076][F036] [F048][F051]	[F051]	[M040][M088]	
Board of directors	[M024]	[M080][a][F059]		[M024][M047]	
Financial information		[A04][A011] [A016]			[A016]
Governance quality	[F040]	[F040]			

Panel B	Enforcement	ICRG[c]	Media coverage (Dyck & Zingales, 2004)	National culture (GLOBE)	Hard vs. soft law
Capital structure	[F051]	[F052][M088]			[M097]
Board of directors		[F059]		[M024]	
Financial information			[A016]		
Governance quality		[F040]			

[a]Kim and Ozdemir (2014) [M080] also use indexes from The Heritage Foundation.
[b]*International Country Risk Guide* (ICRG): All studies in this column use only the Law & Order Index, except for Driffield, Mickiewicz, and Temouri (2014) [M088], which uses the Law & Order and Corruption indexes.

firm governance mechanisms (18 studies), such as capital structure, board composition, and financial disclosure, including one study that examines an aggregate score of firm governance quality; and (2) cross-national studies that examine whether external and internal governance mechanisms explain certain strategic decisions made by firms (22 studies), such as mergers and acquisitions, capital costs, or risk taking.

This preliminary classification led to two general observations. The cross-national governance research has generally equated governance effectiveness with shareholder wealth maximization. Relatively little emphasis has been placed on other intended governance outcomes such as strategic decisions or internal governance structure. Researchers have cast doubt upon the commonly used financial and stock price performance measures, which have traditionally been considered complete, and timeliness measures to capture governance-related outcomes (Schiehll & Bellavance, 2009). As Aguilera et al. (2015 point out, "It is imperative to understand governance effectiveness beyond shareholder value maximization." In future, researchers should attempt to operationalize governance effectiveness in relation to other firm-level outcomes.

Although the interplay between country- and firm-level governance mechanisms – whether to explain economic performance, strategic decisions, or internal governance mechanisms – is a central research question, very few studies explicitly predict a complementarity or substitution effect among these mechanisms. In our view, the equifinality perspective (Fiss, 2007), or the idea that different combinations of country- and firm-level governance mechanisms can lead to similar outcomes, as suggested by Aguilera and Jackson (2010), Aoki and Jackson (2008), and Filatotchev et al. (2013), has not been directly tested. One exception is the study by Garcia-Castro et al. (2013) [M081], which examines bundles of internal governance mechanisms to compare firms operating under two contrasting ideal-type national governance models: outsider (shareholder-oriented, Anglo-American) versus insider (stakeholder-oriented, Continental). Although very informative on how external governance forces shape different firm internal governance configurations, with similar effects on firm performance, their study dichotomizes the sample firms into two national governance systems, and the authors do not predict any specific effects of country-level factors on specific bundles of firm-level governance factors.

In the second group of studies, cross-national differences have been investigated as dependent variables in 18 studies (Table 3). Most of these studies examine whether country-level governance attributes explain national differences in financial market development[7] or related variables such as foreign investment (Aggarwal & Goodell, 2011; Cuervo-Cazurra & Genc, 2008; Honig, 2008; Kho, Stulz, & Warnock, 2009) or investor protection (Allen, Qian, & Qian, 2005; Ayyagari, Demirgüç-Kunt, & Maksimovic, 2008; Stulz & Williamson, 2003). Only two studies examine national differences in the adoption of national governance codes (Haxhi & van Ees, 2010; Zattoni & Cuomo, 2008).

A common and informative feature in these cross-national comparative and macro-level studies is the strong influence of LLSV, who hypothesize that differences in ownership structure observed among countries around the world are due mainly to the extent to which a country's laws are designed to protect investor rights and are enforced. These factors are considered fundamental determinants of how corporate finance and corporate governance evolve in a given country. At the same time, and apparently contradictory to this view, these studies assume that a country's legal origin is exogenous to the investigated country-level attributes, and that the various legal systems remained constant (invariant) over the time

© 2016 John Wiley & Sons Ltd

of study.[8] However, other governance scholars (e.g., Roe, 2005) question the exogeneity of legal systems as well as their dominant impact on country-level attributes such as investor protection and ownership concentration.

What Country-Level Factors have been Investigated as Independent Variables?

The heads of Tables 4 and 5 present the country-level factors considered as independent variables in the sample studies. Table 4 presents the country-level factors that have been combined with firm-level governance mechanisms to explain firm economic performance, while Table 5 presents the studies that use country-level factors as independent variables to explain firm governance mechanisms (dependent variables). Tables 4 and 5 are discussed in the next sections. In the next paragraphs we first provide an overview of our content analysis of the country-level factors.

Shareholder protection stands out as the most frequently used country-level variable, followed by country's legal origin, generally measured by a dichotomous variable: common law versus civil law origin. Because more attention is generally paid to the degree of enforcement of national governance practices and laws, the interaction between LLSV's antidirector rights index and a proxy for the country's law enforcement effectiveness is used frequently. However, there appears to be little consensus on either labels or measures. To illustrate, the studies by Durnev and Kim (2005) [F037] and Dahya, Dimitrov, and McConnell (2008) [F042] use the law and order index from the *International Country Risk Guide*. Other authors use a combination of indexes for the efficiency of the judicial system, rule of law, and corruption within a country. For instance, Haw, Ho, Ju, and Wu (2010) [F023], Chen, Young, and Zhuang (2013) [A017], and Peng and Jiang (2010) [M05] term this combination as "institutional development." A similar combination (i.e, a combined score for law and order, corruption, and enforcement) is used by Boubakri, Dionne, and Triki (2008) [F015] to measure investor protection. However, Boubakri, Cosset, and Guedhami (2005) [F010], Sarkissian and Schill (2009) [F032], and Fernandes, Lel, and Miller (2010) [F041] use only judicial system efficiency, as proposed by LLSV. Taken together, these studies fail to provide a common definition of either enforcement or investor protection as country-level governance factors. Moreover, we contend that the multidimensional characteristics and the inconsistent measurement methods used to capture country-level governance factors preclude comparisons as well as any theorizing about specific effects on the diffusion and effectiveness of firm-level governance mechanisms.

In addition, we observe substantial variations in the use of country-level factors as independent variables to capture salient dimensions of national institutional, economic, and governance environments. We also find inconsistencies as to whether these country-level factors are assumed to play a monitoring role, and therefore act as external governance mechanisms (Aguilera et al., 2015), or whether they are instead used as national contextual factors. For example, the size of stock and credit markets (relative to GDP) is frequently used as a proxy for a country's financial market development, as in Li, Moshirian, Pham, and Zein (2006) and Fernandes et al. (2010) [F041], whereas Liu and Magnan (2011) [M064] include market capitalization over GDP as a proxy for the efficiency of financial markets in putting governance legislation into effect. In our view, it is unclear whether stock market size plays a monitoring role (thus providing investor protection) or whether it acts as a contextual factor that helps regulators strengthen the legal requirements. These inconsistencies prevent reaching a common understanding of cross-national variations in the dimensions of country-level governance forces, or how these forces affect managerial discretion, which in turn affects the nature and extent of conflicts of interest within firms. Future studies should investigate country-level factors more deeply, and better distinguish country-level (external) governance forces from contextual factors that render firms more or less likely to be influenced by internal and external governance mechanisms.

On the other hand, many studies use all or some of Kaufmann, Kraay and Mastruzzi's (2011) six dimensions of the quality of a country's governance, called the *Worldwide Governance Indicators* (WGI). Studies either use the scores independently, as in Enikolopov, Petrova, and Stepanov (2014) [F062], or else they extract a construct (factor analysis), as in Lensink, Meesters, and Naaborg (2008) [F025].[9] However, scores for the six dimensions tend to be highly correlated, which calls into question the benefits of using them separately. Moreover, Lensink et al. (2008) [F025] use the WGI as a proxy for institutional quality to examine cross-national differences in bank efficiency; van Essen, Engelen, and Carney (2013) [M085] use them as a proxy for the quality of the legal system; and Enikolopov et al. (2014) [F062] use them as a dimension of legal investor protection. These studies illustrate how the same country-level factors can be used in different ways. Note also that only one study in our sample – van Essen et al. (2013) [M085] – distinguishes creditor from shareholder protection, and it is the only study that examines creditor rights as a country-level governance mechanism. This goes against the notion that creditor and shareholder protection are clearly distinct and not necessarily correlated attributes of a country's governance system, as demonstrated by Martins, Schiehll, and Terra (,2015) who also show that even for countries with the same legal origin, the level of either creditor or shareholder protection may differ.[10]

A final noteworthy observation is the emphasis on disclosure practices in the accounting studies: five out of nine consider a measure of the country-level disclosure regime. Again, various proxies for disclosure are used. La Porta, Lopez-de-Silanes, and Shleifer's (2006) disclosure requirements index is used as well as Standard & Poor's Transparency & Disclosure score, the CIFAR index, IASC reports, and differences in disclosure due to IFRS adoption (e.g., Chen et al., 2013 [A017]; Francis, Khurana, & Pereira, 2005 [A011]; Hail & Leuz, 2006; Khanna, Palepu, & Srinivasan, 2004; Maffet, 2012; Sarkissian & Schill, 2009 [F032]). Information disclosure can be viewed as either a firm-level choice (Schiehll & Bellavance, 2009) or the effect of an external governance mechanism (Aguilera et al., 2015). In any case, it influences the monitoring effects of other firm-level mechanisms (e.g., board monitoring, incentive compensation, stock price informativeness, institutional shareholdings). Future studies could explore how national disclosure regimes and financial

© 2016 John Wiley & Sons Ltd

disclosure practices interact to influence the monitoring role of independent outside directors, debt holders, financial analysts, and external equity holders.

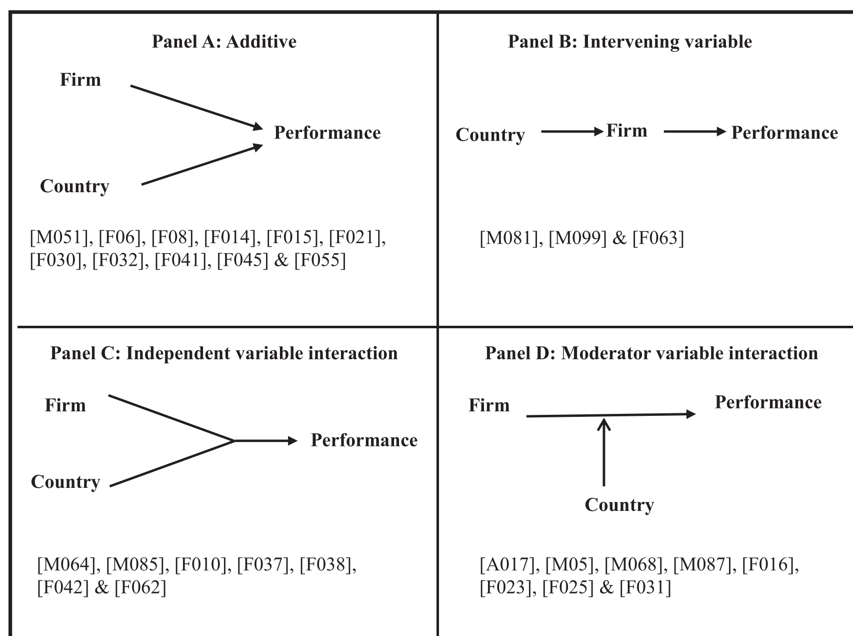
What Country- and Firm-Level Governance Mechanisms have been Combined to Explain Firm Performance?

Table 4 presents the combined sets of country-level factors and firm-level governance mechanisms that have been used to explain firm economic performance. Studies are represented by identification codes (complete study references and codes are provided in the Appendix). Table 4 reveals that ownership structure is the firm-level governance mechanism that is most often combined with country-level factors to explain firm economic performance. Of the many country-level factors it has been combined with, the most common are country's legal origin, enforcement, and LLSV's investor protection index. Again, this is not unexpected, given the large number of finance studies in the sample. Board composition is the second most frequent firm-level governance mechanism that is combined with country-level factors, and particularly in management studies. Notably, firm transparency is combined with country's legal enforcement in only three studies. Only one study investigates executive compensation, which is combined with country-level investor protection, as proposed by LLSV, and public perception about how authority is exercised, measured by the WGI. Only one study, by Durnev and Kim (2005) [F037], combines investor protection with an aggregate index for firm internal governance quality.

Although it is relatively straightforward to identify the combined country-level factors and firm-level governance mechanisms that explain firm performance, comparing and summarizing the findings is a more complex undertaking. As discussed above, the measurements and interpretations of the country-level variables used to capture the external governance mechanisms vary across the studies. More importantly, from a methodological perspective, there are substantial variations in how the intervening effects of country-level governance factors are operationalized. To delve further into these relationships and to extract more information from the studies in Table 4, we adapted Luft and Shields' (2003) framework to categorize the causal relationships considered.[10] We identified four different causal forms, as graphically represented in Figure 1, Panels A to D. The studies are again represented by identification codes.

We analyzed the 30 studies in Table 4 and classified them into four causal subgroups. Albeit somewhat subjective, this categorization is intended to provide a more nuanced understanding of the relationships that are considered and how they are empirically operationalized. We began by examining the theoretical grounds for the inclusion of particular country- and firm-level governance variables in the analysis. We then addressed the empirical model used to investigate the expected associations. The simplest case is when a linear regression model is used and includes both country- and firm-level variables as independent explanatory variables. If there are no preliminary assumptions or discussion about interactions between country- and firm-level variables, we classify the model as causal additive

FIGURE 1
Causal Model Forms of Studies Included in Table 4.Note:



Note: The study by Cope, Piche and Walter (2012) [F050] uses a very particular research design, and is therefore not classified in terms of casual form.

© 2016 John Wiley & Sons Ltd

(Panel A) (Bühlmann, Peters, & Ernest, 2014). For example, if the authors include a variable in the right-hand side of the model to capture a feature of firm ownership structure with no assumptions about whether its effect on the dependent variables is conditional on country governance factors (e.g., legal origin), we classified the article into Panel A. Thus, all studies that focus on the performance effect of a specific firm-level governance variable while controlling for country-level variables fall into this group (e.g., Ferreira & Matos, 2008 [F08]).

Conditional relationships between firm- and country-level variables can be represented by two different kinds of causal models: an intervening variable model (Panel B) or interaction models (Panels C and D) (Hartmann & Moers, 1999; Luft & Shields, 2003). The criteria for a Panel B study is that country-level governance affects firm-level governance and firm-level governance in turn affects the investigated outcome, which is firm economic performance in the case of Table 4. In other words, the models are classified as intervening variable (Panel B) when no direct relationship is expected between country-level variables and firm performance, but the country-level variable is assumed to have a significant effect on the firm-level governance mechanism, which in turn affects firm performance. For example, minority shareholder protection has no effect on firm performance except for a potential effect on firm ownership concentration, or large shareholder control-to-cash flow ratio. Note that some of the studies in Panel B do not necessarily use a standard regression model whereby firm- and country-level governance mechanisms are used to explain an outcome.

As mentioned above, interaction models can involve two different forms of conditional relationships. When both the firm- and country-level governance interacting variables are used as explanatory variables (Panel C), both are considered to exert a causal influence on the dependent variable. In other words, it is assumed that the magnitude of the influence on firm performance of each independent variable – here, the firm- and country-level governance indicators – depends on the magnitude of the influence of the other variable. This is considered an independent variable interaction model (Luft & Shields, 2003). The second form, moderator variable interaction (Panel D), is used when only the country-level variable (moderator) exerts no influence on either the dependent or independent variables, and shows no correlation with them (Hartmann & Moers, 1999; Sharma, Durand, & Gur-Arie, 1981). We therefore classified studies into Panel C if the empirical analysis reveals an explicit interaction term between firm- and country-level governance mechanisms. Thus, except for the study by Chua, Eun, and Lai (2007) [F016], a common feature among the articles in Panel C is that both these variables plus an interaction term act as explanatory variables (i.e, each term has its own direct effect on the outcome). In contrast, Panel D includes studies that use country-level governance variables only as moderators of the effect of firm governance on performance. The main difference with Panel C is that the studies in Panel D adopt the assumption that country-level governance factors have no effect on performance, except for moderating the effect of firm-level governance configuration on performance. Panel D articles may include an interaction term, but they do not necessarily include the country-level variable as an independent variable.[11]

According to the above criteria, we analyzed, compared, and summarized the empirical evidence obtained from all 30 studies in Table 4. Because Cope, Piche, and Walter (2012) [F050] use a unique approach and do not consider any firm-level governance variables, their study is not included in any of the four subgroups. The remaining 29 studies are classified in terms of casual form in Panels A, B, C, and D. We summarize the main findings below.

Eleven of the 30 studies analyze the direct effects of firm-level governance mechanisms on economic performance while controlling for country-level governance factors. According to our framework, these studies use the assumption of additive causality (Figure 1, Panel A) (Bühlmann et al., 2014) to examine the effects of country and firm governance attributes on firm economic performance. Each independent variable – here, firm-level governance mechanisms (*Firm*) and country-level factors (*Country*) – has an incremental effect on firm performance. That is, the effect of each variable is analyzed independently of the effect and value of the remaining independent variables, and no other effect exists. This implies that there is no explicit theorization about whether or how the country-level factors influence the effectiveness of firm-level mechanisms. This also implies the assumption that the effect of each firm-level governance mechanism is constant across countries, and that the performance effect is concurrent or simultaneous with the effects of the country-level factors. The common underlying argument in this subgroup is that the strength of the country-level governance factor acts directly on agency costs, but there is no explicit prediction as to whether or how this effect operates through internal governance mechanisms.

To illustrate, some studies in Panel A examine the additive effects of ownership structure and country-level governance factors. Ferreira and Matos (2008) [F08] find a positive performance effect of foreign institutional ownership, whereas the performance effect of a country's investor protection indicator is negative and disclosure index is positive. Similarly, Aggarwal, Erel, Ferreira, and Matos (2011) [F021] find a positive association between international institutional investor ownership and firm value, with an additional positive effect if the investors are located in a country with high investor protection. Note, however, that these authors do not consider an interaction between international institutional ownership and country of origin. The assumption would therefore be that the two variables have an additive and independent effect on firm performance. Nenova (2003) [F045] demonstrates that a country's investor protection, enforcement, market for corporate control, and corporate charter provisions help explain cross-national differences in the market value of the control block of votes. The logic is that this is the equity premia of minority shareholders when a firm's internal configuration includes dual-class shares and controlling shareholders. Similarly, Beck, Demirgüç-Kunt, and Maksimovic (2006) [F055] show that both ownership concentration – as a proxy for the probability of the controlling shareholder being a member of a business group – and a country's contract enforcement quality are negatively related to firm market capitalization. Beltratti and Stulz (2012) [F06], focusing on financial institutions, find that shareholder-friendly boards perform significantly worse during a subprime crisis, but that this adverse effect

© 2016 John Wiley & Sons Ltd

is compensated by a positive effect of the country's investor protection level (antidirector rights).

Disclosure is also investigated in this subgroup. Chandar, Patro, and Yezegel (2009) [F014] compare firms operating in countries with different disclosure requirements and find that greater "voice and accountability" and stronger common law have positive effects on firm value. Similarly, Sarkissian and Schill (2009) [F032] find some evidence of permanent valuation gains in firms without large shareholders that are listed in countries with stricter disclosure rules. Fernandes et al. (2010) [F041] report negative stock returns in response to the announcement by the Securities and Exchange Commission (SEC) that foreign firms could opt out of the US disclosure regulations – especially for firms in countries with weak disclosure requirements, weak civil law, and low judicial efficiency.

Other authors in this subgroup (Panel A), such as Chuanrommanee and Swierczek (2007) [M051], find no association between internal corporate governance and economic performance in Thai, Malaysian, or Singaporean financial corporations. Boubakri et al. (2008) [F015] show that higher investor protection in the country of the target firm leads to smaller positive mergers and acquisitions (M&A) returns in the insurance industry. Mersland and Strøm (2009) [F030] find that a female CEO is positively associated with the performance of microfinance institutions, whereas board size, inside directors, and bank regulation have no association.

Figure 1, Panel B reveals that three of the 30 studies in Table 4 use an intervening variable causal form (Luft & Shields, 2003). The underlying premise here is that country-level factors affect firm-level governance mechanisms, which in turn affect firm economic performance. In other words, country-level governance factors have no direct effect on firm performance. For instance, the study of microfinance firms by Strøm, D'Espallier, and Mersland (2014) [F063] examines whether national culture – measured by the Gender Inequality Index (GII) – is associated with female leadership of the firm (i.e, a female CEO, Chair, or Director), and whether female leadership explains firm economic performance. A similar causal form is used by Garcia-Castro et al. (2013) [M081]. Using fuzzy set qualitative comparative analysis (fsQCA), they examine how national governance systems with significant differences in terms of market for corporate control explain different bundles of internal governance mechanisms, and how different bundles are in turn associated with similar firm economic performance. In like manner, Crossland and Hambrick (2007) [M099] propose that a country's national system shapes the level of CEO discretion, which in turn explains firm economic performance. Instead of regression models with performance as the dependent variable, Crossland and Hambrick (2007) [M099] partition the performance variance to investigate whether there are between-country differences in the portion of variance that can be attributed to CEO discretion.

Several of the studies in Table 4 (7 of 30) use some form of explicit interaction between country- and firm-level variables to explain firm economic performance. According to Luft and Shields (2003), the assumption in this case is an independent variable interaction (Figure 1, Panel C) as the causal form, whereby country-level governance factors interact with firm-level governance mechanisms to help explain firm economic performance. These studies interact country- and firm-level variables of interest and use the product (combined effect) as an independent variable, assuming that the performance effect of firm-level governance mechanisms is conditional on the strength of country-level governance factors. Importantly, although country- and firm-level mechanisms are independent and not mutually influential, they both influence performance (Sharma et al., 1981). As mentioned above, the most frequent interaction is between a country's investor protection level and firm ownership structure. For example, the seminal study by La Porta, Lopez-de-Silanes, Shleifer and Vishny (2002) [F038] demonstrates higher firm valuation in countries with better shareholder protection and in firms with higher cash flow ownership by the controlling shareholder. Although the interaction between cash flow rights and investor protection (antidirector rights) is not significant, it renders the coefficient of investor protection significant. Liu and Magnan (2011) [M064] show that the greater the difference between shareholder control and cash flow rights, the less positive the association between private control of self-dealing regulations and firm value, but that it has no effect on the negative association between public control regulations and firm value. Boubakri et al. (2005) [F010] find a positive effect of ownership concentration on firm performance after company privatization, with a stronger effect in countries with weak investor protection.

The study by van Essen et al. (2013) [M085] goes beyond ownership structure to examine the performance effects of CEO duality and board size during the financial crisis of 2008–2009. However, their research design is unique in this subgroup in that they use the hierarchical linear model, which considers firm-level variables as nested within country-level variables. Their results suggest that the positive effects of CEO duality and board size as well as the negative effect of ownership structure are conditional on country-level factors such as the country's rule of law and creditor rights, and that shareholder protection does not affect these associations. The performance effect of board composition is examined by Dahya et al. (2008) [F042], who find that the positive effect of the proportion of independent directors on firm value depends on the magnitude of the country's investor protection. More specifically, they document that independent boards improve firm performance only in countries with weak investor protection. Enikolopov et al. (2014) [F062] investigate firm-level transparency and country-level factors (investor protection, WGI, and ICRG) during the above-mentioned financial crisis and find that they are complementary in explaining firm value. Firm-level transparency had little or no effect on firms' stock price reaction during the crisis in countries with low-quality country-level institutions. However, it had greater informativeness for firm valuation in countries with high-quality country-level institutions. Durnev and Kim (2005) [F037] report that firms with better governance scores have higher value, and that this association is stronger in weak investor protection countries. They suggest that firms adapt to poor legal environments by establishing effective governance practices within the firm.

Eight of the 30 studies in Table 4 consider a moderator variable interaction causal form (Figure 1, Panel D) where, in contrast to the independent variable interaction, country-level factors are assumed to moderate the association between firm-level mechanisms and performance. Thus, country-level factors are assumed to influence the firm's governance–

© 2016 John Wiley & Sons Ltd

performance association but to have no direct effect on firm performance.

Several studies in this subgroup focus on financial institutions. For example, Yeh, Chung, and Liu (2011) [M068] find that financial institutions with more independent directors sitting on auditing and risk committees showed better performance during the financial crisis of 2008–2009, and a civil law dummy strengthens this positive association. Chakrabarty and Bass (2014) [M087] show that microfinance institutions with boards that include more socioeconomic expertise and female members incur lower operating costs, and this positive performance effect is strengthened by industry-specific regulatory institutions. Haw et al. (2010) [F023] find that concentrated control is related to poor performance by banks, and that this negative effect is mitigated by legal origin (common law), enforcement, and private monitoring. These relationships are nonlinear as well as conditional on owner type. For instance, state-owned banks underperform widely held banks. Another example provided by Lensink et al. (2008) [F025] is that foreign ownership has a positive effect on bank performance, but this positive association is moderated by the interaction between foreign investors and the WGI. In contrast, higher WGI in the home country and greater similarity between home and host country's WGI improves bank performance.

Looking at different mechanisms, Chen et al. (2013) [A017] find a positive association between a country's disclosure regimes (IFRS adoption) and firm performance. They show that IFRS demands for increased disclosure and transparency improve investment efficiency. This spillover effect is stronger if the invested firm is located in a country with strong enforcement, indicating that enforcement makes firm financial disclosure more credible. Peng and Jiang (2010) [M05] find that family control and pyramid structures do not significantly explain firm value. However, when they interact these variables with the country's law enforcement, they find a positive effect on firm value. Biggs and Shah (2006) [F031] find that small and medium-sized enterprises (SMEs) in sub-Saharan African countries that have European or Asian networks via their leadership attributes have better productivity, higher growth, and larger start-up size.

In contrast to other studies in this subgroup, Chua et al. (2007) [F016] examine the moderating effect of ownership concentration, which acts as a firm-level moderator. They find that antidirector rights, rule of law, and enforcement of insider trading laws have a direct positive effect on firms' Tobin's Q. However, the interaction between antidirector rights and firm ownership concentration shows a negative effect. The variable ownership concentration is not included as an explanatory variable, and the authors conclude that the performance effect of a country's investor protection, measured by antidirector rights, depends on the concentration of firm ownership, which is consistent with the causal form in Panel D.

What Country-Level Governance Factors have been used to Explain Firm-Level Governance Mechanisms?

In order to compare the 18 studies in Table 5 that examined the effect of country-level governance factors on firm-level governance mechanisms, we applied the same steps used above to analyze the studies in Table 4. We first identified the dependent variables that were investigated (the firm-level governance mechanisms that were explained) and the main country-level factors that were used as independent variables. The dependent variables are presented in the first column of Table 5, Panels A and B, where the table headings indicate the country-level factors. Studies are represented by identification codes (complete study references and codes are provided in the Appendix).

The firm-level governance mechanisms examined in the 18 studies are grouped into four categories. Capital structure, the most frequently investigated firm-level governance mechanism in the entire sample, includes attributes related to firm ownership structure and debt financing, such as debt maturity structure, cost of debt, and initial public offering (IPO). Surprisingly, only four studies attempt to explain cross-country variations in composition of the board of directors, and only one study examines firm-level governance quality. The financial information category refers to examinations of firms' financial disclosure and earnings quality. As expected, country's legal origin and investor protection are the most frequently used country-level factors to explain cross-country differences in firm-level governance mechanisms.

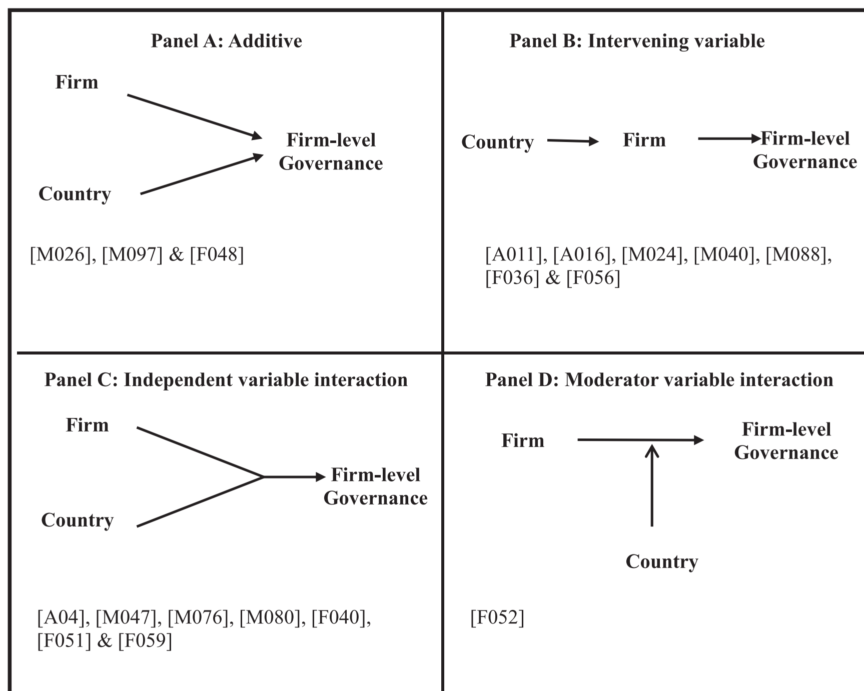
Using the same framework that was applied to the studies in Table 4, we further analyzed and categorized the causal relationships considered in all the sampled studies. The studies and their respective causal models are graphically represented in Figure 2, Panels A to D. It is worth noting that even though certain studies were classified as using a similar causal model (same panel), they often explain different firm-level governance mechanisms. The findings are summarized below.

Three of the 18 studies use an additive causal model (Bühlmann et al., 2014; Luft & Shields, 2003). For example, Boubakri et al. (2010) [F048] find that both the ultimate owner control rights and the focal firm country's antidirector rights index are significant and independent determinants of the type of American Depositary Receipts (ADRs) that cross-listing firms choose. Moore, Bell, Filatotchev, and Rasheed (2012) [M097] examine the capital market choice made by firms that issue an IPO. From an institutional perspective, these authors find that foreign IPO firms select a host capital market where the firm's governance attributes make a good fit with the host market's institutional environment. Hence, a firm's capital market choice is driven by the additive effect of internal and external governance mechanisms. Jansson and Larsson-Olaison (2010) [M026] examine the effect of cross-listing, used as a proxy for Swedish firms exposed to a different legal origin and higher takeover threats, on firms' stock repurchase decisions. They find that Swedish firms that are cross-listed in the US or the UK increase the propensity for stock repurchases.

As shown in Figure 2, Panel B, seven of the 18 studies in Table 5 use an intervening variable causal form (Luft & Shields, 2003). In this subgroup, the premise is that country-level factors affect firm-level governance mechanisms, which in turn may affect other firm-level governance mechanisms. Two studies included in Panel B explain cross-country variation in a firm's financial disclosure by the intervening effect of country- on firm-level variables. Francis et al. (2005) [A011] show a positive effect of a country's antidirector rights on the quality of firms' financial disclosure, which in turn reduces its cost of capital. Haw, Hu, Lee, and Wu (2012) [A016]

© 2016 John Wiley & Sons Ltd

FIGURE 2
Causal Model Forms of Studies Included in Table 5.



document that countries with more stringent financial disclosure requirements (CIFAR index), higher earnings quality, and greater media coverage tend to have stock prices that are more informative about firms' future earnings. Examining cross-country variations in board composition, the study by Grosvold and Brammer (2011) [M024] finds a higher proportion of women on corporate boards (board diversity) of firms operating in English and Scandinavian legal systems compared to Germanic and French legal systems. Driffield et al. (2014) [M088] show that when investing in countries with weak investor protection, foreign investors leave higher proportions of equity to minority local shareholders. Similarly, Roy (2012) [M040] provides evidence that a country's governance quality (Kaufmann et al., 2011) influences firms' partner selection criteria for international joint ventures. Ferris, Jayaraman, and Sabherwal (2009) [F056] show that compared to civil law countries, firms operating in common law countries present a greater catering effect of dividends. The study by Bae and Goyal (2009) [F036] documents that cross-country differences in contract enforceability, measured by the International Country Risk Guide (ICRG), adversely affect how loans are structured and priced.

Moving to the use of an interaction model, seven studies consider country- and firm-level governance mechanisms as independent interacting variables (Figure 2, Panel C). The premise is that both country- and firm-level variables have a causal and simultaneous influence on other firm governance mechanisms. Hence, unlike the studies in Figure 2, Panel B, the assumption is that the magnitude of the effect of firm- and country-level governance attributes on other firm-level governance mechanisms depends on their mutual influence. Doidge et al. (2007) [F040] investigate whether country investor protection is associated with the pros and cons of firms that decide to improve their overall governance structure. They find that country-level governance factors contribute more than firm ownership structure to explain firm-level governance quality, and that in countries with weaker investor protection, firms invest less in mechanisms to improve governance and transparency. Guedhami, Pittman, and Saffar (2009) [A04] examine the simultaneous effect of firm ownership structure and a country's antidirector rights index on firms' auditor choice. They show that shareholdings by international investors increase the probability of choosing a Big Four auditor, and that this effect is stronger in countries with weaker investor protection. Van Veen and Elbertsen (2008) [M047] find that wider board national diversity is explained by both the country's legal origin and the focal firm's board type (executive or supervisory). Li and Song (2013) [F059], focusing on financial institutions, investigate whether country-level investor protection and contract enforcement as well as firm-level attributes (cross-listing and two-tier boards) increase board independence. These authors also show that investor protection strengthens the effects of both types of regulatory agency (state and private monitoring) on board independency. Vanacker, Heughebaert, and Manigart (2014) [M076] provide evidence that higher antidirector rights index and venture capital ownership simultaneously increase the likelihood for firms to choose equity over debt financing. Kim and Ozdemir (2014) [M080] use a multi-level model to show that firm-level governance attributes such as board size with investor protection and market for corporate control affect board structure. They document that in countries with stronger investor protection, boards tend to focus on wealth protection (monitoring) over wealth creation (advice). Engelen and van Essen (2010) [F051] find that the presence of a venture capitalist in a firm's ownership structure

© 2016 John Wiley & Sons Ltd

simultaneously with country-level governance factors, such as the antidirector rights index, rule of law, control of corruption, and contract enforcement, reduces IPO underpricing.

Only one study in Table 5 considers a moderator variable interaction (Figure 2, Panel D). Thus, Lau and Yu (2010) [F052] examine the moderating effect of investor protection on the association between geographic proximity, used as a proxy for information asymmetry, and firm's cost of international bond market. They find that the cost reduction of geographic proximity between the firm and the lead underwriter is significantly lower in countries with legal systems that provide better investor protection.

CONCLUDING REMARKS

The purpose of this review was to synthesize and appraise the cross-national corporate governance research to date that empirically investigates the interplay between country- and firm-level governance mechanisms and the effects on firm-level outcomes. Using a systematic literature review, we examined 192 articles published in 23 scholarly journals in the fields of accounting, economics, finance, and management for the period 2003 to 2014. The content analysis of the final sample of 89 studies reveals that although relevant cross-national governance research has been conducted, the message is far from clear or conclusive.

As could be expected, the cross-national governance research has been largely informed by LLSV's classification of a country's degree of investor protection, with the vast majority of studies considering this country-level factor among the independent variables. Although a country's legal origin is a rather broad measure for capturing differences in national governance systems, it is the most commonly used measure in the studies, followed by Kaufmann et al.'s (2011) six dimensions of national governance quality. Overall, the results provide consistent evidence that investor protection has a fundamental effect on financial market development as well as firm ownership structure. However, the evidence on the effects of country-level factors on the use of other firm-level governance mechanisms and their effectiveness is considerably less consistent. This could be explained by the wide variation in the operationalization and interpretation of these external forces. Moreover, cross-national governance research has examined only a small number of informal institutions to date, comprising voluntary codes, social norms, relationships, and networks. This could most probably be explained by the challenges related to the conceptualization and measurement of the monitoring power of informal institutions.

We observed that, for many countries, there is little or no comparative empirical evidence on external governance mechanisms other than legal origin, investor protection, and their interplay with ownership structure. Hence, more research is needed in this area. As emerging markets around the world look to developed systems on which to model their governance standards and firm-level practices, it becomes increasingly vital to understand how other country-level governance factors influence firm internal governance structures. In addition, the time-invariant nature of country-level factors should be challenged. In fact, some countries have implemented major changes in their legal and governance structures, opening up opportunities for natural experiments in cross-national governance. It is therefore imperative for future cross-national governance studies to adopt more institutionally embedded governance frameworks, as suggested by Filatotchev et al. (2013), and to expand the research scope beyond shareholder protection and wealth maximization by improving the measurement of governance effectiveness, as proposed by Aguilera et al. (2015).

In this systematic review, we reveal that country-level variables are conceived and applied differently across studies, and that different causal models (Figures 1, 2) are used to describe relationships between similar variables. These research and methodological design issues need to be addressed in order to improve our understanding of the interplay between country- and firm-level governance mechanisms and the effects on firm outcomes. Whereas cross-level models are required for a more complete and accurate explanation of the intervening effects of external governance mechanisms on the effectiveness of firm governance configurations, it would also be important to better consider the causal forms of these associations. Our findings suggest that the assumptions involved in causal relationships should be inferred with caution, and the empirical measures used to test these associations should be thoughtfully designed. This might require the use of additional statistical tools besides interaction terms and/or subsamples (e.g., Bell et al., 2014). We believe that a more conscientious match between theorized associations and empirical tests would be essential for developing a "rigorous and relevant global theory of comparative corporate governance" (Schiehll et al., 2014: 179).

In light of the above-presented evidence, we also contend that extant cross-national governance research is inconsistent with respect to whether country-level factors act as external governance mechanisms by constraining managerial discretion within firms (e.g., investor protection, disclosure regimes, market for corporate control) or whether these country-level attributes capture the national context and the outcomes of the quality of national governance systems. For example, in some of the studies that explain cross-national differences in firm economic performance (e.g., Enikolopov et al., 2014 [F062]; van Essen, Engelen, & Carney, 2013 [M085]), corruption control, legal enforcement, and economic development are combined with legal origin, market for corporate control, and shareholder protection (antidirector rights index) to capture differences in monitoring forces afforded by the state. Another example is a country's financial market development, which is conceived as a dependent variable (an outcome) explained by other country-level factors such as legal origin, investor protection, and ownership concentration in the studies by Djankov, McLiesh, and Shleifer (2007), Ergungor (2004), and Liu and Magnan (2011) [M064]. Alternatively, financial market development is used as an independent variable to explain country-level disclosure practices in the study by Khanna et al. (2004).

These discrepancies support Kaufmann et al.'s (2011) argument that governance research would benefit from a finer distinction between rules-based and outcome-based indicators of national governance. Whereas rules-based indicators measure whether countries have adequate anticorruption

© 2016 John Wiley & Sons Ltd

legislation or agencies, outcome-based indicators capture whether anticorruption laws are actually enforced. Accordingly, and based on our systematic review, we contend that in order to improve our understanding of cross-national differences in governance mechanisms, more refined research designs are required. We need to better isolate the sets of country-level attributes that make firms more or less likely to be influenced by external governance mechanisms – which we call contextual factors – from the country-level factors that act as external mechanisms by reducing managerial discretion and defining the nature of agency conflicts within the firm. Consistent with Aguilera et al. (2015), this would be a first step in an attempt to obtain a more nuanced picture of the salient dimensions in which external (country-level) monitoring mechanisms vary among countries and how they mediate the effectiveness of firm-level governance practices.

This systematic literature review contributes to the cross-national corporate governance literature in several ways. We summarize and organize the empirical research to date, identify certain research gaps, and point to ways to conduct more nuanced studies on the interplay between country- and firm-level governance mechanisms and the effects on firm-level outcomes. We document the country-level factors and firm-level governance mechanisms that have been investigated and combined to date, discuss how they are measured, and assess the causal forms that have been used to investigate their combined effects. Although the substantial variations in research design (measures and casual forms) make comparisons difficult, they underscore the need for grounded theoretical frameworks to better guide the use of causal associations in future empirical studies in this area. Although such a framework is not within the scope of this paper, we hope that our review and assessment can provide the motivation and guidance for further research. Finally, we highlight some salient findings that improve our understanding of the interplay between country- and firm-level governance mechanisms. In short, cross-national governance research is an exciting and fruitful area for further exploration.

ACKNOWLEDGEMENTS

The authors acknowledge financial support from the Social Sciences and Humanities Research Council (435-2013-1179), Brazilian Research Council (CNPq), and HEC Montréal (Canada). Also acknowledged are the helpful comments by Krista B. Lewellyn (University of Wyoming), Paulo Renato Terra Soares (EAESP-FGV), Luiz Ricardo Kabbach de Castro (EESC-USP), Samuel Tardif-Menard (HEC Montreal), Seppo Ikäheimo Ilya Okhmatovskiy (McGill), (Aalto BIZ), and participants of the research workshops at HEC Montréal. The authors are also grateful to the Guest-Editors of this Special Issue and two anonymous reviewers for their helpful comments on earlier versions of this article.

NOTES

1. Aoki and Jackson (2008) use the term "standard" to refer to the traditional economic and micro-level agency perspective, where corporate governance is viewed as simply dealing with the ways in which suppliers of finance to corporations ensure that they get a return on their investment.
2. Studies that are included in table 4 and 5 are represented by identification codes in square brackets. Complete study references and codes are provided in the Appendix.
3. A systematic review differs from a meta-analysis in the sense that it does not uses statistical (i.e, inferential) or econometric procedures to synthesize the findings and analyze the data (Tranfield et al., 2003).
4. http://search.proquest.com/abicomplete/index?accountid=11357
5. Articles were classified as "empirical" if they applied inductive logic, clearly described the research methods used, and used data obtained using either qualitative or quantitative methods. In contrast, articles were classified as "conceptual" if they were based solely on deductive reasoning, without using empirical methods. These include reviews, perspectives, and commentaries.
6. An in-depth review of the compensation–governance related literature is provided by Boyd et al. (2012).
7. We use the expression "financial market" to include studies that investigated capital and/or debt market development. These studies use the size of stock and credit markets relative to a country's GDP as a proxy for financial market development.
8. The study by Djankov, McLiesh, and Shleifer (2007) is an exception. They cover a 25-year period taking into account reforms made to the creditor's rights index in any of these years.
9. The advantages of using the WGI are that: (1) it is time-variant (starts in 1996 and is continuously actualized for more than 200 economies); and (2) the scores for each dimension are based on (recent) perceptions of a large number of citizens, experts, and companies, which mitigates concerns about measurement errors.
10. (For more details, see the discussion in Martins, Schiehll, and Terra (2015) of the distinct effects of shareholder protection and creditor rights. Constructing bundles on these two dimensions, these authors show a pairwise correlation of roughly 0.17.)
11. The endogenous nature of corporate governance makes empirical causal-form predictions challenging and often incomplete, as explained by Brown et al. (2011). A discussion of endogeneity and its challenges for governance research is beyond the scope of our review. For the purposes of our analysis, we simply interpret the causal-form predictions in the sample studies according to the authors' expected associations between the investigated dependent and independent variables.
12. Three articles in Panel D use an explicit interaction term, with all interacted variables included as independent variables, similar to the articles in Panel C. Nevertheless, their hypothesis may be stated as: "The positive effect of X on Y is stronger in countries in which the variable Z is high." The articles are by Chen, Young, and Zhuang (2013) [A017], Yeh, Chung, and Liu (2011) [M068], and Chakrabarty and Bass (2014) [M087].

APPENDIX

The following list contains the studies presented in Tables 4,5 and their respective codes. The initial letter in the article's code identifies the discipline as follows: Accounting (A), Finance (F), and Management (M). Note that, given the fact that several studies examine more than one firm-level mechanism or country-level factor, they may appear more than once in each table.

[A04] Guedhami, O., Pittman, J. A., & Saffar, W. 2009. Auditor choice in privatized firms: Empirical evidence on the role of state and foreign owners. ***Journal of Accounting and Economics***, 48: 151–171.

[A011] Francis, J. R., Khurana, I. K., & Pereira, R. 2005. Disclosure incentives and effects on cost of capital around the world. ***Accounting Review***, 80: 1125–1162.

 © 2016 John Wiley & Sons Ltd

[A016] Haw, I. M., Hu, B., Lee, J. J., & Wu, W. 2012. Investor protection and price informativeness about future earnings: International evidence. ***Review of Accounting Studies***, 17: 389–419.

[A017] Chen, C., Young, D., & Zhuang, Z. 2013. Externalities of mandatory IFRS adoption: Evidence from cross-border spillover effects of financial information on investment efficiency. ***The Accounting Review***, 88: 881–914.

[F06] Beltratti, A. & Stulz, R. M. 2012. The credit crisis around the globe: Why did some banks perform better? ***Journal of Financial Economics***, 105: 1–17.

[F08] Ferreira, M. A. & Matos, P. 2008. The colors of investors' money: The role of institutional investors around the world. ***Journal of Financial Economics***, 88: 499–533.

[F010] Boubakri, N., Cosset, J.-C., & Guedhami, O. 2005. Postprivatization corporate governance: The role of ownership structure and investor protection. ***Journal of Financial Economics***, 76: 369–399.

[F014] Chandar, N., Patro, D. K., & Yezegel, A. 2009. Crises, contagion and cross-listings. ***Journal of Banking & Finance***, 33: 1709–1729.

[F015] Boubakri, N., Dionne, G., & Triki, T. 2008. Consolidation and value creation in the insurance industry: The role of governance. ***Journal of Banking & Finance***, 32: 56–68.

[F016] Chua, C. T., Eun, C. S., & Lai, S. 2007. Corporate valuation around the world: The effects of governance, growth, and openness. ***Journal of Banking & Finance***, 31: 35–56.

[F021] Aggarwal, R., Erel, I., Ferreira, M., & Matos, P. 2011. Does governance travel around the world? Evidence from institutional investors. ***Journal of Financial Economics***, 100: 154–181.

[F023] Haw, I.-M., Ho, S. S. M., Hu, B., & Wu, D. 2010. Concentrated control, institutions, and banking sector: An international study. ***Journal of Banking & Finance***, 34: 485–497.

[F025] Lensink, R., Meesters, A., & Naaborg, I. 2008. Bank efficiency and foreign ownership: Do good institutions matter? ***Journal of Banking & Finance***, 32: 834–844.

[F030] Mersland, R. & Strøm, R. Ø. 2009. Performance and governance in microfinance institutions. ***Journal of Banking & Finance***, 33: 662–669.

[F031] Biggs, T. & Shah, M. K. 2006. African SMEs, networks, and manufacturing performance. ***Journal of Banking & Finance***, 30: 3043–3066.

[F032] Sarkissian, S. & Schill, M. J. 2009. Are there permanent valuation gains to overseas listing? ***Review of Financial Studies***, 22: 371–412.

[F036] Bae, K. H. & Goyal, V. K. 2009. Creditor rights, enforcement, and bank loans. ***The Journal of Finance***, 64: 823–860.

[F037] Durnev, A. & Kim, E. 2005. To steal or not to steal: Firm attributes, legal environment, and valuation. ***The Journal of Finance***, 60: 1461–1493.

[F038] La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. 2002. Investor protection and corporate valuation. ***The Journal of Finance***, 57: 1147–1170.

[F040] Doidge, C., Karolyi, G. A., & Stulz, R. M. 2007. Why do countries matter so much for corporate governance? ***Journal of Financial Economics***, 86: 1–39.

[F041] Fernandes, N., Lel, U., & Miller, D. P. 2010. Escape from New York: The market impact of loosening disclosure requirements. ***Journal of Financial Economics***, 95: 129–147.

[F042] Dahya, J., Dimitrov, O., & McConnell, J. J. 2008. Dominant shareholders, corporate boards, and corporate value: A cross-country analysis. ***Journal of Financial Economics***, 87: 73–100.

[F045] Nenova, T. 2003. The value of corporate voting rights and control: A cross-country analysis. ***Journal of Financial Economics***, 68: 325–351.

[F048] Boubakri, N., Cosset, J. C., & Samet, A. 2010. The choice of ADRs. ***Journal of Banking & Finance***, 34: 2077–2095.

[F050] Cope, E. W., Piche, M. T., & Walter, J. S. 2012. Macroenvironmental determinants of operational loss severity. ***Journal of Banking & Finance***, 36: 1362–1380.

[F051] Engelen, P. J., & van Essen, M. 2010. Underpricing of IPOs: Firm-, issue- and country-specific characteristics. ***Journal of Banking & Finance***, 34: 1958–1969.

[F052] Lau, S. T., & Yu, J. 2010. Does proximity matter in international bond underwriting? ***Journal of Banking & Finance***, 34: 2027–2041.

[F055] Beck, T., Demirgüç-Kunt, A., & Maksimovic, V. 2006. The influence of financial and legal institutions on firm size. ***Journal of Banking & Finance***, 30: 2995–3015.

[F056] Ferris, S. P., Jayaraman, N., & Sabherwal, S. 2009. Catering effects in corporate dividend policy: The international evidence. ***Journal of Banking & Finance***, 33: 1730–1738.

[F059] Li, L., & Song, F. M. 2013. Do bank regulations affect board independence? A cross-country analysis. ***Journal of Banking & Finance***, 37: 2714–2732.

[F062] Enikolopov, R., Petrova, M., & Stepanov, S. 2014. Firm value in crisis: Effects of firm-level transparency and country-level institutions. ***Journal of Banking & Finance***, 46, 72–84.

[F063] Strøm, R. Ø., D'Espallier, B., & Mersland, R. 2014. Female leadership, performance, and governance in microfinance institutions. ***Journal of Banking & Finance***, 42, 60–75.

[M05] Peng, M. W., & Jiang, Y. 2010. Institutions behind family ownership and control in large firms. ***Journal of Management Studies***, 47: 253–273.

[M024] Grosvold, J. & Brammer, S. 2011. National institutional systems as antecedents of female board representation: An empirical study. ***Corporate Governance: An International Review***, 19: 116–135.

[M026] Jansson, A. & Larsson-Olaison, U. 2010. The effect of corporate governance on stock repurchases: Evidence from Sweden. ***Corporate Governance: An International Review***, 18: 457–472.

[M040] Roy, J. P. 2012. IJV partner trustworthy behaviour: The role of host country governance and partner selection criteria. ***Journal of Management Studies***, 49: 332–355.

[M047] van Veen, K. & Elbertsen, J. 2008. Governance regimes and nationality diversity in corporate boards: A comparative study of Germany, the Netherlands and the United Kingdom. ***Corporate Governance: An International Review***, 16: 386–399.

[M051] Chuanrommanee, W. & Swierczek, F. W. 2007. Corporate governance in ASEAN financial corporations: Reality or illusion? ***Corporate Governance: An International Review***, 15: 272–283.

[M064] Liu, M. & Magnan, M. 2011. Self-dealing regulations, ownership wedge, and corporate valuation:

© 2016 John Wiley & Sons Ltd

International evidence. ***Corporate Governance: An International Review***, 19: 99–115.

[M068] Yeh, Y.-H., Chung, H., & Liu, C.-L. 2011. Committee independence and financial institution performance during the 2007–08 credit crunch: Evidence from a multi-country study. ***Corporate Governance: An International Review***, 19: 437–458.

[M076] Vanacker, T., Heughebaert, A., & Manigart, S. 2014. Institutional frameworks, venture capital and the financing of European new technology-based firms. ***Corporate Governance: An International Review***, 22: 199–215.

[M080] Kim, Y. U. & Ozdemir, S. Z. 2014. Structuring corporate boards for wealth protection and/or wealth creation: The effects of national institutional characteristics. ***Corporate Governance: An International Review***, 22: 266–289.

[M081] García-Castro, R., Aguilera, R. V., & Ariño, M. A. 2013. Bundles of firm corporate governance practices: A fuzzy set analysis. ***Corporate Governance: An International Review***, 21: 390–407.

[M085] van Essen, M., Engelen, P.-J., & Carney, M. 2013. Does "good" corporate governance help in a crisis? The impact of country- and firm-level governance mechanisms in the European financial crisis. ***Corporate Governance: An International Review***, 21: 201–224.

[M087] Chakrabarty, S. & Bass, A. E. 2014. Corporate governance in microfinance institutions: Board composition and the ability to face institutional voids. ***Corporate Governance: An International Review***, 22: 367–386.

[M088] Driffield, N., Mickiewicz, T., & Temouri, Y. 2014. Institutions and equity structure of foreign affiliates. ***Corporate Governance: An International Review***, 22: 216–229.

[M097] Moore, C. B., Bell, R. G., Filatotchev, I., & Rasheed, A. A. 2012. Foreign IPO capital market choice: Understanding the institutional fit of corporate governance. ***Strategic Management Journal***, 33, 914–937.

[M099] Crossland, C. & Hambrick, D. C. 2007. How national systems differ in their constraints on corporate executives: A study of CEO effects in three countries. ***Strategic Management Journal***, 28: 767–789.

REFERENCES

Aggarwal, R. & Goodell, J. W. 2011. International variations in expected equity premia: Role of financial architecture and governance, ***Journal of Banking & Finance***, 35: 3090–100.

Aguilera, R. V., Desender, K., Bednar, M. K., & Lee, J. H. 2015. Connecting the dots, ***The Academy of Management Annals***, 9: 483–573.

Aguilera, R. V., Filatotchev, I., Gospel, H., & Jackson, G. 2008. An organizational approach to comparative corporate governance: Costs, contingencies, and complementarities, ***Organization Science***, 19: 475–92.

Aguilera, R. V. & Jackson, G. 2010. Comparative and international corporate governance, ***The Academy of Management Annals***, 4: 485–556.

Allen, F., Qian, J., & Qian, M. 2005. Law, finance, and economic growth in China, ***Journal of Financial Economics***, 77: 57–116.

Aoki, M. & Jackson, G. 2008. Understanding an emergent diversity of corporate governance and organizational architecture: An essentiality-based analysis, ***Industrial and Corporate Change***, 17: 1–27.

Ayyagari, M., Demirgüç-Kunt, A., & Maksimovic, V. 2008. How well do institutional theories explain firms' perceptions of property rights? ***The Review of Financial Studies***, 21: 1833–71.

Bell, G., Filatotchev, I., & Aguilera, R. V. 2014. Corporate governance and investors' perceptions of foreign IPO value: An institutional perspective, ***Academy of Management Journal***, 57: 301–20.

Boyd, B. K., Santos, M. F., & Shen, W. 2012. International developments in executive compensation, ***Corporate Governance: An International Review***, 20: 511–8.

Brown, P., Beekes, W., & Verhoeven, P. 2011. Corporate governance, accounting and finance: A review, ***Accounting and Finance***, 51: 96–172.

Bühlmann, P., Peters, J., & Ernest, J. 2014. CAM: Causal additive models, high-dimensional order search and penalized regression, ***The Annals of Statistics***, 42: 2526–56.

Bushman, R. M. & Smith, A. J. 2001. Financial accounting information and corporate governance, ***Journal of Accounting and Economics***, 32: 237–333.

Cuervo-Cazurra, A. & Genc, M. 2008. Transforming disadvantages into advantages: Developing-country MNEs in the least developed countries, ***Journal of International Business Studies***, 39: 957–79.

Denis, D. K. & McConnell, J. J. 2003. International corporate governance, ***Journal of Financial and Quantitative Analysis***, 38: 1–36.

Desai, M. A., Dyck, A., & Zingales, L. 2007. Theft and taxes, ***Journal of Financial Economics***, 84: 591–623.

Djankov, S., McLiesh, C., & Shleifer, A. 2007. Private credit in 129 countries, ***Journal of Financial Economics***, 84: 299–329.

Durisin, B. & Puzone, F. 2009. Maturation of corporate governance research, 1993–2007: An assessment, ***Corporate Governance: An International Review***, 17: 266–91.

Dyck, A. & Zingales, L. 2004. Private benefits of control: An international comparison, ***The Journal of Finance***, 59: 537–600.

Eisenhardt, K. 1989. Agency theory: An assessment and review, ***Academy of Management Review***, 14: 57–74.

Ergungor, O. E. 2004. Market- vs. bank-based financial systems: Do rights and regulations really matter? ***Journal of Banking & Finance***, 28: 2869–87.

Filatotchev, I., Jackson, G., & Nakajima, C. 2013. Corporate governance and national institutions: An emerging research agenda, ***Asia Pacific Journal of Management***, 30: 965–86.

Fiss, P. C. 2007. A set-theoretic approach to organizational configurations, ***Academy of Management Review***, 32: 1180–98.

Hail, L. & Leuz, C. 2006. International differences in the cost of equity capital: Do legal institutions and securities regulation matter? ***Journal of Accounting Research***, 44: 485–531.

Hambrick, D. C. & Finkelstein, S. 1987. Managerial discretion: A bridge between polar views on organizations. In L. L. Cummings & M. Staw (Eds.), ***Research in organizational behavior***, vol. 9: 369–406. Greenwich, CT: JAI Press.

Hartmann, F. G. H. & Moers, F. 1999. Testing contingency hypotheses in budgetary research: An evaluation of the use of moderated regression analysis, ***Accounting, Organizations and Society***, 24: 291–315.

Haxhi, I. & van Ees, H. 2010. Explaining diversity in the worldwide diffusion of codes of good governance, ***Journal of International Business Studies***, 41: 710–26.

Honig, A. 2008. Do improvements in government quality necessarily reduce the incidence of costly sudden stops? ***Journal of Banking & Finance***, 32: 360–73.

Hoskisson, R. E., Castleton, M., & Withers, M. 2009. Complementarity in monitoring and bonding: More intense monitoring leads to higher executive compensation, ***Academy of Management Perspectives***, 23: 57–74.

Jackson, G. & Deeg, R. 2008. Comparing capitalism: Understanding institutional diversity and its implications for international business, ***Journal of International Business***, 39: 540–61.

Judge, W. 2009. The complexity of international corporate governance research, ***Corporate Governance: An International Review***, 17: 525.

© 2016 John Wiley & Sons Ltd

Judge, W. 2012. Pioneering research in comparative corporate governance: The role of special issues, ***Corporate Governance: An International Review***, 20: 1–2.
Judge, W., Douglas, T., & Kutan, A. 2009. Institutional antecedents of corporate governance legitimacy, ***Journal of Management***, 34: 765–85.
Judge, W., Filatotchev, I., & Aguilera, R. 2010. Comparative corporate governance and international business research, ***Corporate Governance: An International Review***, 18: 493–5.
Kaufmann, D., Kraay, A., & Mastruzzi, M. 2011. The worldwide governance indicators: Methodology and analytical issues, ***Hague Journal on the Rule of Law***, 3: 220–46.
Khanna, T., Palepu, K. G., & Srinivasan, S. 2004. Disclosure practices of foreign companies interacting with US markets, ***Journal of Accounting Research***, 42: 475–508.
Kho, B.-C., Stulz, R. M., & Warnock, F. E. 2009. Financial globalization, governance, and the evolution of the home bias, ***Journal of Accounting Research***, 47: 597–635.
La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. 2006. What works in securities laws? ***The Journal of Finance***, 61: 1–32.
La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. W. 1998. Law and finance, ***Journal of Political Economy***, 106: 1113–55.
Li, D., Moshirian, F., Pham, P. K., & Zein, J. 2006. When financial institutions are large shareholders: The role of macro corporate governance environments, ***The Journal of Finance***, 61: 2975–3007.
Luft, J. & Shields, M. D. 2003. Mapping management accounting: Graphics and guidelines for theory-consistent empirical research, ***Accounting, Organizations and Society***, 28: 169–249.
Maffet, M. 2012. Financial reporting opacity and informed trading by international institutional investors, ***Journal of Accounting and Economics***, 54: 201–20.
Martins, H. C., Schiehll, E., & Terra, P. R. S. 2015. Debt maturity and ownership structure: The distinctive effects of shareholder protection and creditor rights, ***Academy of Management Proceedings***, 2015: 17737.
Millar, C. C. J. M., Eldomiaty, T. I., Choi, C. J., & Hilton, B. 2005. Corporate governance and institutional transparency in emerging markets, ***Journal of Business Ethics***, 59: 163–74.
Misangyi, V. F. & Acharya, A. G. 2014. Substitutes or complements? A configurational examination of corporate governance mechanisms, ***Academy of Management Journal***, 57: 1681–705.
North, D. C. 1990. ***Institutions, institutional change and economic performance***. New York: Cambridge University Press.
Peng, M. W. 2004. Outside directors and firm performance during institutional transitions, ***Strategic Management Journal***, 25: 453–71.
Prior, D., Surroca, J., & Tribó, J. A. 2008. Are socially responsible managers really ethical? Exploring the relationship between earnings management and corporate social responsibility, ***Corporate Governance: An International Review***, 16: 160–77.
Rediker, K. J. & Seth, A. 1995. Boards of directors and substitution effects of alternative governance mechanisms, ***Strategic Management Journal***, 16: 85–99.
Roe, M. 2005. The institutions of corporate governance. In C. Menard & M. Shirley (Eds.), ***Handbook of new institutional economics***. New York: Springer.
Schiehll, E., Ahmadjian, C., & Filatotchev, I. 2014. National governance bundles perspective: Understanding the diversity of corporate governance practices at the firm and country levels, ***Corporate Governance: An International Review***, 22: 179–84.
Schiehll, E. & Bellavance, F. 2009. Boards of directors, CEO ownership, and the use of non-financial performance measures in the CEO bonus plan, ***Corporate Governance: An International Review***, 17: 90–106.
Sharma, S., Durand, R. M., & Gur-Arie, O. 1981. Identification and analysis of moderator variables, ***Journal of Marketing Research***, 18: 291–300.
Stulz, R. M. & Williamson, R. 2003. Culture, openness, and finance, ***Journal of Financial Economics***, 70: 313–49.
Tranfield, D., Denyer, D., & Smart, P. 2003. Towards a methodology for developing evidence-informed management knowledge by means of systematic review, ***British Journal of Management***, 14: 207–22.
van Essen, M., Heugens, P. P. M. A. R., Otten, J., & van Oosterhout, J. H. 2012. An institutional-based view of executive compensation: A multilevel meta-analytic test, ***Journal of International Business Studies***, 43: 396–423.
Ward, A. J., Brown, J. A., & Rodriguez, D. 2009. Governance bundles, firm performance and the substitutability and complementarity of governance mechanisms, ***Corporate Governance: An International Review***, 17: 646–60.
Weimer, J. & Pape, J. 1999. A taxonomy of systems of corporate governance, ***Corporate Governance: An International Review***, 7: 152–66.
Zattoni, A. & Cuomo, F. 2008. Why adopt codes of good governance? A comparison of institutional and efficiency perspectives, ***Corporate Governance: An International Review***, 16: 1–15.

Eduardo Schiehll is Associate Professor of Accounting at HEC Montreal (Canada), and also holds a position as Visiting Professor in Corporate Governance at the Aalto Business School, Helsinki University, Finland. Professor Schiehll is a Fellow of the Society of Management Accountants of Canada (CMA) and of the Ordre des Comptables Professionnels Agréés du Québec (CPA). His research and teaching activities are focused in the areas of corporate governance, management control systems design, and performance management.

Henrique Castro Martins is a PhD candidate in Accounting & Finance at *Escola de Administração – Universidade Federal do Rio Grande do Sul* (EA-UFRGS), Porto Alegre, Brazil. His research interests include corporate governance, corporate finance, agency theory, and financial markets.

© 2016 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 200–221

State Control and Corporate Governance in Transition Economies: 25 Years on from 1989

Anna Grosman*, Ilya Okhmatovskiy and Mike Wright

ABSTRACT

Manuscript type: Review
Research Question/Issue: Which forms of state control over corporations have emerged in countries that made a transition from centrally-planned to marked-based economies and what are their implications for corporate governance? We assess the literature on variation and evolution of state control in transition economies, focusing on corporate governance of state-controlled firms. We highlight emerging trends and identify future research avenues.
Research Findings/Insights: Based on our analysis of more than 100 articles in leading management, finance, and economics journals since 1989, we demonstrate how research on state control evolved from a polarized approach of public–private equity ownership comparison to studying a variety of constellations of state capitalism.
Theoretical/Academic Implications: We identify theoretical perspectives that help us better understand benefits and costs associated with various forms of state control over firms. We encourage future studies to examine how context-specific factors determine the effect of state control on corporate governance.
Practitioner/Policy Implications: Investors and policymakers should consider under which conditions investing in state-affiliated firms generates superior returns.

Keywords: Corporate Governance, Transition Economies, State Capitalism, China, Russia

INTRODUCTION

Over a quarter of a century since the fall of the Berlin Wall, former communist regimes have transitioned to democratic or semi-democratic regimes, although the process of becoming market economies has advanced at different rates and directions across countries. Transition economies represent a large sub-category of emerging economies (Hoskisson, Eden, Lau, & Wright, 2000; Hoskisson, Wright, Filatotchev, & Peng, 2013). Given the 25 years since 1989, it is timely to review how means of state control have changed in these transition economies.

While developed economies have seen a gradual demise of state-owned enterprises (SOEs) and there has been extensive privatization in emerging economies, state capitalism is a popular choice among transition economies (Wooldridge, 2012). Accordingly, we address the following research question: "Which forms of state control over corporations have emerged in countries that made a transition from centrally planned to marked-based economies and what are their implications for corporate governance?" To address this question, we suggest a taxonomy of state control used to structure our literature review.

*Address for correspondence: Anna Grosman, Aston Business School, Aston University, Aston Triangle, Birmingham B4 7ET, UK. Tel: +44 121 204 3815; E-mail: a.grosman@aston.ac.uk

We consider the transformation of state control in transition economies focusing on the emergence of contemporary forms of state capitalism following privatizations of the 1990s. Earlier reviews focused on privatization comparing performance of state-owned and privatized companies (Djankov & Murrell, 2002; Estrin & Wright, 1999; Megginson & Netter, 2001), but interactions between state and private sector have evolved and new forms of state control have emerged. Our motivation is driven by a lack of comprehensive reviews encompassing the evolution and variety of state control over firms and their governance implications. We fill this gap by bringing together studies scattered across several disciplines and identifying relevant theoretical perspectives that suggest positive and negative effects of state control, as summarized in Table 1.

We searched for studies that examine state control and corporate governance of firms in transition economies. The first category of studies considered various mechanisms of state control: partial ownership, board of directors, veto rights, managerial incentives, loans, and regulation. The second category analyzed relationships between state control and corporate governance. We did not cover studies about performance implications of state control; these implications have been discussed by Musacchio, Lazzarini, and Aguilera (2015).

We analyzed more than 100 articles published since 1989, focusing on peer-reviewed studies (Pugliese, Bezemer,

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12145

TABLE 1
Positive and Negative Effects of State Control According to Different Theoretical Perspectives

Theoretical perspective	Negative effects of state control	Forms of state control that can minimize its negative effects	Positive effects of state control	Forms of state control that can maximize its positive effects
Agency theory	State as principal provides weak monitoring. Not clear who acts as principal on behalf of state. Soft budget constraints create weak incentives for managers as agents.	Active state involvement in Corporate Governance (CG). Creation of asset management companies to manage state assets defines principal responsible for monitoring. Firms with partial state ownership benefit from diligent monitoring by private investors.	Under conditions of entrenched management and diffused ownership, state shareholders can exercise influence over management even with relatively small stake.	State ownership accompanied by CG mechanisms enabling effective control.
Transaction cost economics	State control increases costs of transacting by increasing risk that firm may not fulfill contract obligations due to politically motivated interference.	Partial state ownership gives private shareholders enough influence to prevent unilateral decision-making by state shareholders. Indirect state ownership isolates political actors from direct involvement in CG.	State control decreases costs of transacting by reducing risk of fraudulent behavior on behalf of firms.	State ownership accompanied by CG mechanisms enabling active involvement of state shareholders in monitoring.
Institutional theory	Performing simultaneously functions of regulator and owner of economic actors creates conflicts of interest.	Isolating state agencies acting as shareholders from state agencies acting as regulators.	State control solves some problems associated with institutional voids. State leverages control over firms when acting as "institutional entrepreneur."	State ownership accompanied by CG mechanisms enabling monitoring. Regulations enabling "institutional entrepreneurship" by state-controlled firms.
Industrial policy perspective	More opportunities for corruption. Obstacles created for independent firms competing with state-supported industry champions.	Partial state ownership gives private shareholders influence to prevent unilateral decision-making by state shareholders. Regulations that protect private firms in industries dominated by state-supported firms.	State control enables implementation of industrial policy through coordination of investments made by state-supported industry champions.	Transparent CG mechanisms to be used by the state for coordinating firms receiving state support.
Resource-based view	Endowment with state resources makes state-controlled firms reluctant to develop skills to obtain these resources without state support.	Providing managers of state-controlled firms with sufficient autonomy and creating strong incentives to focus on increasing competitiveness of their firms.	State-controlled firms benefit from access to valuable resources belonging to the state.	CG mechanisms engaging state as shareholder increase chances of gaining access to state resources. Regulation that constrains potential corruption associated with distribution of these resources.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1
(Continued)

Theoretical perspective	Negative effects of state control	Forms of state control that can minimize its negative effects	Positive effects of state control	Forms of state control that can maximize its positive effects
Political embeddedness perspective	Political connections that firms use to obtain benefits from the state also constrain firms' strategic choices.	Formalization of state expectations and high transparency of governance process limit politicians' ability to exercise informal influence over firms' strategic choices.	Political connections facilitate firms' access to valuable resources controlled by the state.	Formalization of state commitment to provide state-affiliated firms with privileged access to resources. Regulation that constrains potential corruption associated with distribution of state resources.

Zattoni, Huse, Van den Bosch, & Volberda, 2009; Seglen, 1994), but also included in our review books and book chapters containing significant empirical material. We did not review studies about traditional SOEs with state as the sole shareholder – such enterprises were covered by earlier reviews on privatization (Megginson & Netter, 2001). Instead we focused on partial state ownership and indirect state ownership via intermediaries. We generally refer to such firms as SOEs. Key studies representing different theoretical perspectives and different transition economies are shown in Table 2.

We adopt a broad definition of "transition economies" to include former socialist countries of Central and Eastern Europe, former republics of the Soviet Union, and Asian countries emerging from a socialist-type command economy towards a market-based economy (China, Laos, Cambodia, Mongolia, and Vietnam). Many of these economies have completed transition to a market economy. The countries that joined the EU (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, and Slovenia in 2004, followed by Romania and Bulgaria in 2007, and Croatia in 2013) are no longer in transition.

We focus mainly on the two largest transition economies, China and Russia (drawing some comparisons with smaller transition economies), because of the economic and political importance of SOEs in these countries and because studies overwhelmingly relate to these two countries (Bruton, Peng, Ahlstrom, Stan, & Xu, 2015; Musacchio et al., 2015). Comparing China and Russia helps identify context-specific factors affecting corporate governance of state-controlled companies. Timelines of the main events affecting state control and corporate governance in China and Russia are shown in Tables 3 and 4, respectively.

The paper is structured as follows. First, we outline a range of forms of state control going beyond dominant ownership positions, including government loans, appointments of state officials to board or top management positions, party committees, special veto rights, regulation, and business–government networks, and consider how these have evolved over time in China, Russia and other transition economies. Second, we review the literature on governance structures and processes with particular attention to board composition and independence, transparency and disclosure, and executive compensation in state-controlled firms operating in transition economies. Finally, we elaborate an agenda for future research on corporate governance implications of state control taking into account the variety of transition economies.

MEANS OF STATE CONTROL: VARIATION AND EVOLUTION OVER TIME

Over the last 25 years, public perception and academic reasoning about the role of state in transition economies have fluctuated sharply. During the early 1990s, the pro-market and anti-state climate reigned following the collapse of communist regimes. Research on SOEs in transition economies during our focal period started with privatization studies (Aharoni, 1986; Djankov & Murrell, 2002; Estrin & Wright, 1999; Ramamurti & Vernon, 1991). These studies viewed SOEs as a temporary organizational form because privatization of SOEs was widely anticipated (Dewenter & Malatesta, 2001; Spicer, McDermott, & Kogut, 2000). In the second half of the 1990s, initial euphoria over privatization in planned economies began to wane as the hard work of enterprise restructuring continued. Since the mid-2000s, the pace of privatization and deregulation has slowed. During this period, private investors were often offered minority stakes, with the state keeping a controlling stake. A new form of state capitalism developed, influenced by increasing globalization and market orientation. To address this transformation, a more recent literature emerged devoted to partial state ownership (Inoue, Lazzarini, & Musacchio, 2013) and other forms of state control. As the overwhelming majority of studies about state control have been conducted in China (Bruton et al., 2015), we begin by reviewing these studies and then consider studies about state control in Russia and other transition economies.

Variation and Evolution of State Control in China

SOEs with Partial State Ownership. China took a reform approach of "gradualism" (Wang, Guthrie, & Xiao, 2011), preserving state control while implementing new institutional

© 2015 John Wiley & Sons Ltd

TABLE 2
Summary of Key Studies Representing Different Theoretical Perspectives

	Author(s) (Year)	Theory	Data	Key findings	Empirical setting
1.	Chen (2015)	AT	World Bank survey of 2,400 public and private firms across 18 Chinese cities in 2003.	Weaker helping hand from government associated with higher number and proportion of outsiders on board.	China
2.	Cull et al. (2015)	AT	World Bank 120 city survey of 12,400 Chinese manufacturing firms conducted in 2005.	Government connections associated with substantially less severe financial constraints.	China
3.	Liang et al. (2015)	AT, IT, IP	2,394 listed non-financial Chinese firms, 80% market capitalization of which are SOEs, 2001–2011, Datastream, WIND, CSMAR, and CCER.	Diminishing effect of executive political connections and increasing effect of state ownership control on globalization decisions and degree of globalization of SOEs with full or partial state ownership.	China
4.	Lin et al. (2015)	AT	All firms with listed A-shares on Shenzhen or Shanghai stock exchange, 2005–2009. Publicly available data.	Firms spending resources to bond with new government via CSR activities receive higher levels of government subsidies or have greater propensity to receive future government subsidies. They outperform firms not investing in political networking via CSR.	China
5.	Qian and Yeung (2015)	AT	All Chinese listed firms, 1995–2009. CSMAR database.	Controlling shareholders' tunneling activity positively associated with firms' state-owned bank loan access.	China
6.	Sun et al. (2015)	PE	154 firms listed on Hong Kong, Shanghai, and Shenzhen stock exchanges. Event study analysis surrounding removal of the Communist Party Chief in Shanghai in 2006.	An unanticipated high-profile political event triggers a negative stock market evaluation effect of managerial ties to municipal government, but the effect of government ownership ties is insignificant. Companies combining managerial and ownership ties experienced less post-shock reduction in market value than those holding only managerial political ties.	China
7.	Zheng et al. (2015)	RBV, PE	280 television manufacturing firms in China, 1993–2003. China Statistical	Political ties to local governments improve both firm survival ("buffering") and performance ("enabling"); central ties do not provide buffering or enabling benefits.	China

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2
(Continued)

Author(s) (Year)	Theory	Data	Key findings	Empirical setting
		Yearbook and the China Electronics Industry Yearbook.	Effects contingent upon prior performance.	
8. Li et al. (2014)	IT, IP	Sixteen illustrative case examples from South East Asia and China	Restructuring of central SOEs into "national champions" exposes them to stronger institutional pressures from home and host country governments; local SOEs with fewer obligations to serve national strategic prerogatives display greater managerial autonomy and market orientation.	South East Asia and China
9. Meyer et al. (2014)	IT	386 foreign investments of listed Chinese firms, 2009, public data.	SOEs face more complex institutional pressures in host countries than private firms, adapting mode and control decisions differently.	China
10. Zeng et al. (2013)	IT, RBV	Chinese beer industry, 1995–2004 (661 firms 1995 and 231 in 2004, and 93 acquisitions). 70% founded as SOEs; CNBS.	Firms founded as SOEs or COEs (collectively owned enterprises) desire acquisition, unless have undertaken multiple changes, or attracted more private investment. Acquisition likelihood has U-shaped relationship with investment in marketing resources.	China
11. Chernykh (2011)	AT	153 privately controlled firms, 2003.	Formerly privatized and domestically owned companies in strategically important sectors face highest risks of transfers from private to state control. Renationalization not driven by firm profitability.	Russia
12. Wang et al. (2011)	IT	Chinese listed firms, 1994–2003.	Analysis of how SASAC impacts ownership concentration and allows firm owners to monitor and stabilize firm behavior.	China
13. Okhmatovskiy (2010)	PE	450 Russian banks 2001, 640 banks 2002, and 555 banks 2003, Central Bank of Russia, Interfax and financial statements.	Banks demonstrate higher profitability when they have ties to SOEs but not when they have direct ties to state agencies.	Russia
14. Sun et al. (2010)	PE	Qualitative case study based on 142 interviews, Chinese	Declining, and even negative, value of deep political embeddedness by MNEs in	China

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2
(Continued)

Author(s) (Year)	Theory	Data	Key findings	Empirical setting
		automotive industry, 1980–2005	a politically stable host emerging economy.	
15. Chernykh (2008)	AT	Russian listed firms.	Federal and regional governments' control is exercised through elaborate pyramid structures.	Russia
16. Fan et al. (2007)	AT	790 newly partially privatized firms in China, covering 7,255 CEOs and directors, 1993–2001. IPO prospectuses and other public sources.	Firms with politically connected CEOs underperform those without and have poorer growth. Firms led by politically connected CEOs more likely to appoint other bureaucrats to the board rather than directors with relevant professional backgrounds.	China
17. Ralston et al. (2006)	Competing values of organizational culture	Survey of 435 SOEs, privately owned enterprises, and foreign-controlled businesses in manufacturing, 2001 and 2002.	SOEs in China have transitioned from their pre-reform culture into a market-oriented one.	China
18. Thun (2004)	IP	China's automotive industry case studies	Industrial policy by the state to regulate and control certain types of FDI resulted in firms under state control tightly integrated into global production networks.	China
19. Uhlenbruck et al. (2003)	RBV, Organizational learning	Theoretical models leading to normative propositions	Privatized SOEs improve learning ability by actively searching for information in product and factor markets rather than relying on information provided by established networks. They should also adapt organizational structure to allow for more efficient information processing by integrating resources to achieve strategic fit.	Central and Eastern Europe
20. Ferguson et al. (2002)	Cost–benefit framework	145 Hong Kong stock exchange firms, 1995–1996.	Chinese formerly wholly owned SOEs cross-listed on Hong Kong stock exchange disclose more information than other firms listed in China.	China
21. Filatotchev et al. (2000)	AT	Medium and large industrial firms; questionnaire interviews, 1997–1998.	Downsizing following privatization influenced by corporate governance and institutional change caused by business crisis.	CIS
22. White (2000)	TCE, RBV, and RDT			China

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2
(Continued)

Author(s) (Year)	Theory	Data	Key findings	Empirical setting
		China's pharmaceutical SOEs 1985–1994.	SOEs' M&A decisions are outcomes of a simultaneous consideration of external competitive and internal capabilities-related factors.	
23. Cao et al. (1999)	IP	Business history narrative	Privatization and reforms in China driven by the federal government.	China
24. Claessens and Djankov (1999)	AT	706 Czech firms, 1992–1997.	Firm productivity and profitability increases with ownership concentration contingent upon state and other types of ownership.	Czech Republic
25. Brouthers and Bamossy (1997)	Stakeholder theory	Case studies of eight dyads of Western European and Central/Eastern European firms	Transitional governments intervene at different stages of negotiation process and can change the balance of power, sometimes to detriment of their own SOEs.	Central and Eastern Europe

Review studies are not included. AT: agency theory; TCE: transaction cost economics; IT: institutional theory; RBV: resource-based view; IP: industrial policy; PE: political embeddedness; RDT: resource dependence theory.

forms. In the 1980s, China decentralized state control to provincial, municipal, township, and village level governments, at the same time allowing private sector emergence. During the 1990s reforms, China's state vowed to "hold on to the big and let go of the small" (*zhua da fang xiao*) (Fernandez-Stembridge & Fernandez, 2007). As a result, China developed a complex system of state ownership with elaborate control mechanisms (Delios, Wu, & Zhou, 2006). The Chinese state retained stakes (often non-controlling) in privatized medium-sized SOEs and imposed restrictions on non-state share transfers. Large SOEs remained under government control, but some were partly privatized later (Cao, Qian, & Weingast, 1999). Gradualism had two benefits. First, it allowed the state to retain its stabilizing role. Second, the central government pushed ownership control down to localities, creating an incentive structure similar to those experienced by managers of large industrial firms.

Continuing central government commitment to support employment in SOEs implied state-owned banks usually bailed out loss-making SOEs, creating "soft budget" constraints (Zhu, 2012). This strategy resulted in "reform without losers" (Lau, Qian, & Roland, 2000) and helped minimize social instability and reduce resistance to reform. In contrast, central government had no commitment to support employment in township and village enterprises (TVEs). Thus, TVEs faced a much tighter budget constraint and stronger market discipline than SOEs controlled by central government. However, from the mid-1990s, central government progressively reduced commitment to support employment in SOEs, and many small and medium-sized SOEs went bankrupt or were privatized. More diversified ownership was introduced with some larger SOEs being converted into shareholding companies, with the majority of shares controlled by the state.

This restructuring led to productivity growth and a decline in SOEs' share of labor (Zhu, 2012). The Chinese government aimed at selectively fortifying SOE presence in specific industries (Nolan, 2001) and in developing SOEs into globally competitive firms (Ralston, Terpstra-Tong, Terpstra, Wang, & Egri, 2006). In 2000, China launched its "Go Global" policy, establishing some SOEs as "national champions" and leading to their globalization (Liang, Ren, & Sun, 2015; Thun, 2004). The culture of SOEs became similar to those of privately and foreign-owned businesses (Granrose, Huang, & Reigadas, 2000). However, the Chinese government did not desire to completely eradicate former hierarchical structures.

A key ingredient of reforms was "corporatization" of SOEs which meant that they fell under the jurisdiction of the 1994 Company Law, aimed at promoting corporate property rights and corporate governance structures. Corporatized SOEs were subsequently listed on the Shanghai and Shenzhen stock exchanges (Firth, Fung, & Rui, 2006) to access private and foreign capital. Moreover, China started the split-share structural reform in 2006 as part of its program to transfer state shares in SOEs to private investors (Haveman & Wang, 2013) and to transform the corporate governance model from administrative to more market-oriented (Ralston et al., 2006). Typically, when a Chinese SOE was listed, only a small proportion of equity was sold to private investors (Conyon & He, 2011) with the state and parent SOEs keeping voting control. Sheng and Zhao (2013) show that recently the "state advance and private retreat" phenomenon (*guo jin min tui*)

© 2015 John Wiley & Sons Ltd

TABLE 3
Events that Affected State Control and Corporate Governance in China during last 25 Years

Year	Event	What has changed as a result of this event	Implications for state control and corporate governance
1990–1991	Shanghai stock exchange opens in December 1990, Shenzhen stock exchange opens in July 1991	Organized share trading makes it easy for companies to sell shares and for investors to buy shares. Category of minority shareholders dramatically expanded to include different types of return-seeking investors.	Principal reason for opening Shanghai and Shenzhen stock exchanges was to provide an opportunity for SOEs to raise funds. By selling shares to private investors, the state diluted its holdings in SOEs.
1992	CSRC established	The China Securities Regulatory Commission (CSRC) is an analogue of the SEC in the US. The CSRC formulates and enforces rules regulating how securities are issued and traded.	CSRC gradually gained significant influence as an independent regulatory agency that reports directly to the State Council. CSRC regulations restrict state shareholders in how they exercise control.
1993–1994	Company Law passed in December 1993, effective since July 1994	Company Law formulated general rules applying to all limited liability companies and joint stock corporations.	Once corporatized, SOEs fall under jurisdiction of the Company Law. The state, as the main shareholder, is constrained by this law in how it exercises control over SOEs (and has to respect rights of private minority shareholders).
2001	Accession to WTO	Substantial increase in foreign investments into sectors that used to be closed to foreign ownership.	SOEs become partners of foreign investors in newly created joint ventures, exposing SOEs to technologies and management practices of foreign partners.
2002	Code of Corporate Governance issued	Code provides general non-mandatory guidelines addressing most important aspects of corporate governance; companies are expected to disclose information about non-compliance.	Code requires that independent directors play an important role so that they potentially may prevent unilateral control of the board by state representatives.
2003	Removing restrictions on ownership of A-shares by domestic shareholders only	Qualified foreign institutional investors permitted to invest in A-shares, expanding significantly the number of companies that could be potential investment targets for foreign institutional investors.	Range of SOEs exposed to foreign institutional investors expands from 107 companies that issued B-shares to all traded companies. Number of companies where state shareholders have to interact with foreign shareholders increases dramatically.
2003	SASAC established	Companies previously owned directly by state agencies now owned by State-Owned Assets Supervision and Administration Commission (SASAC). SASAC oversees SOEs on behalf of the State Council (Central Government).	SASAC becomes intermediary between central government agencies and SOEs thus decreasing politically motivated interventions in corporate governance of SOEs.
2005	Conversion of non-tradable shares into tradable shares	Before 2005, companies would have two classes of shares: tradable and non-tradable shares. Most shares were non-tradable.	Once non-tradable shares are converted into tradable shares, state shareholders (and top executives appointed by state shareholders) become interested in increasing share price as shares now potentially can be sold for profit.
2008–2012	State support after the global financial crisis helped SOEs to gain ground over private companies	As companies felt effects of 2008 worldwide financial crisis, the Chinese state focused on providing support to SOEs, while refusing to provide similar support to private enterprises.	SOEs expand operations at the expense of private enterprises (the process described as “guo jin min tui” or “the state advances, the private sector retreats”).

© 2015 John Wiley & Sons Ltd

TABLE 4
Events that Affected State Control and Corporate Governance in Russia during Last 25 Years

Year	Event	What has changed as a result of this event	Implications for state control and corporate governance
1987–1988	USSR law on state enterprises (effective 1988)	Creating legal basis for operation of SOEs as relatively autonomous economic actors.	State retains full control over SOEs, but managers of SOEs granted more autonomy. With launch of *perestroika*, SOE managers are encouraged to take initiative and assume responsibility for enterprise performance.
1990–1991	Laws on ownership, enterprises, and banking (1990); law on privatization (1991) enacted	Creating legal basis for operation of enterprises with different forms of ownership, including private ownership and state ownership. Creating legal basis for privatization.	SOEs for the first time face competition from privately owned firms.
1992–1994	Mass privatization	Voucher privatization begins 1992. Monetary privatization begins 1994.	State releases control over SOEs in sectors not considered strategic. Some completely privatized, others partially privatized.
1995	Loans-for-shares privatization begins	Privatization of large enterprises in most attractive sectors of the Russian economy through "loans-for-shares" auctions.	State releases control over some "jewels" of the national economy, most engaged in extraction of natural resources and generating significant revenues from export.
1996	Law on Corporations and Law on Securities are enacted	Creating legal basis for operation of stock markets.	Large partially privatized SOEs become blue chips of Russian stock market while state retained majority stakes.
1998	Financial crisis, default on government debt	Government default and devaluation of ruble led to sharp decline in imports and prompted development of local producers.	Many SOEs on verge of bankruptcy since mid-1990s benefited from increasing demand for local products after 1998 crisis – became viable, made investments, but needed to improve efficiency.
2000	Putin's first term as President begins	Under Putin, trend of "state capture" by oligarchs reversed; soon after Putin's election, several influential oligarchs fled Russia, others expressed willingness to cooperate.	State begins to reassert control over economy largely lost under Yeltsin. State shareholders remained passive in the 1990s but after 2000 state began to leverage its rights as a major shareholder and assumed a more active role in corporate governance.
2002	Corporate Governance Code enacted	Russian Corporate Governance Code provided detailed guidelines, officially endorsed by the government. Not mandatory, but publicly traded companies required to report and explain non-compliance.	Corporate Governance Code formulates standards of good corporate governance targeting primarily publicly traded companies including companies with partial state ownership. Recommends mechanisms preventing controlling shareholders from taking actions harming interests of minority shareholders. Such policies constrain control by state as majority shareholder.
2003	Arrest of Yukos's largest shareholder	Arrest of Khodorkovsky, the wealthiest Russian in 2003, demonstrated toughness	Assets of Yukos purchased by state-controlled Rosneft. Expansion of state-controlled companies through

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 4
(Continued)

Year	Event	What has changed as a result of this event	Implications for state control and corporate governance
	Khodorkovsky, re-nationalization of Yukos begins	of Putin's administration toward non-loyal oligarchs, after which no other oligarchs explicitly opposed Putin's policies.	purchasing assets from private companies continued, with proportion of total market capitalization accounted for by SOEs increasing from 20% in 2003 to 50% in 2010.
2006–2007	IPOs of Rosneft (2006) and VTB (2007) on LSE	Two large Russian corporations with majority state ownership conducted IPOs on London Stock Exchange attracting significant interest of foreign investors.	SOEs interested in attracting foreign investors through IPOs at foreign stock exchanges improved corporate governance practices to comply with standards expected by foreign investors.
2007	Establishment of state-controlled "national corporations"	State corporations "Rosnanotech" and "Rostekhnologii" are established.	"National corporations" consolidate state-controlled assets in high-tech industries and channel funds allocated for development of technology-intensive businesses.
2011	Removal of high-ranked government officials from boards of SOEs	Replacing significant proportion of state representatives on boards with independent directors and attorneys voting according to government directives.	Initiative intended to demonstrate de-politicization of governance of SOEs. In practice, did not increase autonomy of SOEs because lower ranked government officials retained director positions and voted according to directives received from top level officials.
2012	Russia joins WTO	Liberalization of trade: 500 legal measures adopted, amended, or modified to bring legal regime into conformity with the WTO rules. Russia agreed that SOEs participate in international trade in a manner consistent with the WTO regulations. Russia took steps to eliminate special privileges for many SOEs.	WTO challenges some government policies and actions involving SOEs. In 2015, US opposed new resolutions that would authorize Russian government to frame procurement plans or tender rules to effectively require SOEs to purchase Russian goods only as inconsistent with Russia's WTO obligations.
2014	New version of Corporate Governance Code introduced	The revised version of the Code contains stricter corporate governance requirements compared with the original version.	Top government officials, including Prime Minister Medvedev, emphasize that SOEs should make special efforts to comply with requirements of the new Code.
2014	Crimea conflict	Trade wars between Russia and EU; international sanctions imposed by US and EU; weak ruble.	SOEs in oil, gas, and defense industries suffered from the imposed sanctions.

© 2015 John Wiley & Sons Ltd

has been gaining ground – China's government has strengthened control over SOEs with private capital being forced to withdraw from major industries, especially those related to national security.

Indirect State Ownership Control. The state maintained indirect control after corporatization as state shares were "placed" in the State-Owned Asset Management Companies (SOAMCs); and under the control of the State-Owned Assets Supervision and Administration Commission (SASAC), charged with transforming and controlling the largest and most powerful SOEs. SASAC was also responsible for appointing and removing top executives at SOEs, setting executive compensation, improving corporate governance and setting SOEs' operating budgets, and ensuring workplace safety at SOEs (Jiang & Kim, 2015). From 1998 to 2003, shares directly owned by the state declined from 67.3 percent to 23.5 percent, while state *institutional* shares (owned by SOAMCs/SASAC) rose from 1.8 percent to 44.4 percent (Wang et al., 2011). Researchers still have to explore how much autonomy SOAMCs enjoy.

Means of Control beyond Ownership. In transition economies the state often supported and influenced distressed firms through soft budgets (Djankov & Murrell, 2002). In China, the state responded to the 2008 global financial crisis with a monetary stimulation entailing internal transfers between arms of the government, banking, and corporate sectors (Deng, Morck, Wu, & Yeung, 2015). However, monitoring of controlling shareholders by state banks was often inefficient, with banks lending to firms even when firms' controlling shareholders were tunneling resources from these firms (Qian & Yeung, 2015).

Appointments of former or current state officials to board or top management positions in China were common in the 1990s. Such political ties are used by managers to access officials and resources (Walder, 1995). However, bureaucrats seek rents from firms and there is evidence of lower performance and growth in politically connected firms (Fan, Wong, & Zhang, 2007). Moreover, the effect on performance is contingent upon tie type. Political ties to local governments can improve firm survival ("buffering") and performance ("enabling"), unlike ties to the central government (Zheng, Singh, & Mitchell, 2015). Such effects are also contingent upon firm's prior performance.

State involvement in listed SOEs is enabled by the often overlapping dual governance structure: the corporate board and the Party Committee (headed by its Party Secretary). Even where the two structures do not overlap, real power still flows through the Party Committee, which often simply follows Communist Party orders (Morck, Yeung, & Zhao, 2008). The latter also appoints CEOs of the largest SOEs.

Networks of Private and State Actors. China's economy is characterized as "networked capitalism," involving complex partnerships between firms and state (Boisot & Child, 1996). Decentralization processes in the 1990s led to central ministries retaining control over larger strategic SOEs and leaving smaller SOEs under interdependent control of local governments and private entrepreneurs. The connections (or *quanxi*) with the bureaucracy may lead to the creation of special networks for channeling resources and forging mutual partner alliances between private businesses and the state (Wank, 1995). Start-ups may strategically appoint outside directors to seek help in dealing with government (Chen, 2015). State connections are associated with less severe financial constraints (Cull, Li, Sun, & Xu, 2015). Firms are actively looking for various means of building their business–state networks and rendering favors to government officials, for example, by engaging in corporate social responsibility that promotes social welfare (Lin, Tan, Zhao, & Karim, 2015).

Political connections helped China's tycoons amass phenomenal wealth in real estate, finance, high tech, and mining. In 2015, China had over 200 billionaires, ranking second after the US (Dolan & Kroll, 2015). However, unlike Russian oligarchs, China's tycoons were mostly self-made, did not obtain their assets from privatizations, and were not former bureaucrats.

Variation and Evolution of State Control in Russia

SOEs with Partial State Ownership. Russian mass privatization in the early/mid-1990s was radical compared with the gradualism in China. Such aggressive privatization has been criticized as premature given the weakness of the institutional infrastructure (Black, Kraakman, & Tarassova, 2000) and justified as the only feasible option given the political environment at the time (Boycko, Shleifer, & Vishny, 1995). Privatization methods in Russia favored employees, and especially managers, leading to managerial entrenchment (Filatotchev, Wright, & Bleaney, 1999). The powerful position of managers and the weakness of corporate governance mechanisms often left the state as passive minority shareholder during the early reform period (Estrin & Wright, 1999; Pistor & Turkewitz, 1996).

Since 2000 the state has adopted a different approach by transforming selected SOEs into profitable, rapidly expanding industry leaders and by offering minority stakes in these enterprises to private investors – such investments could bring a good return but minimal control rights. This approach allowed the state to enhance control over large strategically important enterprises while divesting holdings in relatively insignificant enterprises (Chernykh, 2011). This trend stimulated interest in the implications of dominant state ownership for minority investors (Yakovlev, 2009).

Indirect State Ownership Control. State ownership of Russian companies would be dramatically underestimated if we considered just direct ownership (Chernykh, 2008). Indirect state ownership reflects the prominence of state holding companies (such as UES or Svyazinvest) as well as aggressive acquisition strategies of some SOEs (such as Gazprom, Rosneft, or VTB). Adding indirect state ownership increases the proportion of publicly listed companies controlled by the state from 14.1 percent to 37 percent with a conservative 50 percent control threshold and to 57.5 percent with a 25 percent control threshold (Chernykh, 2008). Since 2004, acquisition of substantial stakes in formerly privatized companies by large SOEs became a systematic practice, gradually increasing the state-owned share of market capitalization from 20 percent in 2003 to 50 percent by 2012 (Enikolopov & Stepanov, 2013). These aggressive acquisition strategies of several large SOEs resulted in *de facto*

© 2015 John Wiley & Sons Ltd

renationalization of many enterprises that had been privatized in the 1990s (Chernykh, 2011). This practice substantially boosted state control over the Russian economy even though *de jure* there was no renationalization during this period.

Means of Control beyond Ownership. Appointment of acting government officials as board members and appointment of former government officials as top executives of companies with partial or indirect state ownership represent one means of enhancing state control beyond ownership. The presence of government officials on Russian boards has been examined in several studies (e.g., Frye & Iwasaki, 2011; Wright, Buck, & Filatotchev, 1998).The presence of state representatives appears persistent even when state ownership declines following privatization (Radygin, Entov, Gontmakher, Mezheraups, & Turuntseva, 2004). Studies of Russian firms with government board representatives provide evidence of collusive relationships: firms with state directors are more likely to receive state benefits and to provide services that benefit the state (Frye & Iwasaki, 2011).

In the 1990s, the state often acted as a passive shareholder and rarely used the board as a mechanism for exercising control over management. However, in the early 2000s, the state became a more active shareholder and appointed senior government officials to the boards of SOEs. In 2011 President Medvedev initiated the removal of top government officials from the boards of directors of SOEs, but this initiative has recently been reversed.

While we have systematic evidence about appointment of government officials to boards and their involvement in corporate governance, there are no systematic studies about the appointment of *former* government officials as executives of SOEs and the implications of such appointments for strategic choices. It would be useful to examine systematically the professional background of top management teams to identify how often executives had government careers before assuming positions in SOEs. Another aspect of the "revolving door" between business and government is represented by government appointments of prominent business leaders. This practice has not been studied systematically, but appointments of business leaders to key government positions were common in the 1990s under President Yeltsin's administration.

A second means of enhancing control beyond ownership occurs through veto rights provided by a "golden share" (Frye & Iwasaki, 2011). Golden shares were frequently used in the 1990s, but more recently the Russian government has abandoned its special voting rights in some SOEs. In other firms, the government increased its stake substantially thus making obsolete special voting rights provided by the golden share.

A third mechanism that allows the state to exercise influence beyond ownership is based on companies' dependence on the state as a provider of resources. Thus, the state-controlled Vneshekonombank was providing refinancing to many large "strategically important" companies in a critical condition after the 2008 financial crisis (Radygin, 2008). The recipients were expected to reciprocate by avoiding massive lay-offs, salary cuts, or significant increases in output prices (Simachev & Kuzyk, 2012). These *de facto* bailouts were not associated with a substantial increase in the number of SOEs (Enikolopov & Stepanov, 2013), but provided state agencies with significant leverage over private companies to demand that they avoid taking actions with high social costs.

Fourth, regulation represents another state control channel. Limited effectiveness of the Russian government as a regulator is reflected not only in problems with enforcement of rules (Spicer & Okhmatovskiy, 2015), but also in the practice of modifying general rules to create favorable conditions for specific companies loyal to federal or regional governments. Such favoritism creates strong incentives for private companies to coordinate actions with government agencies to the extent that these private companies initiate large business transactions only after informal approval from government agencies (Radygin, 2008). SOEs often rely on regulatory support from the government and this practice benefits private shareholders investing in SOEs. However, by playing simultaneously the roles of owner and regulator, the state creates conflicts of interest that perpetuate the perception of market regulations in Russia as biased and inconsistent.

Networks of Private and State Actors. Of particular relevance to the study of state control is the relationship between the Russian top politicians and industrial tycoons ("oligarchs") (Guriev & Rachinsky, 2005). When Mr. Putin came to power, he offered to accept oligarchs' ownership rights obtained through the opaque privatization process if they did not get involved in politics (Puffer & McCarthy, 2007). Some oligarchs adapted by befriending the state and generating synergies from operating together (Melkumov, 2009). The state "authorized" these tycoons to get rich and they were inclined to cooperate with the state (Adachi, 2013). Oligarch-owned firms were often structured as pyramids or through cross-shareholdings. In these structures, the oligarch achieved control of constituent firms via a chain of ownership relations, often including the state as another controlling shareholder. These oligarchic–state network structures filled the institutional vacuum left by the collapsed communist economy, ensuring access to the requisite resources for investments and improving assets' productivity (Grosman & Leiponen, 2013). However, the power of oligarchs over the companies within their control also created opportunities for tremendous private gains, often at the expense of minority shareholders and potentially to the detriment of the overall economy.

For many oligarchs, close connections to the state are rooted in their affiliation with nomenklatura circles through early careers or personal connections. Others started as "outsiders" but over the years developed a special relationship with the state (Braguinsky, 2009). The oligarchs' relationships with the state also took more formal formats as exemplified by official meetings of Mr. Yeltsin and Mr. Putin with the group of the most prominent oligarchs and by establishment of a powerful lobbying association, Russian Union of Industrialists and Entrepreneurs, representing mostly the interests of large business owners (Hanson & Teague, 2005).

The emergence of networks where private and state actors were interconnected through joint ownership of partially privatized property created conditions for mutual influence. The balance of such influence shifted over time. In the 1990s, relationships between business and the state were described as "state capture" (Hellman, Jones, & Kaufmann, 2003). After

© 2015 John Wiley & Sons Ltd

2000, when political leaders gained strength and obtained broad public support, relationships shifted to "business capture" as political leaders leveraged their powerful position by dictating the conditions of continuing partnership with private actors (Yakovlev, 2006).

Variation and Evolution of State Control in Other Transition Economies

SOEs with Partial State Ownership. Research on SOEs in transition economies of Central and Eastern Europe (CEE) and in former Soviet republics (CIS countries) has primarily concerned challenges associated with privatization and restructuring (Claessens & Djankov, 1999; Uhlenbruck, Meyer, & Hitt, 2003), governance structures (Filatotchev, Buck, & Zhukov, 2000), and more recently, divergent paths in transition (Lane & Myant, 2007), and European integration (Hashi, Welfens, & Wziatek-Kubiak, 2007).

From the historical perspective, it is most useful to compare state control transformation and evolution in Russia and in other former Soviet republics. Amongst countries that have transitioned most towards the democratic model with the state reducing its control over key assets are the Baltic States (stabilized by the EU anchor), Georgia (aided by Western intellectual and financial support), and Kyrgyz Republic. Countries retaining considerable state power, where state and business elites have close ties, are Belarus, Tajikistan, Turkmenistan, Uzbekistan and Ukraine.

Indirect State Ownership Control. Similar to Russia, indirect state ownership is quite common in CEE and CIS countries. The state often created multiple institutions through which to exercise control, such as investment funds or pension funds (Pahor, Prasnikar, & Ferligoj, 2004). The state also maintained control over some financial and industrial groups, which in turn controlled individual firms (Kočenda & Hanousek, 2012).

Means of State Control beyond Ownership. Financial support through government loans was common in CEE and CIS economies, similar to Russia and China (Mickiewicz, 2010). However, in these economies, ruling political parties did not exercise direct control over firms through governance structures similar to China's Party committees. Similar to Russia and China, the state in other transition economies frequently executed veto rights through golden shares to prevent entry by new shareholders or to block the sale of property (Kočenda & Hanousek, 2012).

Networks of Private and State Actors. Partial privatization in CEE produced many firms with mixed private and state ownership described as "recombinant property" by Stark (1996). Several studies analyzed privatized firms not as isolated economic units but as nodes in corporate networks created by the relationships of control and interdependence (Pahor et al., 2004). These dense corporate networks connected domestic owners, foreign owners, and the state thus blurring boundaries between private and state ownership. In many firms, the state assumed the the role of a passive shareholder by letting private partners take control (Frydman, Gray, Hessel, & Rapaczynski, 1999). In others, the state was quite active, with the relationships between state and private shareholders ranging from mutually beneficial cooperation to hostile battles for control.

CEE minimized opportunities for rent-seeking activities of the ruling elite by reducing major distortions of government policies and liberalizing prices (Havrylyshyn, 2005). Oligarchs played a more prominent role in CIS countries, where they were connected with the state either through upper-echelon nomenclature or relatives and close associates of the countries' presidents. In other former Soviet republics, the "revolving door" between the government and business was often even more pronounced than in Russia; for example, only recently an oligarch in food products, Mr. Poroshenko, became President of Ukraine. Further, across all CIS countries, there was considerable continuity from the political power leaders of the Soviet period to the oligarchs.

CORPORATE GOVERNANCE STRUCTURES AND PROCESSES

Board Composition and Independence

The notion and functions of independent directors vary remarkably across different jurisdictions (Ferrarini & Filippelli, 2014). In China, all listed companies are required to have at least one third of independent directors on their boards and, if board committees are established, that proportion should be raised to at least half (Clarke, 2006; Zhao, 2011). The role of independent directors in Chinese audit committees is negligible (Liu & Pissler, 2013). As to nomination and remuneration committees, the corporate governance code recommends a composition based on a majority of independent directors. However, the influence of such committees on decisions about executive compensation is also modest. The positive relationship between board independence and firm operating performance is stronger in state-controlled firms relative to other listed firms in China, as it reduces tunneling and improves investment efficiency in SOEs (Liu, Miletkov, Wei, & Yang, 2015). Former government officials comprise a large share of outside board members in Chinese firms (Chen, 2015). Several studies examine the effect of political connections at the board level (Cull et al., 2015; Fan et al., 2007; Liang et al., 2015; Zheng et al., 2015).

The Russian corporate governance code recommends that boards comprise at least one-third of independent directors. It also recommends that audit committees consist entirely of independent directors or are chaired by an independent director and include only non-executives. Board composition may affect investments in productive assets. For Russian publicly traded firms, Grosman and Wright (2015) find a positive effect of cash-flows on capital expenditures when SOEs appoint independent board directors to assume the role of monitoring. However, these positive effects are substantially reduced when oligarchs appoint independent directors, indicating that independent directors are afforded insufficient autonomy to play their monitoring role. The authors find foreign independent directors to be influential, while foreign affiliated directors exercise little influence on tunneling.

The adoption of best corporate governance practices in state-controlled firms remains quite limited. According to

© 2015 John Wiley & Sons Ltd

a study by the Russian Institute of Directors (2014), the proportion of Russian SOEs with committees composed of only independent or non-executive directors is still low (51 percent of nomination and remuneration committees and 57 percent of audit committees). While it is common practice in SOEs to establish board committees, only half of them meet regularly. Only 11 percent of SOEs conducted evaluations of board practice in 2013. Great heterogeneity is observed between partially controlled SOEs and wholly owned SOEs in their board processes and practices, representing good standards in 74 percent of the former and only 56 percent of the latter.

Transparency and Disclosure

An important question concerns whether state control is associated with a higher or lower degree of transparency and disclosure. Relative to other facets of corporate governance, voluntary disclosure by Russian SOEs is higher, but still lags behind the level of disclosure in publicly traded firms without the controlling state shareholder (Russian Institute of Directors, 2014). Partially owned SOEs have higher disclosure than wholly owned SOEs. In Russia, SOEs are more sensitive than oligarch-owned enterprises to improved transparency as demonstrated by its effect on fixed investments (Grosman, 2015). Closer ties to foreign multinationals can improve transparency; for example, such ties lead to greater wage reporting in Russian companies (Braguinsky & Mityakov, 2015).

In China, SOEs face strong incentives to voluntarily disclose additional information to ease investor concerns regarding management quality, the risk of tunneling, and the role of government as major shareholder (Wang, Sewon, & Claiborne, 2008). However, lack of emphasis on efficiency and profitability by state shareholders or their direct access to corporate information might undermine the need for voluntary disclosure. The empirical results are mixed: some demonstrate that the level of voluntary disclosure is positively related to the proportion of state ownership (Wang et al., 2008), particularly for those SOEs with foreign listings (Ferguson, Lam, & Lee, 2002), while others report no significant relation (Xiao & Yuan, 2007) or a negative relation between the two constructs (Xiao, Yang, & Chow, 2004). There are indications that China's SOEs manage earnings to boost their chances of being selected for IPOs because earnings performance is a government-stated criterion for listing (Aharony, Lee, & Wong, 2000).

In China, informal institutions often substitute for ineffective formal corporate governance institutions (Ahlstrom, Bruton, & Yeh, 2008). Both firm owners and local governments are motivated to foster economic growth and both will do whatever is necessary to achieve this. This means *de facto* enforcement of ownership rights and various types of regulation. In contrast, in Russia, formal institutions are undermined through corruption and lack of enforcement, and government often does not have mutually complementary goals with large shareholders – there is often an antagonistic relationship between state and oligarchs with state interventions taking the form of arbitrary inspections and asset stripping aided by lack of court independence (Estrin & Prevezer, 2010). The Russian government often interferes in business affairs through selectively applying and enforcing formal rules toward firms and owners (Adachi, 2013).

Executive Compensation

Studies of executive compensation in SOEs of transition economies are rare. The legacy of communism constrained CEO pay in the early stages of economic reforms (Firth et al., 2006) and there is generally a relatively small pay gap between organization levels in SOEs (Chen, Ezzamel, & Cai, 2011).The average salary of a manager in a Chinese SOE was only one-fifth of a manager's salary in a foreign MNE, but this gap is closing (Wooldridge, 2012). Pay-for-performance incentive schemes emerged as the profit objective took hold in SOEs. Average CEO compensation nearly doubled in the 1980s. SOEs controlled by the central government link CEO pay to stock returns and shareholders' wealth, whereas SOEs controlled by local government base performance-related CEO pay on profitability measures (Firth et al., 2006). Initially, studies suggested that state ownership in China is negatively associated with cash compensation (Adithipyangkul, Alon, & Zhang, 2011; Conyon & He, 2011; Firth et al., 2006; Li, Moshirian, Nguyen, & Tan, 2007). However, since a new law in 2005 encouraging SOEs to design incentive mechanisms to motivate managers to perform better, managers and directors of SOEs often receive higher compensation than their counterparts at non-SOEs (Jiang & Kim, 2015).

There may be other influences on executive behavior than compensation. Executive positions in listed SOEs are filled by state bureaucrats rather than professional managers, and are steps in the career of a successful civil servant (Morck et al., 2008). For those with real control but little personal ownership in their company, supporting unprofitable, but politically important projects is a good strategy for career advancement in the state echelons. Executive performance evaluations and promotion decisions are often still based on whether the managers act in the interests of the Chinese Communist Party (Firth et al., 2006). CEO duality in Chinese SOEs is relatively rare. The board chairman, acting as the legal representative of the firm according to the Company Law, is usually appointed by the state as the largest shareholder (Jiang & Kim, 2015).

In general, governments in transition economies have embraced corporate governance mechanisms based on shareholder rights as an alternative to direct intervention in management of SOEs that was a norm in centrally planned economies. However, state-controlled firms in transition economies often lag in adopting best corporate governance practices intended to protect the interests of minority shareholders.

DISCUSSION AND FUTURE RESEARCH

We summarized the range of theories used to study state control in Table 1. While this range is broad, agency theory (Young, Peng, Ahlstrom, Bruton, & Jiang, 2008) and, more recently, institutional theory (Child & Yuan, 1996; Puffer & McCarthy, 2011; Suhomlinova, 1999) are the most used in the context of transition economies. Only a few recent studies on SOEs in transition economies rely on novel theoretical frameworks (e.g., Okhmatovskiy, 2010; Sun, Mellahi, & Wright, 2012). Further research on SOEs in transition economies should put more emphasis on developing theoretical

© 2015 John Wiley & Sons Ltd

frameworks that take into account unique challenges faced by state-controlled firms to address questions about state control and corporate governance summarized in Table 5.

Means of State Control

State control over enterprises of strategic importance takes different forms and has different consequences as researchers have just started to explore (Musacchio et al., 2015). Modern state capitalism demonstrates more sophisticated forms of state control that adapt to the conditions of a market-based economy. A company with substantial state ownership may adopt certain corporate governance mechanisms that put constraints on state involvement in the corporate governance process and protect interests of other shareholders. Unlike traditional SOEs, modern state-controlled companies in transition economies are often publicly traded and thus state shareholder interests must be reconciled with private shareholder interests, suggesting a need for further research using principal–principal agency theory.

Researchers need to analyze more closely a wide variation of corporate governance configurations in companies under partial state control. The framework of Musacchio et al. (2015) examines under which conditions different forms of state control mitigate the "*liability of stateness*" and lead to improved performance. While their work is conceptual, further research can test this framework on data from transition economies to provide fine-grained understanding of state control beyond the state–private dichotomy.

Research on indirect state ownership is scarce, due to limitations of data availability and reliability. More research is needed to explore the shift from direct to indirect forms of state ownership in transition economies. In particular, growing attention has been devoted to sovereign wealth funds (SWFs) (Aguilera, Capapé, & Santiso, in press; Fotak, Gao, & Megginson, 2013; Wood & Wright, 2015), but there remains little empirical evidence regarding their control mechanisms as few funds disclose key organizational details. Further, researchers have focused primarily on the impact of SWFs on developed economies (Dewenter, Han, & Malatesta, 2010), with little attention to their role in emerging economies. Amongst transition economies, SWFs are particularly active in China. Their portfolio organizational structure allows SWFs to have a better separation of management and control thus mitigating the typical principal–principal agency conflict (Young et al., 2008) present in state-controlled firms. However, SWFs are reluctant to engage in active governance, especially when the portfolio firm is foreign (Fotak et al., 2013). To some extent this lack of involvement alleviates concerns that SWFs may pursue objectives other than profit maximization, such as political objectives or even tunneling (Jiang, Lee, & Yue, 2010).

We have discussed non-equity mechanisms of political interference but several questions remain unanswered and invite future research. How are different forms of state control and state support interrelated? Can private firms compete with state-supported firms that receive privileged access to financial and other resources? Furthermore, scholars should differentiate between the different geographic regions or administrative levels when studying state control in such large and diverse economies as China and Russia as such studies remain rare.

Dependence on the state creates opportunities for exercising influence beyond firms where the state is a shareholder. Through its leverage over key actors in business groups, the state can exercise influence over other business group members. Growth of such business groups meant that new firms were added to the network of interconnected private and state actors; joining this network brought these firms into the state's sphere of influence (Guthrie, Okhmatovskiy, Schoenman, & Xiao, 2012). The role of the state in creating and promoting business groups in transition economies deserves more attention among scholars of state capitalism. Transaction cost theory may, for example, yield insights into the effects of such state interference on firm behavior. Conceptual analyses of the relative benefits to private actors of autonomous versus integrated forms of public–private partnerships (Kivleniece & Quelin, 2012) provide the basis for future empirical studies of private–public governance arrangements in transition economies. Further, the variety of private–public ownership forms we have identified may provide scope for the development of a more contingent approach to private–public sector governance.

Private and state actors are also connected through networks of political ties (Danis, Chiaburu, & Lyles, 2010; Sun et al., 2012). Despite significant progress in building market institutions, political ties continue to play a critical role in transition economies. The political embeddedness perspective emphasizes that connections with politicians serving an instrumental function for the firm can also be leveraged by these politicians to constrain firms' strategic choices, while state control ties also provide firms with an opportunity to influence state actors. Given the prominence of political ties in China and Russia, it is not surprising that most studies about political embeddedness have been conducted in these transition economies (Okhmatovskiy, 2010; Sun, Mellahi, & Thun, 2010; Sun, Mellahi, Wright, & Xu, 2015). The importance of political connections does not necessarily decline with the development of market institutions (Michelson, 2007; Shi, Markoczy, & Stan, 2014) because of the impact of multiple contingency factors (Peng & Zhou, 2005; Sun et al., 2012). Recent developments emphasize both the roles of political tie heterogeneity (Holburn & Zelner, 2010; Zheng et al., 2015) and the interrelationships between personal-level and ownership-related political ties (Kilduff & Brass, 2010). Further research built upon the political embeddedness perspective is needed to examine the implications of these relationships for the governance of firms in transition economies. For example, research might examine how voluntary or forced departures of politically connected executives and external board members influence governance through changes to the nature of personal- versus organizational-level political ties.

It is difficult to capture mechanisms of informal influence in empirical studies. Studies have usually relied on self-reported evidence obtained through surveys of top managers (Yakovlev, 2009). Unlike state ownership or state representatives on boards, phone calls from top government officials to CEOs cannot be traced by researchers, but these might be as consequential as formal mechanisms of state control. However, even with limited empirical evidence, we can estimate

© 2015 John Wiley & Sons Ltd

TABLE 5
Transition Economies: Agenda for Further Research

Theme	Research questions
	State Control
State Control through Ownership	• What are the impacts of different forms of state ownership and affiliation on governance, strategy and performance? • How have different forms of state ownership and affiliation evolved? Is this evolution unidirectional away from state involvement? • How are the interests of private and public shareholders reconciled? • How do corporate governance bundles vary between different forms of state ownership and affiliation? • What are the forms of indirect state ownership and how do these impact governance and performance? • What new forms of state ownership and affiliation are emerging and how do their forms of control vary? • How does state ownership vary across geographic regions and administrative levels (i.e. federal vs. municipal)?
Means of State Control beyond Ownership	• How do channels of state non-equity control and support differ from each other and what is their impact? • What are the implications for private firms' ability to compete with state-supported firms and SOEs receiving financial and other resources from the state?
Networks of Private and State Actors	• What is the nature of private-public governance mechanisms and networks and what is their impact? • How does the variety of private-public ownership forms relate to different approaches to private-public sector governance? • How does personal and organizational embeddedness in specific political networks influence governance? How does this change when executives and board members change?
Evolution of State Control	• How has state ownership and control of enterprises evolved in different types of transition economies and what has been the impact upon enterprises in these economies?
	Corporate Governance
Boards	• To what extent do transition economy state-owned and controlled firms recruit overseas directors or expatriates who can provide the expertise required? • How do the dimensions of board diversity (political/commercial, gender, age/experience, etc.) differ in firms with different configurations of state control? • What board roles do politically connected directors play in different types of state-owned and affiliated enterprises? • What is the pattern of political and commercial expertise in Chair and CEO board roles? • To what extent does duality of Chair and CEO vary between different forms of state ownership and affiliation? • What is the nature of board turnover and its drivers in different types of state ownership and affiliation? • To what extent does social capital of state directors evolve (e.g., decline or metamorphose) with the progress of market reforms? • How does the nature of board processes in firms with different configurations of state control vary?
Outsourcing of Corporate Governance Regulation	• How does the selection of market tier at foreign stock exchanges impact SOE's corporate governance and performance? How does the country in which the stock exchange is located affect implications of the foreign listing? • How do different formal stock exchange rules and informal enforcement mechanisms impact corporate governance and performance of SOEs listed at foreign stock exchanges?
Transparency and Disclosure	• What are the similarities and differences in transparency and disclosure practices between different transition economies and developed economies? • What drives these differences?

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 5
(Continued)

Theme	Research questions
	• How does the enforcement and application of transparency and disclosure practices vary between different transition economies? • How does the enforcement and application of transparency and disclosure practices vary between different types of state ownership/affiliation and private sector enterprises?
Executive Compensation	• How does executive compensation in state-owned/affiliated enterprises in transition economies differ from executive compensation in non-state firms and in enterprises from non-transition economies? • How does the status of state-owned/affiliated enterprises in transition economies affect the scope of executive compensation mechanisms available?
Evolution of Governance Mechanisms	• How have governance mechanisms and processes evolved in state-owned/affiliated enterprises in different types of transition economies and what has been the impact upon enterprises in these economies? • To what extent do the presence and roles of politically connected directors in state-owned/affiliated enterprises change as transition economies evolve?

the importance of informal state influence in transition economies as a function of firms' dependence on decisions made by state officials. Preferential treatment and selective punitive actions are frequently observed in transition economies, implying that state officials have plenty of opportunities to exercise influence over firms using informal mechanisms. Further research on such mechanisms is needed to complement existing evidence on formal mechanisms of state control – this is essential for understanding how the state exercises control over firms in transition economies.

Corporate Governance Structures and Processes

According to the resource-based view (Lazzarini, 2015; Makhija, 2003), an important issue is not just the monitoring role of boards but also the value-adding role of directors due to their human and social capital. Research on the role of directors' international experience in transition economies remains limited. Further research is needed on the extent to which transition economy firms recruit overseas directors or expatriates, who can provide the international expertise required. Studies have emphasized the importance of board connections to government agencies, but we have little analysis of the evolution of these relationships. Expectations that the relevance of such social capital would decline over time need to be examined through longitudinal studies of board composition and processes. Important questions concern the extent to which social capital associated with political ties has declined or metamorphosed over time.

There is relatively little analysis of how state involvement on boards affects board processes. Notwithstanding challenges regarding access to board operations, which researchers in developed economies have overcome (Pye, 2013), fine-grained studies of board processes in firms operating with different configurations of state control will likely be highly insightful. Finally, studies of board interlocks involving networks of SOEs and private firms (Salvaj & Couyoumdjian, 2015) could be validated in transition economies.

SOEs can outsource regulation of corporate governance practices to developed economies by listing on foreign exchanges or by acquiring foreign assets. Several studies on cross-listings of foreign firms on Western exchanges observe improved corporate governance standards and performance of foreign firms as they "bond" to a better governance and regulatory regime (Bell, Filatotchev, & Aguilera, 2014; Ferguson et al., 2002; Khanna, Palepu, & Srinivasan, 2004), but more empirical research is needed to test the boundaries of bonding theory in the context of SOEs in transition economies. As more SOEs from transition economies get listed on foreign exchanges, future studies could explore the impact of corporate governance across institutional regimes of these stock exchanges. For example, how does the selection of market tier between main, secondary, or lower tier impact SOE's corporate governance? Would listing on the London Stock Exchange improve corporate governance of an SOE in the same way as listing under a different corporate governance regime, such as the Singapore or Frankfurt Stock Exchange? Institutional analysis would help differentiate between formal stock exchange rules and informal rules or enforcement mechanisms that firms are subject to in practice. Such analysis

© 2015 John Wiley & Sons Ltd

could be linked to internationalization of SOEs through foreign direct investment, acquisitions or joint ventures (Brouthers & Bamossy, 1997; Choudhury & Khanna, 2014; Li, Cui, & Lu, 2014; Liang et al., 2015; Lu, Liu, Wright, & Filatotchev, 2014; Meyer, Ding, Li, & Zhang, 2014; White, 2000; Zeng, Douglas, & Wu, 2013) as moderating effects of foreign listings. Further, the role of foreign multinational enterprises (MNEs) entering transition economies as agents of change in state control and corporate governance (Meyer & Lieb-Doczy, 2003) may be a fruitful avenue to explore.

Outsourcing corporate governance regulation may increase accountability and transparency as most SOEs adopted International Financial Reporting Standards (IFRS) and appointed international audit firms (Grosman & Leiponen, 2013). Researchers could compare transparency and disclosure practices of SOEs in transition and developed economies using institutional theory, as the nature of such practices may be affected by institutional environment. Specific areas for study might include misrepresenting financial results or withholding information about shareholders' identities and board members' backgrounds and affiliations (Puffer & McCarthy, 2011).

There is a shortage of research on top management team (TMT) selection and compensation in SOEs, primarily due to data scarcity and non-disclosure. However, we see the following trends emerging regarding TMT selection mechanisms: (1) appointment of trusted state officials to top management positions, making them ultra-powerful state "nominees"; and (2) appointments of the new generation of sophisticated managers who learned about business in the world's best business schools, worked abroad, and were exposed to better governance practices and business ethics than their predecessors (Wooldridge, 2012). However, the latter category of managers may only fulfill technical or operational roles, with decision making being made at the level of state shareholder.

Future studies should consider how SOEs can attract new talent given competition with compensation and benefits offered by domestic private firms and MNEs. Further research can explore how equity-linked long-term incentives of top managers influence decision making at SOEs. A formal theory is needed to distinguish the use of equity-linked compensation to solve principal–agent problems from the use of such compensation to resolve conflicting interests of state and private shareholders.

Contextual Factors

Transition economies were not homogeneous in 1989 and are even less homogeneous now. Some have progressed to become EU members, while others have progressed little or even regressed after initial reforms. This variety is vividly illustrated in Hoskisson et al.'s (2013) analysis, which categorizes emerging economies, including transition economies, into five different clusters according to their institutional and infrastructure development. Further research is needed to analyze the relationships between the evolution of state control and institutional development. For example, recent studies demonstrate how home country institutional contextual factors complement or substitute for director human and social capital (Lu et al., 2014) and there is a need to apply this analysis to the role of state directors.

In transition economies, managers have relied excessively on informal institutions due to weak formal institutions. Continuing reliance on informal institutions under conditions of formal institutional voids creates major obstacles for badly needed reforms (Puffer & McCarthy, 2011). A specific contextual issue requiring further analysis concerns the problem of corruption in the governance of firms with some element of state control. Governments in transition economies have made moves to tackle corruption by removing and imprisoning implicated government officials, often after changes in ruling cliques. Such changes will affect firms closely connected to the former officials. Analyses of the effects of removing corrupt officials and politicians on the firms closely associated with them would likely yield interesting insights. Such issues suggest scope for the development and application of political embeddedness and institutional perspectives.

CONCLUSION

Twenty-five years on from 1989, SOEs in transition economies are far from the centrally planned behemoths, and state control has evolved into different organizational and governance forms. Recent studies on state-controlled firms in transition economies, other than China and Russia, are rare. This omission is unfortunate as these economies have become more diverse and continue to change. We encourage context-specific research on SOEs to understand the evolution of state control in particular countries, as well as comparative research, which can provide insights into whether state capitalism varies between transition economies. If so, insights generated are context-bound. Both context-specific and comparative studies could provide opportunities to extend mainstream theory by examining interfaces between theory and context, by both contextualizing theory and theorizing about context. With this review, we lay the foundation for such further examination.

ACKNOWLEDGEMENTS

The authors gratefully acknowledge constructive and insightful comments provided by Ruth Aguilera, Guest Editor for this special issue, and the anonymous reviewers.

REFERENCES

Adachi, Y. 2013. ***Building big business in Russia: The impact of informal corporate governance practices***. London: Routledge.

Adithipyangkul, P., Alon, I., & Zhang, T. 2011. Executive perks: Compensation and corporate performance in China, ***Asia Pacific Journal of Management***, 28: 401–425.

Aguilera, R. V., Capapé, J., & Santiso, J. (in press). Sovereign wealth funds: A strategic governance view, ***Academy of Management Perspectives***.

Aharoni, Y. 1986. ***Evolution and management of state owned enterprises***. Cambridge, MA: Ballinger.

Aharony, J., Lee, J., & Wong, T. 2000. Financial packaging of IPO firms in China, ***Journal of Accounting Research***, 38: 103–126.

© 2015 John Wiley & Sons Ltd

Ahlstrom, D., Bruton, G. D., & Yeh, K. S. 2008. Private firms in China: Building legitimacy in an emerging economy, ***Journal of World Business***, 43: 385–399.

Bell, G., Filatotchev, I., & Aguilera, R. 2014. Corporate governance and investors' perceptions of foreign IPO value: An institutional perspective, ***Academy of Management Journal***, 57: 301–320.

Black, B., Kraakman, R., & Tarassova, A. 2000. Russian privatization and corporate governance: What went wrong?, ***Stanford Law Review***, 52: 1731–1808.

Boisot, M. & Child, J. 1996. From fiefs to clans and network capitalism: Explaining China's emerging economic order, ***Administrative Science Quarterly***, 41: 600–628.

Boycko, M., Shleifer, A., & Vishny, R. W. 1995. ***Privatizing Russia***. Boston, MA: MIT Press.

Braguinsky, S. 2009. Postcommunist oligarchs in Russia: Quantitative analysis, ***Journal of Law and Economics***, 52: 307–349.

Braguinsky, S. & Mityakov, S. 2015. Foreign corporations and the culture of transparency: Evidence from Russian administrative data, ***Journal of Financial Economics***, 117: 139–164.

Brouthers, K. D. & Bamossy, G. J. 1997. The role of key stakeholders in international joint venture negotiations: Case studies from Eastern Europe, ***Journal of International Business Studies***, 28: 285–308.

Bruton, G., Peng, M., Ahlstrom, D., Stan, C., & Xu, K. 2015. State-owned enterprises as hybrid organizations, ***The Academy of Management Perspectives***, 29: 92–114.

Cao, Y., Qian, Y., & Weingast, B. R. 1999. From federalism, Chinese style to privatization, Chinese style, ***Economics of Transition***, 7: 103–131.

Chen, J., Ezzamel, M., & Cai, Z. 2011. Managerial power theory, tournament theory, and executive pay in China, ***Journal of Corporate Finance***, 17: 1176–1199.

Chen, T. 2015. Institutions, board structure, and corporate performance: Evidence from Chinese firms, ***Journal of Corporate Finance***, 32: 217–237.

Chernykh, L. 2008. Ultimate ownership and control in Russia, ***Journal of Financial Economics***, 88: 169–192.

Chernykh, L. 2011. Profit or politics? Understanding renationalizations in Russia, ***Journal of Corporate Finance***, 17: 1237–1253.

Child, J. & Yuan, L. 1996. Institutional constraints on economic reform: The case of investment decisions in China, ***Organization Science***, 7: 60–77.

Choudhury, P. & Khanna, T. 2014. Toward resource independence – Why state-owned entities become multinationals: An empirical study of India's public R&D laboratories, ***Journal of International Business Studies***, 45: 943–960.

Claessens, S. & Djankov, S. 1999. Ownership concentration and corporate performance in the Czech Republic, ***Journal of Comparative Economics***, 27: 498–513.

Clarke, D. C. 2006. The independent director in Chinese corporate governance, ***Delaware Journal of Corporate Law***, 31: 125–228.

Conyon, M. J. & He, L. 2011. Executive compensation and corporate governance in China, ***Journal of Corporate Finance***, 17: 1158–1175.

Cull, R., Li, W., Sun, B., & Xu, L. C. 2015. Government connections and financial constraints: Evidence from a large representative sample of Chinese firms, ***Journal of Corporate Finance***, 32: 271–294.

Danis, W. M., Chiaburu, D. S., & Lyles, M. A. 2010. The impact of managerial networking intensity and market-based strategies on firm growth during institutional upheaval: A study of small and medium sized enterprises in a transition economy, ***Journal of International Business Studies***, 41: 287–307.

Delios, A., Wu, Z. J., & Zhou, N. 2006. A new perspective on ownership identities in China's listed companies, ***Management and Organization Review***, 2: 319–343.

Deng, Y., Morck, R., Wu, J., & Yeung, B. 2015. China's pseudo-monetary policy, ***Review of Finance***, 19: 55–93.

Dewenter, K. L., Han, X., & Malatesta, P. H. 2010. Firm values and sovereign wealth fund investments, ***Journal of Financial Economics***, 98: 256–278.

Dewenter, K. L. & Malatesta, P. H. 2001. State-owned and privately owned firms: An empirical analysis of profitability, leverage, and labor intensity, ***American Economic Review***, 91: 320–334.

Djankov, S. & Murrell, P. 2002. Enterprise restructuring in transition: A quantitative survey, ***Journal of Economic Literature***, 40: 739–792.

Dolan, K. A. & Kroll, L. 2015. Inside the 2015 Forbes billionaires list: Facts and figures. Forbes. http://www.forbes.com/sites/kerryadolan/2015/03/02/inside-the-2015-forbes-billionaires-list-facts-and-figures/ (accessed October 20, 2015).

Enikolopov, R. & Stepanov, S. 2013. Corporate governance in Russia. In M. Alexeev & S. Weber (Eds.), ***The Oxford handbook of the Russian economy***: 221–245. Oxford: Oxford University Press.

Estrin, S. & Prevezer, M. 2010. A survey on institutions and new firm entry: How and why do entry rates differ in emerging markets?, ***Economic Systems***, 34: 289–308.

Estrin, S. & Wright, M. 1999. Corporate governance in the former Soviet Union: An overview, ***Journal of Comparative Economics***, 27: 398–421.

Fan, J. P., Wong, T. J., & Zhang, T. 2007. Politically connected CEOs, corporate governance, and post-IPO performance of China's newly partially privatized firms, ***Journal of Financial Economics***, 84: 330–357.

Ferguson, M. J., Lam, K. C., & Lee, G. M. 2002. Voluntary disclosure by state-owned enterprises listed on the stock exchange of Hong Kong, ***Journal of International Financial Management & Accounting***, 13: 125–152.

Fernandez-Stembridge, L. & Fernandez, J. A. 2007. ***China's state owned enterprise reforms: An industrial and CEO approach***. London: Routledge.

Ferrarini, G. A. & Filippelli, M. 2014. Independent directors and controlling shareholders around the world. European Corporate Governance Institute (ECGI) Law Working Paper 258.

Filatotchev, I., Buck, T., & Zhukov, V. 2000. Downsizing in privatized firms in Russia, Ukraine, and Belarus, ***Academy of Management Journal***, 43: 286–304.

Filatotchev, I., Wright, M., & Bleaney, M. 1999. Privatization, insider control and managerial entrenchment in Russia, ***Economics of Transition***, 7: 481–504.

Firth, M., Fung, P. M., & Rui, O. M. 2006. Corporate performance and CEO compensation in China, ***Journal of Corporate Finance***, 12: 693–714.

Fotak, V., Gao, J., & Megginson, W. L. 2013. The financial role of sovereign wealth funds. In M. Wright, D. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***The Oxford handbook of corporate governance***: 581–604. Oxford: Oxford University Press.

Frydman, R., Gray, C., Hessel, M., & Rapaczynski, A. 1999. When does privatization work? The impact of private ownership on corporate performance in the transition economies, ***Quarterly Journal of Economics***, 114: 1153–1191.

Frye, T. M. & Iwasaki, I. 2011. Government directors and business–state relations in Russia, ***European Journal of Political Economy***, 27: 642–658.

Granrose, C. S., Huang, Q., & Reigadas, E. 2000. Changing organizational cultures in Chinese firms. In N. M. Ashkanasy, C. P. M. Wilderom, & M. F. Peterson (Eds.), ***Handbook of organizational culture and climate***: 483–496. Thousand Oaks, CA: Sage.

Grosman, A. 2015. Corporate governance as a mechanism to mitigate financing constraints on investment. Working paper, available at http://ssrn.com/abstract=2638434.

Grosman, A. & Leiponen, A. 2013. Who is monitoring the monitor? The influence of ownership networks and organizational transparency on long-term resource commitment in Russian listed firms, ***Academy of Management Proceedings***, 1: 17171.

© 2015 John Wiley & Sons Ltd

Grosman, A. & Wright, M. 2015. The good, the great and the independent: Implications of board and ownership structures on investment, ***Academy of Management Proceedings***, Working paper.

Guriev, S. & Rachinsky, A. 2005. The role of oligarchs in Russian capitalism, ***Journal of Economic Perspectives***, 19: 131–150.

Guthrie, D., Okhmatovskiy, I., Schoenman, R., & Xiao, Z. 2012. Ownership networks and new institutional forms in transition from plan to market. In B. Kogut (Ed.), ***The small worlds of corporate governance***: 117–149. Cambridge, MA: MIT Press.

Hanson, P. & Teague, E. 2005. Big business and the state in Russia, ***Europe-Asia Studies***, 57: 657–680.

Hashi, I., Welfens, P. J., & Wziatek-Kubiak, A. (Eds.). 2007. ***Industrial competitiveness and restructuring in enlarged Europe: How accession countries catch up and integrate in the European Union***. Basingstoke: Palgrave Macmillan.

Haveman, H. A. & Wang, Y. 2013. Going (more) public: Institutional isomorphism and ownership reform among Chinese firms, ***Management and Organization Review***, 9: 17–51.

Havrylyshyn, O. 2005. ***Divergent paths in post-communist transformation: Capitalism for all or capitalism for the few?*** Basingstoke: Palgrave Macmillan.

Hellman, J. S., Jones, G., & Kaufmann, D. 2003. Seize the state, seize the day: State capture and influence in transition economies, ***Journal of Comparative Economics***, 31: 751–773.

Holburn, G. L. F. & Zelner, B. A. 2010. Political capabilities, policy risks, and international investment strategy: Evidence from the global electric power generation industry, ***Strategic Management Journal***, 31: 1290–1315.

Hoskisson, R. E., Eden, L., Lau, C. M., & Wright, M. 2000. Strategy in emerging economies, ***Academy of Management Journal***, 43: 249–267.

Hoskisson, R. E., Wright, M., Filatotchev, I., & Peng, M. W. 2013. Emerging multinationals from mid-range economies: The influence of institutions and factor markets, ***Journal of Management Studies***, 50: 1295–1321.

Inoue, C., Lazzarini, S., & Musacchio, A. 2013. Leviathan as a minority shareholder: Firm-level implications of equity purchases by the state, ***Academy of Management Journal***, 56: 1775–1801.

Jiang, F. & Kim, K. A. 2015. Corporate governance in China: A modern perspective, ***Journal of Corporate Finance***, 32: 190–216.

Jiang, G., Lee, C. M., & Yue, H. 2010. Tunneling through intercorporate loans: The China experience, ***Journal of Financial Economics***, 98: 1–20.

Khanna, T., Palepu, K. G., & Srinivasan, S. 2004. Disclosure practices of foreign companies interacting with US markets, ***Journal of Accounting Research***, 42: 475–508.

Kilduff, M. & Brass, D. J. 2010. Organizational social network research: Core ideas and key debates, ***Academy of Management Annals***, 4: 317–357.

Kivleniece, I. & Quelin, B. V. 2012. Creating and capturing value in public-private ties: A private actor's perspective, ***Academy of Management Review***, 37: 272–299.

Kočenda, E. & Hanousek, J. 2012. State ownership and control in the Czech Republic, ***Economic Change and Restructuring***, 45: 157–191.

Lane, D. S. & Myant, M. R. (Eds.). 2007. ***Varieties of capitalism in post-communist countries***. Basingstoke: Palgrave Macmillan.

Lau, L. J., Qian, Y., & Roland, G. 2000. Reform without losers: An interpretation of China's dual-track approach to transition, ***Journal of Political Economy***, 108: 120–143.

Lazzarini, S. G. 2015. Strategizing by the government: Can industrial policy create firm-level competitive advantage?, ***Strategic Management Journal***, 36: 97–112.

Li, D., Moshirian, F., Nguyen, P., & Tan, L. W. 2007. Corporate governance or globalization: What determines CEO compensation in China?, ***Research in International Business and Finance***, 21: 32–49.

Li, M. H., Cui, L., & Lu, J. 2014. Varieties in state capitalism: Outward FDI strategies of central and local state-owned enterprises from emerging economy countries, ***Journal of International Business Studies***, 45: 980–1004.

Liang, H., Ren, B., & Sun, S. L. 2015. An anatomy of state control in the globalization of state-owned enterprises, ***Journal of International Business Studies***, 46: 223–240.

Lin, K. J., Tan, J., Zhao, L., & Karim, K. 2015. In the name of charity: Political connections and strategic corporate social responsibility in a transition economy, ***Journal of Corporate Finance***, 32: 327–346.

Liu, J. & Pissler, K. B. 2013. China – Corporate governance of business organizations. In A. M. Fleckner & K. J. Hopt (Eds.), ***Comparative corporate governance: A functional and international analysis***: 156–207. Cambridge: Cambridge University Press.

Liu, Y., Miletkov, M. K., Wei, Z., & Yang, T. 2015. Board independence and firm performance in China, ***Journal of Corporate Finance***, 30: 223–244.

Lu, J., Liu, X., Wright, M., & Filatotchev, I. 2014. International experience and FDI location choices of Chinese firms: The moderating effects of home country government support and host country institutions, ***Journal of International Business Studies***, 45: 428–449.

Makhija, M. 2003. Comparing the resource-based and market-based views of the firm: Empirical evidence from Czech privatization, ***Strategic Management Journal***, 24: 433–452.

Megginson, W. L. & Netter, J. M. 2001. From state to market: A survey of empirical studies on privatization, ***Journal of Economic Literature***, 39: 321–389.

Melkumov, D. 2009. Institutional background as a determinant of boards of directors' internal and external roles: The case of Russia, ***Journal of World Business***, 44: 94–103.

Meyer, K. E., Ding, Y., Li, J., & Zhang, H. 2014. Overcoming distrust: How state-owned enterprises adapt their foreign entries to institutional pressures abroad, ***Journal of International Business Studies***, 45: 1005–1028.

Meyer, K. E. & Lieb-Doczy, E. 2003. Post-acquisition restructuring as evolutionary process, ***Journal of Management Studies***, 40: 459–482.

Michelson, E. 2007. Lawyers, political embeddedness, and institutional continuity in China's transition from socialism, ***American Journal of Sociology***, 113: 352–414.

Mickiewicz, T. 2010. ***Economics of institutional change: Central and Eastern Europe***. Basingstoke: Palgrave Macmillan.

Morck, R., Yeung, B., & Zhao, M. 2008. Perspectives on China's outward foreign direct investment, ***Journal of International Business Studies***, 39: 337–350.

Musacchio, A., Lazzarini, S., & Aguilera, R. 2015. New varieties of state capitalism: Strategic and governance implications, ***The Academy of Management Perspectives***, 29: 115–131.

Nolan, P. 2001. ***China and the global economy: National champions, industrial policy and the big business revolution***. London: Palgrave Macmillan.

Okhmatovskiy, I. 2010. Performance implications of ties to the government and SOEs: A political embeddedness perspective, ***Journal of Management Studies***, 47: 1020–1047.

Pahor, M., Prasnikar, J., & Ferligoj, A. 2004. Building a corporate network in a transition economy: The case of Slovenia, ***Post-Communist Economies***, 16: 307–331.

Peng, M. W. & Zhou, J. Q. 2005. How network strategies and institutional transitions evolve in Asia, ***Asia Pacific Journal of Management***, 22: 321–336.

Pistor, K. & Turkewitz, J. 1996. Coping with Hydra: State ownership after privatization. In R. Frydman, C. W. Gray, & A. Rapaczynski (Eds.), ***Corporate governance in Central Europe and Russia***: 192–246. Budapest: Central European University Press.

Puffer, S. M. & McCarthy, D. J. 2007. Can Russia's state-managed, network capitalism be competitive? Institutional pull versus institutional push, ***Journal of World Business***, 42: 1–13.

© 2015 John Wiley & Sons Ltd

Puffer, S. M. & McCarthy, D. J. 2011. Two decades of Russian business and management research: An institutional theory perspective, ***The Academy of Management Perspectives***, 25: 21–36.
Pugliese, A., Bezemer, P. J., Zattoni, A., Huse, M., Van den Bosch, F. A., & Volberda, H. W. 2009. Boards of directors' contribution to strategy: A literature review and research agenda, ***Corporate Governance: An International Review***, 17: 292–306.
Pye, A. 2013. Boards and governance: 25 years of qualitative research with directors of FTSE companies. In M. Wright, D. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***Oxford handbook of corporate governance***: 135–162. Oxford: Oxford University Press.
Qian, M. & Yeung, B. 2015. Bank financing and corporate governance, ***Journal of Corporate Finance***, 32: 258–270.
Radygin, A. 2008. State capitalism and the financial crisis: Interdependence, inefficiencies, and future directions, ***Economic Policy***, 6: 88–105(in Russian).
Radygin, A., Entov, R., Gontmakher, A., Mezheraups, I., & Turuntseva, M. 2004. Economic and legal factors and constraints to the emergence of corporate governance models. Institute of Economics of Transition Working Paper No. 7. IET, Moscow (in Russian).
Ralston, D. A., Terpstra-Tong, J., Terpstra, R. H., Wang, X., & Egri, C. 2006. Today's state-owned enterprises of China: Are they dying dinosaurs or dynamic dynamos?, ***Strategic Management Journal***, 27: 825–843.
Ramamurti, R. & Vernon, R. (Eds.). 1991. ***Privatization and control of state-owned enterprises***. Washington, DC: The World Bank.
Russian Institute of Directors (RID). 2014. ***A study of corporate governance practices in SOEs during the 2008–2013 period***. Moscow: RID (in Russian).
Salvaj, E. & Couyoumdjian, J. P. 2015. Interlocked business groups and the state in Chile (1970–2010), ***Business History***. DOI:10.1080/00076791.2015.1044517.
Seglen, P. O. 1994. Causal relationship between article citedness and journal impact factor, ***Journal of the America Society for Information Science***, 45: 1–11.
Sheng, H. & Zhao, N. 2013. ***China's state-owned enterprises: Nature, performance and reform***. Singapore: World Scientific.
Shi, W., Markoczy, L., & Stan, C. V. 2014. The continuing importance of political ties in China, ***Academy of Management Perspectives***, 28: 57–75.
Simachev, Y. V. & Kuzyk, M. G. 2012. Anti-crisis state intervention in the Russian economy: Support and limitations, ***Journal of the New Economic Association***, 1: 100–125 (in Russian).
Spicer, A., McDermott, G., & Kogut, B. 2000. Entrepreneurship and privatization in Central Europe: The tenuous balance between destruction and creation, ***Academy of Management Review***, 25: 630–649.
Spicer, A. & Okhmatovskiy, I. 2015. Multiple paths to institutional-based trust production and repair: Lessons from the Russian bank deposit market, ***Organization Studies***, 36: 1143–1170.
Stark, D. 1996. Recombinant property in East European capitalism, ***American Journal of Sociology***, 101: 993–1027.
Suhomlinova, O. O. 1999. Constructive destruction: Transformation of Russian state-owned construction enterprises during market transition, ***Organization Studies***, 20: 451–483.
Sun, P., Mellahi, K., & Thun, E. 2010. The dynamic value of MNE political embeddedness: The case of the Chinese automobile industry, ***Journal of International Business Studies***, 41: 1161–1182.
Sun, P., Mellahi, K., & Wright, M. 2012. The contingent value of corporate political ties, ***Academy of Management Perspectives***, 26: 68–82.
Sun, P., Mellahi, K., Wright, M., & Xu, H. 2015. Political tie heterogeneity and the impact of adverse shocks on firm value, ***Journal of Management Studies***. DOI:10.1111/joms.12165.
Thun, E. 2004. Industrial policy, Chinese style: FDI, regulation, and dreams of national champions in the auto sector, ***Journal of East Asian Studies***, 4: 453–489.
Uhlenbruck, K., Meyer, K. E., & Hitt, M. A. 2003. Organizational transformation in transition economies: Resource-based and organizational learning perspectives, ***Journal of Management Studies***, 40: 257–282.
Walder, A. G. 1995. Local governments as industrial firms: an organizational analysis of China's transitional economy, ***American Journal of Sociology***, 101(2): 263–301.
Wang, J., Guthrie, D., & Xiao, Z. 2011. The rise of SASAC: Asset management, ownership concentration, and firm performance in China's capital markets, ***Management and Organization Review***, 8: 253–281.
Wang, K., Sewon, O., & Claiborne, M. C. 2008. Determinants and consequences of voluntary disclosure in an emerging market: Evidence from China, ***Journal of International Accounting, Auditing and Taxation***, 17: 14–30.
Wank, D. L. 1995. Private business, bureaucracy, and political alliance in a Chinese city, ***Australian Journal of Chinese Affairs***, 33: 55–71.
White, S. 2000. Competition, capabilities, and the make, buy, or ally decisions of Chinese state-owned firms, ***Academy of Management Journal***, 43: 324–341.
Wood, G. & Wright, M. 2015. Corporations and new statism: Trends and research priorities, ***Academy of Management Perspectives***, 29: 271–286.
Wooldridge, A. 2012. The visible hand. *The Economist*, January, 21.
Wright, M., Buck, T., & Filatotchev, I. 1998. Bank and investment fund monitoring of privatized firms in Russia, ***Economics of Transition***, 6: 361–387.
Xiao, H. & Yuan, J. 2007. Ownership structure, board composition and corporate voluntary disclosure: Evidence from listed companies in China, ***Managerial Auditing Journal***, 22: 604–619.
Xiao, J. Z., Yang, H., & Chow, C. W. 2004. The determinants and characteristics of voluntary Internet-based disclosures by listed Chinese companies, ***Journal of Accounting and Public Policy***, 23: 191–225.
Yakovlev, A. A. 2006. The evolution of business–state interaction in Russia: From state capture to business capture?, ***Europe-Asia Studies***, 58: 1033–1056.
Yakovlev, A. A. 2009. State–business relations and improvement of corporate governance. In T. Dolgopyatova, I. Iwasaki, & A. A. Yakovlev (Eds.), ***Organization and development of Russian business: A firm-level analysis***: 284–306. Basingstoke: Palgrave Macmillan.
Young, M. N., Peng, M. W., Ahlstrom, D., Bruton, G. D., & Jiang, Y. 2008. Corporate governance in emerging economies: A review of the principal–principal perspective, ***Journal of Management Studies***, 45: 196–220.
Zeng, Y., Douglas, T. J., & Wu, C. 2013. The seller's perspective on determinants of acquisition likelihood: Insights from China's beer industry, ***Journal of Management Studies***, 50: 673–698.
Zhao, Y. 2011. Review of the incentive system of independent directors in China, ***Business Law International***, 12: 215–233.
Zheng, W., Singh, K., & Mitchell, W. 2015. Buffering and enabling: The impact of interlocking political ties on firm survival and sales growth, ***Strategic Management Journal***, 36: 1615–1636.
Zhu, X. 2012. Understanding China's growth: Past, present, and future, ***Journal of Economic Perspectives***, 26: 103–124.

Anna Grosman is Assistant Professor of Corporate Finance at Aston Business School, Birmingham, UK. She graduated from Dauphine University with an MSc in Business Administration, from Panthéon-Assas University with an MSc in International Business, and from Imperial College London with a PhD in Corporate Finance. Her main fields of research are corporate governance, corporate finance, and transition economies. She was previously Director of Corporate

© 2015 John Wiley & Sons Ltd

Development at Koch Industries' Georgia-Pacific, and worked in corporate finance at Citigroup.

Ilya Okhmatovskiy is Assistant Professor of Strategy and Organization at the Desautels Faculty of Management, McGill University, Montreal, Canada. He received his PhD in Business Administration from Marshall School of Business at the University of Southern California. His research on corporate governance standards and performance implications of ties with the state has been published in the *Journal of Management Studies*, *Organization Science*, and *Organization Studies*.

Mike Wright is Professor of Entrepreneurship, Head of the Innovation and Entrepreneurship Department, Director of the Centre for Management Buyout Research and Associate Director of the Enterprise Research Centre at Imperial College Business School, London, UK. He is also a visiting professor at the University of Ghent. His research focuses on corporate governance, private equity, entrepreneurial mobility and emerging economies on which he has published in many leading journals. He is an editor of *Strategic Entrepreneurship Journal* and *Academy of Management Perspectives*.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 222–241

Corporate Governance Codes: A Review and Research Agenda

Francesca Cuomo*, Christine Mallin and Alessandro Zattoni

ABSTRACT

Manuscript Type: Review
Research Question/Issue: This study reviews previous country-level and firm-level studies on corporate governance codes up to 2014 in order to highlight recent trends and indicate future avenues of research.
Research Findings/Results: Our data show that research on codes increases over time consistently with the diffusion and the relevance of the empirical phenomenon. Despite previous studies substantially enriching our knowledge of the antecedents and consequences of governance codes, our study shows there are still several opportunities to make significant contributions in this area.
Theoretical Implications: Agency theory is the dominant theoretical framework, although other theoretical perspectives (especially the institutional one) are increasingly adopted. Future studies should be aimed at widening and combining various theoretical lenses so as to develop new interpretations and a better understanding of governance codes.
Practical Implications: Legislators and policymakers should continue to develop and update the recommendations of national governance codes in order to address the potential failures of corporate governance mechanisms in place.

Keywords: Corporate Governance, Good Governance Codes, Corporate Governance Guidelines

INTRODUCTION

Since the publication of the Cadbury Code in 1992, there has been a proliferation of corporate governance codes and guidelines (hereafter codes). As a result, over the last two decades codes have become a popular means of encouraging corporations to increase their transparency and accountability (Mallin, 2013). Simultaneously with the worldwide diffusion of corporate governance codes, governance scholars have devoted increasing attention to understanding codes' characteristics, the rationale behind their diffusion, and the implications for governance effectiveness and firm performance.

Despite the increasing attention by governance scholars, a previous review (Aguilera & Cuervo-Cazurra, 2009) covering publications on this topic until the middle of 2008 showed that there was still "an apparent lag between advances in the creation of codes and the studies analyzing the importance of codes" (p. 385). To address this lag, the review invited governance scholars to extend their studies in several directions, for example to provide a more careful examination of the codes' content, to analyze the effects of the code's issuer on its content and enforceability, to examine the consequences of codes issued by transnational institutions, to analyze the evolution of codes over time, and to explore in more depth the relationship between code compliance and firm performance.

*Address for correspondence: Francesca Cuomo, Lecturer in Corporate Governance, Norwich Business School, University of East Anglia (UEA), Norwich NR4 7TJ, UK. Tel: +44 (0) 1603 591506, E-mail: f.cuomo@uea.ac.uk

In addition, the recent financial crisis and the related corporate scandals have underlined the failure of existing governance mechanisms, including good governance codes. Therefore scholars, public opinion, and politicians have invited legislators and the financial community to reinforce both regulations (hard law) and governance codes (soft law) in order to increase transparency and accountability of, and to restore battered reputations and investor confidence in, financial and non-financial companies (e.g., Mallin, 2013; Zattoni & Cuomo, 2010). As a consequence, since the first appearance of the global financial crisis in 2007–08, the number of corporate governance codes has increased exponentially over time.

Consistent with the growing diffusion of codes and the call for new research on this topic (Aguilera & Cuervo-Cazurra, 2009), there has been a proliferation of studies on governance codes, so that the number of papers published since 2008 is significantly higher than the number of papers published before then. After such a recent and intense effort to reform corporate governance practices and to investigate the characteristics and the effectiveness of corporate governance codes, it is time to undertake a comprehensive review of the contribution of such a large flow of studies to the advancement of our understanding of codes.

That being said, the aim of this article is to undertake a review of previous country-level and firm-level studies on corporate governance codes in order to take stock of the knowledge accumulated and to highlight future avenues of research. This study extends the results of a previous review on codes (Aguilera & Cuervo-Cazurra, 2009) by significantly increasing

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12148

the number of papers and by expanding the length of the period under investigation. The review focuses on more recent phenomena, such as transnational codes, the diffusion of soft law, the impact of the global financial crisis on the developments of governance codes, and the co-existence of hard and soft law. At the same time, the review devotes particular attention to more recent studies, i.e. those published between 2009 and 2014.

In order to reach this goal, we first empirically analyze the speed and the path of the worldwide diffusion of corporate governance codes issued until the end of 2014. For this purpose, we take a wide view of 'codes', that is, we analyze formal as well as informal codes, including also national and transnational principles and guidelines, e.g. Pan-European and Organisation for Economic Co-operation and Development (OECD) principles. Then, following previous reviews (e.g., Pugliese, Bezemer, Zattoni, Huse, Van der Bosch, & Volberda, 2009), we analyze the literature and codify previous studies on corporate governance codes using the following criteria: (i) the type of articles (i.e., conceptual, empirical), (ii) the theories used (i.e., agency, institutional, other theories, multiple theories), (iii) the research topics (at both country level and firm level). In addition, only for empirical studies, we also consider: (iv) the research setting (i.e., single country or multiple countries), and (v) the data analysis (qualitative, quantitative, mixed methods, experiment). Finally, for each paper we identify the major findings.

The plan of the paper is straightforward. First, we describe the diffusion and the characteristics of corporate governance codes around the world. Second, we present the method used to select and analyze previous studies on codes and we summarize their characteristics. Third, we outline the results of our review of recent country-level and firm-level studies on corporate governance codes. Then, in the discussion section, we integrate previous literature and empirical evidence on corporate governance codes, highlight new directions for future research, and discuss the main limitations of our review. Finally, we present the main conclusions of our study.

CORPORATE GOVERNANCE CODES

Aims and Scope of Codes

Contrary to other forms of regulation (i.e., hard law or hard regulation such as the Sarbanes-Oxley Act of 2002), governance codes (i.e., a form of soft law or soft regulation) are "formally nonbinding and voluntary in nature, issued by multi-actor committees, flexible in their application, built on the market mechanism for evaluation of deviations and evolutionary in nature" (Haxhi & Aguilera, 2014, p. 2). They provide a voluntary means for innovation and improvement of corporate governance practices as the "comply or explain" and the "freedom with accountability" principles form the foundation of their application (Aguilera & Cuervo-Cazurra, 2004, 2009; Mallin, 2013). This means that companies have the option to comply with codes' recommendations or to explain the reasons why they do not comply. The rationale behind these principles is to allow firms some flexibility – i.e. to choose which corporate governance structure to adopt to better pursue their objectives – while guaranteeing better transparency to the market.

Following the dominant agency theory (e.g. Fama & Jensen, 1983; Jensen & Meckling, 1976), corporate governance codes encourage the board of directors to play an active and independent role in controlling the behavior of top management. Consistent with this view, the main codes' recommendations on boards suggest increasing the number of non-executive and independent directors, the splitting of Chairman and CEO roles, the creation of board committees (audit, remuneration, and nomination committees) made up of independent non-executive directors, and several other practices aimed at increasing board accountability and effectiveness (see Aguilera & Cuervo-Cazurra, 2009; Zattoni & Cuomo, 2008).

Corporate governance codes can be designed at three hierarchical levels: international, national, and individual firm level. First, there are codes issued by transnational institutions (such as Pan-European, Commonwealth, OECD, International Corporate Governance Network [ICGN]) to promote the diffusion of good governance practices around the world or to increase governance standards in a specific geographic region. Second, there are codes issued – individually or jointly – by several institutions within individual countries (e.g., the stock exchange, the government, and also investors', directors', managers' or professional associations) with the objective of positively influencing corporate governance practices in that specific national environment. Third, there are codes issued by individual firms (such as the code issued by General Motors) whose objective is to establish, and to communicate to investors and other stakeholders, the governance principles adopted by the firm.

Regarding national codes, Aguilera and Cuervo-Cazurra (2004) show that the type of issuer differs across and within countries. In addition, they show that the type of institutional pressure to adopt codes' recommendations varies with the type of issuer: it is a coercive pressure when codes are issued by the stock exchange or investors, a mimetic pressure when codes are issued by a managers' association, and a normative pressure when they are issued by the remaining types of issuers.

National and international codes are generally issued for listed companies, although there are also codes designed for non-listed companies or even for both listed and non-listed companies. More recently, there has also been the issuance of codes designed for companies with a specific ownership structure (e.g., state-owned or family-owned), for different types of financial institutions (e.g., commercial banks, institutional investors, mutual funds), or for voluntary and charitable organizations.

The disclosure of the compliance with national corporate governance codes differs among countries. More precisely, the disclosure on the adoption or explanation can be mandatory (i.e. voluntary adoption and mandatory disclosure) or voluntary (i.e., voluntary adoption and voluntary disclosure). On the one hand, this mandatory disclosure can be required by the listing authority (as, e.g., in Australia, Canada, Estonia, Luxembourg, Malta, Malaysia, Russia, Singapore, and the UK,) or by law (as, e.g., in several EU countries, including Belgium, France, Germany, Italy, the Netherlands, and Spain[1]). When the disclosure of governance practices is mandatory, the effectiveness of governance codes increases, because the external (i.e., market) disciplinary mechanism can work well only with informative disclosure on adoption and/or explanation.

© 2015 John Wiley & Sons Ltd

On the other hand, the voluntary adoption and the voluntary disclosure of corporate governance practices, which is standard in some emerging economies (e.g. Algeria, Lebanon, Tunisia, and Yemen) and even for companies listed on the Alternative Investment Market in the UK until August 2014, is less informative and noisier because when the company does not disclose its governance practices, investors cannot understand if the company does not adopt the best practices or adopts the best practices, but does not disclose their adoption. Such lack of disclosure may decrease the effectiveness of governance codes (soft law), because external (i.e., market) disciplinary mechanisms cannot work well without informative disclosure on adoption and/or explanation.

Despite the several positive aspects of the "comply or explain" approach, scholars cast doubt on its effectiveness (e.g., Pietrancosta, 2011). First, contrary to hard law regulation, codes cannot improve the governance practices of all companies as they leave them free to comply, or not, with the requirements of the code. In addition, the empirical evidence also shows that when companies comply with codes' recommendations, they comply more in form than in substance (e.g., Krenn, 2014). As a result, codes can help avoid, or significantly reduce, the use of bad governance practices, but they are unable to promote the universal adoption of best governance practices (Haxhi & Aguilera, 2014).

At the same time, hard law regulation also has both positive and negative implications for governance practices. Previous studies show, in fact, that the Sarbanes-Oxley Act favored de-listings and discouraged IPOs in the US due to the increased costs of compliance with regulation (Sasseen & Weber, 2006). These costs can be particularly high for some types of firms, such as small firms (Block, 2004; Engel, Hayes, & Wang, 2007) and poorly performing firms (Leuz, Triantis, & Wang, 2008). On the other hand, some recent studies show that the benefits of being cross-listed on US stock exchanges continue to exceed the costs and that it is more beneficial to be cross-listed in the US than in the UK (Bartlet, 2009; Zingales, 2007).

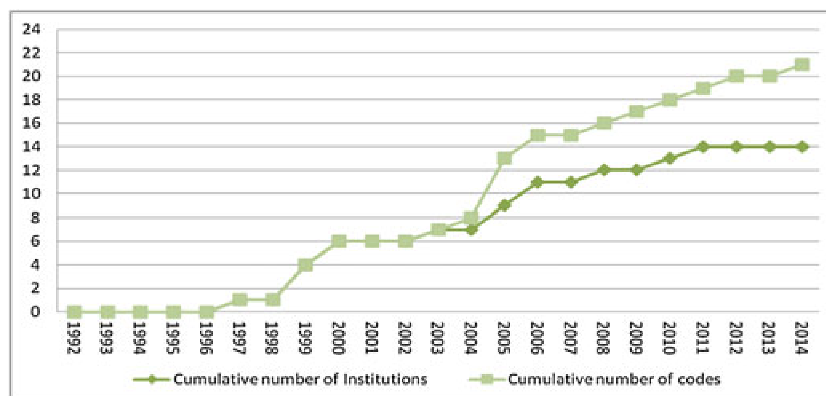
In sum, it is still too early to judge the efficacy of both the hard law and the soft law approaches. First, the effectiveness of these two approaches can vary in different contexts (Aguilera, Goyer, & Kabbach-Castro, 2013; Pietrancosta, 2011). Second, soft law is increasingly seen as a complementary rather than an alternative way to solve corporate governance problems (Hopt, 2011). A few recent studies (Carvalho & Pennacchi, 2012; Chavez & Silva, 2009) show that Brazil is successfully adopting hybrid versions of these two forms of regulation to overcome the rent-seeking action by interest groups opposed to reforms. Coherently, scholars call for additional studies on the co-existence of hard and soft law regulations in the field of corporate governance (Aguilera et al., 2013).

Diffusion of Codes Around the World

We collected information on the speed and the path of the diffusion of governance codes around the world up to the end of 2014 in order to update the results of previous studies (Aguilera & Cuervo-Cazurra, 2004, 2009) and to highlight both the role of transnational institutions and the impact of the global financial crisis. We took a wide view of codes and we built a database of all corporate governance codes, including formal as well as informal codes, and national as well as transnational ones. Our main source of information was the "Codes and Principles" section on the European Corporate Governance Institute website (http://www.ecgi.org). For reasons of consistency, we excluded laws and legal regulations, reports on compliance with codes already issued, initial drafts, consulting firm reports, and codes targeting individuals (such as codes of conduct for top managers). Furthermore, in order to avoid double counting of codes, we included only the final version of each code.

We classified codes into two groups: transnational and national ones. The first group is composed of codes issued by transnational institutions (such as Pan-European, Commonwealth, OECD, ICGN) and the second group is composed of codes issued by institutions within individual countries. Figure 1 shows that 14 transnational institutions issued 21 corporate governance codes by the end of 2014. Corporate governance codes issued by transnational institutions diffused very slowly. In particular, the issue of codes started at the end of the 1990s, in parallel with the Asian and Russian stock market crashes that probably gave impetus to their issue, and accelerated between 2004 and 2006 – a few years after the deflation of the internet bubble in 2000 and various high profile corporate scandals including Enron,

FIGURE 1
The Diffusion of Transnational Corporate Governance Codes Around the World (1992–2014)



© 2015 John Wiley & Sons Ltd

Worldcom, and Parmalat. There was then a second wave immediately after the recent financial crisis in 2007–2008.

Figure 1 also shows that the number of institutions and codes were aligned before 2004 as it was only after that year that some institutions (i.e., OECD and ICGN) started both to revise their codes as a reaction to governance scandals or to issue codes targeted at particular types of firms (e.g., the OECD issued new guidelines for non-listed companies in emerging markets and for state-owned enterprises in 2005).

Data show that international institutions were more active than all other transnational institutions (i.e., Baltic countries, Commonwealth, Latin American, and Pan-European) as they issued 13 out of the 21 codes. In addition, only 3 international institutions out of 14 transnational institutions revised or issued new corporate governance codes over time. Amongst international institutions, the OECD and the ICGN were the most active as they issued 8 out of 21 codes. In particular, the OECD issued its first code in 1999, following the influential report "Corporate Governance: Improving Competitiveness and Access to Capital in Global Markets" ("the Millstein Report"). Still in 1999, the ICGN issued its first international corporate governance code building on and extending the OECD principles. In the following years, the two institutions continued to update and extend their corporate governance codes: the OECD in 2004 and more recently in 2015; the ICGN in 2005, 2009 and in 2014.

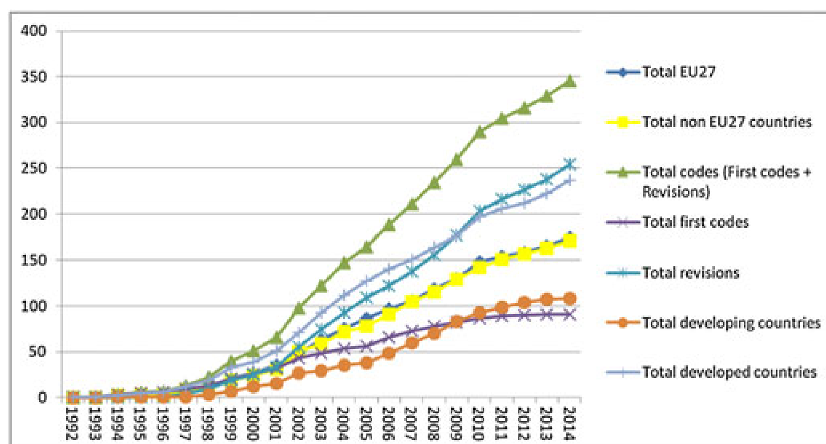
Regarding the scope of codes issued by transnational institutions, the vast majority of them are designed for all listed companies. However, an increasing number of institutions are also issuing governance codes for non-listed firms, for specific types of companies (e.g., state-owned) and for different types of financial institutions (e.g., institutions offering Islamic financial services, microfinance institutions, and sovereign wealth funds).

Regarding governance codes issued by individual countries, Figure 2 shows that 91 countries issued a code and that a total of 345 codes (91 first codes and 254 revisions) have been developed around the world by the end of 2014. The figure also shows that developed countries – and especially European ones – play a significant role in the diffusion of codes. More precisely, European countries issued more than half of codes issued by all countries (174 out of 345) and were among the first ones to adopt a code. The first national code included in our sample is the Cadbury Code issued in the UK in 1992.[2] From 1992 to 1998 four other EU countries followed the UK example by issuing their first national code – France with the Vienot Report in 1995, the Netherlands with the Peters Report in 1997, Belgium with the Cardon Report in 1998, and Spain with the Olivencia Code in 1998.

In addition, our analysis shows that a smaller number of developed countries issued more codes than a larger number of developing countries. In particular, between 1992 and 1998 only three developing countries issued a code – South Africa in 1994, and India and Thailand in 1998. Moreover, developing countries were reluctant to revise their first code, as only 30 out of 53 developing countries issued more than one code and only 15 out of 53 issued more than two codes.

Table 1 shows that countries vary not only in the speed of adoption, but also in the scope of their codes. The vast majority of countries issued codes targeted at all listed companies. However, an increasing number of countries also issued governance codes for specific types of companies (e.g., state-owned, family-owned, and small and medium enterprises), for different types of financial institutions (e.g., commercial banks, institutional investors, mutual funds) and for voluntary and charitable organizations. In particular, our data show that, by the end of 2014, nine countries issued 11 codes for specific types of companies such as state-owned enterprises (Egypt, Pakistan, the Netherlands, and the UK), family-owned enterprises (Colombia, Morocco, and Switzerland) and small and medium enterprises (Colombia, France, New Zealand, and the United Arab Emirates). In addition, there are also some codes encouraging institutional investors to play an active role in engaging with boards of directors on key issues like governance, strategy, and performance. By the end of 2014, 20 countries, including Ireland, Italy, Japan, Luxembourg, Malaysia, Malta, South Africa, and Nigeria, issued 30 codes targeted at institutional investors or other financial institutions. Their number increased significantly after the recent financial crisis and the issuance of the UK Stewardship

FIGURE 2
The Diffusion of National Corporate Governance Codes Around the World (1992–2014)



© 2015 John Wiley & Sons Ltd

TABLE 1
The Issuance of Corporate Governance Codes by Countries (1992–2014)

Country	Developing countries	Year of first code	Total stock of codes (2014)	Number of codes issued for listed companies or all companies	Codes targeting specific companies or managers (year)
Albania	1	2008	1	0	Non-listed firms (2008)
Algeria	1	2009	1	1	
Argentina	1	2004	1	1	
Armenia	1	2010	1	1	
Australia	0	1995	9	6	Investment managers (1999), Fund managers (2002), Charity (2013)
Austria	0	2002	6	6	
Azerbaijan	1	2011	1	1	
Bahrain	1	2010	1	1	
Bangladesh	1	2004	1	1	
Barbados	1	2013	1	1	
Belgium	0	1998	7	6	Non-listed firms (2005)
Bosnia and Herzegovina	1	2006	3	3	
Brazil	1	1999	4	4	
Bulgaria	1	2007	2	2	
Canada	0	1994	8	7	Voluntary organizations (1999)
China	1	2001	2	2	
Colombia	1	2007	3	1	Closed Societatis and family firms (2009), Small and medium-size Enterprises (2004)
Croatia	1	2009	2	2	
Cyprus	0	2002	4	4	
Czech Republic	0	2001	2	2	
Denmark	0	2000	11	10	Private equity funds (2008)
Egypt	1	2006	3	1	State-owned firms (2006), Private sector (2006)
Estonia	0	2006	1	1	
Finland	0	2003	4	3	Non-listed firms (2006)
France	0	1995	12	11	Small and medium-size enterprises (2009)
Georgia	1	2009	1	0	Commercial banks (2009)
Germany	0	1998	17	16	Asset management companies (2005)
Ghana	1	2010	1	1	
Greece	0	1999	4	4	
Guernsey	0	2011	1	0	Finance sector (2011)
Hong Kong	0	1999	4	4	
Hungary	0	2002	4	4	
Iceland	0	2004	4	4	
India	1	1998	3	3	
Indonesia	1	2000	3	3	
Ireland	0	1999	9	8	Reinsurance undertakings (2007), NGOs (2008), Credit institutions and insurance undertakings (2010, 2013), Investment funds (2010), Domiciled collective investment schemes (2010), Collective investment schemes (2011), Community, voluntary and charitable organizations (2012)
Israel	0	2006	1	1	

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1
(Continued)

Country	Developing countries	Year of first code	Total stock of codes (2014)	Number of codes issued for listed companies or all companies	Codes targeting specific companies or managers (year)
Italy	0	1999	6	5	Banks (2008)
Jamaica	1	2006	1	1	
Japan	0	1997	5	4	Institutional investors (2014)
Jordan	1	2007	3	2	Banks (2007)
Kazakhstan	1	2007	1	1	
Kenya	1	2002	2	2	
Korea	0	1999	2	2	
Latvia	0	2005	2	2	
Lebanon	1	2006	2	2	
Lithuania	0	2003	1	1	
Luxembourg	0	2006	5	3	Investment funds (2009, 2013)
Macedonia	1	2006	1	1	
Malawi	1	2010	1	1	
Malaysia	1	2000	4	3	Institutional investors (2014)
Malta	0	2001	4	3	Investment companies and collective investment schemes (2014)
Mauritius	1	2004	2	2	
Mexico	1	1999	2	2	
Moldova	1	2007	1	1	
Mongolia	1	2007	1	1	
Montenegro	1	2009	1	1	
Morocco	1	2008	3	2	Small and medium-size enterprises and family firms (2008)
New Zealand	0	2003	2	2	
Nigeria	1	2003	5	2	Banks and discount houses (2014), Licensed pension operators (2008), Banks (2006)
Norway	0	2004	9	7	
Oman	1	2002	1	1	
Pakistan	1	2002	3	2	State-owned firms (2013)
Peru	1	2001	2	2	
Poland	1	2002	6	5	
Portugal	0	1999	10	10	
Qatar	1	2008	2	1	Banks and financial institutions (2008)
Romania	1	2000	2	2	
Russia	1	2002	2	2	
Saudi Arabia	1	2006	2	2	
Serbia	1	2008	1	1	
Singapore	0	2001	4	3	Banks, financial holding companies and direct insurers (2010)
Slovakia	0	2002	2	2	
Slovenia	0	2004	4	4	
South Africa	1	1994	4	3	Institutional investors (2011)
Spain	0	1996	8	7	Non-listed firms (2005)
Sri Lanka	1	2008	1	1	

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1
(Continued)

Country	Developing countries	Year of first code	Total stock of codes (2014)	Number of codes issued for listed companies or all companies	Codes targeting specific companies or managers (year)
Sweden	0	2001	6	6	
Switzerland	0	2002	3	2	Family firms (2006)
Taiwan	0	2002	3	3	
Thailand	1	1998	5	4	Investors (2006)
The Netherlands	0	1997	8	5	Insurance companies (2010), Banks (2009), State-owned firms (2000)
The Philippines	1	2000	3	3	
Trinidad and Tobago	1	2006	2	2	
Tunisia	1	2008	1	1	
Turkey	1	2003	2	2	
Ukraine	1	2003	1	1	
United Arab Emirates	1	2007	2	1	Small and medium-size enterprises (2011)
UK	0	1992	31	23	Institutional investors (2010, 2012), State-owned firms (2005, 2011), Non-listed firms (2010), Banks and other financial industry entities (2009), Private equity (2007), Voluntary and community sector (2005)
USA	0	1997	14	13	Asset managers (2004)
Yemen	1	2010	1	1	

Code (2010, 2012). Finally, it is interesting to note that a few countries (Australia, Canada, the UK, and Ireland) also issued a code for voluntary and charitable organizations.

Figure 2 shows that after the issuance of the Cadbury Code, the diffusion of codes has been initially slow and accelerated only after the issuance of both the OECD Principles of Corporate Governance and the ICGN Statement on Global Corporate Governance Principles in 1999. Only nine countries around the world issued a corporate governance code by 1997, while a further 34 countries joined the group by issuing their first code by 2002. Among European countries, the total number of corporate governance codes issued increased after the publication of two influential reports (the European Union Action Plan on "Modernising Company Law and Enhancing Corporate Governance in the EU" published in 2003 and the report by the High-Level Group on Financial Supervision in the EU published in 2009) aimed at furthering the convergence of company law and corporate governance practices within the EU.

Our data show a first peak of new and updated national codes issued in 2002 just after several corporate frauds and financial scandals (e.g., Enron, WorldCom, Tyco in the US). Interestingly, the development of new corporate governance codes happened in parallel with the promulgation of stricter legal norms aimed at increasing investor protection, like the Sarbanes-Oxley Act in the US. A second peak of national codes development (first code and revisions) happened between 2009 and 2010, just after the corporate scandals and collapses related to the global financial crisis. After 2011, the number of new codes issued per year decreased over time – only a few small countries (i.e., Azerbaijan, Barbados, Guernsey) issued their first codes in this period – and the same is true for the issuance of revisions and updates of codes, with the exception of the last two years considered.

To sum up, our analysis of the corporate governance codes issued by national countries and transnational institutions around the world shows that the number of codes (first issues and revisions) increased over time. The most active countries were the developed ones, with the UK and the US issuing the greatest number of codes. Moreover, the creation of national corporate governance codes usually accelerated after the issuance of influential transnational codes and the occurrence of corporate scandals and frauds. Finally, it is interesting to note that, beyond the traditional codes aimed at addressing corporate governance deficiencies of all listed companies, there is an increasing proliferation of codes aimed at improving the governance of specific types of companies, of financial institutions and institutional investors, and of voluntary and charitable organizations.

© 2015 John Wiley & Sons Ltd

REVIEW OF THE LITERATURE ON CORPORATE GOVERNANCE CODES

Method

We undertook a review of previous studies on corporate governance codes around the world up to early November 2014 in order to understand what we know and what is still missing. Regarding the search criteria, the main databases (i.e., Business Source Complete, Scopus, Science Direct and JSTOR) provided by EBSCOhost were used to search for all publications (only peer-reviewed articles) in English containing the terms "Governance code" or "Governance guideline" in their Title/Abstract or Subject terms. We considered all journals included in the above-mentioned databases.

Our initial search resulted in 860 articles. Then, after a detailed reading of the abstracts, and sometimes also of the content of papers, we excluded papers on other types of codes (e.g., codes of ethics, IT codes, fishery codes), book reviews, duplicates, case studies, letters from the editors, papers published by university journals, and student papers. In this phase, we also excluded papers focused on different topics or on related topics not relevant to our study.[3] This careful analysis enabled us to identify a final sample of 149 articles published in 82 journals from 1993 to November 2014.

Following previous reviews (e.g., Aguilera & Cuervo-Cazurra, 2009; McNulty, Zattoni, & Douglas, 2013; Pugliese et al., 2009; Zattoni & van Ees, 2012), we did a content analysis of the selected papers in order to codify the selected articles using the following criteria: (i) the "empirical" or "conceptual" nature of the article, (ii) the theories employed, (iii) the research topics. For empirical studies, we also considered: (iv) the research setting, and (v) the data analysis (see Table 2). Regarding the coding scheme and the procedure followed to

TABLE 2
The Criteria used to Review Articles on Corporate Governance Codes (1992–2014)

Criteria	Meaning	Variables
Type of articles	*Nature of the article*	0 = conceptual, 1 = empirical
Use of theories	*Type of theories employed*	0 = No theory or implicit theories, 1 = Agency theory only, 2 = Institutional theory only, 3 = Other theories only, 4 = Multiple theories (including agency theory), 5 = Multiple theories (excluding agency theory)
Research topics	*Country-level studies*	0 = no, 1 = yes
	Studies on the mechanisms for code implementation – mandatory versus voluntary regulation	
	Reasons behind the adoption of codes	
	Analyses of the content of a specific national code	
	Comparisons of the content of national codes at international level (at least two countries)	
	Reflection on the internationalization and the convergence-divergence of corporate governance codes	
	Studies on codes issued by transnational institutions	
	Firm-level studies	
	Surveys of compliance statements at national level	
	Surveys of compliance statements at international level	
	Studies on the explanations for deviations from a corporate governance code	
	Studies on the relationship between code compliance and firm performance	
Method (only empirical articles)	*Research setting*	1 = UK, 2 = Liberal market economies (excluding UK and US), 3 = Liberal market economies (including UK and US), 4 = Continental European countries, 5 = Emerging economies, 6 = Transition economies, 7 = More than one economies (excluding UK and US), 8 = More than one economies (including US and UK)
	Data analysis	1 = Qualitative, 2 = Quantitative, 3 = Mixed method, 4 = Experiment

© 2015 John Wiley & Sons Ltd

codify the selected articles, three coders initially developed and tested the coding scheme on a sample of 16 articles. Then, we randomly split the selected articles into two equal subsamples and we assigned them to two different coders to codify them independently. Moreover, a third coder codified all of the studies independently. Then, we matched the three sets of data in order to measure inter-rater reliability using percentage agreement (Dewey, 1983). We found a high overlap as the percentage agreement was 94 per cent and 93 percent, respectively, and above the appropriate minimum level of reliability. Finally, we met to discuss the few cases where there was a difference of opinion in order to reach agreement about them.

Results

Following previous reviews (e.g., Saggese, Sarto, & Cuccurullo, 2015), we identified the most influential articles to illustrate the evolution of previous studies on codes. A common view among scholars is that relevant changes in a field of study often happen after the publication of influential articles (Bergh, Perry, & Hanke, 2006; Kuhn, 2012). Coherently, we ranked all 149 articles according to the number of citations on Google Scholar at the end of January 2015 (Furrer, Thomas, & Goussevskaia, 2008; Saggese et al., 2015). Our search shows that the articles published by Aguilera & Cuervo-Cazurra, 2004 (411 citations), by Drobetz, Schillhofer, & Zimmermann, 2004 (457 citations), and the previous review by Aguilera & Cuervo-Cazurra, 2009 (189 citations), have been very influential in the development of research on corporate governance codes. Consistent with our criteria, we identified 2004 and 2009 as the initial years of a new period. Then, following a common practice in previous review papers in the field of corporate governance (Pugliese et al., 2009; Saggese et al., 2015), we assigned each article to one of the three resulting research periods (i.e., 1993–2003, 2004–2008, or 2009–2014) according to the year of publication.

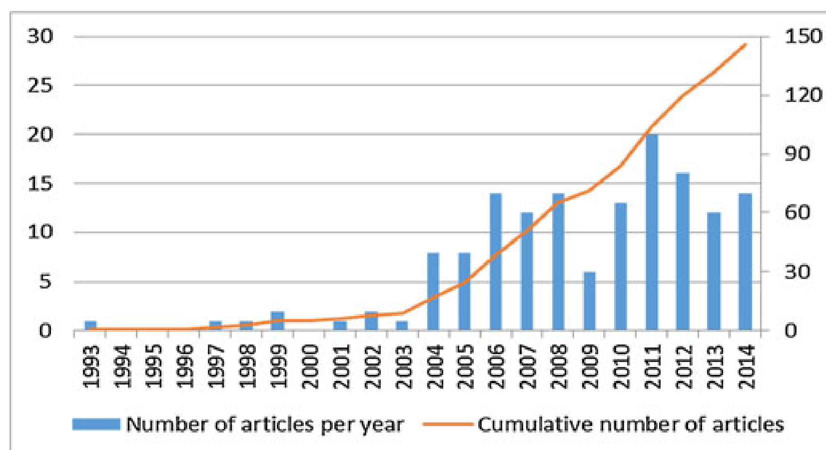
Figure 3 shows that the number of articles on corporate governance codes increased over time. Parallel to the slow development of codes, the years after the publication of the first paper in our sample (Stiles & Taylor, 1993), published just one year after the issuance of the Cadbury Code in the UK, saw a low interest in the topic. Only 10 out of 149 papers (7 percent) were, in fact, published between 1993 and 2003. The number of papers on codes increased significantly in the second period, with a total of 58 articles published between 2004 and 2008. This trend continued in the third period, which includes the majority of the papers in our sample, and reached a peak of 20 papers in 2011.

Tables 3 summarizes the characteristics of previous studies on corporate governance codes. Our results show that the large majority of articles are empirical, while conceptual papers are much less common. In addition, our data highlight that the majority of articles on codes are not built on an explicit theory or that the theoretical grounding can be found only inductively. At the same time, the increasing use of explicit theories over time underlines the maturation of the academic debate on the development of good governance codes.

Several theories from a variety of disciplines (including finance, economics, law, politics, and organizational theory) have been used to explore corporate governance phenomena (see, e.g., Aguilera & Jackson, 2010; Clarke, 2004; Cohen, Krishnamoorthy, & Wright, 2008). Historically, researchers have mostly focused on governance practices at firm level using the agency lens (see, e.g., Fama & Jensen, 1983; Jensen & Meckling, 1976) to study governance issues (e.g., compensation policy, composition of the board of directors, CEO duality, relationship between firm governance practices and firm performance, etc.), whereas, on the other hand, they have mostly focused on the role of the national institutional environment and its influence on governance practices at country level in order to explain differences across countries (see, e.g., Aguilera & Cuervo-Cazurra, 2004; Aguilera & Jackson, 2003). More recently, scholars (Aguilera, Filatotchev, Gospel, & Jackson, 2008; Judge, 2009) suggest using multiple lenses to address governance issues, as previous studies using a single lens have failed to explain governance phenomena.

Among these several theories, our data indicate that agency theory has affected the development of research on codes the most, often as a unique theoretical lens and sometimes also

FIGURE 3
The Evolution of Research on Corporate Governance Codes (1992–2014)



© 2015 John Wiley & Sons Ltd

TABLE 3
Evolution of Previous Studies on Corporate Governance Codes

	1993–2003		2004–2008		2009–2014		Overall	
	N	%	N	%	N	%	N	%
Type of articles								
Conceptual	4	40%	14	24%	15	18%	33	22%
Empirical	6	60%	44	76%	66	82%	116	80%
Total	10	100%	58	100%	81	100%	149	100%
Use of theories								
Agency theory only	3	30%	14	24%	27	33%	44	30%
Institutional theory only	0	0%	3	5%	7	9%	10	7%
Other theories only	1	10%	3	5%	7	9%	11	7%
Multiple theories (including agency theory)	0	0%	6	10%	9	11%	15	10%
Multiple theories (excluding agency theory)	0	0%	2	3%	4	5%	6	4%
No theory or implicit theories	6	60%	30	52%	27	33%	63	42%
Research topics								
Country-level studies								
Studies on the mechanisms for code implementation – mandatory versus voluntary regulation	2	20%	20	34%	21	26%	43	29%
Reasons behind the adoption of codes	0	0%	2	3%	5	6%	7	5%
Analyses of the content of a specific national code	4	40%	14	24%	22	27%	40	27%
Comparisons of the content of national codes at international level (at least two countries)	0	0%	13	22%	10	12%	23	15%
Studies on codes issued by transnational institutions	0	0%	3	5%	6	7%	9	6%
Reflection on the internationalization and the convergence-divergence of corporate governance codes	0	0%	15	26%	13	16%	28	19%
Firm-level studies								
Surveys of compliance statements at national level	5	50%	22	38%	31	38%	58	39%
Surveys of compliance statements at international level	0	0%	3	5%	4	5%	7	5%
Studies on the explanations for deviations from a corporate governance code	1	10%	8	14%	8	10%	17	11%
Studies on the relationship between code compliance and firm performance	2	20%	12	21%	18	22%	32	21%

in combination with other theories. As codes are developed to address agency issues related to the principal-agent problem in widely held companies and to the principal-principal problems in companies controlled by large shareholders, agency theory has been used – mostly in firm-level studies – as the main theory or as the implicit theoretical background. The second most used theory is institutional theory, which has been used both in firm-level studies to explain the (legitimation) reasons behind compliance with codes' recommendations and in country-level studies to explore the (legitimation) reasons behind the diffusion of governance codes and to explain diversity in the worldwide diffusion of this practice. Other theories (e.g., stakeholder theory, political theory, efficiency theory, stewardship theory, contingency theory, conflict and signaling theories, and financial system theory) are rarely adopted. This result confirms both the dominance of agency theory and the increasing use of institutional theory – alone or in combination with other theories (especially agency) – in the explanation and interpretation of governance phenomena (Judge, 2008).

Regarding the research topics,[4] country-level studies are mostly focused on the mechanisms for code implementation, on the content of a national code, and on the internationalization and the convergence-divergence of corporate governance principles. On the other hand, firm-level studies are mostly focused on compliance with a national code and on the relationship between code compliance and firm performance. While our review of governance codes underlines the influence that both some national and transnational codes had on their diffusion across countries, it is interesting to note that our review of previous studies shows that there is still a relatively scarce number of studies investigating codes at international level.

Regarding the country setting of the empirical studies, Table 4 shows that emerging economies are the most common empirical setting, followed by Continental European countries and the UK. However, our results vary significantly over the three periods mainly due to the different times of the diffusion of codes. In the first period, the UK provides the most common setting, due to the importance of the Cadbury Code and the UK experience in influencing not only the diffusion of

© 2015 John Wiley & Sons Ltd

TABLE 4
Evolution of the Method used in the Empirical Articles on Corporate Governance Codes

	1993–2003		2004–2008		2009–2014		Overall	
	N	%	N	%	N	%	N	%
Research setting								
UK	5	84%	6	14%	7	11%	18	16%
Liberal market economies (excluding UK and US)	0	0%	1	2%	4	6%	5	4%
Liberal market economies (including UK and US)	0	0%	0	0%	0	0%	0	0%
Continental European countries	1	16%	14	31%	12	18%	27	23%
Emerging economies	0	0%	10	23%	28	42%	38	33%
Transition economies	0	0%	3	7%	6	9%	9	8%
More than one economy (excluding UK and US)	0	0%	0	0%	1	2%	1	1%
More than one economy (including US and UK)	0	0%	10	23%	8	12%	18	15%
Total	6	100%	44	100%	66	100%	116	100%
Data analysis								
Qualitative	2	50%	17	39%	21	32%	41	35%
Quantitative	2	50%	20	45%	34	52%	57	49%
Mixed method	0	0%	7	16%	9	14%	16	14%
Experiment	0	0%	0	0%	2	2%	2	2%
Total	4	100%	44	100%	66	100%	116	100%

codes, but also the academic debate on governance practices. In the second period, Continental European countries provide the most common setting, followed by emerging economies and the UK. In the third period, emerging economies provide the most common setting, consistent with the increasing attention of governance scholars to governance mechanisms and issues in those countries. As stated above, studies on more than one economy are still limited probably due to the difficulties in data collection.

Finally, our analysis on the evolution of the methods shows an increasing number of studies with quantitative data analysis and mixed methods. This trend highlights the continuous maturation of the empirical research on codes.

THE EVOLUTION OF COUNTRY-LEVEL STUDIES ON CODES

Our review of the existing literature on corporate governance codes shows that a first stream of research on this topic consists of country-level studies investigating: (i) the mechanisms for the implementation of codes, (ii) the reasons behind the adoption of codes, (iii) the content of a specific national code, (iv) the comparisons of the content of national codes at international level, (v) the internationalization and the convergence-divergence of governance codes, and (vi) the consequences of codes issued by transnational institutions.

Studies on the Mechanisms for Code Implementation

A first set of articles includes studies on the mechanisms for the implementation of codes (i.e., mandatory versus voluntary regulation). Our data show that a large number of existing studies focused on this topic and that the debate evolved over time and is still alive, especially with regard to emerging and transition countries.

Several conceptual studies focus on the advantages and disadvantages of the two regulatory mechanisms used to solve agency problems and to implement codes (i.e., hard versus soft law regulation). In particular, some articles in the first two periods cast doubt on the efficacy of the soft law approach, as lack of monitoring and weak enforcement reduce its effectiveness, and suggest different ways to solve the deficiencies of this approach (see, e.g., Cuervo, 2002; Dewing & Russell, 2004). More recently, scholars ask for the use of directives and mandatory rules (i.e., hard law) and for the strengthening of institutional enforcement mechanisms in transition and emerging economies (Osemeke & Adegbite, 2014; Wanyama, Burton, & Helliar, 2009). In their opinion, in fact, the soft law approach is not efficient – i.e. it is useful, but not sufficient – to improve governance practices in poor institutional environments, that is, in countries characterized by weak investor rights, poor enforcement of law, and undeveloped capital markets. Consistent with this view, Wanyama et al. (2009, p. 159) argue that "the mere emergence of detailed governance codes in developing countries does not necessarily mean that de facto practices will improve." Moreover, Keay (2014) suggests introducing a regulatory body and some sanctions for non-compliance or for the failure to adequately explain the reasons for non-compliance. Finally, arguing against such emphasis on the hard and soft law mechanisms, some papers (e.g., Chiu, 2012) focus on the role of institutional investors (i.e., shareholder empowerment) as a complementary "market-based" governance mechanism whose effectiveness has been reinvigorated by the issuance of the UK Stewardship Code.

© 2015 John Wiley & Sons Ltd

Studies on the Reasons Behind the Adoption of Codes

A second set of articles focused on the reasons behind the diffusion of national codes as a particular type of best practice. In 2004, the pivotal work of Aguilera and Cuervo-Cazurra (2004) opened up the debate on the reasons behind the adoption of codes. Building on institutional theory, the study aims at investigating whether "efficiency" or "legitimation" reasons explain the worldwide diffusion of codes. Following this perspective, several studies have been published in the subsequent years (e.g., Enrione, Mazza, & Zerboni, 2006; Zattoni & Cuomo, 2008). Their results show that both reasons contribute to explain the diffusion of codes around the world. On the one hand, they find that there is a positive association between the issuance of codes and country's economic integration, government liberalization, size of the capital market, and the degree of investor protection (Aguilera & Cuervo-Cazurra, 2004; Zattoni & Cuomo, 2008). On the other hand, they find that civil law countries – characterized by lower investor rights than common law countries – are more inclined to extend codes' recommendations to non-listed companies (Zattoni & Cuomo, 2008).

Thereafter, the variety of theoretical perspectives increase over time from the efficiency and institutional views to the cultural and political ones. For example, building on Aguilera and Cuervo-Cazurra (2004) and Hofstede (2001), Haxhi and van Ees (2010) show that informal institutions (i.e., national culture) matter in the development of corporate governance codes. In particular, their results show that individualistic cultures develop more governance codes than collectivistic cultures, the stock exchange and investors' groups of issuers (i.e., the coercive group) are more likely to issue the first code in countries with low power distance, while the government, directors' or professional associations (i.e., the normative group) are more likely to issue the first code in countries with high power distance (Haxhi & van Ees, 2010).

Finally, a few recent studies building on political theory show that various interests play a relevant role in the development of codes. Among them, Haxhi, van Ees, and Sorge (2013) argue that the issuance of codes in the UK has been affected by the national business elites, while Mosley (2010) argues that political institutions have hindered the diffusion of codes in middle-income OECD countries.

Studies on the Content of a Specific National Code

A third set of articles focused on the analysis of a specific national code. Up to the end of 2008, these articles (e.g., Cromme, 2005; Fernández-Fernández, 1999; Roberts, 2004; Webb, Beck, & McKinnon, 2003) describe the content of the first national code issued in a single country (e.g., Germany, UK, Russia, and Spain). In more recent years, our results show that studies extend their focus in two directions: first, they go beyond the experience of Western European countries and start to analyze emerging countries' codes (e.g., Nigeria, Hungary, Indonesia, Malaysia) and, second, they focus on the evolution of the content of national codes in several institutional settings (e.g., Martin, 2010 for Hungary; Haxhi et al., 2013 and Nordberg & McNulty, 2013 for the UK). For example, a recent article published by Haxhi et al. (2013), on the development of corporate governance codes in the UK since the publication of the Cadbury Code, shows how good governance practices evolve over time in relation to several characteristics of boards of directors, such as board composition and independence, criteria for identifying an independent director, board performance evaluation, and composition of board sub-committees. Finally, our analysis shows that the issuance of the Stewardship Code (2010, 2012) in the UK led to a new avenue of research on the role of institutional shareholders (e.g., Chiu, 2012; Reisberg, 2011).

Studies on Comparisons of the Content of National Codes at International Level

Despite the proliferation of codes around the world, our analysis shows that a limited number of articles focused on the comparisons of the content of different national codes over time. Early articles on this topic are published only after 2004 and their number decreased in the last period. The majority of them analyze and compare the content of codes issued by a small number of countries (i.e., between two and seven). Regarding the country setting, the EU is the most common one as half the articles review the content of codes issued by a number of EU countries (e.g., Collier & Zaman, 2005; Hermes, Postma, & Zivkov, 2006, 2007). This empirical emphasis is consistent with the increasing political pressure by the EU to harmonize several elements of regulation across European countries, including corporate law and governance codes.

Despite the increasing pressure coming from institutional investors and supra-national organizations to homogenize the content of codes, studies using a large international sample (see, e.g., Heugens & Otten, 2007; Zattoni & Cuomo, 2008) are very uncommon and are published only after 2007. Among them, Zattoni and Cuomo (2008), by analyzing the content of codes issued in 60 countries around the world, find that the content of codes varies across countries (i.e., civil law countries issue codes with less stringent and rigid recommendations than common law countries). Studies on this topic also remain very limited in the third period. Among them, Cicon, Ferris, Kammel, and Noronha (2012) find that the difference and changes across 23 European countries are explained by both the strength of the legal protection and the type of issuer. Coherently, Zattoni and Cuomo (2010) find that the definition of independent directors differs across 44 international countries and that the origin of the legal system in the various countries only partially explains these differences.

Finally, regarding the methods, it is interesting to note that less than one quarter (i.e., 4 out of 15) of the empirical studies on this topic use quantitative or mixed methods (Cicon et al., 2012; Hermes et al., 2007; Zattoni & Cuomo, 2008, 2010) and only one (Cicon et al., 2012) is based on a longitudinal sample.

Studies on the Internationalization and the Convergence-Divergence of Corporate Governance Codes

Another set of articles in this line of research focused on the reflections on the internationalization and the convergence-

© 2015 John Wiley & Sons Ltd

divergence of corporate governance principles. The first studies on the internationalization of codes have been published only recently, that is, after 2004. Despite the strong pressure for convergence toward the Anglo-American corporate governance model, these studies show that divergence prevails around the world and that the content of codes is not converging either in European or in emerging countries (e.g., Collier & Zaman, 2005; Hermes et al., 2006; Roberts, 2004; Zattoni & Cuomo, 2008). Several recent studies focused on this topic confirm that divergence prevails around the world (e.g., Böhm, Bollen, & Hassink, 2013; Cicon et al., 2012; Davies & Hopt, 2013; Johanson & Østergren, 2010; Zattoni & Cuomo, 2010). Overall, these results support the limited convergence of the different corporate governance systems toward the Anglo-American governance model (for a recent review, see Aguilera & Jackson, 2010).

Studies on the Consequences of Codes Issued by Transnational Institutions

Finally, there are studies focused on the consequences of codes issued by transnational institutions. Governance scholars argue that transnational codes have undoubtedly had a key influence on the development of national corporate governance codes around the world (Aguilera & Cuervo-Cazurra, 2009; Mallin, 2013; Reid, 2003). The empirical evidence shows, in fact, that the key recommendations advanced by codes issued by transnational organizations have been incorporated in many national codes (e.g., in Greece, China, Czech Republic, Egypt, and Hungary) and that international organizations (like the World Bank, the OECD and the International Monetary Fund) promoted and assessed the implementation of these codes around the world.

Despite the importance of this topic, our data show that academic research is still limited. In particular, only a few empirical articles assess the extent to which the principles and recommendations of these transnational codes have been incorporated in the content of corporate governance codes around the world. Regarding the empirical articles, the EU is the leading geographical setting, as most of the articles review the content of codes issued by a relatively small number of European countries in order to analyze the codes' coverage of EU company law directives (e.g., Böhm et al., 2013; Hermes et al., 2007; Soltani & Maupetit, 2015). Their findings show that European countries deviate substantially from the EU recommendations and that the rate of coverage of each recommendation differs across countries.

THE EVOLUTION OF FIRM-LEVEL STUDIES ON CODES

A second stream of research on corporate governance codes consists of firm-level studies investigating: (i) compliance statements at national level, (ii) compliance statements at international level, (iii) explanations for deviations from a corporate governance code, and (iv) the relationship between code compliance and firm performance.

Studies on Compliance Statements at National Level

A first group of firm-level studies includes surveys of compliance statements at national level, exploring if, and how, national companies tend to comply with codes' recommendations. Our data show that the literature on this topic is very extensive. In particular, comparative analyses of governance practices before and after the introduction of a code show the positive effect of codes on the evolution of corporate governance practices (e.g., Chen & Nowland, 2011; Conyon, 1994; Jones, Li, & Cannella, 2015; Peasnell, Pope, & Young, 2000; Stiles & Taylor, 1993). Companies tend to comply with codes' recommendations for several reasons, mostly for increasing their legitimation among investors and improving the effectiveness of their governance practices (Zattoni & Cuomo, 2008).

In addition, previous studies show that several factors can influence the rate of compliance with codes' recommendations. For example, a number of studies find that firm size is a powerful driver of firm compliance. This relationship has been supported in several countries, such as the UK (Conyon & Mallin, 1997), Germany (Von Werder, Talaulicar, & Kolat, 2005), and the Netherlands (Akkermans et al., 2007). The main explanations behind this evidence are that the costs of compliance grow more than proportionally with firm size, larger companies need more sophisticated governance practices, and the pressure to comply is higher for larger companies as their ownership structure is more dispersed and they are under more scrutiny from the external environment.

Furthermore, previous studies find that the extent of compliance with codes' recommendations and the level of detail of the information disclosed on corporate governance increase over time (Akkermans et al., 2007; MacNeil & Li, 2006; O'Shea, 2005; Price, Román, & Rountree, 2011). So a second factor explaining firm compliance is increasing market pressure over time.

The level of compliance varies across codes' recommendations, as some of the more controversial recommendations are associated with a higher level of non-compliance. For example, studies on the German Corporate Governance Code find a lower level of compliance with some critical recommendations, such as personal liability and compensation of management and/or of supervisory board members (see, e.g., Andres & Theissen, 2008; Chizema, 2008). So a third factor affecting the compliance is the overall institutional environment, including both the legal norms and the cultural values. In addition, the presence of a multiplicity of corporate governance codes and of potential conflicts among their recommendations can allow firms to comply with a limited and strategically selected number of items (see the empirical evidence on Nigerian firms collected by Osemeke & Adegbite, 2014). Finally, further studies show that the level of compliance with codes varies significantly across countries, being higher in developed countries like the UK (Conyon & Mallin, 1997), Italy (Bianchi, Ciavarella, Novembre, & Signoretti, 2011), and Germany (Von Werder et al., 2005), and lower in less developed countries that lack a tradition of sound corporate governance, such as Cyprus (Krambia-Kapardis & Psaros, 2006). So another variable of importance is the development of the national economy.

© 2015 John Wiley & Sons Ltd

Studies on Compliance Statements at International Level

A second set of articles along this line of research includes surveys of compliance statements at international level, investigating if, and how, there are significant differences in the compliance of firms located in different countries.

Among them, Nowland (2008) analyzing data for several East Asian countries (i.e., Hong Kong, Indonesia, Malaysia, Philippines, Singapore, South Korea, Taiwan, and Thailand) finds that the level of compliance of small and family-owned firms is lower than the level of compliance of firms with larger size and more dispersed ownership. Furthermore, in an empirical study aimed at comparing the governance practices of Greek firms with three governance standards characterized by different strictness of their recommendations (i.e., low, the Greek law; medium, the Greek Code; and high, the UK Combined Code), Florou and Galarniotis (2007) show that the average rating of compliance is very low and largely decreases for more stringent standards. More recently, Salterio, Conrad, and Schmidt (2013), in an empirical study on Canadian and Australian listed companies, show that companies in the two countries adhere to the "comply or explain" principle differently. In more detail, compliance in terms of adoption of best practices is more common in Canada, whereas compliance in terms of either adoption or explanation is more common in Australia. In addition, the study shows that the companies in the two countries comply with different sets of recommendations. As Canada and Australia can be considered broadly similar countries, this study encourages governance scholars to analyze firm compliance behavior across countries more extensively.

Studies on Deviations from a Corporate Governance Code

A further set of articles includes searches on the explanations for deviations from codes' recommendations. The limited existing literature on this topic shows that smaller firms tend to have a lower level of compliance with codes' recommendations than larger firms (e.g., Talaulicar & von Werder, 2008 for Germany; Hooghiemstra & van Ees, 2011 for the Netherlands; Arcot, Bruno, & Faure-Grimaud, 2010 for the UK). In addition, they find that family-owned firms are less likely to comply with voluntary recommendations than non-family firms (e.g., Arcot et al., 2010 for the UK; Zeidan, 2014 for Brazil).

More recently, the few studies on this topic have also started to explore the quality and type of explanations for non-compliance and whether the characteristics of some firms contribute to their choice to provide more or less informative explanations. A study by Arcot et al. (2010) finds that both widely held and family-owned non-financial UK companies are more likely to use standard explanations for deviations from compliance. Furthermore, recent studies in the Netherlands find that Dutch firms with concentrated ownership structure, a larger number of analysts following them, and stronger boards are more likely to provide more informative explanations (Hooghiemstra, 2012). Moreover, empirical evidence suggests that firms complying with the same recommendations are more likely to use similar explanations for non-compliance (Hooghiemstra & van Ees, 2011).

Seidl, Sanderrson, and Roberts (2013) analyze the application of the "comply or explain" principle by the 130 largest companies in Germany and the UK and find that non-compliance is not uncommon both in Germany and in the UK. Following institutional theory, they also empirically derive a "taxonomy for explanations" (p. 803). More recently, Shrives and Brennan (2015) expand Seidl et al.'s (2013) study by developing six criteria to analyze the explanations for non-compliance used by UK FTSE companies. Their study underlines that the level of compliance increases over time, but the quality of explanations for non-compliance remains very low and presents only marginal improvements. Furthermore, they show that some differences exist between non-compliance explanations for FTSE100 and FTSE250 companies. Finally, regarding the research setting, our review shows that the majority of articles focus on a single country and refer mostly to a limited number of European economies (i.e., Germany, the Netherlands, and the UK).

Studies on the Relationship Between Code Compliance and Firm Performance

A further set of articles within this line of research consists of studies on the relationship between code compliance and firm performance. Our review shows that several studies have explored this topic over time. Regarding the research setting, our review shows that the majority of articles focus on a single country and that only two cross-country studies have been published until now on this topic (i.e., Nowland, 2008; Renders, Gaeremynck, & Sercu, 2010). In addition, while early studies focus on UK companies, more and more studies are developed with regard to emerging economies.

Despite considerable research effort, the empirical findings from a number of studies on several countries around the world are mixed and inconclusive as to whether a higher level of code compliance enhances firm performance, even though several measures for performance have been used and scholars have significantly improved the methodology over time. In particular, some studies find that higher code compliance enhances firm performance (e.g., Del Brio, Maria-Ramires, & Perote, 2006 and Fernández-Rodríguez, Gómez-Ansón, & Cuervo-García, 2004 for Spain; Luo & Salterio, 2014 for Canada; Machuga & Teitel, 2007 for Mexico; Nowland, 2008 for seven East-Asian countries; and Renders et al., 2010 for 14 European countries) or that stock markets appreciate firm compliance (e.g., Goncharov, Werner, & Zimmermann, 2006 and Chavez & Silva, 2009 for Germany and Brazil, respectively). Contrarily, some studies find no association (e.g., Haniffa & Hudaib, 2006 for Malaysia; Price et al., 2011 for Mexico) or provide mixed results (e.g., McKnight & Weir, 2009 and Weir, Lang, & McKinght, 2002 for the UK) on the relationship between compliance with codes and firm performance.

An extensive debate is continuing on the reasons that might explain the lack of conclusive findings on the relationship between firm compliance with good governance codes and performance. In particular, the mixed results of previous studies seem to be due to both conceptual and methodological issues. Among the conceptual issues, previous studies did not adequately explore the role of the national institutional environment, whilst recent studies find that it can have a

© 2015 John Wiley & Sons Ltd

significant impact on this relationship. For example, Renders et al. (2010) argue that the content of codes (i.e., the definition of independent directors and, in general, the strictness of their recommendations) and national institutional environment (e.g., the level of corruption, the quality of law enforcement, the strength of investor protection, and the cultural and political environments) may significantly affect this relationship.

With regard to the methods employed, scholars have highlighted a number of limitations of previous studies, including: (i) the lack of control for specific firm characteristics (e.g., firm leverage, size, type of owners, presence of institutional investors); (ii) the use of OLS regression and the lack of control for endogeneity and selection bias (see Renders et al., 2010; Weir et al., 2002), (iii) the use of proxies to measure good governance (i.e., governance index), shareholder protection (e.g. the "anti-director rights index" developed by La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1998) and firm performance (e.g., book or market value; see Aguilera & Desender, 2012; Renders et al., 2010). Therefore future studies should also try to address all these deficiencies from a methodological point of view.

DISCUSSION

The recent global financial crisis reinvigorated the debate on good governance practices and consequently stimulated a further wave of new codes or the revision of existing ones. As a consequence, the number of studies on codes published after 2008 is larger than the number of studies published previously. This growing interest in codes shows that the academic debate is still hot and will probably also be lively in the coming years, especially after recent scandals such as Petrobras in Brazil, Deutsche Bank and Volkswagen in Germany, and Toshiba in Japan. The 2015 G20/OECD Principles of Corporate Governance are also likely to give further impetus to the debate on corporate governance practices around the world.

Our results show that recent research on codes is evolving in its sophistication. While agency theory is still the dominant framework, other theoretical perspectives (especially institutional theory) are gaining ground as well as multi-theory studies. In terms of geographical settings, the majority of recent studies explore governance codes in transition and emerging economies, while research on the UK and Continental European countries still persists. Finally, empirical papers explore a wide set of research questions using different research methods including mixed methods and experiments.

Our analysis of publications on good governance codes up to the end of 2014 indicates that some of the gaps highlighted by a previous review on codes (Aguilera & Cuervo-Cazurra, 2009) have been appropriately, or at least partly, addressed. First, recent studies have started both to investigate how codes change over time (Johanson & Østergren, 2010; Nordberg & McNulty, 2013) and to explore the role of institutional actors and the business elite in the code-issuing political process (Haxhi et al., 2013). Second, some recent works have explored the impact of formal and informal institutions (including cultural variables) on the issuance of codes and on the types of issuer in different countries (Haxhi & van Ees, 2010). Third, some studies have contributed to enrich the comparative analysis of the content of codes (Cicon et al., 2012), and have devoted attention to analyze the differences in the definition of director independence across national codes (Zattoni & Cuomo, 2010). Fourth, recent studies have started to investigate the consequences of codes issued by transnational institutions in the EU (Böhm et al., 2013; Cicon et al., 2012). Finally, some papers have investigated how firm compliance/noncompliance evolves over time (Arcot et al., 2010; Chen & Nowland, 2011) and have provided richer empirical evidence on the explanations for deviations from a corporate governance code (Hooghiemstra, 2012; Shrives & Brennan, 2015).

Despite recent studies having significantly contributed to advance our knowledge on good governance codes, research on this topic is still full of interesting opportunities for further exploration. Based on our extensive review of previous studies, in the next subsections we provide a roadmap for future research on codes at country level and firm level, respectively.

Country-Level Studies on Codes

An interesting way to extend previous country-level studies is to further analyze how codes diffuse, evolve, and adapt over time. Institutional theory seems to be a promising theoretical lens to address this objective (e.g., DiMaggio & Powell, 1983). Based on this theory, few practices, if any, come out of the diffusion process unchanged as an adopter strives to create a better fit between an external practice and the need to increase its "zone of acceptance" during implementation (Lewis & Seibold, 1993). Consistent with this view, some studies suggest that the diffusion of a practice is a dynamic process, and that diffusing practices may be modified or "adapted" by adopters (Ansari, Fiss, & Zajac, 2010; Fiss, Kennedy, & Davis, 2012). So, following institutional theory, governance scholars could explore patterns of practice variation in the diffusion of governance codes across time and countries, for example to understand if early and late adopters follow different rationales as in the diffusion of other contested practices (Fiss & Zajac, 2004).

A second topic that may deserve further attention by governance scholars is the consequence of codes issued by transnational organizations. Despite the fact that these codes could have significantly influenced the diffusion and content of national codes, a limited number of studies explore this issue and mostly with regard to the EU experience (Böhm et al., 2013; Soltani & Maupetit, 2015). So future studies could, for example, explore to what extent the codes issued by influential transnational organizations have affected the issue, revision, and content of national codes. This research would facilitate the development of a better understanding of the links between the governance debate at the international and at the national level.

Moreover, further studies could focus on the process of the development of codes. On this issue it would be important to get a better understanding of which subjects play an influential role in code development, which interests shape their content, and which parties are interested or not in their proper implementation (e.g., Haxhi et al., 2013; Nordberg & McNulty, 2013). Future studies could, for example, analyze the political process leading to the development of codes and shaping their content, in order to better understand the role of institutional investors, directors' associations, large shareholders, government authorities, and other parties. Finally, the extension of

© 2015 John Wiley & Sons Ltd

studies beyond the UK can help scholars develop a more contextualized view of the political process leading to the development of codes and to their implementation. The issuance of the revised OECD Code in 2015, and the various comments received on the preliminary draft, could also be an area worth exploring.

Furthermore, our results show a growing diffusion of codes targeted at specific types of companies, such as family- or state-owned companies. So an additional topic that can be further investigated is the development of codes relevant to firms with specific characteristics (i.e., ownership structure, size, or industry). This recent phenomenon is based on the idea that these types of companies have a significant impact on national economies (think, e.g., of the relevance of state-owned companies in some emerging economies like China, Brazil, and Russia) and that good governance practices can increase their accountability and performance. As such, future studies should explore both the soundness of the conceptual reasons behind the issue of these specific codes (e.g., do we need further codes if good governance codes are flexible in their nature?), and their effectiveness in improving the governance practices of targeted companies (e.g., their impact on firm adoption and performance).

Finally, we believe that the extension of studies on the coexistence of hard and soft law is crucial to the better understanding of this topic. The debate about the efficacy of both hard and soft law mechanisms in solving agency problems is still open. Recent studies show that soft law does not solve governance issues in poor institutional environments (Wanyama et al., 2009), and advance the idea that more regulation (e.g., better rules or the introduction of regulatory bodies) are necessary to improve governance practices (Chiu, 2012; Keay, 2014). Based on these findings, future studies should try to better explore the effects of the interaction between codes' recommendations and the quality of the institutional environment on governance practices and effectiveness. The careful consideration of the national (formal and informal) institutional context can be crucial for the development of a better understanding of these issues (Aguilera & Cuervo-Cazurra, 2004; Haxhi & van Ees, 2010; Zattoni & Cuomo, 2008).

Firm-Level Studies on Codes

A first topic that seems to be worthy of further exploration is the understanding of the reasons behind compliance and deviations from good governance codes' recommendations. Governance codes have been conceived as flexible tools to promote the diffusion of best practices, as they leave companies the possibility to deviate from their recommendations if this allows them to design the most appropriate corporate governance in light of their specific characteristics. Future studies are invited to collect more empirical evidence on the reasons (e.g., spillover or contagion effect) behind compliance and non-compliance (e.g., Salterio et al., 2013), and on the type and quality of explanations provided to justify deviations from codes' recommendations (Seidl et al., 2013; Shrives & Brennan, 2015).

A second topic that may be usefully investigated by governance scholars is the interaction between board best practices – as proposed by national codes – and the configuration of other governance mechanisms. A relatively unexplored perspective in corporate governance suggests that governance mechanisms interact amongst themselves, creating substitution and complementarity effects (e.g. Rediker & Seth, 1995; Ward, Brown, & Rodriguez, 2009). Following this view, the understanding of the effectiveness of governance best practices requires that scholars go beyond the analysis of a single mechanism and consider all mechanisms at the same time. While this approach can enrich the understanding of the reasons behind deviations and explanations of non-compliance, it may also provide avenues of research in other directions. This view questions, for example, the possibility of developing universal governance indexes or best practices, or at least invites scholars and practitioners to think in term of bundles of governance practices (García-Castro, Aguilera, & Ariño, 2013; Schiehll, Ahmadjian, & Filatotchev, 2014). Furthermore, additional studies can analyze the role of some key firm variables (e.g., the identity of the major shareholder or the capital structure of the firm) in affecting the relationship between code compliance and firm performance.

Finally, another line of investigation involves the collection of international samples combining data about national institutional variables and firm governance variables (e.g., Kumar & Zattoni, 2013). This further avenue of research can contribute to addressing the long lasting question of convergence and divergence of governance practices. Recent publications show, in fact, that national economies and governance models continue to differ and that pressure to converge does not automatically produce the diffusion of the Anglo-American practices everywhere (e.g., Zattoni & Cuomo, 2008; Zattoni & Judge, 2012).

Limitations

Our literature review has some limitations. First, following previous review papers in the field of corporate governance (Pugliese et al., 2009; Saggese et al., 2015), we selected and analyzed only peer-reviewed articles in English. As such, other types of publications on this topic have not been included in our review (e.g., academic books such as van den Berghe, 2002 or consultancy reports such as Gregory & Simmelkjaer, 2002). So future studies could also include other types of publications or explore if, and how, they have contributed to the development of our knowledge on governance codes.

Second, we excluded papers focused on the impact of code compliance on the effectiveness and efficiency of firm operation (e.g., internal control) and the quality of information disclosure (e.g., financial accounting information). So future studies could enrich our review by analyzing some related areas of research such as these two.

Third, we assigned previous studies on codes to three research periods based on the year of journal publication of very influential articles. We acknowledge that assigning papers based on the year of publication is a crude proxy as it could take some years before a paper is published and because publication date and sample period are not necessarily linked. At the same time, the year of publication is when the article receives most exposure and influences subsequent work in the area. This criterion allowed us to also classify conceptual papers with no empirical data collection. Therefore, whilst we

© 2015 John Wiley & Sons Ltd

recognize the crude nature of the proxy, we believe that the year of publication is the most appropriate criterion for this study.

CONCLUSION

Our review contributes to corporate governance research by both analyzing the diffusion of governance codes and reviewing all previous studies on codes. Our study underlines the increasing importance of governance codes and the key role of supranational institutions and corporate frauds in stimulating their worldwide diffusion and revision. In addition, it describes key theoretical and methodological trends in recent research on codes. Our findings provide a roadmap for future research on codes both at country and firm level.

ACKNOWLEDGEMENTS

The authors would like to thank the Associate Editor Ruth Aguilera and the four anonymous reviewers for their helpful and insightful comments and suggestions on earlier versions of the manuscript.

NOTES

1. From 2006 EU Directives state that companies listed on an EU listed market must publish a separate corporate governance statement in the annual report in order to mandatorily disclose their level of voluntary adoption of a legally non-binding code or to explain the reasons for non-compliance with it.
2. For a review of history on codes, see Aguilera and Cuervo-Cazurra (2009) and Haxhi and Aguilera (2012).
3. Articles on different topics may be focused, for example, on the adoption of ethics codes, the role of institutional investors, banks and financial market law, and the compensation of executive and non-executive directors, while articles on related topics not relevant to our study focus on, for example, the relationship between code compliance and the effectiveness and efficiency of the operation (e.g., internal control), the quality of information disclosure (e.g., financial accounting information), and the adoption of IFRS.
4. As some articles analyze more than one research topic within the same study, multiple coding is possible and so the total related to this item can exceed the number of papers considered.

REFERENCES

Aguilera, R. V. & Cuervo-Cazurra, A. 2004. Codes of good governance worldwide: What is the trigger?, ***Organization Studies***, 25: 415–443.

Aguilera, R. V. & Cuervo-Cazurra, A. 2009. Codes of good governance, ***Corporate Governance: An International Review***, 17: 376–387.

Aguilera, R. V. & Desender, K. 2012. Methodological challenges in comparative corporate governance and strategic issues. In C. L. Wang, D. Ketchen, & D. Bergh (Eds.), ***Research methodology in strategy and management***: 289–321. Bingley: Emerald Group Publishing Limited.

Aguilera, R. V., Filatotchev, I., Gospel, H., & Jackson, G. 2008. An organizational approach to comparative corporate governance: Costs, contingencies and complementarities, ***Organization Science***, 19: 475–492.

Aguilera, R. V., Goyer, M., & Kabbach-Castro, L. R. 2013. Regulation and comparative corporate governance. In M. Wright, D. S. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***The Oxford handbook of corporate governance***. Oxford: Oxford University Press.

Aguilera, R. V. & Jackson, G. 2003. The cross-national diversity of corporate governance: Dimensions and determinants, ***Academy of Management Review***, 28: 447–465.

Aguilera, R. V. & Jackson, G. 2010. Comparative and international corporate governance, ***Annals of the Academy of Management***, 4: 485–556.

Akkermans, D., van Ees, H., Hermes, N., Hooghiemstra, R., Van der Laan, G., Postma, T., & van Witteloostuijn, A. 2007. Corporate governance in the Netherlands: An overview of the application of the Tabaksblat code in 2004, ***Corporate Governance: An International Review***, 15: 1106–1118.

Andres, C. & Theissen, E. 2008. Setting a fox to keep the geese: Does the comply or explain principle work?, ***Journal of Corporate Finance***, 14: 289–301.

Ansari, S., Fiss, P. C., & Zajac, E. J. 2010. Made to fit: How practices vary as they diffuse, ***Academy of Management Review***, 35: 67–92.

Arcot, S., Bruno, V., & Faure-Grimaud, A. 2010. Corporate governance in the UK: Is the comply or explain approach working?, ***International Review of Law and Economics***, 30: 193–201.

Bartlet, R. 2009. Going private but staying public: Re-examining the effect of Sarbanes-Oxley on firms' going-private decisions, ***University of Chicago Law Review***, 76: 7–44.

Bergh, D. D., Perry, J., & Hanke, R. 2006. Some predictors of SMJ article impact, ***Strategic Management Journal***, 27: 81–100.

Bianchi, M., Ciavarella, A., Novembre, V., & Signoretti, R. 2011. Comply or explain: Investor protection through the Italian corporate governance code, ***Journal of Applied Corporate Finance***, 23: 107–121.

Block, S. B. 2004. The latest movement to going private: An empirical study, ***Journal of Applied Finance***, 14: 36–44.

Böhm, F., Bollen, L. H., & Hassink, H. F. 2013. Spotlight on the design of European audit committees: A comparative descriptive study, ***International Journal of Auditing***, 17: 138–161.

Carvalho, A. G. & Pennacchi, G. G. 2012. Can a stock exchange improve corporate behavior? Evidence from firms' migration to premium listings in Brazil, ***Journal of Corporate Finance***, 18: 883–903.

Chavez, G. A. & Silva, A. C. 2009. Brazil's experiment with corporate governance, ***Journal of Applied Corporate Finance***, 21: 34–44.

Chen, E. & Nowland, J. 2011. The effectiveness of corporate governance codes: Long-term analysis from East Asia, ***Journal of International Commerce, Economics and Policy***, 2: 229–250.

Chiu, I. H. Y. 2012. Institutional shareholders as stewards: Toward a new conception of corporate governance, ***Brooklyn Journal of Corporate Financial and Commercial Law***, 6: 387–432.

Chizema, A. 2008. Institutions and voluntary compliance: The disclosure of individual executive pay in Germany, ***Corporate Governance: An International Review***, 16: 359–374.

Cicon, J. E., Ferris, S. P., Kammel, A. J., & Noronha, G. 2012. European corporate governance: A thematic analysis of national codes of governance, ***European Financial Management***, 18: 620–648.

Clarke, T. 2004. ***Theories of corporate governance: The philosophical foundations of corporate governance***. London: Routledge.

Cohen, J. R., Krishnamoorthy, G., & Wright, A. M. 2008. Form versus substance: The implications for auditing practice and research of alternative perspectives on corporate governance, ***Auditing: A Journal of Practice and Theory***, 27: 181–198.

Collier, P. & Zaman, M. 2005. Convergence in European corporate governance: The audit committee concept, ***Corporate Governance: An International Review***, 13: 753–768.

Conyon, M. 1994. Corporate governance changes in UK companies between 1988 and 1993, ***Corporate Governance: An International Review***, 2: 87–100.

© 2015 John Wiley & Sons Ltd

Conyon, M. & Mallin, C. 1997. A review of compliance with Cadbury, ***Journal of General Management***, 22: 24–37.
Cromme, G. 2005. Corporate governance in Germany and the German corporate governance code, ***Corporate Governance: An International Review***, 13: 362–367.
Cuervo, A. 2002. Corporate governance mechanisms: A plea for less code of good governance and more market control, ***Corporate Governance: An International Review***, 10: 84–93.
Davies, P. L. & Hopt, K. J. 2013. Corporate boards in Europe – Accountability and convergence, ***American Journal of Comparative Law***, 61: 301–375.
Del Brio, E. B., Maria-Ramires, E., & Perote, J. 2006. Corporate governance mechanisms and their impact on firm value, ***Corporate Ownership and Control***, 4: 25–36.
Dewey, M. E. 1983. Coefficients of agreement, ***British Journal of Psychiatry***, 143: 487–489.
Dewing, I. P. & Russell, P. O. 2004. Regulation of UK corporate governance: Lessons from accounting, audit and financial services, ***Corporate Governance: An International Review***, 12: 107–115.
DiMaggio, P. & Powell, W. 1983. The iron cage revisited: Institutional isomorphism and collective rationality, ***American Sociological Review***, 48: 147–160.
Drobetz, W., Schillhofer, A., & Zimmermann, H. 2004. Corporate governance and expected stock returns: Evidence from Germany, ***European Financial Management***, 10: 267–93.
Engel, E., Hayes, R. M., & Wang, X. 2007. The Sarbanes-Oxley Act and firms' going-private decisions, ***Journal of Accounting and Economics***, 44: 116–145.
Enrione, A., Mazza, C., & Zerboni, F. 2006. Institutionalizing codes of good governance, ***American Behavioral Scientist***, 49: 961–973.
Fama, E. & Jensen, M. 1983. Separation of ownership and control, ***Journal of Law and Economics***, 26: 301–325.
Fernández-Fernández, J. L. 1999. Ethics and the board of directors in Spain: The Olivencia code of good governance, ***Journal of Business Ethics***, 22: 233–247.
Fernández-Rodríguez, E., Gómez-Ansón, S., & Cuervo-García, A. 2004. The stock market reaction to the introduction of best practices codes by Spanish firms, ***Corporate Governance: An International Review***, 12: 29–46.
Fiss, P. C., Kennedy, M. T., & Davis, G. F. 2012. How golden parachutes unfolded: Diffusion and variation of a controversial practice, ***Organization Science***, 23: 1077–1099.
Fiss, P. C. & Zajac, E. J. 2004. The diffusion of ideas over contested terrain: The (non) adoption of a shareholder value orientation among German firms, ***Administrative Science Quarterly***, 49: 501–534.
Florou, A. & Galarniotis, A. 2007. Benchmarking Greek corporate governance against different standards, ***Corporate Governance: An International Review***, 15: 979–998.
Furrer, O., Thomas, H., & Goussevskaia, A. 2008. The structure and evolution of the strategic management field: A content analysis of 26 years of strategic management research, ***International Journal of Management Reviews***, 10: 1–23.
García-Castro, R., Aguilera, R., & Ariño, M. A. 2013. Bundles of firm corporate governance practices: A fuzzy set analysis, ***Corporate Governance: An International Review***, 21: 390–407.
Goncharov, I., Werner, J. R., & Zimmermann, J. 2006. Does compliance with the German corporate governance code have an impact on stock valuation? An empirical analysis, ***Corporate Governance: An International Review***, 14: 432–445.
Gregory, J. H. & Simmelkjaer, T. R. 2002. ***Comparative study of corporate governance codes relevant to the European Union and its member states***. New York: Weil, Gotshal & Manges LLP.
Haniffa, R. & Hudaib, M. 2006. Corporate governance structure and performance of Malaysian listed companies, ***Journal of Business Finance & Accounting***, 33: 1034–1062.
Haxhi, I. & Aguilera, R. V. 2012. Are codes fostering convergence in corporate governance? An institutional perspective. In A. Rasheed & T. Yoshikawa (Eds.), ***Convergence of corporate governance: Promise and prospects***: 234–248. Basingstoke: Palgrave Macmillan.
Haxhi, I. & Aguilera, R. V. 2014. Corporate governance through codes. In C. Cooper (Ed.), ***Wiley encyclopedia of management***, 3rd edn. Oxford: Wiley-Blackwell.
Haxhi, I. & van Ees, H. 2010. Explaining diversity in the worldwide diffusion of codes of good governance, ***Journal of International Business Studies***, 41: 710–726.
Haxhi, I., van Ees, H., & Sorge, A. 2013. A political perspective on business elites and institutional embeddedness in the UK code-issuing process, ***Corporate Governance: An International Review***, 21: 535–546.
Hermes, N., Postma, T. J. B. M., & Zivkov, O. 2006. Corporate governance codes in the European Union: Are they driven by external or domestic forces?, ***International Journal of Managerial Finance***, 2: 280–301.
Hermes, N., Postma, T. J. B. M., & Zivkov, O. 2007. Corporate governance codes and their contents: An analysis of Eastern European codes, ***Journal for East European Management Studies***, 12: 53–74.
Heugens, P. P. M. A. R. & Otten, J. A. 2007. Beyond the dichotomous worlds hypothesis: Towards a plurality of corporate governance logics, ***Corporate Governance: An International Review***, 15: 1288–1300.
Hofstede, G. H. 2001. ***Culture's consequences: Comparing values, behaviors, institutions, and organizations across nations***, 2nd edn. Thousand Oaks, CA: Sage.
Hooghiemstra, R. B. H. 2012. What determines the informativeness of firms' explanations for deviations from the Dutch corporate governance code?, ***Accounting and Business Research***, 42: 1–27.
Hooghiemstra, R. B. H. & van Ees, H. 2011. Uniformity as response to soft law: Evidence from compliance and non-compliance with the Dutch corporate governance code, ***Regulation & Governance***, 5: 480–498.
Hopt, K. J. 2011. Comparative corporate governance: The state of the art and international regulation, ***American Journal of Comparative Law***, 59: 1–73.
Jensen, M. C. & Meckling, W. H. 1976. Theory of the firm: Managerial behavior, agency costs, and capital structure, ***Journal of Financial Economics***, 3: 305–360.
Johanson, D. & Østergren, K. 2010. The movement toward independent directors on boards: A comparative analysis of Sweden and the UK, ***Corporate Governance: An International Review***, 18: 527–539.
Jones, C. D., Li, M., & Cannella, A. A., Jr.. 2015. Responses to a governance mandate: The adoption of governance committees by NYSE firms, ***Journal of Management***, 41: 1873–1897.
Judge, W. Q. 2008. Agency and institutions, ***Corporate Governance: An International Review***, 16: ii–iii.
Judge, W. Q. 2009. Toward a global theory of corporate governance, ***Corporate Governance: An International Review***, 17: iii–iv.
Keay, A. 2014. Comply or explain in corporate governance codes: In need of greater regulatory oversight?, ***Legal Studies***, 34: 279–304.
Krambia-Kapardis, M. & Psaros, J. 2006. The implementation of corporate governance principles in an emerging economy: A critique of the situation in Cyprus, ***Corporate Governance: An International Review***, 14: 126–139.
Krenn, M. 2014. Decoupling as a sustainable firm response to pressures for convergence and divergence in corporate governance: The case of codes of good corporate governance, ***Journal of Management Policy and Practice***, 15: 103–117.
Kuhn, T. S. 2012. ***The structure of scientific revolutions***, 4th edn. Chicago, IL: University of Chicago Press.
Kumar, P. & Zattoni, A. 2013. How much do country-level or firm-level variables matter in corporate governance studies?, ***Corporate Governance: An International Review***, 21: 199–200.

© 2015 John Wiley & Sons Ltd

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. 1998. Law and finance, ***Journal of Political Economy***, 106: 1113–1155.

Leuz, C., Triantis, A., & Wang, Y. 2008. Why do firms go dark? Causes and economic consequences of voluntary SEC deregistrations, ***Journal of Accounting and Economics***, 45: 181–208.

Lewis, L. K. & Seibold, D. R. 1993. Innovation modification during intraorganizational adoption, ***Academy of Management Review***, 18: 322–354.

Luo, Y. & Salterio, S. E. 2014. Governance quality in a "comply or explain" governance disclosure regime, ***Corporate Governance: An International Review***, 22: 460–481.

Machuga, S. & Teitel, K. 2007. The effects of the Mexican corporate governance code on quality of earnings and its components, ***Journal of International Accounting Research***, 6: 37–55.

MacNeil, I. & Li, X. 2006. "Comply or explain": Market discipline and non-compliance with the Combined Code, ***Corporate Governance: An International Review***, 14: 486–496.

Mallin, C. A. 2013. ***Corporate governance***, 4th edn. Oxford: Oxford University Press.

Martin, R. 2010. Transferring corporate governance codes: Form or substance? Corporate governance in Hungary, ***Europe-Asia Studies***, 62: 145–171.

McKnight, P. & Weir, C. 2009. Agency costs, corporate governance mechanisms and ownership structure in large UK publicly quoted companies: A panel data analysis, ***Quarterly Review of Economics and Finance***, 49: 135–158.

McNulty, T., Zattoni, A., & Douglas, T. 2013. Developing corporate governance research through qualitative methods: A review of previous studies, ***Corporate Governance: An International Review***, 21: 183–198.

Mosley, L. 2010. Regulating globally, implementing locally: The financial codes and standards effort, ***Review of International Political Economy***, 17: 724–761.

Nordberg, D. & McNulty, T. 2013. Creating better boards through codification: Possibilities and limitations in UK corporate governance, 1992–2010, ***Business History***, 55: 348–374.

Nowland, J. 2008. Are East Asian companies benefiting from Western board practices?, ***Journal of Business Ethics***, 79: 133–150.

O'Shea, N. 2005. Corporate governance. How we've got where we are and what's next, ***Accountancy Ireland***, 37: 33–37.

Osemeke, L. & Adegbite, E. 2014. Regulatory multiplicity and conflict: Towards a combined code on corporate governance in Nigeria, ***Journal of Business Ethics***. DOI:10.1007/s10551-014-2405-3.

Peasnell, K. V., Pope, P. F., & Young, S. 2000. Accrual management to meet earnings targets: UK evidence pre- and post-Cadbury, ***British Accounting Review***, 32: 415–445.

Pietrancosta, A. 2011. Enforcement of corporate governance codes, ***Revue Trimestrielle de Droit Financier***, 1: 27–39.

Price, R., Román, F. J., & Rountree, B. 2011. The impact of governance reform on performance and transparency, ***Journal of Financial Economics***, 99: 76–96.

Pugliese, A., Bezemer, P., Zattoni, A., Huse, M., Van der Bosch, F., & Volberda, H. 2009. Boards of directors' contribution to corporate strategy: A literature review and research agenda, ***Corporate Governance: An International Review***, 17: 292–306.

Rediker, K. & Seth, A. 1995. Boards of directors and substitution effects of alternative governance mechanisms, ***Strategic Management Journal***, 16: 85–99.

Reid, A. S. 2003. The internationalisation of corporate governance codes of conduct, ***Business Law Review***, 24: 233–238.

Reisberg, A. 2011. The notion of stewardship from a company law perspective: Re-defined and re-assessed in light of the recent financial crisis?, ***Journal of Financial Crime***, 18: 126–147.

Renders, A., Gaeremynck, A., & Sercu, P. 2010. Corporate-governance ratings and company performance: A cross-European study, ***Corporate Governance: An International Review***, 18: 87–106.

Roberts, G. H. 2004. Convergent capitalisms? The internationalisation of financial markets and the 2002 Russian Corporate Governance Code, ***Europe-Asia Studies***, 56: 1235–1248.

Saggese, S., Sarto, F., & Cuccurullo, C. 2015. Evolution of the debate on control enhancing mechanisms: A systematic review and bibliometric analysis, ***International Journal of Management Reviews***. DOI:10.1111/ijmr.12072.

Salterio, S., Conrad, J., & Schmidt, R. 2013. Canadian evidence of adherence to "comply or explain" corporate governance codes: An international comparison, ***Accounting Perspectives***, 12: 23–51.

Sasseen, J. & Weber, J. 2006. Taking their business elsewhere, ***Businessweek***, 22: 33–34.

Schiehll, E., Ahmadjian, C., & Filatotchev, I. 2014. National governance bundles perspective: Understanding the diversity of corporate governance practices at the firm and country levels, ***Corporate Governance: An International Review***, 22: 179–184.

Seidl, D., Sanderson, P., & Roberts, J. 2013. Applying the "comply or explain" principle: Discursive legitimacy tactics with regard to codes of corporate governance, ***Journal of Management and Governance***, 17: 791–826.

Shrives, P. J. & Brennan, N. M. 2015. A typology for exploring the quality of explanations for non-compliance with UK corporate governance regulations, ***The British Accounting Review***, 47: 85–99.

Soltani, B. & Maupetit, C. 2015. Importance of core values of ethics, integrity and accountability in the European corporate governance codes, ***Journal of Management and Governance***, 19: 259–284.

Stiles, P. & Taylor, B. 1993. Benchmarking corporate governance: The impact of the Cadbury Code, ***Long Range Planning***, 26: 61–71.

Talaulicar, T. & von Werder, A. 2008. Patterns of compliance with the German Corporate Governance Code, ***Corporate Governance: An International Review***, 16: 255–273.

van den Berghe, L. 2002. ***Corporate governance in a globalising world: Convergence or divergence? A European perspective***. New York: Kluwer Academic Publishers.

Von Werder, A., Talaulicar, T., & Kolat, G. 2005. Compliance with the German Corporate Governance Code: An empirical analysis of the compliance statements by German listed companies, ***Corporate Governance: An International Review***, 13: 178–187.

Wanyama, S., Burton, B., & Helliar, C. 2009. Frameworks underpinning corporate governance: Evidence on Ugandan perceptions, ***Corporate Governance: An International Review***, 17: 159–175.

Ward, A., Brown, J., & Rodriguez, D. 2009. Governance bundles, firm performance, and the substitutability and complementarity of governance mechanisms, ***Corporate Governance: An International Review***, 17: 646–660.

Webb, R., Beck, M., & McKinnon, R. 2003. Problems and limitations of institutional investor participation in corporate governance, ***Corporate Governance: An International Review***, 11: 65–73.

Weir, C. M., Laing, D., & McKnight, P. J. 2002. Internal and external governance mechanisms: Their impact on the performance of large UK public companies, ***Journal of Business Finance & Accounting***, 29: 579–611.

Zattoni, A. & Cuomo, F. 2008. Why adopt codes of good governance? A comparison of institutional and efficiency perspectives, ***Corporate Governance: An International Review***, 16: 1–16.

Zattoni, A. & Cuomo, F. 2010. How independent, competent and incentivized should non-executive directors be? An empirical investigation of good governance codes, ***British Journal of Management***, 21: 63–79.

Zattoni, A. & Judge, W. 2012. ***Corporate governance and initial public offerings: An international perspective***. Cambridge: Cambridge University Press.

Zattoni, A. & van Ees, H. 2012. How to contribute to the development of a global theory of corporate governance? Reflections from submitted and published articles in CGIR, ***Corporate Governance: An International Review***, 20: 106–118.

© 2015 John Wiley & Sons Ltd

Zeidan, R. 2014. Voluntary corporate governance with an empirical application, ***Applied Financial Economics***, 24: 837–851.
Zingales, L. 2007. Is the US capital market losing its competitive edge? ECGI Finance Working Paper No. 192/2007. Available at SSRN: http://ssrn.com/abstract=1028701.

Francesca Cuomo is Lecturer in Corporate Governance at Norwich Business School, University of East Anglia, UK. Her primary research interest is corporate governance, with a focus on corporate governance codes, board of directors, board independence, ownership structure and separation between ownership and control. Her publications include articles in international journals such as British Journal of Management, Corporate Governance: An International Review and Industrial and Corporate Change. In 2008 she received the best paper award from Corporate Governance: An International Review.

Christine Mallin is Professorial Fellow, Norwich Business School, University of East Anglia, and Honorary Professor, Lee Shau Kee School of Business and Administration, The Open University of Hong Kong. She has published widely on corporate governance issues in academic journals including Corporate Governance: An International Review, European Journal of Finance, International Business Review, and the Journal of Business Ethics. The fifth edition of her book Corporate Governance will be published in 2015 by Oxford University Press.

Alessandro Zattoni is Professor of Strategy at Luiss University. He is also Professor of Corporate Governance and Strategy and Associate Dean for the Executive education and lifelong learning at LUISS Business School. He is Editor-in-Chief with Praveen Kumar of Corporate Governance: An International Review and an editorial board member of Journal of Management Studies and Journal of Management & Governance. His primary research interest is corporate governance, with a focus on board of directors, codes of good governance, business groups, and executive compensation. He published several books, book chapters, teaching cases and articles in Italian and international journals.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 242–252

Corporate Governance and Takeover Outcomes

Nihat Aktas, Ettore Croci* and Serif Aziz Simsir

ABSTRACT

Manuscript type: Review
Research Question/Issue: This article reviews how and through which channels corporate governance shapes takeover outcomes.
Research Findings: We summarize the main findings of the empirical literature that investigates the effect of corporate governance mechanisms on takeover outcomes. The internal and external governance mechanisms that we consider are: the board of directors, the takeover market, blockholders, financial markets in general, product market competition, and the labor market.
Theoretical/Academic Implications: This article adopts an agency perspective of the firm and reviews the mergers and acquisitions (M&A) literature through the lens of corporate governance. We highlight how the different corporate governance mechanisms affect the takeover process and outcomes.
Practitioner/Policy Implications: The article systematizes the current state of the research linking corporate governance and takeovers. In doing so, we emphasize which mechanisms policymakers can use to improve the efficiency of the takeover market. Alternatively, the review also offers indications concerning mechanisms that could be used to mitigate agency conflicts and, as such, increase firm value.

Keywords: Corporate Governance, Takeover, Board of Directors, Blockholder, Product Market Competition

INTRODUCTION

Corporate takeovers are one of the most important corporate events with tremendous implications for the reallocation of resources among firms (Harford & Li, 2007). Netter, Stegemoller, and Wintoki (2011) report that the average annual aggregate deal values of US acquirers from 1992 to 2009 was $928 billion, with a peak value of $1,806 billion in 1998. After a substantial drop in takeover activity during the financial crisis, the US mergers and acquisitions market reached new heights in 2014 with a total of $2,034 billion announced deal values [source: Thomson-Reuters]. An important aspect of mergers and acquisitions (M&A) is that they tend to intensify the potential conflict of interest between managers and shareholders in large listed companies (Jensen & Meckling, 1976).

Early studies focusing on deals consummated between public firms note that, on average, gains to acquirer firm shareholders around the deal announcement dates tend to be negative or, at best, zero (Jensen & Ruback, 1983). Apart from several recent studies identifying value increasing deals in specific subsamples (such as acquisitions by small bidders, acquisitions of private targets, and deals financed with cash), in almost half of the deals, acquirers earn negative abnormal returns (for a review of these studies, see Betton, Eckbo, & Thorburn, 2008).[1] For instance, Moeller, Schlingemann, and Stulz (2004) report an average acquirer announcement return of +1.1 percent for a large sample of US deals announced from 1980 to 2001. However, in monetary value, this average gain translates into an average loss of $25.2 million upon announcement, suggesting the existence of a strong size effect (i.e., with large acquirers completing, on average, worse deals than smaller ones). The evidence in Moeller, Schlingemann, and Stulz (2005) is even more striking. They find an aggregate loss for acquiring firms' shareholders of $216 billion from 1991 to 2001.

The literature has proposed several explanations as to why acquirers tend to break even and why a substantial proportion of deals lead to negative returns for acquirer shareholders at the merger announcement dates. Some of the proposed explanations include competition in the M&A market (Bradley, Desai, & Kim, 1988), the free rider problem (Grossman & Hart, 1980), CEO hubris (Roll, 1986), price pressure from hedge funds (Mitchell, Pulvino, & Stafford, 2004), and rational overbidding (Akdogu, 2011). According to Jensen (1986), firms with greater free cash flow, but no significant investment opportunities are more likely to undertake value-destroying acquisitions rather than returning cash to the shareholders (i.e., the free cash flow hypothesis). In support of the free cash flow hypothesis, Lang, Stulz, and Walkling (1991) provide evidence that the acquiring firm's operating cash flow is negatively associated with announcement abnormal returns. Harford (1999), focusing on cash holdings, indicates that cash-rich firms undertake poorer deals than their cash-poor counterparts. Therefore, given that the potential for value destruction is high, M&A transactions require strict monitoring,

*Address for correspondence: Ettore Croci, Università Cattolica del Sacro Cuore. Largo Gemelli 1, 20123 Milan, Italy. Tel.: +39-02 7234 3012; Fax: +39-02 7234 2670; E-mail: ettore.croci@unicatt.it

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12116

especially if CEOs are richly rewarded for growth through acquisitions and their remuneration entails bonuses for completing M&As (Grinstein & Hribar, 2004; Harford & Li, 2007).

Conflicts of interest between managers and shareholders during M&As are restricted not only to acquirers. Takeovers are likely to exacerbate agency issues at the target firms as well. Target CEOs have a significant chance of dismissal by the acquirers after mergers (Hartzell, Ofek, & Yermack, 2004). Upon departure from their firms, the employment opportunities for target CEOs for similar positions remain quite limited (Agrawal & Walkling, 1994). Even if target CEOs are retained by the acquirers, their turnover rates are higher in the post-takeover period than in other periods (Hadlock, Houston & Ryngaert, 1999). Given that a takeover may put the careers of the target CEOs at risk, their incentive during this process may deviate significantly from that of their shareholders. Consistent with this conjecture, several studies have found that target shareholder gains in acquisitions are lower when target CEOs are retained by the acquirers (Brewer, Jackson, & Wall, 2006; Qiu, Trapkov, & Yakoub, 2014; Wulf, 2004) and when target CEOs receive extraordinary personal compensation from the acquirers (Fich, Cai, & Tran, 2011; Hartzell et al., 2004).

According to Shleifer and Vishny (1997), corporate governance "deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment." Indeed, in large companies, which are characterized by the separation of ownership and control, managers, without proper incentives and monitoring mechanisms, may be tempted to divert corporate resources from shareholders to pursue their own goals (Shleifer & Vishny, 1997) or to simply enjoy the quiet life (Bertrand & Mullainathan, 2003; Hicks, 1935). To control and incentivize managers, firms may implement internal governance procedures, such as supervision by the board of directors, monitoring by large shareholders, and the use of performance-based compensation packages. In addition to these internal mechanisms, the external environment in which the firm operates exerts control over managers and affects firm-level outcomes, particularly when internal mechanisms are deficient.

This article adopts an agency perspective of the firm and reviews the M&A literature from the lens of corporate governance. Our goal is to summarize the main findings of the empirical literature that investigates the effect of corporate governance mechanisms on the takeover process and outcomes. The internal and external governance mechanisms that we consider include the board of directors and executive compensation (discussed in the next section), the takeover market and pressure from financial market participants (discussed in the third section), product market competition (discussed in the fourth section), and the labor market (discussed in the fifth section). The final section presents our conclusions and discusses avenues for future research.

THE BOARD OF DIRECTORS AND EXECUTIVE COMPENSATION

The board of directors has two broad functions within a firm: monitoring and advisory (Jensen, 1993).[2] The monitoring role refers to the board's responsibility to incentivize managers to act in the best interests of their shareholders, to oversee management's execution of previously planned strategies, and to track the overall performance of the firm. The advisory role refers to the directors' involvement in assisting management in creating and implementing business strategies to maximize shareholder value. While boards are responsible for monitoring and advising management under normal business conditions, their roles become even more critical during large corporate events, such as takeovers. For instance, when a corporate sale is under consideration by a firm, its board may have to manage a more serious conflict of interest between the firm's executives and shareholders. Moreover, target board members themselves may have conflicts of interests with their shareholders during a corporate sale, especially when the board members have post-takeover employment concerns (Harford, 2003; Harford & Schonlau, 2013). In short, boards play a crucial role in establishing the necessary governance mechanisms within their organizations to minimize the adverse effects of the double-barreled conflict of interest inherent in takeover negotiations.

One of the monitoring duties of the board of directors is to design top executives' compensation contracts. A long tradition in finance recognizes managerial compensation as an important internal governance device to alleviate agency costs (Jensen & Meckling, 1976). It is widely accepted that equity-based compensation (EBC) helps to align managerial interests with those of shareholders. In the M&A setting, Datta, Iskandar-Datta, and Raman (2001) find that acquiring managers' EBC is positively related with the firm's announcement return and long-run stock performance, and negatively related to the bid premium. In addition, acquirers with high EBC tend to buy riskier targets and targets with high growth opportunities.[3] Boulton, Braga-Alves, and Schlingemann (2014) examine the relation between CEO's EBC and firm acquisitiveness. Consistent with the notion that EBC encourages managerial risk taking, the authors note a positive effect of CEO's EBC on both acquisition likelihood and intensity. Croci and Petmezas (2015) also study the effect of risk-taking incentives, captured by the sensitivity of CEO wealth to firm stock return volatility (i.e., vega) on acquisition investments. They find that CEOs with risk-taking incentives are more likely to invest in risky acquisitions and that the quality of acquisitions improves with vega. Alternatively, Gormley, Matsa, and Milbourn (2013) demonstrate that convexity from options-based pay reduces the incentive of managers to engage in diversifying acquisitions, a risk-reducing activity, after an exogenous change in a firm's business environment that increases left-tail risk.[4]

Weak board monitoring might lead CEOs to extract compensation at the expense of shareholder wealth. Grinstein and Hribar (2004) find a positive correlation between a CEO's cash bonus and the completion of an M&A transaction, and that this result is noticeably stronger for those firms with powerful CEOs. Harford and Li (2007) conclude that the compensation policies of acquiring firms change following M&As. More precisely, acquiring firm CEOs' total compensation becomes insensitive to negative stock performance and it increases with positive stock performance. However, the insensitivity of CEO compensation to negative stock performance is confined to the subsample of firms with weak board monitoring. The results in Grinstein and Hribar (2004) and Harford

© 2015 John Wiley & Sons Ltd

and Li (2007) suggest that the board of directors play an important role in alleviating the risk of shareholder expropriation by CEOs.

The effectiveness of the board in monitoring executives is considered to be a function of its independence. In contrast with affiliated board members, independent board members have minimal economic ties with their firms. As such, they are viewed as more objective and effective monitors. Cotter, Shivdasani, and Zenner (1997) investigate the association between target board independence and the wealth effects of tender offers for target shareholders. The authors find that target firm shareholders receive significantly higher bid premiums when the majority of the board of directors is independent. Using a sample of mergers from the 1990s, Moeller (2005) indicates that the existence of staggered boards in target firms is detrimental to bid premiums when the majority of the directors are insiders. Contrary to these findings, Bange and Mazzeo (2004) find that target board independence had no effect on bid premiums for mergers that occurred during the 1980s. Furthermore, the authors conclude that target shareholder gains are higher when the target CEO is also the chairman of the board, which is inconsistent with the conjecture that board monitoring is less effective for powerful CEOs.

Several studies have also examined the effect of board characteristics on the performance of acquiring firms. Byrd and Hickman (1992) find that acquirer board independence is positively associated with acquirer announcement returns in tender offers in the 1980s, while Masulis, Wang, and Xie (2007) fail to find a similar effect in their sample of merger announcements from the 1990s. More recently, Fracassi and Tate (2012) determine that powerful CEOs are more likely to appoint directors that have social ties to them. The authors also indicate that in the absence of other governance mechanisms that substitute for board monitoring, firms with greater CEO–director ties are associated with lower market valuation and are more likely to engage in more value-destroying acquisitions. El-Khatib, Fogel, and Jandik (2015) map the entire social network between CEOs and directors and find that board monitoring intensity prevents, to some extent, connected CEOs from making value-destroying acquisitions.

The advisory role of the boards has drawn significant interest from academics over the past few years, partially owing to the recent interest in social network research. Stuart and Yim (2010) find that firms are more likely to be targeted by private equity firms when their directors have previously experienced a similar takeover event during their directorship at other firms. The authors argue that target directors with prior deal experience could play a crucial advisory role when their firms evaluate strategic alternatives to staying as a stand-alone independent company. Schmidt (2015) indicates that tighter social ties between the acquirer CEO and the acquirer board members (i.e., friendly boards), which should enable a more efficient information flow between the parties and a better quality of board advice, lead to higher acquirer abnormal returns. Cai and Sevilir (2012) find that acquirer announcement period abnormal returns are higher and the takeover premiums are lower when the acquirer and the target boards are connected (e.g., share common directors on their boards). In addition, the authors indicate that connected boards pay fewer fees to their advisors, which is consistent with the conjecture that connected boards substitute for the advisory role of financial advisors. Using a sample of mergers from the UK, Renneboog and Zhao (2014) determine that the duration of takeover negotiations is shorter and the likelihood of director retention and merger completion is higher when the merging firms share common directors on their boards. Ishii and Xuan (2014) note that the existence of social ties between the acquirer and the target director and senior executives has a significant negative effect on acquirer CARs, a positive effect on the probability that the target CEO and directors are retained by the acquirer after the takeover, and a positive effect on the likelihood that targets are subsequently divested for performance-related reasons. The authors argue that social ties between the merging firm directors lead to familiarity bias in decision making, which outweighs the positive effect of improved information sharing. Finally, social ties may take the form of connections with bankers, whose financial expertise may affect the acquisition policy of the firm. Güner, Malmendier, and Tate (2008) demonstrate that firms with investment bankers on their boards enter into poorer acquisitions. The authors attribute this negative relation to the conflict of interest arising from directors' concurrent affiliation with the investment bank involved in the takeover process. A more positive view of financial expertise comes from Huang, Jiang, Lie, and Yang (2014) who examine how directors with investment banking experience affect firms' acquisition behavior. Focusing on a sample of firms with directors that are not exposed to conflicting interests, they find that firms with directors with investment banking experience are more likely to make acquisitions. They also determine that these acquisitions are of better quality than those executed by firms without directors with financial expertise.

The board of directors only has a limited amount of time and resources to perform its monitoring and advisory roles. Thus, there may be situations where the board must choose between monitoring and advising management. Assuming that the board's primary role in acquisitions is advisory, Faleye, Hoitash, and Hoitash (2011) examine how the allocation of resources between the two substitute roles affects a firm's acquisition performance. The authors find that acquirer abnormal returns around merger announcement dates are lower when the acquirer board spends more of its time monitoring rather than advising. Special committees offer a partial solution to this resource constraint, especially prior to the start of merger negotiations. These special committees act as substitutes for the boards, and they assume the board's monitoring and advisory roles during the negotiation process. Boone and Mulherin (2014) find that special committees are more likely to be formed when agency costs are high. Committees tend to choose competitive selling procedures (i.e., auctions) and hire separate financial advisors more often, though their presence in the takeover process does not affect target premiums.[5]

In summary, previous studies focused on the effects of the two main roles of the board of directors on merger outcomes. Directors' monitoring and advising activities during takeover negotiations seem to affect acquirer and target firm stock returns, bid premiums, and other merger agreement characteristics. Thus, internal control mechanisms play a crucial role in creating shareholder value during acquisitions. The subsequent sections investigate the extent to which external mechanisms achieve the same objective.

© 2015 John Wiley & Sons Ltd

TAKEOVER MARKET AND PRESSURE FROM FINANCIAL MARKET PARTICIPANTS

The Takeover Market

In his seminal article, Manne (1965) emphasizes the role of the takeover market as an external control mechanism over incumbent managers. In the same vein, Jensen and Ruback (1983: 42) propose a precise definition of the takeover market. It is as "an arena in which alternative management teams compete for the rights to manage corporate resources." In an economy with a competitive and liquid takeover market, the resources of the economy are expected to be managed by the most efficient management teams, with value-destroying managers replaced by value-creating ones thanks to the takeover market (Jensen, 1986). Consistent with Jensen's (1986) prediction that the solution to agency-driven mergers lies in the takeover market, Mitchell and Lehn (1990) empirically demonstrate that firms whose managers carry out value-destroying deals are more likely to be subsequently taken over (i.e., bad bidders become good targets).

Kini, Kracaw, and Mian (2004) also empirically examine the disciplinary role of corporate takeovers. The authors compare the 1980s and the 1990s, two periods with intense M&A activity and distinct governance control. The earlier period is characterized by a wave of disciplinary and hostile takeovers targeting poorly performing companies. In reaction to this wave, firms implemented antitakeover defenses, such as poison pills, and many US states adopted antitakeover laws. The responses of the firms and the government potentially raised managerial discretion and agency costs. At the same time, this evolution virtually eliminated hostile takeovers during the 1990s, which is known as an era of friendly deals (Betton et al., 2008; Boone & Mulherin, 2007). During these two decades, the intensity of internal governance mechanisms was also different. It was weak during the earlier decade and more structured in the latter. Kini et al. (2004) analyze CEO turnover at the target firm level, and report findings consistent with the view of the takeover market as a "court of last resort." Despite its high cost, the takeover market acts as an effective external control mechanism when internal control mechanisms, such as board monitoring, are relatively weak.

The adoption of antitakeover provisions (ATPs) by firms has also attracted the attention of the academic community. Several studies note a negative correlation between ATPs and firm value (Bebchuk & Cohen, 2005; Cremers & Nair, 2005; Gompers, Ishii, & Metrick, 2003). In particular, Gompers et al. (2003) use a governance index of 24 provisions to proxy for shareholder rights, and find that firms with weaker shareholder rights (i.e., higher index) are associated with lower firm value and a higher degree of acquisitiveness in the takeover market. Masulis et al. (2007) study a potential channel through which ATPs negatively affect firm value. The authors determine that acquirers with more ATPs experience significantly lower abnormal returns. This result supports the hypothesis that managers who are immune to the disciplinary power of the takeover market are more likely to engage in empire-building acquisitions that destroy shareholder value. This finding is also confirmed by Harford, Mansi, and Maxwell (2008), who confirm that firms with weaker governance will spend cash more readily on value-destroying acquisitions than those with stronger governance.

To assess the effect of takeover pressure on firm value and firm-level outcomes, several studies employ the passage of antitakeover laws by US states as a negative shock to corporate governance. Karpoff and Malatesta (1989) find that the initial press announcement of an antitakeover law in a particular state is associated with a negative stock price reaction for firms incorporated in the corresponding state. Consistent with the increase in managerial discretion after the passage of antitakeover laws, Bertrand and Mullainathan (1999) report that managerial compensation increased by 1–2 percent in affected firms. In a follow-up paper, Bertrand and Mullainathan (2003) find that when managers are insulated from takeover pressure, the wages of white collar workers increase, fewer old plants are destroyed, and very few new plants are created. The evidence appears to be consistent with unmonitored managers enjoying the quiet life rather than pursuing empire-building strategies. In a recent article, Gormley and Matsa (2014) find that managers insulated from disciplinary takeover pressures tend to "play it safe" by reducing firm risk. Following the adoption of an antitakeover law, managers take on less risk by undertaking diversifying acquisitions and increasing their firms' cash holdings. Consistent with the "play it safe" hypothesis, this increase in diversifying acquisitions is concentrated among riskier firms (i.e., firms with greater leverage and less cash flow prior to the passage of the antitakeover law).

Servaes and Tamayo (2014) analyze how the investment and financing policies of firms in an industry change when the industry experiences a hostile (disciplinary) takeover attempt. Consistent with a reduction in agency costs following an increase in control threats, industry firms cut their capital spending and cash holdings, and increase their leverage and dividend payouts to shareholders. In summary, hostile deals exercise a disciplinary effect not only on the targeted firms, but also on their industry peers.

The evidence provided in this subsection emphasizes the role of the takeover market as an important external governance mechanism to discipline firms and their managers, in particular when internal mechanisms are deficient. The role of the takeover market becomes even more pronounced when other external governance mechanisms are simultaneously at play, such as outside blockholders and activist investors as discussed in the next subsection.

Outside Blockholders and Activist Investors

Recent literature has made it abundantly clear that the outcome of an acquisition investment does not depend exclusively on the acquiring and target firms and other potential bidders. In fact, external players may affect the arrival of a bid, its success, its price, and the type of consideration offered. In this section, we discuss the role played by blockholders and activist investors in determining takeover outcomes.

Institutional investors' ownership of common stock has increased considerably over the past few decades (Chen, Harford, & Li, 2007; Ferreira & Matos, 2008). Institutional investors face the choice between monitoring the management of a company, providing a free good for all shareholders, and trading for private gain. This choice has clear implications for the frequency and quality of firms' acquisition decisions. Gaspar, Massa, and Matos (2005) find that institutional

© 2015 John Wiley & Sons Ltd

investors with high turnover portfolios and short investment horizons exert little influence on managers with regard to acquisition decisions. However, Chen et al. (2007) argue that independent long-term institutions with large ownership stakes alleviate the agency conflicts between shareholders and managers. The authors find that the existence of these types of institutional investors in acquiring firms is associated with superior post-merger acquirer performance. Firms with independent long-term institutions as shareholders are more likely to listen to market feedback and withdraw bad bids. Ferreira, Massa, and Matos (2010) note another important role played by institutional investors. They act as facilitators in the international market for corporate control. Institutional investors are instrumental in connecting firms in their portfolios and reducing the transaction costs and the information asymmetry between bidders and targets, which are particularly high in cross-border deals.

Recent empirical research has examined the effect of liquidity on firm outcomes, including governance. Stock liquidity can either encourage monitoring (more informative prices and more realistic threats of exit by a large shareholder) or weaken it (low cost to exit the firm). Roosenboom, Schlingemann, and Vasconcelos (2014) test how stock liquidity affects monitoring using acquisitions, finding support for the tradeoff between stock liquidity and institutional monitoring. However, this result is limited to the acquisition of private targets (no relation in the case of acquisitions of public targets).

Institutional investors may affect the outcome of an acquisition with their votes. Institutional investors' incentives to monitor and prevent acquisitions may be weakened by cross-ownership in the target firms. Indeed, it is not uncommon for large institutional investors to own shares in both the target and the acquiring firms, generating a conflict of interest. Matvos and Ostrovsky (2008) provide evidence that cross-owners have greater incentive to vote in favor of a merger than do other institutional investors, even when the deal destroys value for the acquirer. However, they do not find differences in the voting behavior of the two groups when the acquisition creates value. Voting the shares they own in favor or against a merger is not the only possibility that institutional investors have. In an attempt to affect merger outcomes, institutions may buy additional shares and the attached voting rights immediately before the merger record dates. Indeed, Bethel, Hu, and Wang (2009) find evidence consistent with this behavior in their examination of the market for voting rights around M&As. In particular, institutions' trading is positively correlated with voter turnout and negatively related to shareholder support of merger proposals.

Shareholder activism, especially hedge fund activism, has increased substantially over the past two decades. Several recent articles note a positive reaction around the announcement of shareholder activism, suggesting that hedge funds might be up to the task of monitoring management (Becht, Franks, Grant, & Wagner, 2014; Brav, Jiang, Partnoy, & Thomas, 2008; Klein & Zur, 2009). Aggressive investors have been a driving force behind a large number of deals in recent years (Mattioli & Cimilluca, 2014). Brav et al. (2008) find that activist hedge funds are primarily after the sale or breakup of the companies they invest in. They also demonstrate that this type of activism, aimed at rectifying relatively large inefficiencies, is also associated with large positive abnormal returns, suggesting that these deals would benefit the target company's shareholders. Klein and Zur (2009) determine that hedge funds are more concerned with potential M&A activity than other activist shareholders. Indeed, hedge fund activism acts as a catalyst for acquisitions, putting target companies in play. Greenwood and Schor (2009) explore what accounts for the return of hedge fund activism and find that returns to investor activism are primarily explained by activists' success at taking over target firms.

Overall, it is evident that institutional and activist investors play an important part in disciplining management during takeover decisions. They often play a multifaceted role and affect different phases of the takeover process, from the decision to propose and execute the acquisition down to the details of the deal and its implementation.

Other Financial Market Participants

Blockholders and activist investors are not the only external players that can affect the outcome of a takeover. In this section, we review the literature that focuses on the financial market at large, credit rating agencies, financial analysts, and banks.[6]

Financial markets are not just a sideshow, but they produce real effects on corporate investments. In particular, they may impose discipline on managers by triggering takeover threats. Edmans, Goldstein, and Jiang (2012) argue that the lack of clear evidence linking stock market valuation to takeover probabilities in previous empirical research is due to endogeneity problems (anticipation effects, omitted variables, and measurement error). Using an instrument for stock price changes (i.e., mutual fund redemptions) to overcome these endogeneity concerns, they identify a strong effect of market prices on takeover activity. Investors may even apply pressure to managers through their trading activities to change the terms of a pending M&A deal or even to withdraw it. This pressure is particularly valuable when investors have more information than the companies. In particular, Luo (2005) finds that the market reaction to an M&A announcement predicts whether the companies will later consummate the deal. This effect is primarily due to the information that managers extract from their companies' stock prices.

Credit rating agencies (CRAs) may also affect acquisition decisions. CRAs evaluate the credit quality of debt issuers and allow rated firms to access the public debt market. In a recent study, Harford and Uysal (2014) find that ratings relax financing constraints and have a real effect on M&A decisions by allowing rated firms to overcome the underinvestment problem. Nevertheless, Graham and Harvey (2001) provide survey evidence that corporate managers put particular emphasis on their firms' credit rating levels when making financial decisions. Boot, Milbourn, and Schmeits (2006) argue that credit ratings derive their values essentially from the monitoring role of the CRAs and the investment policies of institutional investors. In particular, rating agencies do not only provide a rating for a specific company, but also continuously monitor the existing rating and, as such, the financial decisions of the firm.

Financial analysts produce research that is generally relevant to investors and managers. While much of the academic research on financial analysts focuses on the conflicts of

© 2015 John Wiley & Sons Ltd

interest between analysts and their clients, resulting in an optimistic bias in earnings forecasts (for a review of this literature, see Firth, Lin, Liu, & Xuan, 2013), there are a few recent papers that analyze the role of analysts on the firm's corporate governance and policies. Chen, Harford, and Lin (2015) find that analysts reduce the propensity to undertake value-destroying acquisitions. Derrien and Kecskés (2013) investigate the causal effects of analyst coverage on corporate investment and financing policies. A decrease in analyst coverage increases information asymmetry. Greater information asymmetry leads to a higher cost of capital, which, in turn, reduces investments and financing. Among the investments, acquisition expenditures decrease by about 1 percent of the firm's total assets. These are not, however, the only effects related to financial analysts' coverage: Degeorge, Derrien, Kecskés, and Michenaud (2013) find that firms cater to the preferences of sell-side analysts when they choose their investment policies to obtain more favorable treatment. Sell-side financial analysts also impact the premium paid for target firms. Fich, Juergens, and Officer (2014) note that the premium paid in acquisitions is positively affected by analysts' monitoring. They interpret this result as evidence that the monitoring by financial analysts induces target managers to bargain harder to extract a higher premium for their shareholders, avoiding trading merger premiums for personal benefits (Hartzell et al., 2004).

Finally, even banks may exert a disciplinary role in the market for corporate control (Ivashina, Nair, Saunders, Massoud, & Stover, 2008). As suppliers of loans, banks may gather information unavailable to outside investors, which can position banks as valuable monitors. Ivashina et al. (2008) finds evidence consistent with a role for banks in facilitating takeovers through information production via bank lending and the transmission of generated information to potential acquirers. In fact, greater bank lending intensity to a firm results in a greater likelihood that it will receive a takeover bid. They also find that firms that have lending relationships with banks that have additional clients in the same industry are more likely to be subject to a takeover attempt.

In this section, we have documented the existence of several external corporate governance mechanisms related to financial markets other than holding large blocks of shares. In fact, pressure from small investors, as well as banks and gatekeepers like financial analysts and credit rating agencies, may induce firms to behave in a certain way when they are involved in an acquisition. However, outside pressures are not limited to shareholders and players that operate in the financial markets. In fact, firms often make acquisition decisions in response to actions that their rivals take or are expected to take. For this reason, the next section deals with the effects of product market interaction on corporate takeovers to examine whether competition fosters discipline and takeover efficiency.

PRODUCT MARKET INTERACTIONS

Adam Smith was one of the first economists to recognize that "monopoly […] is a greater enemy to good management" (Smith, 1904 [1776]). In non-competitive industries and without proper incentives, managers might be tempted to enjoy the quiet life (Bertrand & Mullainathan, 2003; Hicks, 1935) and to avoid difficult decisions or costly efforts. Theoretically, the relation between product market competition and managerial shirking is ambiguous, with the relation appearing to be negative in Hart (1983), and positive in Scharfstein (1988). However, recent empirical studies provide evidence consistent with product market competition mitigating managerial slack (Giroud & Mueller, 2010, 2011; Masulis et al., 2007).

Masulis et al. (2007) find that firms operating in more competitive industries make better acquisitions. This result suggests that competition acts as an important corporate governance device that discourages management from wasting corporate resources. Hoberg and Phillips (2010) also find that deals create more value when the acquirer operates in a more competitive product market. The authors demonstrate that firms in competitive product markets are also more likely to choose targets that help them to increase product differentiation. Giroud and Mueller (2010) argue that the effect of product market competition on managerial slack is only effective when internal governance mechanisms are deficient. The authors analyze the effect of antitakeover laws on firm-level outcomes in relation to product market competition. Consistent with their intuition, the adoption of the laws is followed by a drop in operating performance only in non-competitive industries. The authors also find that in non-competitive industries, input costs, wages, and overhead costs all increase after the passage of antitakeover laws. Another interesting finding is that there is a negative correlation between the adoption of antitakeover laws and the likelihood of being acquired, but the effect is statistically significant only in competitive industries. All these results are consistent with the "enjoying the quiet life" hypothesis. Product market competition also affects the relation between firm value and governance. Giroud and Mueller (2011) revisit Gompers et al.'s (2003) study and find that the positive relationship between firm value and the quality of firm governance is confined to firms operating in non-competitive industries. The authors also explore the causes of the inefficiencies for firms with weak governance in non-competitive industries, and find that the implementation of value-destroying M&A deals is one of the causes of firm underperformance.

Using the reduction in import tariffs as a natural experiment, Aktas and Dupire-Declerck (2015) examine how an increase in competitive intensity impacts firms' acquisition decisions. The results indicate that M&As are a means for deploying assets more efficiently among the merging firms when the competitive intensity in the industry is high. Another interesting finding is that after import tariff reductions, the selection of targets by the acquirers in non-horizontal deals becomes more efficient. In addition, industry rivals react more positively to those deals, suggesting that efficient non-horizontal deals signal the existence of investment opportunities outside the industry. Relying on a similar approach, Alimov (2014) investigates the effect of the 1989 Canada–US Free Trade Agreement on acquirer performance and finds evidence that intensified competition disciplines managers. In particular, the author notes that following trade liberalization, acquirers exposed to a greater increase in competitive pressure undertake deals of better quality. The positive effect of increased competition on acquirer abnormal returns is stronger when acquirers have higher agency costs prior to the

© 2015 John Wiley & Sons Ltd

liberalization. Competition also accentuates the costs of completing bad deals for executives. Managers of acquiring companies facing an increase in competition are more likely to lose their jobs following value-destroying deals.

This section illustrates that competition in the product market affects a firm's acquisition likelihood and deal quality. The next section explores to what extent the dynamics of the labor market affect firm behavior in the M&A market.

LABOR MARKETS

The conflict of interest between a firm's managers and its shareholders and its implications on the acquisition decisions of a firm may be influenced by the characteristics of its labor force. The role of workers on the governance of firms depends heavily on the differences in legal systems, industry structures, and the political culture (Blair & Roe, 2010). The proponents of a more powerful labor force claim that the interests of shareholders and employees are aligned when the employees hold more of a firm's equity (Aoki, 1984; Drucker, 1978; Vanek, 1965). A better alignment of interests between the two parties brings superior firm performance. In contrast, Jensen and Meckling (1979) point out that labor's high equity ownership in a firm may result in an entrenched workforce, which may force managers to maximize the welfare of the firm's employees rather than its shareholders (for a review of the empirical evidence supporting these alternative views, see Faleye, Mehrotra, & Morck, 2006).[7]

Takeovers are major corporate events that have implications regarding the interests of all of the stakeholders of the merging firms. Therefore, they provide a venue for researchers to investigate the link between the incentives of different stakeholders and takeover outcomes. Pagano and Volpin (2005) is the first theoretical study to analyze the incentives of a firm's shareholders, managers, and employees in a corporate control event. The authors indicate that both the managers and the employees of a firm are likely to resist a takeover threat, especially when the share ownership of the managers is low and their private benefits are high. Under this "natural alliance" (Hellwig, 2000), managers make their firms less attractive to corporate raiders by offering their employees long-term and rewarding contracts, while employees oppose the takeover by not selling their shares to the raiders or through lobbying. This alliance blocks the takeover and reduces shareholder value.

The collusion hypothesis put forth by Pagano and Volpin (2005) is consistent with several empirical studies. Loderer and Zgraggen (1999) provide anecdotal evidence of the alliance between managers and employees in their analysis of the proxy fight at the Union Bank of Switzerland (UBS) in 1994. UBS employees, who owned a considerable amount of votes, sided with the incumbent managers to fend off an unsolicited offer from Martin Ebner, a Swiss corporate raider. Chaplinsky and Niehaus (1994) and Rauh (2006) find that the employee share ownership plan (ESOP) offered to employees, resulting in a substantial increase in employee compensation (Kim & Ouimet, 2014), reduces the chances of a future takeover threat. Wang and Xie (2013) find that acquirers tend to make value-decreasing acquisitions when their employees have greater equity stakes. Furthermore, the likelihood of receiving a takeover bid is significantly lower for these types of firms. John, Knyazeva, and Knyazeva (forthcoming) use the variation in labor rights laws in the US to demonstrate that acquirers with strong labor rights experience lower abnormal returns around merger announcement dates. Atanassov and Kim (2009) find that asset sales in poorly performing firms promote further deterioration in firm performance, especially when the firm's labor force is unionized. The authors argue that managers of the poorly performing firms refrain from firing employees or cutting wages even though these restructuring activities are superior to asset sales. Becker (1995) confirms that the bid premiums received by targets with unionized labor are higher than those of non-unionized targets, consistent with the conjecture that the wage premium earned by unionized labor is transferred to target shareholders through a takeover. Finally, using a regression discontinuity modeling approach that isolates the causal effect of unionization on takeover exposure, Tian and Wang (2014) find that unionization reduces a firm's future chances of receiving takeover bids. This result adds to the evidence that managers could use unionization to entrench themselves.

The studies discussed in this section demonstrate how the characteristics of a firm's labor force affect a firm's acquisition performance in the takeover market, the chances of the firm actually being taken over, and the premiums it would receive if the takeover is successfully completed. The empirical evidence supports the view that managers and employees tend to form alliances to maximize their joint benefits when their firms are subject to a takeover, even though such an alliance would be harmful to the wealth of their shareholders.

CONCLUDING REMARKS AND AVENUES FOR FUTURE RESEARCH

This article reviews how corporate governance mechanisms affect corporate takeovers, both the process and the outcomes. This strand of the literature is clearly well developed and growing. The relation between corporate governance and takeovers is not simple. Adopting an agency perspective of the firm, this review has highlighted the fact that corporate governance does not have a single and unique impact on takeovers. In fact, there are several effects that influence the entire takeover process, from its conception to the moment the deal is either completed or cancelled. Corporate governance mechanisms may help to avoid costly acquisitions that destroy shareholder value (e.g., effective board of directors, discipline induced by product market completion, or activist investors), but they can also facilitate the completion of a deal by lowering the defenses entrenched managers could put up and the cost of acquiring information. By systematizing the literature linking corporate governance and acquisitions, we shed light on which mechanisms policymakers can use to improve the efficiency of the takeover market. We also offer indications about mechanisms that could be used to mitigate agency conflicts and increase firm value.

Despite the voluminous literature, we believe there is still room for new contributions regarding this line of research. The prior literature has primarily analyzed the impact of corporate governance on the short-term outcomes of takeover decisions (arrival of the offer, success, market reaction around

© 2015 John Wiley & Sons Ltd

the announcement day). To the best of our knowledge, there are only a few studies that investigate the effect of governance on a firm's long-term financial performance. For example, while we know that stock prices increase when activist hedge funds and institutional investors disclose large equity stakes in a company anticipating a takeover, we are unaware of any studies that examine whether deals facilitated by activist hedge funds or institutional investors perform well in the long run.

Other future studies that could improve our knowledge of the correlation between corporate governance and takeovers are those that account for the interaction between the different mechanisms. Researchers have typically investigated governance mechanisms in isolation from each other, without paying too much attention to the substitution/complementarity effects that link the alternative governance mechanisms. Some attempts in this direction have recently started to appear (e.g., product market competition and hedge fund activism by Brav, Jiang, & Kim, 2015), but we are still in the infancy of this avenue of research. This line of research could produce new insights that would allow us to have a more complete view of the phenomenon at hand. In fact, it is quite difficult to distinguish the individual effects of the competing mechanisms. Think about outside blockholders and board of directors, for example. The literature indicates that, on average, increased monitoring due to an outside blockholder is beneficial to the firm. However, if a representative of this outside blockholder joins the company's board, these benefits could also be ascribed to more effective monitoring by the board of directors. In fact, we do not know if without board representation, an outside blockholder could have improved monitoring. Decomposing all of the effects that, at the same time, are influencing the relation is of paramount importance to fully understand the role of corporate governance in takeovers.

A related avenue of research whose importance is growing is the use of quasi-natural experiments. In fact, while some of the reviewed articles already use sophisticated approaches to deal with endogeneity (see, e.g., Edmans et al., 2012; Fracassi & Tate, 2012; or the literature concerning the passage of takeover laws), other parts of the literature are less advanced from this point of view (e.g., the shareholder activism literature). Since corporate governance is often affected by regulatory changes, this area is certainly suitable for this type of investigation. Often, this approach has the advantage that it permits the researcher to examine the effect of a single mechanism without worrying about the contemporaneous role played by other mechanisms.

ACKNOWLEDGEMENTS

We are grateful to Chris Florackis, the associate editor and guest editor for this special issue, Jean-Gabriel Cousin, and Dimitris Petmezas for helpful comments and suggestions.

NOTES

1. The empirical evidence for non-US markets, which is not discussed in this review, suggests that the low acquirer returns in mergers are primarily confined to countries with competitive takeover markets. Acquirers located in countries with less competitive markets tend to create value in their acquisitions of listed targets (Alexandridis, Petmezas, & Travlos, 2010).
2. The literature regarding the role of boards of directors in corporate governance is quite extensive. As such, interested readers are referred to a recent survey by Adams, Hermalin, and Weisbach (2010). In this section, we focus on the studies that exclusively analyze the role of boards on takeover outcomes.
3. In a recent study, Zhao (2013) also provides evidence concerning the positive impact of EBC (and the existence of CEO contracts) on acquiring firm performance. In a study devoted to learning-by-doing in M&A deal making, Aktas, de Bodt, and Roll (2013) indicate that EBC prompts the CEO to pay more attention to the learning process, which is associated with superior acquisition performance.
4. The considered exogenous shock in Gormley et al. (2013) is the discovery of a chemical's carcinogenicity.
5. The monitoring and advisory roles of the boards serve as ex ante actions to mitigate shareholder–management conflicts of interest. The boards may also "ex-post settle up" with the executives of the surviving firm in the post-acquisition period. For instance, Lehn and Zhao (2006) find that acquirer CEOs are more likely to be replaced by their boards following value-destroying M&A deals.
6. Recent literature has also investigated the role of the media in M&A decisions (Liu & McConnell, 2013) and during merger negotiation (Ahern & Sosyura, 2014).
7. Equity ownership is not necessary for employees to be represented on the firm's board. In "stakeholder system countries," such as Germany, France, and Japan, the interests of employees are represented on corporate boards even though employees do not have equity ownership in their firms (Fauver & Fuerst, 2006).

REFERENCES

Adams, R. B., Hermalin, B. E., & Weisbach, M. S. 2010. The role of boards of directors in corporate governance: A conceptual framework and survey. ***Journal of Economic Literature***, 48: 58–107.

Agrawal, A. & Walkling, R. A. 1994. Executive careers and compensation surrounding takeover bids. ***Journal of Finance***, 49: 985–1014.

Ahern, K. R. & Sosyura, D. 2014. Who writes the news? Corporate press releases during merger negotiations. ***Journal of Finance***, 69: 241–291.

Akdogu, E. 2011. Value-maximizing managers, value-increasing mergers and overbidding. ***Journal of Financial and Quantitative Analysis***, 46: 83–110.

Aktas, N., de Bodt, E., & Roll, R. 2013. Learning from repetitive acquisitions: Evidence from the time between deals, ***Journal of Financial Economics***, 108: 99–117.

Aktas, N. & Dupire-Declerck, M. 2015. Increased entry threat and merger activity, ***Finance***, 36: 77–118.

Alexandridis, G., Petmezas, D., & Travlos, N. 2010. Gains from mergers and acquisitions around the world: New evidence. ***Financial Management***, 39: 1671–1695.

Alimov, A. 2014. Does product market competition discipline managers? Evidence from exogenous trade shock and corporate acquisitions. Working Paper, City University of Hong Kong.

Aoki, M. 1984. ***The co-operative game theory of the firm***. Oxford: Clarendon Press.

Atanassov, J. & Kim, E. H. 2009. Labor and corporate governance: International evidence from restructuring decisions. ***Journal of Finance***, 64: 341–374.

Bange, M. M. & Mazzeo, M. A. 2004. Board composition, board effectiveness, and the observed form of takeover bids. ***Review of Financial Studies***, 17: 1185–1215.

© 2015 John Wiley & Sons Ltd

Bebchuk, L. A. & Cohen, A. 2005. The costs of entrenched boards. ***Journal of Financial Economics***, 78: 409–433.

Becht, M., Franks, J. R., Grant, J., & Wagner, H. F. 2014. The returns to hedge fund activism: An international study. Working paper, Université Libre de Bruxelles.

Becker, B. E. 1995. Union rents as a source of takeover gains among target shareholders. ***Industrial & Labor Relations Review***, 49: 3–19.

Bertrand, M. & Mullainathan, S. 1999. Is there discretion in wage setting? A test using takeover legislation. ***Rand Journal of Economics***, 3: 535–554.

Bertrand, M. & Mullainathan, S. 2003. Enjoying the quiet life? Corporate governance and managerial preferences. ***Journal of Political Economy***, 111: 1043–1075.

Bethel, J. E., Hu, G., & Wang, Q. 2009. The market for shareholder voting rights around mergers and acquisitions: Evidence from institutional daily trading and voting. ***Journal of Corporate Finance***, 15: 129–145.

Betton, S., Eckbo, B. E., & Thorburn, K. S. 2008. Corporate takeovers. In B. E. Eckbo (Ed.), ***Handbook of corporate finance: Empirical corporate finance***, vol. 2: 291–429. Amsterdam: North Holland.

Blair, M. M. & Roe, M. J. 2010. ***Employees and corporate governance***. Washington, DC: Brookings Institution Press.

Boone, A. L. & Mulherin, J. H. 2007. How are firms sold? ***Journal of Finance***, 62: 847–875.

Boone, A. L. & Mulherin, J. H. 2014. Who monitors the monitor? The use of special committees by target firms in corporate takeovers. ***Journal of Corporate Finance***. doi: 10.1016/j.jcorpfin.2014.02.002.

Boot, A. W. A., Milbourn, T., & Schmeits, A. 2006. Credit ratings as coordination mechanisms. ***Review of Financial Studies***, 19: 81–118.

Boulton, T. J., Braga-Alves, M. V., & Schlingemann, F. 2014. Does equity-based compensation make CEOs more acquisitive? ***Journal of Financial Research***, 37: 267–293.

Bradley, M., Desai, A., & Kim, E. H. 1988. Synergistic gains from corporate acquisitions and their division between the stockholders of target and acquiring firms. ***Journal of Financial Economics***, 21: 3–40.

Brav, A., Jiang, W., & Kim, H. 2015. The real effects of hedge fund activism: Productivity, asset allocation, and labor outcomes. Working paper, Duke University.

Brav, A., Jiang, W., Partnoy, F., & Thomas, R. 2008. Hedge fund activism, corporate governance, and firm performance. ***Journal of Finance***, 63: 1729–1775.

Brewer, E., Jackson, W. E., & Wall, L. D. 2006. When target CEOs contract with acquirers: Evidence from bank mergers and acquisitions. Working paper no. 2006-28, Federal Reserve Bank of Atlanta.

Byrd, J. W. & Hickman, K. A. 1992. Do outside directors monitor managers?: Evidence from tender offer bids. ***Journal of Financial Economics***, 32: 195–221.

Cai, Y. & Sevilir, M. 2012. Board connections and M&A transactions. ***Journal of Financial Economics***, 103: 327–349.

Chaplinsky, S. & Niehaus, G. 1994. The role of ESOPs in takeover contests. ***Journal of Finance***, 49: 1451–1470.

Chen, T., Harford, J., & Lin, C. 2015. Do analysts matter for governance? Evidence from natural experiments. ***Journal of Financial Economics***, 115: 383–410.

Chen, X., Harford, J., & Li, K. 2007. Monitoring: Which institutions matter? ***Journal of Financial Economics***, 86: 279–305.

Cotter, J. F., Shivdasani, A., & Zenner, M. 1997. Do independent directors enhance target shareholder wealth during tender offers? ***Journal of Financial Economics***, 43: 195–218.

Cremers, M. K. J. & Nair, V. B. 2005. Governance mechanisms and equity prices. ***Journal of Finance***, 60: 2859–2894.

Croci, E. & Petmezas, D. 2015. Do risk-taking incentives induce CEOs to invest? Evidence from acquisitions. ***Journal of Corporate Finance***, 32: 1–23.

Datta, S., Iskandar-Datta, M., & Raman, K. 2001. Executive compensation and corporate acquisition decisions. ***Journal of Finance***, 56: 2299–2336.

Degeorge, F., Derrien, F., Kecskés, A., & Michenaud, S. 2013. Do analysts' preferences affect corporate policies? Working paper, HEC Paris.

Derrien, F. & Kecskés, A. 2013. The real effects of financial shocks: Evidence from exogenous changes in analyst coverage. ***Journal of Finance***, 68: 1407–1440.

Drucker, P. F., 1978. ***The future of industrial man: A conservative approach***. Westport, CT: Greenwood Press.

Edmans, A., Goldstein, I., & Jiang, W. 2012. The real effects of financial markets: The impact of prices on takeovers. ***Journal of Finance***, 67: 933–971.

El-Khatib, R., Fogel, K., & Jandik, T. 2015. CEO network centrality and merger performance. ***Journal of Financial Economics***, 116: 349–382.

Faleye, O., Hoitash, R., & Hoitash, U. 2011. The costs of intense board monitoring. ***Journal of Financial Economics***, 101: 160–181.

Faleye, O., Mehrotra, V., & Morck, R. 2006. When labor has a voice in corporate governance. ***Journal of Financial and Quantitative Analysis***, 41: 489–510.

Fauver, L. & Fuerst, M. E. 2006. Does good corporate governance include employee representation? Evidence from German corporate boards. ***Journal of Financial Economics***, 82: 673–710.

Ferreira, M., Massa, M., & Matos, P. 2010. Shareholders at the gate? Institutional investors and cross-border mergers and acquisitions. ***Review of Financial Studies***, 23: 601–644.

Ferreira, M. & Matos, P. 2008. The colors of investors' money: The role of institutional investors around the world. ***Journal of Financial Economics***, 88: 499–533.

Fich, E. M., Cai, J., & Tran, A. L. 2011. Stock option grants to target CEOs during private merger negotiations. ***Journal of Financial Economics***, 101: 413–430.

Fich, E. M., Juergens, J. L., & Officer, M. O. 2014. Analyst coverage and acquisition returns: Evidence from natural experiments. Working paper, Drexel University.

Firth, M., Lin, C., Liu, P. P., & Xuan, Y. 2013. The client is king: Do mutual fund relationships bias analyst recommendations? ***Journal of Accounting Research***, 51: 165–200.

Fracassi, C. & Tate, G. 2012. External networking and internal firm governance. ***Journal of Finance***, 67: 153–194.

Gaspar, J.-M., Massa, M., & Matos, P. 2005. Shareholder investment horizons and the market for corporate control. ***Journal of Financial Economics***, 76: 135–165.

Giroud, X. & Mueller, H. M. 2010. Does corporate governance matter in competitive industries? ***Journal of Financial Economics***, 95: 312–331.

Giroud, X. & Mueller, H. M. 2011. Corporate governance, product market competition, and equity prices. ***Journal of Finance***, 66: 563–600.

Gompers, P. A., Ishii, J., & Metrick, A. 2003. Corporate governance and equity prices. ***Quarterly Journal of Economics***, 118: 107–155.

Gormley, T. A. & Matsa, D. A. 2014. Playing it safe? Managerial preferences, risk, and agency conflicts. Working paper, Northwestern University.

Gormley, T. A., Matsa, D. A., & Milbourn, T. 2013. CEO compensation and corporate risk: Evidence from a natural experiment. ***Journal of Accounting and Economics***, 56: 79–101.

Graham, J. R. & Harvey, C. R. 2001. The theory and practice of corporate finance: Evidence from the field. ***Journal of Financial Economics***, 60: 187–243.

Greenwood, R. & Schor, M. 2009. Hedge fund investor activism and takeovers. ***Journal of Financial Economics***, 92: 362–375.

Grinstein, Y. & Hribar, P. 2004. CEO compensation and incentives: Evidence from M&A bonuses. ***Journal of Financial Economics***, 73: 119–143.

© 2015 John Wiley & Sons Ltd

Grossman, S. J. & Hart, O. D. 1980. Takeover bids, the free-rider problem, and the theory of the corporation. ***Bell Journal of Economics***, 11: 42–64.

Güner, A. B., Malmendier, U., & Tate, G. U. 2008. Financial expertise of directors. ***Journal of Financial Economics***, 88: 323–354.

Hadlock, C., Houston, J., & Ryngaert, M. 1999. The role of managerial incentives in bank acquisitions. ***Journal of Banking & Finance***, 23: 221–249.

Harford, J. 1999. Corporate cash reserves and acquisitions. ***Journal of Finance***, 54: 1969–1997.

Harford, J. 2003. Takeover bids and target directors' incentives: The impact of a bid on directors' wealth and board seats. ***Journal of Financial Economics***, 69: 51–83.

Harford, J. & Li, K. 2007. Decoupling CEO wealth and firm performance: The case of acquiring CEOs. ***Journal of Finance***, 62: 917–949.

Harford, J., Mansi, S. A., & Maxwell, W. F. 2008. Corporate governance and firm cash holdings in the US. ***Journal of Financial Economics***, 87: 535–555.

Harford, J. & Schonlau, R. J. 2013. Does the director labor market offer ex post settling-up for CEOs? The case of acquisitions. ***Journal of Financial Economics***, 110: 18–36.

Harford, J. & Uysal, V. B. 2014. Bond market access and investment. ***Journal of Financial Economics***, 112: 147–163.

Hart, O. D. 1983. The market mechanism as an incentive scheme. ***Bell Journal of Economics***, 14: 366–382.

Hartzell, J. C., Ofek, E., & Yermack, D. 2004. What's in it for me? CEOs whose firms are acquired. ***Review of Financial Studies***, 17: 37–61.

Hellwig, M. 2000. On the economics and politics of corporate finance and corporate control. In X. Vives (Ed.), ***Corporate governance: Theoretical and empirical perspectives***: 95–136. Cambridge: Cambridge University Press.

Hicks, J. R., 1935. Annual survey of economic theory: The theory of monopoly. ***Econometrica***, 3: 1–20.

Hoberg, G. & Phillips, G. 2010. Product market synergies and competition in mergers and acquisitions: A text-based analysis. ***Review of Financial Studies***, 23: 3773–3811.

Huang, Q., Jiang, F., Lie, E., & Yang, K. 2014. The role of investment banker directors in M&A. ***Journal of Financial Economics***, 112: 269–286.

Ishii, J. & Xuan, Y. H. 2014. Acquirer-target social ties and merger outcomes. ***Journal of Financial Economics***, 112: 344–363.

Ivashina, V., Nair, V., Saunders, A., Massoud, N., & Stover, R. 2008. Bank debt and corporate governance. ***Review of Financial Studies***, 22: 41–77.

Jensen, M. C. 1986. Agency costs of free cash flow, corporate-finance, and takeovers. ***American Economic Review***, 76: 323–329.

Jensen, M. C. 1993. The modern industrial revolution, exit, and the failure of internal control systems. ***Journal of Finance***, 48: 831–880.

Jensen, M. & Meckling, W. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure. ***Journal of Financial Economics***, 3: 305–360.

Jensen, M. & Meckling, W. 1979. Rights and production functions: An application to labor-managed firms and codetermination. ***Journal of Business***, 52: 469–506.

Jensen, M. C. & Ruback, R. S. 1983. The market for corporate control: The scientific evidence. ***Journal of Financial Economics***, 11: 5–50.

John, K., Knyazeva, A., & Knyazeva, D. forthcoming. Employee rights and acquisitions. ***Journal of Financial Economics***.

Karpoff, J. M. & Malatesta, P. H. 1989. The wealth effects of second-generation state takeover legislation. ***Journal of Financial Economics***, 25: 291–322.

Kim, H. & Ouimet, P. 2014. Broad-based employee stock ownership: Motives and outcomes. ***Journal of Finance***, 69: 1273–1319.

Kini, O., Kracaw, W., & Mian, S. 2004. The nature of discipline by corporate takeovers. ***Journal of Finance***, 59: 1511–1552.

Klein, A. & Zur, E. 2009. Entrepreneurial shareholder activism: Hedge funds and other private investors. ***Journal of Finance***, 64: 187–229.

Lang, L., Stulz, R., & Walkling, R. 1991. A test of the free cash flow hypothesis: The case of bidder returns. ***Journal of Financial Economics***, 29: 315–335.

Lehn, K. & Zhao, M. 2006. CEO turnover after acquisitions: Are bad bidders fired? ***Journal of Finance***, 61: 1759–1811.

Liu, B. & McConnell, J. J. 2013. The role of the media in corporate governance: Do the media influence managers' capital allocation decisions? ***Journal of Financial Economics***, 110: 1–17.

Loderer, C. & Zgraggen, P. 1999. When shareholders choose not to maximize value: the Union Bank of Switzerland's 1994 proxy fight. ***Journal of Applied Corporate Finance***, 12: 91–102.

Luo, Y. 2005. Do insiders learn from outsiders? Evidence from mergers and acquisitions. ***Journal of Finance***, 60: 1951–1982.

Manne, H. G. 1965. Mergers and the market for corporate control. ***Journal of Political Economy***, 73: 110–120.

Masulis, R. W., Wang, C., & Xie, F. 2007. Corporate governance and acquirer returns. ***Journal of Finance***, 62: 1851–1889.

Mattioli, D. & Cimilluca, D. 2014. Activist investors gain in M&A push. ***Wall Street Journal***, January 5.

Matvos, G. & Ostrovsky, M. 2008. Cross-ownership, returns and voting in mergers. ***Journal of Financial Economics***, 89: 391–403.

Mitchell, M. L. & Lehn, K. 1990. Do bad bidders become good targets? ***Journal of Political Economy***, 98: 372–398.

Mitchell, M., Pulvino, T., & Stafford, E. 2004. Price pressure around mergers. ***Journal of Finance***, 59: 31–63.

Moeller, T. 2005. Let's make a deal! How shareholder control impacts merger payoffs. ***Journal of Financial Economics***, 76: 167–190.

Moeller, S. B., Schlingemann, F. P., & Stulz, R. M. 2004. Firm size and the gains from acquisitions. ***Journal of Financial Economics***, 73: 201–228.

Moeller, S. B., Schlingemann, F. P., & Stulz, R. M. 2005. Wealth destruction on a massive scale? A study of acquiring-firm returns in the recent merger wave. ***Journal of Finance***, 60: 757–782.

Netter, J. M., Stegemoller, M., & Wintoki, M. B. 2011. Implications of data screens on merger and acquisition analysis: A large sample study of mergers and acquisitions from 1992 to 2009. ***Review of Financial Studies***, 24: 2316–2357.

Pagano, M. & Volpin, P. F. 2005. Managers, workers, and corporate control. ***Journal of Finance***, 60: 841–868.

Qiu, B. H., Trapkov, S., & Yakoub, F. 2014. Do target CEOs trade premiums for personal benefits? ***Journal of Banking & Finance***, 42: 23–41.

Rauh, J. D. 2006. Own company stock in defined contribution pension plans: A takeover defense? ***Journal of Financial Economics***, 81: 379–410.

Renneboog, L. & Zhao, Y. 2014. Director networks and takeovers. ***Journal of Corporate Finance***, 28: 218–234.

Roll, R. 1986. The hubris hypothesis of corporate takeovers. ***Journal of Business***, 59: 197–216.

Roosenboom, P., Schlingemann, F. P., & Vasconcelos, M. 2014. Does stock liquidity affect incentives to monitor? Evidence from corporate takeovers. ***Review of Financial Studies***, 27: 2392–2433.

Scharfstein, D. 1988. Product–market competition and managerial slack. ***Rand Journal of Economics***, 19: 147–155.

Schmidt, B. 2015. Costs and benefits of "friendly" boards during mergers and acquisitions. ***Journal of Financial Economics***, doi: 10.1016/j.jfineco.2015.02.007.

Servaes, H. & Tamayo, A. 2014. How do industry peers respond to control threats? ***Management Science***, 60: 380–399.

Shleifer, A. & Vishny, R. W. 1997. A survey of corporate governance. ***Journal of Finance***, 52: 737–783.

© 2015 John Wiley & Sons Ltd

Smith, A. 1904. ***An inquiry into the nature and causes of the wealth of nations***. In E. Cannan (Ed.), Fifth Edition. London: Methuen and Co.

Stuart, T. E. & Yim, S. 2010. Board interlocks and the propensity to be targeted in private equity transactions. ***Journal of Financial Economics***, 97: 174–189.

Tian, X. & Wang, W. 2014. Hard marriage with heavy burdens: Labor unions as takeover deterrents. Working paper, Indiana University.

Vanek, J. 1965. ***General equilibrium of international discrimination: The case of customs unions***. Cambridge, MA: Harvard University Press.

Wang, C. & Xie, F. 2013. Employee influence, worker–manager alliance, and shareholder returns from acquisitions. Unpublished working paper, Chinese University of Hong Kong.

Wulf, J. 2004. Do CEOs in mergers trade power for premium? Evidence from "mergers of equals". ***Journal of Law, Economics & Organization***, 20: 60–101.

Zhao, J. 2013. Entrechment or incentive? CEO employment contracts and acquisition decisions. ***Journal of Corporate Finance***, 22: 124–152.

Nihat Aktas is Professor of Finance at WHU Otto Beisheim School of Management, Vallendar, Germany. He received his PhD from Louvain School of Management. His research is in empirical corporate finance with a particular focus on mergers and acquisitions.

Ettore Croci is Associate Professor at Università Cattolica del Sacro Cuore, Milan, Italy. He received his PhD from the University of Lugano. His research focuses on empirical corporate finance and corporate governance.

Serif Aziz Simsir is Assistant Professor of Finance at Sabanci School of Management, Istanbul, Turkey. He received his PhD from Cornell University. His research interests are mergers and acquisitions and corporate governance.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 253–273

Looking Inside the Black Box: The Effect of Corporate Governance on Corporate Social Responsibility

Tanusree Jain* and Dima Jamali

ABSTRACT

Manuscript Type: Review
Research Question/Issue: This study provides a systematic multi-level review of recent literature to evaluate the impact of corporate governance mechanisms (CG) at the institutional, firm, group, and individual levels on firm level corporate social responsibility (CSR) outcomes. We offer critical reflections on the current state of this literature and provide concrete suggestions to guide future research.
Research Findings/Insights: Focusing on peer-reviewed articles from 2000 to 2015, the review compiles the evidence on offer pertaining to the most relevant CG mechanisms and their influence on CSR outcomes. At the institutional level, we focus on formal and informal institutional mechanisms, and at the firm level, we analyze the different types of firm owners. At the group level, we segregate our analysis into board structures, director social capital and resource networks, and directors' demographic diversity. At the individual level, our review covers CEOs' demography and socio-psychological characteristics. We map the effect of these mechanisms on firms' CSR outcomes.
Theoretical/Academic Implications: We recommend that greater scholarly attention needs to be accorded to disaggregating variables and yet comprehending how multiple configurations of CG mechanisms interact and combine to impact firms' CSR behavior. We suggest that CG-CSR research should employ a multi-theoretical lens and apply sophisticated qualitative and quantitative methods to enable a deeper and finer-grained analysis of the CG systems and their influence on CSR. Finally, we call for cross-cultural research to capture the context sensitivities typical of both CG and CSR constructs.
Practitioner/Policy Implications: Our review suggests that for structural changes and reforms within firms to be successful, they need to be complemented by changes to the institutional makeup of the context in which firms function to encourage/induce substantive changes in corporate responsible behaviors.

Keywords: Corporate Governance, Corporate Social Responsibility, Corporate Social Performance, Corporate Environmental Performance, Multilevel Review

INTRODUCTION

In a provocative claim, the first decade of the new millennium has been described as the "Decade from Hell," characterized by the worst economic catastrophe since the Great Depression (Serwer, 2009). A Rockefeller study (2010) predicted that the present decade (2010–2020) will be the "Doom Decade," typified by authoritarian leaderships, domination by elites, and social and environmental disasters. In a world marked by grave corporate breaches and systemic governance failures on one hand, and gross societal and environmental excesses on the other, the interface between corporate governance (CG) and corporate social responsibility (CSR) has acquired global resonance and is more intriguing than ever before (Ryan, Buchholtz, & Kolb, 2010; Walls, Berrone, & Phan, 2012). In our attempt to look inside the black box of this vital interface, we provide a timely review of the fast developing yet largely fragmented literature on the effect of multilevel CG mechanisms on firms' CSR outcomes.

Beginning with the conceptualization of CG, the traditional economic perspective emphasizes the shareholder value approach to CG for maximizing firms' financial performance (Shleifer & Vishny, 1997). Toward achieving this objective, the purpose of CG is to specify the rules that shape the relations among boards of directors, shareholders, and managers to resolve assumed agency conflicts (Berle & Means, 1932). However, recent literature, including the OECD revised principles (2004), considers the traditional outlook of CG as narrow and shortsighted, with rising calls to include governance consequences and spillovers for non-financial stakeholders (Gill, 2008; Windsor, 2006). This shift has occurred primarily for three reasons. First, there is some

*Address for correspondence: Tanusree Jain, ESADE, Ramon Llull University, Av. de la Torre Blanca, 59, Sant Cugat, Spain. Tel: +34 93 554 3511; E-mail: tanusree.jain@alumni.esade.edu

© 2016 John Wiley & Sons Ltd
doi:10.1111/corg.12154

evidence that stakeholder engagement can enhance the value of the firm (Brown, Helland, & Smith, 2006; Ntim & Soobaroyen, 2013b), thus intertwining firms' financial and non-financial responsibilities (Donaldson & Preston, 1995). Second, neither corporate statutes nor corporate case laws expressly require shareholder value maximization (Stout, 2012), thus questioning the prioritization of shareholder interests as the default purpose of the firm (Gill, 2008). Finally, rising incidents of corporate frauds and scandals have expanded the idea of CG beyond merely dealing with agency conflicts towards adopting an ethical, accountable, and socially responsible agenda (Elkington, 2006). This has led to redefining CG both as a "structure of rights and responsibilities among the parties with a *stake* in the firm" (Aoki, 2000: 11) as well as a configuration of organizational processes through which different CG mechanisms interact and affect both financial and social outcomes (Aguilera, Desender, Bednar, & Lee, 2015; Aguilera, Filatotchev, Gospel, & Jackson, 2008; Aguilera, Goyer, & Kabbach-Castro, 2012). We adopt this wider perspective on CG in this paper.

Several individual studies have analyzed different CG mechanisms that can affect firms' social performance. At the institutional level, formal institutions such as legal and political systems are known to shape the nature of firms' stakeholder relationships (Judge, 2008). Informal institutions, on the other hand, particularly cultural beliefs and norms, can impact both the form (explicit or implicit) and the extent of CSR practices (Matten & Moon, 2008). At the firm level, ownership structures (Cox, Brammer, & Millington, 2008); Graves & Waddock, 1994), board structural characteristics (Capezio, Shields, & O'Donnell, 2011), and executive compensation contracts (Cordeiro & Sarkis, 2008) capture the effect of owner and managerial incentives (Deckop, Merriman, & Gupta, 2006) as well as boards' monitoring and resource provision capabilities on the propensity to engage in pro-social activities (de Villiers, Naiker, & van Staden, 2011). Furthermore, there is evidence that the continuous rise of financial and social activist pressures is pushing managers to either precipitate or at least deliberate broader corporate issues such as CSR (Eesley, Decelles, & Lenox, 2015; Goranova & Ryan, 2014). At the individual level, managers' and directors' demography and socio-psychological experiences (Borghesi, Houston, & Naranjo, 2014; Chin, Hambrick, & Treviño, 2013) tend to inform their roles and also affect their firms' CSR performance. Interestingly, these different CG variables, functioning at multiple levels, are often interdependent (Aguilera et al., 2015) and work in tandem, creating a complex web of relationships that have not been systematically examined before, particularly in relation to how they affect specific CSR outcomes, whether independently or in combination (Aguilera et al., 2012).

Given the burgeoning field of research on CG and CSR, some excellent reviews have been published to date. Most review studies have tackled either CG (e.g., Aguilera et al., 2015; Bebchuk & Weisbach, 2010; Dalton, Daily, Ellstrand, & Johnson, 1998; Sjöström, 2008; Terjesen, Sealy, & Singh, 2009) or CSR (e.g., Aguinis & Glavas, 2012; Carroll, 1999; Peloza, 2009; Wood, 2010), yet few are focused at the CG and CSR nexus or interface, such as Ryan (2005 and Ryan et al. (2010 who examine the inter-linkage of CG and business ethics, Welford (2007 who reviews issues related to CG and CSR in Asia; and Sparkes and Cowton (2004) who discuss the growth of socially responsible investment and its relationship with CSR.

Our endeavor is to contribute to this existing body of research in three ways. First, we undertake a systematic review of the literature (Petticrew & Roberts, 2006) that specifically examines the effect of CG mechanisms on CSR outcomes in the last decade and a half. Second, drawing on a multi-theoretical lens, we summarize the literature by identifying the various levels at which the CG mechanisms operate (i.e,, institutional, firm, group, and individual) and assess their effect on CSR outcomes. Whenever possible, we also identify the potential interactions between these multi-level mechanisms. Third, we offer critical reflections on the current state of this literature and suggest avenues for advancing research in this direction, both theoretical and methodological. We think this is a timely exercise given the rising call for adopting a "holistic approach" to CG research that examines both the effect of individual CG mechanisms as well as identifying the interdependencies between multiple governance mechanisms and their implications for CSR (Aguilera et al., 2008; Walls et al., 2012).

SCOPE OF THE REVIEW

We carry out a systematic review of relevant literature (Petticrew & Roberts, 2006) based on the content analysis of 94 peer-reviewed journal articles (81 empirical and 13 conceptual) published between 2000 and 2015 that explore the effect of various CG mechanisms on firm level CSR outcomes (see Table 1). We selected these articles using Business Source Complete and Web of Science databases and excluded book chapters, conference papers and book reviews. Although, our review encompassed the entire range of 94 articles, the empirical articles were hand-coded in two stages: first, by three graduate research assistants and second, by the first author of this paper, independently, to identify the variables associated with CG predictors of CSR at the institutional, firm, group, and individual levels of analysis and outcome variables of CSR at the firm level.

MAJOR THEORETICAL LENSES

We begin by shedding light on the core concepts of corporate governance (CG) and corporate social responsibility (CSR). As highlighted below, both CG and CSR have evolved into core managerial concepts, although there are differing interpretations as to what they entail, particularly when viewed from different theoretical perspectives.

Through our content analysis, we find that there are four main theoretical frameworks that guide empirical research at the intersection of CG and CSR. The most influential theoretical framing of CG is rooted in agency theory (Dalton, Hitt, Certo, & Dalton, 2007). Research from this perspective contends that principals (shareholders) and agents (managers and other corporate insiders) have divergent interests, risk tolerance, capacities, and information. Opportunistic managers, motivated by self-interest and guile, will act at the expense of outside investors (Jensen & Meckling, 1976), wherever there

© 2016 John Wiley & Sons Ltd

TABLE 1
List of Journals Included in the Review

Journal name	IF (2014)	Empirical	Theoretical	Total
Academy of Management Perspectives	3.354		1	1
Administrative Science Quarterly	3.333	2		2
Applied Economics Letters	.303	1		1
Business & Society	1.468	3	2	5
Business Strategy and the Environment	2.542	6	1	7
Corporate Governance: An International Review	1.734	8	2	10
Corporate Social Responsibility and Environmental Management	2.321	5	2	7
International Journal of Hospitality Management	1.939	1		1
Journal of Business Ethics	1.326	34	3	37
Journal of Business Finance & Accounting	.914	1		1
Journal of Business Research	1.480	1		1
Journal of Comparative Economics	1.170	1		1
Journal of Corporate Finance	1.193	2		2
Journal of International Business Studies	3.563	1		1
Journal of Management	6.071	3		3
Journal of Management & Organization	.594	2		2
Journal of Management Studies	3.763	1	1	2
Journal of Organizational Behavior	3.038	1		1
Management Decision	1.429	1		1
Management International Review	1.118	1		1
Quality & Quantity: International Journal of Methodology	.720	1		1
Strategic Management Journal	3.341	4		4
The Geneva Papers on Risk and Insurance-Issues and Practice	.328	1	1	2
Total		**81 (86.2%)**	**13 (13.8%)**	**94**

is an opportunity to do so. To counter this aversion, shareholders may resort to various CG mechanisms such as contractual relations, board monitoring structures, and incentives (Shleifer & Vishny, 1997). The adoption of the agency view on CG leads to acceptance of shareholder primacy with an emphasis on economic (financial) efficiency (Gill, 2008). In terms of its effect on CSR, i.e. firms' non-financial performance, agency theorists argue that CG mechanisms should be designed to ensure adoption of CSR activities only when the latter entail efficiency benefits (McWilliams & Siegel, 2001).

Challenging the contention of agency theory, institutional theorists provide an explanation for managerial behavior that defies pure economic rationality (Meyer & Rowan, 1977). Neo-institutional theory suggests that social and economic behaviors are guided by country-specific informal institutions (such as norms, customs, and traditions), which in turn manifest themselves in formal institutions (such as legal, political, and financial systems) (Hofstede, 1984; Ioannou & Serafeim, 2012; Lubatkin, Lane, Collin, & Very, 2005; Williamson, 2000). These institutions develop over time and prescribe behaviors that are legitimized in specific societies (Suchman, 1995). With regard to CSR, institutional theory contends that firms embedded in shareholder-centric CG contexts (e.g., the US) will tend to emphasize shareholder primacy over other stakeholder interests. Therefore, in such contexts, proactive CSR actions will be explicitly undertaken primarily for instrumental and strategic purposes (Matten & Moon, 2008). On the other hand, firms entrenched in pro-stakeholder CG settings (e.g., Continental Europe and Japan) adopt society-oriented strategies that align with norms and laws intended to protect the interests of multiple stakeholder entities (Brammer, Jackson, & Matten, 2012; Matten & Moon, 2008), implicitly as a matter of principle (Aguilera & Jackson, 2003).

Another theoretical perspective that has recently been applied to the CG and CSR domain is provided by the resource dependence theory (RDT) (Pfeffer & Salancik, 1978). According to RDT, firms are open systems and do not just interact with institutional forces, but also transact with each other at the firm level to gain resources needed for survival (Granovetter, 1985). This theory emphasizes the resource provision functions and abilities of the board toward improving firm performance (de Villiers et al., 2011). For example, company directors, being experts, have long-term board experience and hold influential positions in other firms as well. Consequently, they are a rich source of knowledge and guidance (Pfeffer & Salancik, 1978) and can provide critical linkages to resources and leverage social capital through their social networks (Hillman & Dalziel, 2003), enabling managers to adopt specific pro-social practices that could be value-enhancing for the firm (Bansal & Clelland, 2004; Berrone & Gomez-Mejia, 2009).

Lastly, a theoretical paradigm that prominently departs from agency theory in relation to its conceptions of CG and CSR relationship is the stakeholder theory. In contrast to the agency perspective, stakeholder theory asserts that a firm

© 2016 John Wiley & Sons Ltd

has relationships with a broader set of stakeholders, including employees, consumers, governments, environmental advocates, and others, beyond shareholders (Freeman, 1984). It acts as a guide to understand the domain of a firm's responsibilities (Jamali, 2008; Parmar, Freeman, Harrison, Wicks, Purnell, & de Colle, 2010). Drawing on this, stakeholder-agency theory (Hill & Jones, 1992) suggests that the firm has a contractual relationship with all stakeholders, with managers at the center of this nexus, given their direct control over decision making. Accordingly, CG systems must enable firms to be managed for the benefit of all their stakeholders, financial as well as non-financial (de Graaf & Stoelhorst, 2009; Windsor, 2006), with managers having a critical role to play in this regard. In terms of CSR, this view has far reaching consequences in relation to the wider spectrum of managerial responsibilities envisioned (Weber, 2014).

The variety of perspectives on offer, in addition to the soaring interest in CSR from other disciplines such as law and public policy, economics, and finance (Brammer et al., 2012) add complexity in measuring CSR outcomes. The latter are often gauged in terms of stakeholder engagement, philanthropic contributions, adoption of ethical codes, compliance with laws and mandates, impact assessment on stakeholders and the environment, extent of corporate social disclosures, rankings and ratings by third parties, and stock market indicators, among others. To capture these varied outcomes, we categorize social performance into CR (corporate responsibility targeted at multiple stakeholders), CEP (corporate environmental performance), and CR and CEP disclosures, irrespective of whether these behaviors are driven mandatorily or voluntarily. Furthermore, we adopt an inclusive approach and incorporate research based in multiple geographical contexts. Applying comparative institutionalism (Meyer & Rowan, 1977) helps us to tease out how and why the effect of CG mechanisms on CSR may differ across countries, adding to the depth of the findings we compile and present.

RESULTS OF THE MULTI-LEVEL REVIEW

This section is devoted to reviewing the literature on the multi-level corporate governance mechanisms and their impact on CSR. Figure 1 provides an overview of CG mechanisms at different levels of analysis: institutional, firm, group, and individual. We discuss the literature related to each of these levels and their implications for CSR, highlighting the main themes and findings as well as the salient underlying theoretical lens, wherever possible and appropriate.

Institutional Level

There is significant research suggesting that firm structures and strategies as well as managerial choices in relation to CSR practices and engagement cannot be fully comprehended without an understanding of the institutional environment within which firms are embedded (Luoma & Goodstein, 1999; Whitley, 1992). The institutional environment comprises formal institutions in the form of political, legal, and financial systems, as well as informal institutions such as socially valued beliefs and norms (Lubatkin et al., 2005).

Formal Institutional Mechanisms. Within the gamut of formal institutional mechanisms, we focus on two important aspects of CG, namely the nature of the political and legal system and the regulations influencing managerial discretion (see Table 2).

It is argued that the nature of the legal and political system at a country level predicts that regulations in place could promote a narrow pattern of shareholder protection versus a broader pattern of stakeholder orientation (Matten & Moon, 2008). Supporting this, our review suggests that non-US countries, typically falling within the umbrella of coordinated market economies (CME), exhibit better compliance and ratings on CSR in comparison to the US or other liberal market economies (LME) (Galbreath, 2010; Mackenzie, Rees, & Rodionova, 2013).

At the same time, CG regulations influencing managerial discretion (e.g., the market for corporate control and anti-self-dealing laws) work on the assumption that the market has the capacity to discipline managers to avoid agency conflicts. This market for corporate control can also discipline managers with respect to other stakeholder responsibilities. Specifically, poor environmental performance could lead to heavy penalties for erring firms that could prompt a fall in

FIGURE 1
Multi-Level Corporate Governance Mechanisms

Institutional Level CG Mechanisms	Firm Level CG Mechanisms	Group Level CG Mechanisms	Individual Level CG Mechanisms
Formal Institutions: Legal and Political Factors - Rule Based Versus Relation Based - Common Law vs Civil Law - LME versus CME - Anti-Self Dealing Index - Exposure to Market for Corporate Control -Regulatory Stringency *Informal Institutions:* Norms, Values and Culture - Individualism - Power Distance - Gender Gap	*Ownership Structure:* Concentrated Ownership - Institutional Shareholding (i) Pension Funds (ii) Banking and Mutual Funds (iii) Institutional Shareholder Activism - Block Owners (i) Family Owners (ii) State - Managerial/TMT Ownership (i) Inside-Owners (ii) Outside-Director Owners	*Board Structure:* - Board Size - Board Independence - CEO Duality (i) CEO Duality - Executive (CEO) Compensation (i) Base Pay/Salary (ii) Bonus (iii) Equity-Based Pay *Board Social Capital & Resource Network:* - Board Interlocking - Director Experience *Board Demography:* - Gender Diversity	*CEO Demography:* - Age - Gender - Qualification *CEO Socio-Psychological Characteristics:* - Experience - Political Ideology

 © 2016 John Wiley & Sons Ltd

TABLE 2
Institutional Level

CG mechanisms	Variables	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative/ No effect on CR/CEP disclosures
Formal institutions: *Legal* & *Political Factors*	Regulatory stringency; Anti-self-dealing index; Exposure to market for corporate control; Rule-based versus relation-based	**CEP** Gainet, 2010; Galbreath, 2010; Jo & Harjoto, 2011[a]; Mackenzie et al., 2013	**CR** Ioannou & Serafeim, 2012[a]; Kock et al., 2012	**CR** Brown et al., 2006 **CEP** Kassinis & Vafeas, 2002	**CR** Li, Fetscherin, Alon, Lattemann, & Yeh, 2010	
Informal institutions: *Norms*, *Values* & *Culture at Country Level*	Power distance; Individualism; Gender gap	**CR** Ioannou & Serafeim, 2012			**CR** Fernandez-Feijoo et al., 2014	

[a]Ioannou and Serafeim (2012) show that a decrease in managerial discretion due to adoption of anti-self-dealing index reduces CSR performance; Jo and Harjoto (2011) reveal that an increase in managerial discretion through anti-takeover measures increases CSR performance.

share prices leading to possible hostile takeovers, endangering managers' positions and reputation (King & Lenox, 2002).

Broadly, in our review we uncover that pro-shareholder laws that reduce managerial discretion tend to diminish CSR performance (Ioannou & Serafeim, 2012), while laws that increase managerial discretion (Jo & Harjoto, 2011) improve pro-social performance (see Table 2). However, it is possible that adopting stakeholder-centric regulations may prove self-defeating (Lubatkin et al., 2005) by improving CSR performance symbolically while making opportunistic behaviors more difficult to detect (see Brown et al., 2006; Jain, 2015; Kassinis & Vafeas, 2002).

Informal Institutional Mechanisms. In contrast to formal institutions, informal institutions, in the form of cultures and norms, are more finely ingrained and have a ubiquitous influence on the "character of economies" through mimetic or normative adoption of practices (Scott, 2008; Whitley, 1992: 596). A case in point are lingering differences between the US and Continental Europe pertaining to the role of business in society. While the US exhibits an individualistic culture with a higher degree of corporate discretion, reflected primarily through stewardship and philanthropic CSR, Europe has evolved as a collectivist culture that induces consensus and collaboration on CSR, invoking the participation of multiple stakeholders including political parties, labor unions and the state (Matten & Moon, 2008; Wieland, 2005).

As presented in Table 2, we find that only a few studies focus on these differences and how they affect CG systems and related CSR practices. For example, firms located in more gender equal countries were found to employ more women on boards and subsequently disclose more on CSR than firms in gender unequal countries (Fernandez-Feijoo, Romero, & Ruiz-Blanco, 2014). Furthermore, firms in countries that are more individualistic or demonstrate greater power distance adopt explicit CSR activities that are often employed as a voluntary strategic response to stakeholder expectations, whereas firms in societies that are more collectivist or have less power distance tend to assume implicit forms of CSR (Ioannou & Serafeim, 2012).

Thus, our review reveals that although formal institutional mechanisms are important to understand the configuration of CSR practices among firms, it is necessary to explore them in conjunction with prevalent informal institutions that also have a profound influence on managerial behaviors (Campbell, 2007; Jackson & Apostolakou, 2010). With evidence suggesting that pro-shareholder laws promoted in LME countries tend to undermine or attenuate CSR performance, future research should focus on the interaction effects of different types of market economies and their formal institutional structures (Kang & Moon, 2011) with the informal institutions prevalent across different contexts.

Firm Level

In this section, we present our discussion pertaining to firm-level CG mechanisms and their effect on CSR. Specifically, we focus on how concentrated block owners and their different identities such as families, state, institutions, and corporate insiders can influence firm-level CSR outcomes (see Tables 3). Theoretically, we find that there are two arguments that predict the effect of concentrated ownership on CSR (Gedajlovic & Shapiro, 1998). Following the stakeholder logic, concentrated investors will support CSR investment because the latter increases long-term firm value (Barnett, 2007; Harjoto & Jo, 2011). Alternatively, from an agency perspective, concentrated owners will stall CSR investments employed by managers for entrenchment purposes. Accordingly, the shareholder versus

© 2016 John Wiley & Sons Ltd

TABLE 3
Firm Level: Panel A

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative effect on CR/CEP disclosures	No effect on CR/CEP disclosures
Ownership structures: *Block ownership*	**CR** Jo & Harjoto, 2011; Mallin, Michelon, & Raggi, 2013	**CR** Arora & Dharwadkar, 2011; Dam & Scholtens, 2013; Rees & Rodionova, 2015; Sánchez, Sotorrío, & Díez, 2011 **CEP** Walls et al., 2012	**CEP** Chin et al., 2013; Walls et al., 2012 **CR** Brown et al., 2006; Surroca & Tribo, 2008	**CR** Prado-Lorenzo, Gallego-Alvarez, & Garcia-Sánchez, 2009	**CR** Brown et al., 2006; Ntim & Soobaroyen, 2013a, 2013b	**CR** Prado-Lorenzo et al., 2009
Ownership structures: *Family ownership*	**CR** McGuire et al., 2012 **CEP** Berrone et al., 2010	**CR** McGuire et al., 2012; Rees & Rodionova, 2015 **CEP** Mackenzie et al., 2013				
Ownership structures: *State ownership*	**CR** Chang, Li, & Lu, 2015; Li & Zhang, 2010; Surroca & Tribo, 2008 **CEP** Earnhart & Lizal, 2006; Huang, 2010	**CR** Dam & Scholtens, 2012; Zhang et al., 2010	**CR** Huang, 2010 **CEP** Mackenzie et al., 2013	**CR** Meng, Zeng, & Tam, 2013; Ntim & Soobaroyen, 2013a, 2013b; Weber, 2014		

TABLE 3
Firm Level: Panel B

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Effect on CR/CEP disclosures
Ownership structures: *Types of institutional ownership*: Pension funds	**CR** Aguilera, Williams, Conley, & Rupp, 2006; Mallin et al., 2013; Neubaum & Zahra, 2006; Oh et al., 2011		**CEP** Dam & Scholtens, 2012; Mackenzie et al., 2013 **CR** Barnea & Rubin, 2010	
Types of institutional ownership: Banking and mutual funds		**CR** Neubaum & Zahra, 2006; Aguilera et al., 2006 **CEP** Mackenzie et al., 2013	**CR** Dam & Scholtens, 2012 **CEP** Earnhart & Lizal, 2006; Walls et al., 2012	

© 2016 John Wiley & Sons Ltd

TABLE 3
Firm Level: Panel C

CG mechanisms	Variables	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative effect on CR/CEP disclosures	No effect on CR/CEP disclosures
Ownership Structures: *Managerial Ownership*	Proportion of shares held by CEOs		**CR** Arora & Dharwadkar, 2011; Deutsch & Valente, 2013	**CR** McGuire et al., 2003			**CR** Ntim & Soobaroyen, 2013a
Ownership Structures: *Managerial Ownership*	Proportion of shares held by inside-directors		**CR** McGuire et al., 2012	**CR** Borghesi et al., 2014; Rodriguez-Dominguez, Gallego-Alvarez, & Garcia-Sánchez, 2009	**CR** Deutsch & Valente, 2013	Khan, Muttakin, & Siddiqui, 2013	
			CEP Kassinis & Vafeas, 2002	**CEP** de Villiers et al., 2011 ; Kock et al., 2012; Walls et al., 2012			
Ownership Structures: *Managerial Ownership*	Proportion of shares held by TMT		**CR** Barnea & Rubin, 2010; Harjoto & Jo, 2011; Oh et al., 2011; Paek, Xiao, Lee, & Song, 2013	**CR** Paek et al., 2013			
Ownership Structures: *Outside-Director Ownership*	Proportion of shares held by independent directors	**CEP** Kock et al., 2012		**CR** Deutsch & Valente, 2013; Hafsi & Turgut, 2013; Oh et al., 2011 **CEP** de Villiers et al., 2011			

stakeholder orientation of CG will be contingent upon the shareholders' motivations and the extent of their ownership concentration.

Block Ownership. Blocks refer to a bundle of at least 5 percent or more shares in a firm. Supporting the agency logic, the majority of the studies in our review suggest (see Panel A in Table 3) that typically block owners tend to discourage proactive CSR, while complying with minimum required CSR standards to potentially avoid legitimacy risks (Arora & Dharwadkar, 2011). At the same time, block owners may differ in their CSR outlook and aspirations and more research is needed on the identity of block owners to ascertain their real motivations for CSR.

Family Ownership. Family owners are different from other forms of concentrated owners because families invest their own money in their business ventures and dominate the board (McGuire, Dow, & Ibrahim, 2012), which translates into a long-term business outlook and a concern for stakeholder relationships (Yoshikawa, Zhu, & Wang, 2014). There are three key theoretical explanations linking family ownership to CSR outcomes. From an institutional perspective, family firms may respond more normatively to responsible behaviors to preserve their socio-emotional wealth (Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007). From a resource dependence (RD) perspective, stakeholder support (both internal and external) is an important source of social capital necessary to deter legal problems associated with future succession plans (Sirmon & Hitt, 2003). In contrast, the dominance of family-centered motives may create agency conflicts and discourage CSR to maintain or advance family financial interests over other stakeholder interests. Through our review (see Panel A of Table 3), we find

© 2016 John Wiley & Sons Ltd

mixed results with family firms seen as supporting good environmental performance, even at the expense of financial gains, providing support to institutional theory arguments (Berrone, Cruz, Gomez-Mejia, & Larraza-Kintana, 2010). Other studies find support for agency arguments and a negative association of family-dominated firms with CSR (Mackenzie et al., 2013; Rees & Rodionova, 2015). This result is more pronounced in LME countries (e.g., the US) than in CME countries.

State Ownership. Our review reveals that firms with a higher proportion of state ownership are generally associated with a higher CR/CEP performance (see Panel A of Table 3). We conjecture that this supports the neo-institutional perspective, which suggests that the state has coercive powers to scrutinize and regulate firm CSR activities. Furthermore, states may push for CSR as part of an overall welfare agenda (Surroca & Tribo, 2008). However, some studies report a negative effect of state ownership on CSR. We believe that while welfare goals of the state can normally be aligned with CSR activities, it is likely that to further specific political and bureaucratic goals, states may support specific CSR activities, while avoiding others that may result in an overall decline or neutral effect on CSR performance (Zhang, Rezaee, & Zhu, 2010). Alternatively, states may separate their strategic investments in private firms from their social agendas (Dam & Scholtens, 2012).

Institutional Ownership. Institutional shareholders can have different investment horizons and possess both the incentives and the power to monitor corporate decision making (Shleifer & Vishny, 1986). In our review, we find (see Panel B in Table 3) some evidence that pension funds, with a longer-term investment horizon, support CSR investments, while banking and mutual funds, with short-term investment interests, may find the cost of engaging in CSR unjustified. However, we also find the existence of some neutral results contingent upon the presence of stakeholder activists and their motivations for supporting CSR (Lee & Lounsbury, 2011; Neubaum & Zahra, 2006) as well as the availability of organizational slack that increases managerial latitude to respond favorably to activist pressures as per the behavioral theory of the firm (Cyert & March, 1963; Wahba, 2010).

Managerial/Insider Ownership. The impact of managerial ownership on CSR can be understood from two theoretical perspectives. Following the agency logic, increased ownership activates managers' economic self-interest that reduces CSR investments. Alternatively, ownership may inspire insiders to forgo short-term profits in favor of long-term value-creating CSR strategies (Hansen & Hill, 1991; Johnson & Greening, 1999). Drawing upon managerial entrenchment and hubris arguments, managerial ownership will increase managerial discretion in decision making (Hayward & Hambrick, 1997). Although, normatively, managers ought to fulfill their moral duties (Quinn & Jones, 1995), entrenchment is generally found to promote socially irresponsible behaviors.

Our review finds no support for insider ownership encouraging CSR investments, over and above minimum compliance (Arora & Dharwadkar, 2011). We also find several studies capturing a neutral effect (see Panel C of Table 3), suggesting the salience of demographical, psychological, and ideological differences among individuals comprising top management teams (TMTs) (Chin et al., 2013) as well as the complexities of CEO–board relationships and their impact on CSR (Westphal & Zajac, 1997).

Outside-Director Ownership. Outside-directors (with ownership) have an added incentive to articulate, represent, and help enforce shareholder interests inside the board (Walsh & Seward, 1990). Only a few papers in our review explore the effects of outside-director ownership (independently of TMT) on firms' non-financial outcomes (see Panel C in Table 3). With the exception of one study (i.e,, Kock, Santaló, & Diestre, 2012), all others demonstrate that outside-director owners adopt a neutral stand vis-à-vis CSR. It is worth noting that, generally, outside-directors have low ownership stakes (de Villiers et al., 2011; Oh, Chang, & Martynov, 2011), even among large S&P firms (Hafsi & Turgut, 2013). It is likely that the voice of inside owners may overshadow that of outside-director owners in relation to CSR decisions.

On the whole, our review highlights that future research at the firm level should recognize the importance of differences in institutional and economic contexts that potentially influence the motivations of diverse firm owners toward CSR. This is particularly relevant due to institutionalization of family and state ownership in certain countries such as China and South Korea (Choi, Lee, & Park, 2013). Furthermore, beyond the traditional gamut of institutional investors, the motivations of newer categories of institutional investors, namely hedge funds, private equity firms, and sovereign wealth funds (Aguilera, Capapé, & Santiso, 2015), must be assessed. Finally, there is a need for adopting alternative methodologies such as grounded theory to make sense of the dynamics of board processes and CEO–board interactions in framing block owners' motivations for CSR.

Group Level

According to agency theory, boards are mechanisms for monitoring managers to avoid agency conflicts. At the same time, boards represent multiple stakeholder interests in the process of managerial decision making. Recent research goes beyond these two aspects and proposes that boards of directors have their own social networks and can co-opt external linkages to manage resource dependencies of firms (Granovetter, 1985; Pfeffer & Salancik, 1978). In this section, we discuss the effect of structural elements of boards and the roles played by their directors in firms' CSR decisions.

Board Structural Variables. The strength of the monitoring capability of the board is contingent on board size and board independence from managers. At the same time, CEO duality and executive compensation determine managerial power that can weaken the monitoring effect of boards. In this section, we review our findings pertaining to board structural variables and their impact on CSR (see Table 4).

Board Size and Board Independence. Agency theory contends that large-sized boards often face free-rider problems (Dalton et al., 1998) as well as coordination and communication issues (Jensen, 1993). In this scenario, there is a likelihood of boards being dominated by short-term profit-oriented

© 2016 John Wiley & Sons Ltd

TABLE 4
Group Level: Panel A

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative effect on CR/CEP disclosures	No effect on CR/CEP disclosures
BOD structure: *BOD size*	**CR** Brown et al., 2006; Hillman, Keim, & Luce, 2001; Huse et al., 2009; Jo & Harjoto, 2011	**CR** Bai, 2014; Deutsch & Valente, 2013	**CR** Hafsi & Turgut, 2013	**CR** Brown et al., 2006; Frias-Aceituno, Rodriguez-Ariza, & Garcia-Sánchez, 2013; Jizi, Salama, Dixon, & Stratling, 2014; Ntim & Soobaroyen, 2013a		**CR** Amran, Lee, & Devi, 2014; Ntim & Soobaroyen, 2013b
	CEP Ben Barka & Dardour, 2015; de Villiers et al., 2011; Galbreath, 2010; Mackenzie et al., 2013	**CEP** Kassinis & Vafeas, 2002; Walls et al., 2012; Walls & Hoffman, 2013	**CEP** Galbreath, 2011; Walls et al., 2012			
BOD structure: *BOD independence*	**CR** Choi et al., 2013; Deutsch & Valente, 2013; Fabrizi et al., 2014; Harjoto & Jo, 2011; Huang, 2010; Jo & Harjoto, 2011, 2012; Mallin et al., 2013; Rodriguez-Dominguez et al., 2009; Sánchez et al., 2011; Zhang, Zhu, & Ding, 2013	**CR** Arora & Dharwadkar, 2011; Deckop et al., 2006; Surroca & Tribo, 2008	**CR** Ben Barka & Dardour, 2015; Boulouta, 2013; Brown et al., 2006; David, Bloom, & Hillman, 2007; Deutsch & Valente, 2013; Hafsi & Turgut, 2013	**CR** Jizi et al., 2014; Khan et al., 2013; Ntim & Soobaroyen, 2013b; Sharif & Rashid, 2014	**CR** Brown et al., 2006	
	CEP de Villiers et al., 2011; Galbreath, 2011; Kock et al., 2012; Mackenzie et al., 2013	**CEP** Walls et al., 2012	**CEP** Walls et al., 2012; Walls & Hoffman, 2013		**CEP** Prado-Lorenzo & Garcia-Sánchez, 2010	

managers who can steer firms to reduce CSR investments (Walls & Hoffman, 2013). Alternatively, the neo-institutional logic and stakeholder theory predict that large boards are representative of diverse interests (Hillman & Keim, 2001; Kock et al., 2012) and can help garner CSR investments. As per the RDT, larger boards imply better social capital (Pfeffer & Salancik, 1978) and balanced decision making that can result in improved CSR performance.

Independent boards, on the other hand, help reduce agency conflicts and can ensure managerial compliance with a wider spectrum of stakeholder responsibilities (Luoma & Goodstein, 1999). Alternatively, independent directors are known to be appointed for their financial acumen and may be agents of shareholders, not stakeholders (Fligstein, 1991).

Although, in general, we find a positive association between board size and board independence and CSR outcomes, there is also some evidence of mixed results (see Panel A of Table 4). Our explanation is that structurally, board size and board independence could be endogenously determined by powerful CEOs such that their effectiveness as resource enablers and monitors could be compromised (Johnson, Schnatterly, & Hill, 2012). Other board characteristics such as board diversity and experience could also determine board orientations toward CSR (Walls et al., 2012). More importantly, it is time to move beyond a focus on structural aspects of boards, toward understanding board processes and dynamics, specifically the nature of CEO–board interactions that are more accurate proxies for both board involvement and effectiveness, and can critically influence CSR decision making (Forbes & Milliken, 1999).

CEO Duality. In this section, we focus our discussion on CEO duality and dual board leadership structures (DBLS) that we conjecture could have strong implications for managerial power and CSR (see Panel B of Table 4).

© 2016 John Wiley & Sons Ltd

TABLE 4
Group Level: Panel B

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/ CEP	Positive effect on CR/CEP disclosures	Negative effect on CR/CEP disclosures	No effect on CR/CEP disclosures
BOD structure: *CEO duality*	**CR** Bear, Rahman, & Post, 2010; Fabrizi et al., 2014; Mallin et al., 2013	**CEP** Galbreath, 2010	**CR** Bear et al., 2010; Hafsi & Turgut, 2013; Jo & Harjoto, 2011; Surroca & Tribo, 2008 **CEP** de Villiers et al., 2011; Kock et al., 2012; Mackenzie et al., 2013; Post et al., 2011; Walls et al., 2012; Walls & Hoffman, 2013	**CR** Jizi et al., 2014 **CEP** Prado-Lorenzo & Garcia-Sánchez, 2010		**CR** Khan et al., 2013; Ntim & Soobaroyen, 2013b **CEP** Prado-Lorenzo & Garcia-Sánchez, 2010

TABLE 4
Group Level: Panel C

CG mechanisms	Variables	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive/ Negative/ No effect on CR/ CEP disclosures
BOD structure: *Managerial compensation*	Proportion of base pay (fixed salary) to total compensation		**CR** Mahoney & Thorn, 2006; Manner, 2010; McGuire et al., 2003 **CEP** Kock et al., 2012	**CR** Mahoney & Thorn, 2006; McGuire et al., 2003 **CEP** Walls et al., 2012	
BOD structure: *Managerial compensation*	Proportion of bonus payments to total compensation	**CR** Callan & Thomas, 2014; Mahoney & Thorn, 2006	**CR** Deckop et al., 2006; Fabrizi et al., 2014; Manner, 2010	**CR** Mahoney & Thorn, 2006; McGuire et al., 2003 **CEP** Walls et al., 2012	
BOD structure: *Managerial compensation*	Proportion of equity-based pay to total compensation	**CR** Callan & Thomas, 2014; Deckop et al., 2006; Deutsch & Valente, 2013; Mahoney & Thorn, 2005, 2006; McGuire et al., 2003 **CEP** Kock et al., 2012	**CR** Fabrizi et al., 2014; Jiraporn & Chintrakarn, 2013; Mahoney & Thorn, 2005	**CR** Fabrizi et al., 2014; Mahoney & Thorn, 2005, 2006; Manner, 2010; McGuire et al., 2003	

CEO duality occurs when the functional role of the CEO (management) and that of the chairman (control) are vested in the same individual elevating him/her to an entrenched position within the firm (Rechner & Dalton, 1991). From an agency perspective, CEO duality leads to a concentration of managerial power (Surroca & Tribo, 2008), enabling managers to suspend CSR investments, if considered wasteful. In contrast, DBLS separates management and control, consequently

© 2016 John Wiley & Sons Ltd

enhancing boards' monitoring power (Fama & Jensen, 1983). Following RD and stakeholder theories, DBLS can improve social capital and stakeholder representation within boards to positively influence CSR (Finkelstein & Hambrick, 1990).

In our review, we find that primarily entrenched CEOs are indifferent to CSR, but when exposed to market discipline they tend to discourage CSR providing support to agency arguments. At the outset, we deem that regulations that mandate dual board leadership structures (e.g., King II recommendations and the Sarbanes-Oxley Act of 2002) might make it difficult to capture the real effect of powerful CEOs on CSR. Future research should involve studying country contexts where dual board leadership structure is a voluntary practice in order to reveal the inside dynamics. Second, temporal studies should be conducted to uncover underlying path dependencies in relation to CSR being an entrenchment strategy (Surroca & Tribo, 2008), i.e., do CSR investments lead to CEO entrenchment or are entrenched CEOs supportive of CSR? Third, the construct of CEO power (both formal and informal) could be relevant to understand the extent of CEOs' social influence over the management and board for promoting CSR investments (Walls & Berrone, 2015).

Executive Compensation. Executive compensation is a bundle of fixed compensation in the form of salary, short-term financial incentives in the form of bonuses, and long-term incentives such as equity-based pay (Frye, Nelling, & Webb, 2006). The proportions of these constituents in the total compensation package of a CEO are determinants of agency conflicts (Mackenzie, 2007; Zajac & Westphal, 1994).

Traditionally, a high proportion of base salary leads to managerial entrenchment (Hambrick & Finkelstein, 1995). One view suggests that to maintain their positions, entrenched managers may adopt a risk-averse strategy (Zajac & Westphal, 1994) and comply with minimum CSR standards (Mahoney & Thorn, 2006). At the same time, fixed pay structures are based on retrospective short-term financial goals (Mahoney & Thorn, 2006) that discourage proactive CSR (Berman, Wicks, Kotha, & Jones, 1999). Similarly, agency theory also predicts that a higher proportion of bonus payments may drive executives to focus on short-term bottom-line considerations (Stata & Maidique, 1980), leading to diminished CSR. In contrast, equity-based incentives are likely to encourage CSR by aligning managerial and shareholder interests toward long-term share value maximization (Lambert, Larcker, & Weigelt, 1993).

An alternative perspective suggests that pro-social performance requires intense managerial effort (Berrone & Gomez-Mejia, 2009) that could reduce the perceived instrumentality of pro-social performance (McGuire, Dow, & Argheyd, 2003), making the link between good social performance, reputation, and firm value indirect and weak.

From our review (see Panel C of Table 4), we find that a higher proportion of CEO salary is not positively associated with CSR; at the same time there are no clear effects of bonus and equity-based compensation on CSR performance. We suggest that this strand of literature needs to go beyond agency arguments and should consider executive pay as a means to reduce informational asymmetries while maintaining the status quo among CEOs (Capezio et al., 2011). In addition, board determination of CEO pay also necessitates an investigation into the reciprocal dynamics between boards and managers and their impact on CSR decisions (O'Reilly & Main, 2007).

Directors' Social Capital and Resource Network. Aside from the monitoring role of the board propagated by agency theory, RDT asserts that board interlocking and breadth of director experiences enhance the human and social capital of directors and influence the nature and quality of managerial–board interactions (Westphal, 1999), thereby stimulating potential adoption of CSR practices (Shropshire, 2010) (see Table 5).

In line with RDT, our review identifies mostly positive effects between board interlocks, board experience, and CSR (Glass, Cook, & Ingersoll, 2015; Kassinis & Vafeas, 2002; Walls

TABLE 5
Group Level

CG mechanisms	Variables	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive/Negative/ No effect on CR/ CEP disclosures
Director social capital and resource network: *BOD interlocking*	Number of directorship posts held by a corporate director	**CEP** Glass et al., 2015; Kassinis & Vafeas, 2002; Walls & Hoffman, 2013		**CR** Ben Barka & Dardour, 2015 **CEP** de Villiers et al., 2011	
Director social capital and resource network: *Board experience*	Seniority in board, functional experience, occupational experience	**CEP** Walls & Hoffman, 2013 **CSR** Ben Barka & Dardour, 2015			

© 2016 John Wiley & Sons Ltd

& Hoffman, 2013) with some neutral effects (de Villiers et al., 2011). Although social networks of directors have been extensively explored in the CG literature in relation to financial performance, this research is nascent in the context of firms' non-financial outcomes. As motivations are difficult to evaluate, future research could explore shareholding and compensation of interlocked directors as a proxy of their motivations. Furthermore, for boards to function well, it is important for them to be engaged in decision making without being overly unreceptive or involved (Nadler, 2004). Consequently, a U-shaped relationship between director engagement and CSR outcomes could be explored.

Directors' Demographic Diversity. Directors' demographic diversity comprises three main factors including directors' age, gender, and nationality/ethnicity. We focus our attention on the element of gender diversity in boards (see Table 6).

According to the literature on moral reasoning, early gender socialization leads to gender differences (Gilligan, 1982) such that women are more sensitive about the scenarios requiring ethical judgments (Post, Rahman, & Rubow, 2011). Therefore, gender-diverse boards should enable the representation of different stakeholder voices, leading to enhanced CSR performance and disclosures (Ntim & Soobaroyen, 2013a).

Our review supports the contention that gender diverse boards do not discourage CSR. Neutral results could be explained by invoking the critical mass theory (Kramer, Konrad, Erkut, & Hooper, 2006), which argues that women directors are typically minority directors and tend to become mere tokens for their group (Brewer & Kramer, 1985). Policy changes in some countries that encourage a minimum quota for women on boards (e.g., 40 percent in Norway, France, Spain, and the Netherlands) are likely to alleviate this problem of tokenism. While research suggests that introduction of such minimum quotas increases board effectiveness (Nielsen & Huse, 2010), their impact on CSR engagements must be researched further.

Summarizing our review of group-level CG mechanisms, we find a tendency toward positive effects of board size and board independence on CSR outcomes. No clear relationship emerges between CEO compensation and CSR, while powerful CEOs are typically found indifferent to CSR investments. We recommend that future research in this domain needs to progress beyond agency theory and structural aspects of boards toward a psychologically nuanced understanding of CEO–board interactions and reciprocity, given the rise of entrenched CEOs and a positive association between directors' social and resource networks and CSR.

Individual Level

An essential foundation of CG lies in the "personal integrity and business acumen" of executives (Cadbury, 2006). CEOs lead organizations toward value creation, but at the same time they are also individuals who vary in demographics, values, and preferences (Chin et al., 2013). Agency and stewardship theories make different assumptions about managerial motivations, particularly in relation to selecting shareholder versus stakeholder interests (Godos-Díez, Fernández-Gago, & Martínez-Campillo, 2011). While agency theory assumes managerial guile (Jensen & Meckling, 1976), stewardship theory proposes that managers can be honest individuals who can adopt pro-organizational and pro-stakeholder activities (Ghoshal, 2005; Grant & McGhee, 2014). Panels A and B of Table 7 present our review of this literature, addressing the effect of CEOs' individual characteristics, as a product of demographic and socio-psychological factors, on CSR outcomes.

CEO Demographics. We review the effect of three demographic variables on CSR – CEO age, gender, and educational specialization.

TABLE 6
Group Level

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative effect on CR/CEP disclosures	No effect on CR/CEP disclosures
Director demography: *Director's gender diversity*	**CR** Bear et al., 2010; Boulouta, 2013; Hafsi & Turgut, 2013; Mallin et al., 2013; Williams, 2003; Zhang et al., 2013		**CR** Bear et al., 2010; Boulouta, 2013	**CR** Fernandez-Feijoo et al., 2014; Frias-Aceituno et al., 2013; Ntim & Soobaroyen, 2013a		**CR** Amran et al., 2014; Ntim & Soobaroyen, 2013b
	CEP Glass et al., 2015; Post et al., 2011; Walls et al., 2012		**CEP** Galbreath, 2011; Post et al., 2011; Walls et al., 2012	**CEP** Prado-Lorenzo & Garcia-Sánchez, 2010		**CEP** Prado-Lorenzo & Garcia-Sánchez, 2010

© 2016 John Wiley & Sons Ltd

TABLE 7
Individual Level: Panel A

CG mechanisms	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Positive effect on CR/CEP disclosures	Negative/ No effect on CR/ CEP disclosures
CEO demographics: *CEO age*	**CR** Slater & Dixon-Fowler, 2009	**CR** Borghesi et al., 2014	**CR** Fabrizi et al., 2014; Huang, 2013; Slater & Dixon-Fowler, 2009		
CEO demographics: *CEO gender*	**CR** Borghesi et al., 2014; Huang, 2013; Manner, 2010		**CR** Rodriguez-Dominguez et al., 2009 **CEP** Glass et al., 2015		
CEO demographics: *CEO qualification*	**CR** Huang, 2013; Manner, 2010	**CR** Manner, 2010	**CR** Manner, 2010	**CEP** Lewis et al., 2014	

TABLE 7
Individual Level: Panel B

CG mechanisms	Variables	Positive effect on CR/CEP	Negative effect on CR/CEP	No effect on CR/CEP	Effect on CR/CEP disclosures
CEO socio-psychological characteristics: *CEO experience*	Functional experience, occupational experience, international experience	**CR** Manner, 2010; Slater & Dixon-Fowler, 2009		**CR** Manner, 2010; Slater & Dixon-Fowler, 2009	
CEO socio-psychological characteristics: *CEO political inclination*	Liberal or conservative value, CEOs' political contributions	**CR** Borghesi et al., 2014; Chin et al., 2013			

From a moral reasoning perspective, older CEOs have a greater moral capacity to support pro-social behaviors (Kets de Vries & Miller, 1984). In addition, career paths invigorate critical implications for pro-social decisions. Newer and younger CEOs are judged by the market in relation to their capacity to deliver financial results (Fabrizi, Mallin, & Michelon, 2014). Accordingly, as CEOs get older, they may be less pressured by career goals and more willing to give back to society. In our review, we find inconclusive results in this realm. We suggest that instead of linear relationships, future research should look at interactive relationships between age and experience and their collective impact on CSR. This is particularly relevant given the rise of younger but widely experienced CEOs in certain industries (Forbes, 2013).

As discussed earlier, gender socialization theory predicts that women CEOs should be better able to pursue CSR than men CEOs (Brammer, Millington, & Pavelin, 2007). Scholarship on gender and leadership contends that women leaders tend to be more innovative and egalitarian in their view of firm strategy and consequently more long-term and stakeholder focused (Glass et al., 2015). Although, in our review, women CEOs do not discourage CSR, recent research suggests that men CEOs are just as likely to strengthen CSR as women CEOs (see Glass et al., 2015). Clearly, the relationship between the CEO's gender and pro-social decision making is more complex than previously assumed. We conjecture that it is likely that there is not much difference between men and women's decision-making behaviors at the highest levels of authority. Second, diversity, rather than homophily, among and between TMT may be more effective in promoting pro-social behavior (Cox, Lobel, & McLeod, 1991). Finally, diversity and homophily may have different effects on social and environmental decisions when they are broken down into proactive decisions and risk-averse compliance decisions (Glass et al., 2015; Johansen & Pettersson, 2013).

The educational background of CEOs potentially contains complex yet important cues for decision-making behaviors (Hambrick & Mason, 1984). Borrowing from this strand of literature, executives' educational background could also influence their pro-

© 2016 John Wiley & Sons Ltd

social orientations (see Finkelstein, Hambrick, & Cannella, 2009). For example, psychology and sociology involve the study of human behavior where cooperative problem-solving models are more recognized (Davis, Schoorman, & Donaldson, 1997). Consequently, CEOs with this background may be better at appreciating the benefits of stakeholder management. In a similar vein, CEOs with MBAs are said to have greater human capital, and are more adept at strategic decision making (Finkelstein et al., 2009). On the other hand, CEOs with a legal background are likely to be cautious, conservative, and risk averse (Delmas & Toffel, 2008; Lewis, Walls, & Dowell, 2014). Accordingly, CEOs with MBA degrees may look at voluntary CSR more proactively than those with a legal background, who will be more inclined toward compliance-based CSR.

Our review concurs that educational differences in CEO backgrounds could lead to differences in firms' CSR outcomes as predicted above (see Panel A of Table 7). This has important implications for universities and curriculum design decisions. Specifically, the question of why business ethics continues to be conspicuously absent within a conventional business or economics curriculum (Manner, 2010) needs to be revisited. Another promising research area that emerges at the individual level is the effect of racial, gender, ethnic and/or national diversity in leadership positions on CSR. Research in this direction is largely lacking (except Huang, 2013) and assumes relevance given the rise of non-white, immigrant, and women CEOs, at least in the Silicon Valley (Forbes, 2015).

Socio-Psychological Characteristics. In this section, we review two variables to gauge CEOs' socio-psychological characteristics: CEO political ideologies and CEO past experience (see Panel B of Table 7). Political psychologists suggest that executives vary in their political ideologies (Francia, Green, Herrnson, Powell, & Wilcox, 2005), which could impact their CSR decision making. Through our review of research in this field, we find that specifically in the US, liberalist CEOs tend to believe in economic equality and social justice and are more likely to be sensitive to diversity, human rights, and environmental issues (Schwartz, 1996). On the other hand, conservative CEOs tend to value individualism and free markets and are more inclined to focus on business goals over social needs (Schwartz, 1996).

Upper echelons research suggests that executives' experiences can also affect their world view and consequently their strategic CSR choices (Hambrick & Mason, 1984). We find that past work experience that involves processing complex and dynamic information and deriving innovative solutions to complex problems may enable executives to better understand the relevance of CSR from a long-term value-generation perspective (e.g., Manner, 2010; Slater & Dixon-Fowler, 2009).

This domain of work is still new and intriguing. Whereas, the personal values of some CEOs reflect on their patterns of political donations (Chin et al., 2013), for others such donations are a means to enhance political connections often overriding personal ideologies (see Borghesi et al., 2014). Given the increasing involvement of business in politics and recent regulations that have abolished limits on political donations (such as in the US) (Liptak, 2014), more research is called for to understand the extent to which individual values matter for CSR and the degree to which CEOs are willing to circumvent other CG mechanisms to uphold those values.

To conclude, our review at the individual level has focused on CEO demographics and socio-psychological characteristics and their effect on CSR. We suggest that future research in this sphere needs to move beyond linear relationships and emphasize interactive relationships between CEO age and experience; to focus on the importance of diversity, rather than homophily, in TMTs with respect to gender, educational background, and experience; and to broaden the contextual scope of this research beyond the US into other political systems, given the increasing involvement of businesses in political CSR globally (Scherer & Palazzo, 2011). Furthermore, research into individual-level characteristics of CEOs should consider the impact of board structures and processes to highlight the degree to which CSR conforms with CEOs' personal moral compass and value preferences.

DISCUSSION AND DIRECTIONS FOR FUTURE RESEARCH

In this paper, we attempt to look inside the black box of CG-CSR research and critically assess the impact of multiple CG mechanisms on firms' CSR outcomes. Our study highlights that theoretically there is a strong case for CG as an antecedent of CSR and promising patterns are beginning to emerge in the literature. Simultaneously, the empirical evidence remains mixed and inconclusive in some areas. This is understandable, however, given that research at the CG-CSR interface is still emerging. Clear-cut comparative assessments of existing research remain challenging in view of the diversity of theoretical and methodological perspectives adopted, the multiplicity of CG mechanisms operating at different levels of analysis, and the fact that models in the literature vary in terms of their comprehensiveness in including all relevant variables and controls. While we acknowledge these limitations, we also believe that they provide exciting opportunities to advance research in this important field.

The review presented in this paper constitutes a first step in documenting the effects of different CG mechanisms on CSR. Our review suggests that CG variables are often interdependent and interactively shape or create specific CSR outcomes for the firm (Aguilera & Williams, 2009). We propose that in addition to furthering research at the different levels of analysis (i.e,, institutional, firm, group, and individual), scholars must espouse a holistic approach where mechanisms associated with different levels of CG are seen as interacting, i.e., substituting, complementing, or overriding others, to form bundles and configurations of governance practices that in turn influence CSR outcomes. Hence, our review highlights the need to rethink CG mechanisms as bundles rather than piecemeal and to account for the influence of formal/informal, internal/external and structural/psychological dimensions of governance antecedents on CSR outcomes. Our review makes clear that these nuanced considerations of CG are beginning to emerge in the literature, with increasing scholarship directed at teasing apart the tension between financial and non-financial goals of corporations thus challenging traditional agency arguments. Although nascent and fragmented, this scholarship is likely to shape the field in substantively new directions in the future. Keeping the above in mind, we identify four vital areas for future research in relation to CG-CSR interfaces.

© 2016 John Wiley & Sons Ltd

Multi-level Analysis

In this section we tease out some examples that accentuate the need for multi-level research in the field of CG-CSR. The extant literature at the firm level focuses on the different investment horizons and motives of concentrated owners and their impact on CSR. Group-level research focuses on diversity (specifically gender diversity) in boards being supportive of CSR. While existing research on these phenomena is commendable, there are some questions that remain unanswered. For example, if block owners are driven solely by their investment horizons and motives, will they adopt the same behaviors across different geographical locations? Why are diverse boards not as widespread given the general outcry for equality and socially responsible behaviors and why do some firms embrace board gender diversity more readily than others? We conjecture that the institutional environment in which firms are embedded holds the key to some of these questions. In fact, prevalent research demonstrates that firms embedded in shareholder-oriented LME countries perceive CSR activities as provision of public goods by appropriating private capital as opposed to firms embedded in stakeholder-oriented CG systems in CME countries. Similarly, countries that are more gender equal, as a result of informal institutions, tend to reflect greater gender diversity on boards (Fernandez-Feijoo et al., 2014). Hence, agency or stakeholder orientations of shareholder entities could at least partially be the result of the country context in which owners are embedded (e.g., Mackenzie et al., 2013; Rees & Rodionova, 2015). In view of these observations, we recommend that future research needs to focus on *nested CG structures* at different levels such that concentrated owners and board structures are viewed as nested within an institutional environment that influences their CSR aspirations.

To take another example, CG structures at the institutional and board levels are typically designed to curtail managerial entrenchment, hence restricting managerial discretion to safeguard shareholder interests (Hambrick & Finkelstein, 1995; Surroca & Tribo, 2008). Yet managerial discretion is pertinent for conceiving and implementing CSR decisions that involve balancing the interests of investing and non-investing stakeholders. Therefore, CG structures intended to restrict managerial entrenchment position shareholder interests as diametrically opposed to other stakeholder interests, while painting all managers as inherently opportunistic (Ghoshal, 2005). This is akin to falling within the agency trap that, as substantial literature corroborates, takes a rather simplistic view of the business world (Judge, 2008). We believe that research could draw more systematically from the literature at the individual level, which suggests that CEOs' demography and socio-psychological experiences may shape their world view, informing their ideological stance toward ethics and responsibility (Manner, 2010). Future research needs to also consider the multiple-levels that promote reciprocal dynamics between boards and managers and the knowledge and experiential diversity of boards that could significantly impact CSR outcomes (Glass et al., 2015; Huse, Nielsen, & Hagen, 2009; Westphal & Milton, 2000).

Disaggregating CSR Variables

There are different ways in which aggregation has been introduced in CG-CSR research. The impact of CG drastically differs when CSR is considered as a composite construct as compared to when CSR is broken down into people and product dimensions, environmental performance, and CSR weaknesses and strengths (e.g., Mahoney & Thorn, 2006). Firm responses to CEP may be different from other CSR investments as the former is more technical and strategic (Bansal, Gao, & Qureshi, 2014; Kock et al., 2012). Negative CSR or CSR concerns are conceptually different and interpreted as "bad" events that receive a different response from firms than positive CSR or CSR strengths (Chatterji, Levine, & Toffel, 2009; Jamali, Lund-Thomsen, & Khara, 2015; Mattingly & Berman, 2006). Thus, individual CSR elements can capture differences in firms' social orientations (Jain, 2015), emphasizing the need to use precise and disaggregate measures of CSR in future research.

Beyond Existing Theories

Theoretically, there are different directions in which research at the intersection of CG-CSR can forge ahead. One way is to adopt a behavioral strategy approach towards CG and tease out the socio-psychological aspects of management and boards affecting CSR (Chin et al., 2013; Manner, 2010). Another course is to focus on internal and external governance mechanisms (Aguilera et al., 2015) or formal and informal dimensions of CG (Ioannou & Serafeim, 2012) and how each informs the other while collectively influencing CSR decision making. As research progresses to analyze these underlying complexities, there is a growing appreciation that this sort of nuanced understanding may not be fully captured through a single theoretical lens (Finkelstein & Hambrick, 1996). As the newer conception of CG gains traction by emphasizing both financial and non-financial performance of firms (Gill, 2008), recent research draws on multiple theoretical lenses to explain CSR behaviors such as a combination of agency and institutional arguments to explain the effect of stock compensation of outside-directors on CSR (e.g., Deutsch & Valente, 2013) and an amalgam of agency and RD theories to analyze the impact of ownership and board characteristics on CSR (Ntim & Soobaroyen, 2013a). We believe this is a step in the right direction.

In addition, newer theories could also offer insights guiding future research directions. At the group level, the RD perspective emphasizes the importance of board network ties and the diffusion of knowledge and practices through board networks. This is likely to expand the roles of the boards beyond monitors of managerial decision making to counselors and advisors (Forbes & Milliken, 1999). Following the team production theory, directors could also be viewed as mediating entities that balance the divergent claims of different interest groups (Lan & Heracleous, 2010) by evoking trust, instead of solely safeguarding the interest of shareholders. Therefore, future research could draw from sociology and socio-psychology theories such as role theory, and from team production and stewardship theories for better understanding and documenting the expanding roles of boards toward representing multiple stakeholder groups and positively influencing firm CSR behaviors.

© 2016 John Wiley & Sons Ltd

Addressing Methodological Issues

Despite the proliferation of research in the field of CG-CSR, causality still remains elusive. The majority of the studies test association, but not causality. To shed more light on the precise nature of the relationship between CG and CSR, it is imperative for researchers to use extensive data sets, longer time series analysis, lagged models for testing CSR antecedents, and to remove or alleviate the endogeneity bias. Most of the problems in CG-CSR research stem from the fact that several firm-level CG structures are not exogenously determined but rather are affected by unobserved firm characteristics (Johnson et al., 2012). Therefore, future research should strive to model the determinants of CG structures above and beyond testing their effects on CSR.

Part of this problem could also be addressed by experimenting with more sophisticated research methods. Conventional empirical methods, such as linear regression models, that assume independence amongst explanatory factors, do not appropriately capture the complex interactive relationships that we have identified in this paper. In addition, the focus in such models is more on how much variation in CSR is explained by different CG variables, and not on how the different CG variables combine to explain specific CSR outcomes (Aguilera & Williams, 2009). Future research could benefit from the use of innovative methods such as fuzzy sets (Ragin, 2008) that focus on the idea of equifinality, suggesting that there is no one best Pareto optimal practice of CG that could improve firms' CSR performance (Aguilera & Williams, 2009). Moreover, decision tree analysis could be explored to frame nested CG antecedents of CSR.

Finally, to gain a better understanding of the dynamics of board functioning and processes, particularly interpretation of external CG mechanisms by corporate insiders, CEO–board interactions, and the influence of board interlocking, qualitative methods such as grounded theory and alternative theoretical lenses such as sensemaking and sensegiving (Gioia & Chittipeddi, 1991; Walls & Hoffman, 2013) should be adopted. These are likely to offer deeper insights that can in turn enhance our understanding of the linkages between CG and CSR.

CONCLUSION

Through our review, we set out to identify CG mechanisms at four levels of analysis, namely the institutional, firm, group, and individual levels, that independently and interactively impact firm-level CSR outcomes. This investigation is both timely and needed given the complex affinities of CG and CSR and increasing calls to better understand and leverage them (Jamali, Safieddine, & Rabbath, 2008; Kang & Moon, 2011). Our review uncovers that although both CG and CSR are growing independently into mature disciplines, research at the intersection of CG-CSR is still emerging.

The wide scope of our review possibly leaves the reader with more questions than answers. However, we have taken an important first step in terms of teasing out the relationships that lie at the intersection of CG and CSR, consolidating existing knowledge in this domain, and outlining a concrete agenda for guiding future research. We assert that these are important areas for both organizational and non-organizational stakeholders and we invite more research to refine our understanding of the CG-CSR interface.

ACKNOWLEDGEMENTS

We would like to acknowledge the helpful suggestions that we received from the Guest Editor Hicheon Kim and one anonymous reviewer during the process of developing this manuscript. We are extremely grateful to Ruth Aguilera, Jill Brown, and Javier Capapé for their in-depth reviews and thoughts on various versions and iterations of this paper. We would also like to thank Andrew Millington and Kathleen Rehbein for their constructive comments on an earlier version during the manuscript development session at IABS (2015). Words of appreciation to our three graduate assistants, Edwina Zoghbi, Farah Rayes, and Nadine Mohanna, for their help in initial content analysis and coding of the articles. The first author would like to thank M.M. Kumar for his insights on the topic and his review of our work.

REFERENCES

Aguilera, R. V., Capapé, J., & Santiso, J. 2015. Sovereign wealth funds: A strategic governance view, ***Academy of Management Perspectives***. DOI:10.5465/amp.2013.0055.

Aguilera, R. V., Desender, K., Bednar, M. K., & Lee, J. H. 2015. Connecting the dots: Bringing external corporate governance into the corporate governance puzzle, ***The Academy of Management Annals***, 9: 483–573.

Aguilera, R. V., Filatotchev, I., Gospel, H., & Jackson, G. 2008. An organizational approach to comparative corporate governance: Costs, contingencies, and complementarities, ***Organization Science***, 19: 475–92.

Aguilera, R. V., Goyer, M., & Kabbach-Castro, L. R. 2012. Regulation and comparative corporate governance. In M. Wright, D. S. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***The Oxford handbook of corporate governance***: 23–45. Oxford: Oxford University Press.

Aguilera, R. V. & Jackson, G. 2003. The cross-national diversity of corporate governance: Dimensions and determinants, ***Academy of Management Review***, 28: 447–65.

Aguilera, R. V. & Williams, C. A. 2009. 'Law and finance': Inaccurate, incomplete, and important, ***Brigham Young University Law Review***, 6: 1413–34.

Aguilera, R. V., Williams, C. A., Conley, J. M., & Rupp, D. E. 2006. Corporate governance and social responsibility: A comparative analysis of the UK and the US, ***Corporate Governance: An International Review***, 14: 147–58.

Aguinis, H. & Glavas, A. 2012. What we know and don't know about corporate social responsibility: A review and research agenda, ***Journal of Management***, 38: 932–68.

Amran, A., Lee, S. P., & Devi, S. S. 2014. The influence of governance structure and strategic corporate social responsibility toward sustainability reporting quality, ***Business Strategy and the Environment***, 23: 217–35.

Aoki, M. 2000. ***Information, corporate governance, and institutional diversity: Competitiveness in Japan, the USA, and the transnational economies***. Oxford: Oxford University Press.

Arora, P. & Dharwadkar, R. 2011. Corporate governance and corporate social responsibility (CSR): The moderating roles of attainment discrepancy and organization slack, ***Corporate Governance: An International Review***, 19: 136–52.

© 2016 John Wiley & Sons Ltd

Bai, G. 2014. How do board size and occupational background of directors influence social performance in for-profit and non-profit organizations? Evidence from California hospitals, ***Journal of Business Ethics***, 118: 171–87.
Bansal, P. & Clelland, I. 2004. Talking trash: Legitimacy, impression management, and unsystematic risk in the context of the natural environment, ***Academy of Management Journal***, 47: 93–103.
Bansal, P., Gao, J., & Qureshi, I. 2014. The extensiveness of corporate social and environmental commitment across firms over time, ***Organization Studies***, 35: 949–66.
Barnea, A. & Rubin, A. 2010. Corporate social responsibility as a conflict between shareholders, ***Journal of Business Ethics***, 97: 71–86.
Barnett, M. L. 2007. Stakeholder influence capacity and the variability of financial returns to corporate social responsibility, ***Academy of Management Review***, 32: 794–816.
Bear, S., Rahman, N., & Post, C. 2010. The impact of board diversity and gender composition on corporate social responsibility and firm reputation, ***Journal of Business Ethics***, 97: 207–21.
Bebchuk, L. A. & Weisbach, M. S. 2010. The state of corporate governance research, ***Review of Financial Studies***, 23: 939–61.
Ben Barka, H. & Dardour, A. 2015. Investigating the relationship between director's profile, board interlocks and corporate social responsibility, ***Management Decision***, 53: 553–70.
Berle, A. & Means, G. 1932. ***The modern corporation and private property***. New York: Macmillan.
Berman, S., Wicks, A., Kotha, S., & Jones, T. 1999. Does stakeholder orientation matter? The relationship between stakeholder management models and firm financial performance, ***Academy of Management Journal***, 42: 488–506.
Berrone, P., Cruz, C., Gomez-Mejia, L. R., & Larraza-Kintana, M. 2010. Socioemotional wealth and corporate responses to institutional pressures: Do family-controlled firms pollute less? ***Administrative Science Quarterly***, 55: 82–113.
Berrone, P. & Gomez-Mejia, L. 2009. Environmental performance and executive compensation: An integrated agency-institutional perspective, ***Academy of Management Journal***, 52: 103–26.
Borghesi, R., Houston, J. F., & Naranjo, A. 2014. Corporate socially responsible investments: CEO altruism, reputation, and shareholder interests, ***Journal of Corporate Finance***, 26: 164–81.
Boulouta, I. 2013. Hidden connections: The link between board gender diversity and corporate social performance, ***Journal of Business Ethics***, 113: 185–97.
Brammer, S., Jackson, G., & Matten, D. 2012. Corporate social responsibility and institutional theory: New perspectives on private governance, ***Socio-Economic Review***, 10: 3–28.
Brammer, S., Millington, A., & Pavelin, S. 2007. Gender and ethnic diversity among UK corporate boards, ***Corporate Governance: An International Review***, 15: 393–403.
Brewer, M. B. & Kramer, R. M. 1985. The psychology of intergroup attitudes and behavior, ***Annual Review of Psychology***, 36: 219–43.
Brown, W. O., Helland, E., & Smith, J. K. 2006. Corporate philanthropic practices, ***Journal of Corporate Finance***, 12: 855–77.
Cadbury, A. 2006. Corporate social responsibility, ***Twenty-First Century Society***, 1: 5–21.
Callan, S. J. & Thomas, J. M. 2014. Relating CEO compensation to social performance and financial performance: Does the measure of compensation matter? ***Corporate Social Responsibility and Environmental Management***, 21: 202–27.
Campbell, J. L. 2007. Why would corporations behave in socially responsible ways? An institutional theory of corporate social responsibility, ***Academy of Management Review***, 32: 946–67.
Capezio, A., Shields, J., & O'Donnell, M. 2011. Too good to be true: Board structural independence as a moderator of CEO pay for firm performance, ***Journal of Management Studies***, 48: 487–513.
Carroll, A. B. 1999. Corporate social responsibility: Evolution of a definitional construct, ***Business & Society***, 38: 268–95.
Chang, L., Li, W., & Lu, X. 2015. Government engagement, environmental policy, and environmental performance: Evidence from the most polluting Chinese listed firms, ***Business Strategy and the Environment***, 24: 1–19.
Chatterji, A. K., Levine, D. I., & Toffel, M. W. 2009. How well do social ratings actually measure corporate social responsibility? ***Journal of Economics & Management Strategy***, 18: 125–69.
Chin, M. K., Hambrick, D. C., & Treviño, L. K. 2013. Political ideologies of CEOs: The influence of executives' values on corporate social responsibility, ***Administrative Science Quarterly***, 58: 197–232.
Choi, B. B., Lee, D., & Park, Y. 2013. Corporate social responsibility, corporate governance and earnings quality: Evidence from Korea, ***Corporate Governance: An International Review***, 21: 447–67.
Cordeiro, J. J. & Sarkis, J. 2008. Does explicit contracting effectively link CEO compensation to environmental performance? ***Business Strategy and the Environment***, 17: 304–17.
Cox, P., Brammer, S., & Millington, A. 2008. Pension funds and corporate social performance: An empirical analysis, ***Business & Society***, 47: 213–41.
Cox, T., Lobel, S. A., & McLeod, P. L. 1991. Effects of ethnic group cultural differences on cooperative and competitive behavior on a group task, ***Academy of Management Journal***, 4: 827–47.
Cyert, R. M. & March, J. G. 1963. ***A behavioral theory of the firm***. Englewood Cliffs, NJ: Prentice-Hall.
Dalton, D. R., Daily, C. M., Ellstrand, A. E., & Johnson, J. L. 1998. Meta-analytic reviews of board composition, leadership structure, and financial performance, ***Strategic Management Journal***, 19: 269–90.
Dalton, D. R., Hitt, M. A., Certo, S. T., & Dalton, C. M. 2007. The fundamental agency problem and its mitigation: Independence, equity, and the market for corporate control, ***Academy of Management Annals***, 1: 1–64.
Dam, L. & Scholtens, B. 2012. Does ownership type matter for corporate social responsibility? ***Corporate Governance: An International Review***, 20: 233–52.
Dam, L. & Scholtens, B. 2013. Ownership concentration and CSR policy of European multinational enterprises, ***Journal of Business Ethics***, 118: 117–26.
David, P., Bloom, M., & Hillman, A. J. 2007. Investor activism, managerial responsiveness, and corporate social performance, ***Strategic Management Journal***, 28: 91–100.
Davis, J. H., Schoorman, F. D., & Donaldson, L. 1997. Toward a stewardship theory of management, ***Academy of Management Review***, 22: 20–48.
de Graaf, F. J. & Stoelhorst, W. 2009. The role of governance in corporate social responsibility: Lessons from Dutch finance, ***Business & Society***, 52: 282–317.
de Villiers, C., Naiker, V., & van Staden, C. J. 2011. The effect of board characteristics on firm environmental performance, ***Journal of Management***, 37: 1636–63.
Deckop, J. R., Merriman, K. K., & Gupta, S. 2006. The effects of CEO pay structure on corporate social performance, ***Journal of Management***, 32: 329–42.
Delmas, M. A. & Toffel, M. W. 2008. Organizational responses to environmental demands: Opening the black box, ***Strategic Management Journal***, 29: 1027–55.
Deutsch, Y. & Valente, M. 2013. Compensating outside directors with stock: The impact on non-primary stakeholders, ***Journal of Business Ethics***, 116: 67–85.
Donaldson, T. & Preston, L. E. 1995. The stakeholder theory of the corporation: Concepts, evidence, and implications, ***Academy of Management Review***, 20: 65–91.
Earnhart, D. & Lizal, L. 2006. Effects of ownership and financial performance on corporate environmental performance, ***Journal of Comparative Economics***, 34: 111–29.
Eesley, C., Decelles, K. A., & Lenox, M. 2015. Through the mud or in the boardroom: Examining activist types and their strategies in

© 2016 John Wiley & Sons Ltd

targeting firms for social change, ***Strategic Management Journal***. DOI:10.1002/smj.2458.
Elkington, J. 2006. Governance for sustainability, ***Corporate Governance: An International Review***, 14: 522–9.
Fabrizi, M., Mallin, C., & Michelon, G. 2014. The role of CEO's personal incentives in driving corporate social responsibility, ***Journal of Business Ethics***, 124: 311–26.
Fama, E. & Jensen, M. 1983. Separation of ownership and control, ***The Journal of Law and Economics***, 26: 301–26.
Fernandez-Feijoo, B., Romero, S., & Ruiz-Blanco, S. 2014. Women on boards: Do they affect sustainability reporting? ***Corporate Social Responsibility and Environmental Management***, 21: 351–64.
Finkelstein, S. & Hambrick, D. C. 1990. Top management-team tenure and organizational outcomes: The moderating role of managerial discretion, ***Administrative Science Quarterly***, 35: 484–503.
Finkelstein, S. & Hambrick, D. C. 1996. ***Strategic leadership: Top executives and their effects on organizations***. Mason, OH: South-Western Publishing.
Finkelstein, S., Hambrick, D. C., & Cannella, A. A. 2009. ***Strategic leadership: Theory and research on executives, top management teams, and boards***. Oxford: Oxford University Press.
Fligstein, N. 1991. The structural transformation of American industry: An institutional account of the causes of diversification in the largest firms, 1919–1979. In W. W. Powell & P. J. DiMaggio (Eds.), ***The new institutionalism in organizational analysis***: 311–36. Chicago, IL: University of Chicago Press.
Forbes 2013. America's Most Promising CEOs Under 35. Forbes, February 6. Available at: http://www.forbes.com/sites/jjcolao/2013/02/06/americas-most-promising-ceos-under-35/ (accessed January 10, 2016).
Forbes 2015. CEOs of Silicon Valley's top firms are often non-white, immigrants, or women. Forbes, August 15. Available at: http://www.forbes.com/sites/gregoryferenstein/2015/08/14/ceos-of-silicon-valleys-top-firms-are-often-non-white-immigrants-or-women-in-1-graph/ (accessed January 10, 2016).
Forbes, D. P. & Milliken, F. J. 1999. Cognition and corporate governance: Understanding boards of directors as strategic decision-making groups, ***Academy of Management Review***, 24: 489–505.
Francia, P. L., Green, J. C., Herrnson, P. S., Powell, L. W., & Wilcox, C. 2005. Limousine liberals and corporate conservatives: The financial constituencies of the democratic and republican parties, ***Social Science Quarterly***, 86: 761–78.
Freeman, R. E. 1984. ***Strategic management: A stakeholder approach***. Boston, MA: Pitman.
Frias-Aceituno, J. V., Rodriguez-Ariza, L., & Garcia-Sánchez, I. M. 2013. The role of the board in the dissemination of integrated corporate social reporting, ***Corporate Social Responsibility and Environmental Management***, 20: 219–33.
Frye, M. B., Nelling, E., & Webb, E. 2006. Executive compensation in socially responsible firms, ***Corporate Governance: An International Review***, 14: 446–55.
Gainet, C. 2010. Exploring the impact of legal systems and financial structure on corporate responsibility, ***Journal of Business Ethics***, 95: 195–222.
Galbreath, J. 2010. Corporate governance practices that address climate change: An exploratory study, ***Business Strategy and the Environment***, 19: 335–50.
Galbreath, J. 2011. Are there gender-related influences on corporate sustainability? A study of women on boards of directors, ***Journal of Management & Organization***, 17: 17–38.
Gedajlovic, E. R. & Shapiro, D. M. 1998. Management and ownership effects: Evidence from five countries, ***Strategic Management Journal***, 19: 533–53.
Ghoshal, S. 2005. Bad management theories are destroying good management practices, ***Academy of Management Learning & Education***, 4: 75–91.
Gill, A. 2008. Corporate governance as social responsibility: A research agenda, ***Berkeley Journal of International Law***, 26: 452–78.
Gilligan, C. 1982. ***In a different voice: Psychological theory and women's development***. Cambridge, MA: Harvard University Press.
Gioia, D. A. & Chittipeddi, K. 1991. Sensemaking and sensegiving in strategic change initiation, ***Strategic Management Journal***, 12: 433–48.
Glass, C., Cook, A., & Ingersoll, A. R. 2015. Do women leaders promote sustainability? Analyzing the effect of corporate governance composition on environmental performance, ***Business Strategy and the Environment***. DOI:10.1002/bse.1879.
Godos-Díez, J. L., Fernández-Gago, R., & Martínez-Campillo, A. 2011. How important are CEOs to CSR practices? An analysis of the mediating effect of the perceived role of ethics and social responsibility, ***Journal of Business Ethics***, 98: 531–48.
Gómez-Mejía, L. R., Haynes, K. T., Núñez-Nickel, M., Jacobson, K. J., & Moyano-Fuentes, J. 2007. Socioemotional wealth and business risks in family-controlled firms: Evidence from Spanish olive oil mills, ***Administrative Science Quarterly***, 52: 106–37.
Goranova, M. & Ryan, L. V. 2014. Shareholder activism: A multidisciplinary review, ***Journal of Management***, 40: 1230–68.
Granovetter, M. 1985. Economic action and social structure: The problem of embeddedness, ***American Journal of Sociology***, 91: 481–510.
Grant, P. & McGhee, P. 2014. Corporate governance reform: Character building structures, ***Business Ethics: A European Review***, 23: 125–138.
Graves, S. B. & Waddock, S. A. 1994. Institutional owners and corporate social performance, ***Academy of Management Journal***, 37: 1034–46.
Hafsi, T. & Turgut, G. 2013. Boardroom diversity and its effect on social performance: Conceptualization and empirical evidence, ***Journal of Business Ethics***, 112: 463–79.
Hambrick, D. C. & Finkelstein, S. 1995. The effects of ownership structure on conditions at the top: The case of CEO pay raises, ***Strategic Management Journal***, 16: 175–94.
Hambrick, D. C. & Mason, P. A. 1984. Upper echelons: The organization as a reflection of its top managers, ***Academy of Management Review***, 9: 193–206.
Hansen, G. S. & Hill, C. W. 1991. Are institutional investors myopic? A time series study of four technology driven industries, ***Strategic Management Journal***, 12: 1–16.
Harjoto, M. A. & Jo, H. 2011. Corporate governance and CSR nexus, ***Journal of Business Ethics***, 100: 45–67.
Hayward, M. L. & Hambrick, D. C. 1997. Explaining the premiums paid for large acquisitions: Evidence of CEO hubris, ***Administrative Science Quarterly***, 42: 103–27.
Hill, C. W. L. & Jones, T. M. 1992. Stakeholder-agency theory, ***Journal of Management Studies***, 29: 131–54.
Hillman, A. J. & Dalziel, T. 2003. Boards of directors and firm performance: Integrating agency and resource dependence perspectives, ***Academy of Management Review***, 28: 383–96.
Hillman, A. J. & Keim, G. D. 2001. Shareholder value, stakeholder management, and social issues: What's the bottom line? ***Strategic Management Journal***, 22: 125–39.
Hillman, A. J., Keim, G. D., & Luce, R. A. 2001. Board composition and stakeholder performance: Do stakeholder directors make a difference? ***Business & Society***, 40: 295–314.
Hofstede, G. 1984. ***Culture's consequences: International differences in work-related values***. London: Sage Publications.
Huang, C. J. 2010. Corporate governance, corporate social responsibility and corporate performance, ***Journal of Management & Organization***, 16: 641–55.
Huang, S. K. 2013. The impact of CEO characteristics on corporate sustainable development, ***Corporate Social Responsibility and Environmental Management***, 20: 234–44.
Huse, M., Nielsen, S. T., & Hagen, I. M. 2009. Women and employee-elected board members, and their contributions to board control tasks, ***Journal of Business Ethics***, 89: 581–97.

© 2016 John Wiley & Sons Ltd

Ioannou, I. & Serafeim, G. 2012. What drives corporate social performance? The role of nation-level institutions, ***Journal of International Business Studies***, 43: 834–64.
Jackson, G. & Apostolakou, A. 2010. Corporate social responsibility in Western Europe: An institutional mirror or substitute? ***Journal of Business Ethics***, 94: 371–94.
Jain, T. 2015. Decoupling corporate social orientations: A cross-country analysis, ***Business & Society***. DOI:10.1177/0007650315610609.
Jamali, D. 2008. A stakeholder approach to CSR, ***Journal of Business Ethics***, 82: 213–31.
Jamali, D., Lund-Thomsen, P., & Khara, N. 2015. CSR institutionalized myths in developing countries: An imminent threat of selective decoupling, ***Business & Society***. DOI:10.1177/0007650315584303.
Jamali, D., Safieddine, A., & Rabbath, M. 2008. Corporate governance and corporate social responsibility: Synergies and interrelationships, ***Corporate Governance: An International Review***, 16: 443–59.
Jensen, M. C. 1993. The modern industrial revolution, exit, and the failure of internal control systems, ***The Journal of Finance***, 48: 831–80.
Jensen, M. C. & Meckling, W. H. 1976. Theory of the firm: Managerial behaviour, agency costs and ownership structure, ***Journal of Financial Economics***, 3: 305–60.
Jiraporn, P. & Chintrakarn, P. 2013. Corporate social responsibility (CSR) and CEO luck: Are lucky CEOs socially responsible? ***Applied Economics Letters***, 20: 1036–9.
Jizi, M. I., Salama, A., Dixon, R., & Stratling, R. 2014. Corporate governance and corporate social responsibility disclosure: Evidence from the US banking sector, ***Journal of Business Ethics***, 125: 601–15.
Jo, H. & Harjoto, M. A. 2011. Corporate governance and firm value: The impact of corporate social responsibility, ***Journal of Business Ethics***, 103: 351–83.
Jo, H. & Harjoto, M. A. 2012. The causal effect of corporate governance on corporate social responsibility, ***Journal of Business Ethics***, 106: 53–72.
Johansen, T. R. & Pettersson, K. 2013. The impact of board interlocks on auditor choice and audit fees, ***Corporate Governance: An International Review***, 21: 287–310.
Johnson, R. A. & Greening, D. W. 1999. The effects of corporate governance and institutional ownership types on corporate social performance, ***Academy of Management Journal***, 42: 564–76.
Johnson, S. G., Schnatterly, K., & Hill, A. D. 2012. Board composition beyond independence: Social capital, human capital, and demographics, ***Journal of Management***, 39: 232–62.
Judge, W. Q. 2008. What is the dependent variable in corporate governance research? ***Corporate Governance: An International Review***, 16: ii.
Kang, N. & Moon, J. 2011. Institutional complementarity between corporate governance and corporate social responsibility: A comparative analysis of three capitalisms, ***Socio-Economic Review***, 10: 85–108.
Kassinis, G. & Vafeas, N. 2002. Corporate boards and outside stakeholders as determinants of environmental litigation, ***Strategic Management Journal***, 23: 399–415.
Kets de Vries, M. F. & Miller, D. 1984. Neurotic style and organizational pathology, ***Strategic Management Journal***, 5: 35–55.
Khan, A., Muttakin, M. B., & Siddiqui, J. 2013. Corporate governance and corporate social responsibility disclosures: Evidence from an emerging economy, ***Journal of Business Ethics***, 114: 207–23.
King, A. & Lenox, M. 2002. Exploring the locus of profitable pollution reduction, ***Management Science***, 48: 289–99.
Kock, C. J., Santaló, J., & Diestre, L. 2012. Corporate governance and the environment: What type of governance creates greener companies? ***Journal of Management Studies***, 49: 492–514.
Kramer, V. W., Konrad, A. M., Erkut, S., & Hooper, M. J. 2006. ***Critical mass on corporate boards: Why three or more women enhance governance***. Wellesley, MA: Wellesley Centers for Women.
Lambert, R. A., Larcker, D. F., & Weigelt, K. 1993. The structure of organizational incentives, ***Administrative Science Quarterly***, 38: 438–61.
Lan, L. L. & Heracleous, L. 2010. Rethinking agency theory: The view from law, ***Academy of Management Review***, 35: 294–314.
Lee, M. D. P. & Lounsbury, M. 2011. Domesticating radical rant and rage: An exploration of the consequences of environmental shareholder resolutions on corporate environmental performance, ***Business & Society***, 50: 155–88.
Lewis, B. W., Walls, J. L., & Dowell, G. W. S. 2014. Difference in degrees: CEO characteristics and firm environmental disclosure, ***Strategic Management Journal***, 35: 712–22.
Li, S., Fetscherin, M., Alon, I., Lattemann, C., & Yeh, K. 2010. Corporate social responsibility in emerging markets, ***Management International Review***, 50: 635–54.
Li, W. & Zhang, R. 2010. Corporate social responsibility, ownership structure, and political interference: Evidence from China, ***Journal of Business Ethics***, 96: 631–45.
Liptak, A. 2014. Supreme court strikes down overall political donation cap. New York Times, April 2. Available at: http://www.nytimes.com/2014/04/03/us/politics/supreme-court-ruling-on-campaign-contributions.html?_r=0 (accessed January 10, 2016).
Lubatkin, M. H., Lane, P. J., Collin, S. O., & Very, P. 2005. Origins of corporate governance in the USA, Sweden and France, ***Organization Studies***, 26: 867–88.
Luoma, P. & Goodstein, J.. 1999. Stakeholders and corporate boards: Institutional influences on board composition and structure, ***Academy of Management Journal***, 42: 553–63.
Mackenzie, C. 2007. Boards, incentives and corporate social responsibility: The case for a change of emphasis, ***Corporate Governance: An International Review***, 15: 935–43.
Mackenzie, C., Rees, W., & Rodionova, T. 2013. Do responsible investment indices improve corporate social responsibility? FTSE4Good's impact on environmental management, ***Corporate Governance: An International Review***, 21: 495–512.
Mahoney, L. S. & Thorn, L. 2005. Corporate social responsibility and long-term compensation: Evidence from Canada, ***Journal of Business Ethics***, 57: 241–53.
Mahoney, L. S. & Thorn, L. 2006. An examination of the structure of executive compensation and corporate social responsibility: A Canadian investigation, ***Journal of Business Ethics***, 64: 149–62.
Mallin, C. A., Michelon, G., & Raggi, D. 2013. Monitoring intensity and stakeholders' orientation: How does governance affect social and environmental disclosure? ***Journal of Business Ethics***, 114: 29–43.
Manner, M. H. 2010. The impact of CEO characteristics on corporate social performance, ***Journal of Business Ethics***, 93: 53–72.
Matten, D. & Moon, J. 2008. "Implicit" and "explicit" CSR: A conceptual framework for a comparative understanding of corporate social responsibility, ***Academy of Management Review***, 33: 404–24.
Mattingly, J. E. & Berman, S. L. 2006. Measurement of corporate social action: Discovering taxonomy in the Kinder Lydenburg Domini ratings data, ***Business & Society***, 45: 20–46.
McGuire, J., Dow, S., & Argheyd, K. 2003. CEO incentives and corporate social performance, ***Journal of Business Ethics***, 45: 341–59.
McGuire, J., Dow, S., & Ibrahim, B. 2012. All in the family? Social performance and corporate governance in the family firm, ***Journal of Business Research***, 65: 1643–50.
McWilliams, A. & Siegel, D. 2001. Corporate social responsibility: A theory of the firm perspective, ***Academy of Management Review***, 26: 117–27.
Meng, X. H., Zeng, S. X., & Tam, C. M. 2013. From voluntarism to regulation: A study on ownership, economic performance and

© 2016 John Wiley & Sons Ltd

corporate environmental information disclosure in China, ***Journal of Business Ethics***, 116: 217–32.
Meyer, J. W. & Rowan, B. 1977. Institutionalized organizations: Formal structure as myth and ceremony, ***American Journal of Sociology***, 83: 340–63.
Nadler, D. A. 2004. Building better boards, ***Harvard Business Review***, 82: 102–5.
Neubaum, D. O. & Zahra, S. A. 2006. Institutional ownership and corporate social performance: The moderating effects of investment horizon, activism, and coordination, ***Journal of Management***, 32: 108–31.
Nielsen, S. & Huse, M. 2010. The contribution of women on boards of directors: Going beyond the surface, ***Corporate Governance: An International Review***, 18: 136–48.
Ntim, C. G. & Soobaroyen, T. 2013a. Black economic empowerment disclosures by South African listed corporations: The influence of ownership and board characteristics, ***Journal of Business Ethics***, 116: 121–38.
Ntim, C. G. & Soobaroyen, T. 2013b. Corporate governance and performance in socially responsible corporations: New empirical insights from a neo-institutional framework, ***Corporate Governance: An International Review***, 21: 468–94.
OECD. 2004. ***Corporate governance, frequently asked questions about the OECD Principles of Corporate Governance***. Paris: OECD.
Oh, W. Y., Chang, Y. K., & Martynov, A. 2011. The effect of ownership structure on corporate social responsibility: Empirical evidence from Korea, ***Journal of Business Ethics***, 104: 283–97.
O'Reilly, C. A. & Main, B. G. 2007. Setting the CEO's pay: It's more than simple economics, ***Organizational Dynamics***, 36: 1–12.
Paek, S., Xiao, Q., Lee, S., & Song, H. 2013. Does managerial ownership affect different corporate social responsibility dimensions? An empirical examination of US publicly traded hospitality firms, ***International Journal of Hospitality Management***, 34: 423–33.
Parmar, B. L., Freeman, R. E., Harrison, J. S., Wicks, A. C., Purnell, L., & de Colle, S. 2010. Stakeholder theory: The state of the art, ***Academy of Management Annals***, 4: 403–45.
Peloza, J. 2009. The challenge of measuring financial impacts from investments in corporate social performance, ***Journal of Management***, 35: 1518–41.
Petticrew, M. & Roberts, H. 2006. How to appraise the studies: An introduction to assessing study quality. In ***Systematic reviews in the social sciences: A practical guide***: 125–63. Oxford: Blackwell Publishing.
Pfeffer, J. & Salancik, G. R. 1978. ***The external control of organizations: A resource dependence perspective***. New York: Harper & Row.
Post, C., Rahman, N., & Rubow, E. 2011. Green governance: Boards of directors' composition and environmental corporate social responsibility, ***Business & Society***, 50: 189–223.
Prado-Lorenzo, J. M., Gallego-Alvarez, I., & Garcia-Sánchez, I. M. 2009. Stakeholder engagement and corporate social responsibility reporting: The ownership structure effect, ***Corporate Social Responsibility and Environmental Management***, 16: 94–107.
Prado-Lorenzo, J. M. & Garcia-Sánchez, I. M. 2010. The role of the board of directors in disseminating relevant information on greenhouse gases, ***Journal of Business Ethics***, 97: 391–424.
Quinn, D. P. & Jones, T. M. 1995. An agent morality view of business policy, ***Academy of Management Review***, 20: 22–42.
Ragin, C. C. 2008. ***Redesigning social inquiry: Fuzzy sets and beyond***. Chicago, IL: University of Chicago Press.
Rechner, P. L. & Dalton, D. R. 1991. CEO duality and organizational performance: A longitudinal analysis, ***Strategic Management Journal***, 12: 155–60.
Rees, W. & Rodionova, T. 2015. The influence of family ownership on corporate social responsibility: An international analysis of publicly listed companies, ***Corporate Governance: An International Review***, 23: 184–202.
Rockefeller 2010. ***Scenarios for the future of technology and international development***. New York: The Rockefeller Foundation and Global Business Network.
Rodriguez-Dominguez, L., Gallego-Alvarez, I., & Garcia-Sánchez, I. M. 2009. Corporate governance and codes of ethics, ***Journal of Business Ethics***, 90: 187–202.
Ryan, L. V. 2005. Corporate governance and business ethics in North America: The state of the art, ***Business & Society***, 44: 40–73.
Ryan, L. V., Buchholtz, A. K., & Kolb, R. W. 2010. New directions in corporate governance and finance: Implications for business ethics research, ***Business Ethics Quarterly***, 20: 673–94.
Sánchez, J. L. F., Sotorrío, L. L., & Díez, E. B. 2011. The relationship between corporate governance and corporate social behavior: A structural equation model analysis, ***Corporate Social Responsibility and Environmental Management***, 18: 91–101.
Scherer, A. G. & Palazzo, G. 2011. The new political role of business in a globalized world: A review of a new perspective on CSR and its implications for the firm, governance, and democracy, ***Journal of Management Studies***, 48: 899–931.
Schwartz, S. 1996. Value priorities and behavior: Applying a theory of integrated value systems. In U. C. Seligman, J. M. Olson, & M. P. Zanna (Eds.), ***The psychology of values: The Ontario Symposium***, vol. 8: 1–24. Hillsdale, NJ: Erlbaum.
Scott, W. R. 2008. Approaching adulthood: The maturing of institutional theory, ***Theory and Society***, 37: 427–42.
Serwer, A. 2009. The '00s: Goodbye (at last) to the decade from hell. Time, November 24. Available at: http://content.time.com/time/magazine/article/0,9171,1942973,00.html (accessed January 10, 2016).
Sharif, M. & Rashid, K. 2014. Corporate governance and corporate social responsibility (CSR) reporting: An empirical evidence from commercial banks (CB) of Pakistan, ***Quality & Quantity: International Journal of Methodology***, 48: 2501–21.
Shleifer, A. & Vishny, R. W. 1986. Large shareholders and corporate control, ***The Journal of Political Economy***, 94: 461–88.
Shleifer, A. & Vishny, R. W. 1997. A survey of corporate governance, ***The Journal of Finance***, 52: 737–83.
Shropshire, C. 2010. The role of the interlocking director and board receptivity in the diffusion of practices, ***Academy of Management Review***, 35: 246–64.
Sirmon, D. G. & Hitt, M. A. 2003. Managing resources: Linking unique resources, management, and wealth creation in family firms, ***Entrepreneurship Theory and Practice***, 27: 339–58.
Sjöström, E. 2008. Shareholder activism for corporate social responsibility: What do we know? ***Sustainable Development***, 16: 141–54.
Slater, D. J. & Dixon-Fowler, H. R. 2009. CEO international assignment experience and corporate social performance, ***Journal of Business Ethics***, 89: 473–89.
Sparkes, R. & Cowton, C. J. 2004. The maturing of socially responsible investment: A review of the developing link with corporate social responsibility, ***Journal of Business Ethics***, 52: 45–57.
Stata, R. & Maidique, M. A. 1980. Bonus system for balanced strategy, ***Harvard Business Review***, 58: 156–63.
Stout, B. A. 2012. ***Handbook of energy for world agriculture***. New York: Elsevier Applied Science.
Suchman, M. C. 1995. Managing legitimacy: Strategic and institutional approaches, ***Academy of Management Review***, 20: 571–610.
Surroca, J. & Tribo, J. A. 2008. Managerial entrenchment and corporate social performance, ***Journal of Business Finance & Accounting***, 35: 748–89.
Terjesen, S., Sealy, R., & Singh, V. 2009. Women directors on corporate boards: A review and research agenda, ***Corporate Governance: An International Review***, 17: 320–37.
Wahba, H. 2010. How do institutional shareholders manipulate corporate environmental strategy to protect their equity value? A study of the adoption of ISO 14001 by Egyptian firms, ***Business Strategy and the Environment***, 19: 495–511.

© 2016 John Wiley & Sons Ltd

Walls, J. L. & Berrone, P. 2015. The power of one to make a difference: How informal and formal CEO power affect environmental sustainability, ***Journal of Business Ethics***. DOI:10.1007/s10551-015-2902-z.

Walls, J. L., Berrone, P., & Phan, P. H. 2012. Corporate governance and environmental performance: Is there really a link? ***Strategic Management Journal***, 33: 885–913.

Walls, J. L. & Hoffman, A. J. 2013. Exceptional boards: Environmental experience and positive deviance from institutional norms, ***Journal of Organizational Behavior***, 34: 253–71.

Walsh, J. P. & Seward, J. K. 1990. On the efficiency of internal and external corporate control mechanisms, ***Academy of Management Review***, 15: 421–58.

Weber, O. 2014. Environmental, social and governance reporting in China, ***Business Strategy and the Environment***, 23: 303–17.

Welford, R. 2007. Corporate governance and corporate social responsibility: Issues for Asia, ***Corporate Social Responsibility and Environmental Management***, 14: 42–51.

Westphal, J. D. 1999. Collaboration in the boardroom: Behavioral and performance consequences of CEO-board social ties, ***Academy of Management Journal***, 42: 7–24.

Westphal, J. D. & Milton, L. P. 2000. How experience and network ties affect the influence of demographic minorities on corporate boards, ***Administrative Science Quarterly***, 45: 366–98.

Westphal, J. D. & Zajac, E. J. 1997. Defections from the inner circle: Social exchange, reciprocity, and the diffusion of board independence in US corporations, ***Administrative Science Quarterly***, 42: 161–83.

Whitley, R. 1992. ***Business systems in East Asia: Firms, markets and societies***. London: Sage.

Wieland, J. 2005. Corporate governance, values management, and standards: A European perspective, ***Business & Society***, 44: 74–93.

Williams, R. J. 2003. Women on corporate boards of directors and their influence on corporate philanthropy, ***Journal of Business Ethics***, 42: 1–10.

Williamson, O. E. 2000. The new institutional economics: Taking stock, looking ahead, ***Journal of Economic Literature***, 38: 595–613.

Windsor, D. 2006. Corporate social responsibility: Three key approaches, ***Journal of Management Studies***, 43: 93–114.

Wood, D. J. 2010. Measuring corporate social performance: A review, ***International Journal of Management Reviews***, 12: 50–84.

Yoshikawa, T., Zhu, H., & Wang, P. 2014. National governance system, corporate ownership, and roles of outside directors: A corporate governance bundle perspective, ***Corporate Governance: An International Review***, 22: 252–65.

Zajac, E. J. & Westphal, J. D. 1994. The costs and benefits of managerial incentives and monitoring in large U.S. corporations: When is more not better? ***Strategic Management Journal***, 15: 121–42.

Zhang, R., Rezaee, Z., & Zhu, J. 2010. Corporate philanthropic disaster response and ownership type: Evidence from Chinese firms' response to the Sichuan earthquake, ***Journal of Business Ethics***, 91: 51–63.

Zhang, J. Q., Zhu, H., & Ding, H. 2013. Board composition and corporate social responsibility: An empirical investigation in the post Sarbanes-Oxley era, ***Journal of Business Ethics***, 114: 381–92.

Tanusree Jain is a PhD in Management Sciences at ESADE Business School. Her research is focused on comparative corporate social responsibility and corporate governance. She received the Founder's Award for Emerging Scholar of Business Ethics by the Society for Business Ethics (SBE) in 2013. Her research has been published in *Business & Society* and *Journal of Business Ethics*, and she regularly presents her work at the Academy of Management, SBE and IABS conferences. Prior to her PhD, she was an Assistant Professor of Teaching in Business Ethics and CSR at the University of Delhi.

Dima Jamali is Professor in the Olayan School of Business, American University of Beirut and currently holding the Kamal Shair Chair in Responsible Leadership. She has a PhD in Social Policy and Administration from the University of Kent at Canterbury, UK. Her research and teaching revolve primarily around corporate social responsibility (CSR). She is the author/editor of three books (*CSR in the Middle East* – Palgrave, 2012; *Social Entrepreneurship in the Middle East* – Palgrave, 2015; and *Development-Oriented CSR* – Greenleaf, 2015), and over 55 international publications, focusing on different aspects of CSR in developing countries in general and in the Middle East region specifically. She is the winner of the Aspen Institute Faculty Pioneer Award, 2015.

© 2016 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 274–302

Business Groups and Corporate Governance: Review, Synthesis, and Extension

Andrea Colli and Asli M. Colpan*

ABSTRACT

Manuscript Type: Review
Research Question/Issue: This article addresses the diverse and fragmented literature about the corporate governance of business groups. We collected scholarly work on the subject, proposed a conceptualization of the main research questions they addressed, classified them according to their research themes, and identified future research directions.
Research Findings/Insights: Academic research on corporate governance in business groups has been increasing but is still a developing field. Available analyses make use of the main theoretical frameworks in general in corporate governance research. However, there are several areas of analysis that still need stronger conceptualization and empirical work, leaving many opportunities for future studies and a pressing need to substantiate and extend the findings of previous studies.
Theoretical/Academic Implications: Our study identifies four avenues for future research on corporate governance in business groups. This includes the examination of the complex relationships and co-evolutionary processes among corporate governance attributes, and organizational and performance outcomes of business groups; the effects of ownership goals on groups' performance outcomes; the role and the actual functioning of boards inside business groups; and the analyses of cross-national comparison and long-term development of the governance of business groups.
Practitioner/Policy Implications: This research allows practitioners and policymakers to get a better understanding of the crucial areas regarding business groups and their governance, and offers pathways to examine inside the "black-box" of business groups.

Keywords: Corporate Governance, Business Groups, Family Ownership, Ownership Mechanisms, Board Composition

INTRODUCTION

Business groups are broadly defined as the amalgamation of legally-independent companies through various formal and informal ties (Granovetter, 1995, 2005; Khanna & Yafeh, 2007). They have been the dominant form of large enterprise in many emerging markets (Colpan, Hikino, & Lincoln, 2010; Khanna & Palepu, 2010), but they are also important players in a number of developed markets as well (Colpan & Hikino, 2016; Shiba & Shimotani, 1997). While there has been an increasing number of studies on business groups, especially in the last two decades, from various perspectives including management, sociology, and business history, generally focusing on specific areas/countries (Barbero & Jacob, 2008; Feenstra & Hamilton, 2006; Jones, 2000; Kock & Guillén, 2001; Tripathi, 2004), there has not been much work done to organize the governance attributes of business groups into a systematized conceptual framework through the synthesis of the available literature. This paper aims to fill this research gap through an extensive review of the management literature, and proposes a future research agenda that will contribute to our understanding of the issue.

Research on business groups considers governance to be a relevant topic, and a greater part of management research emphasizes an *instrumental* perspective of business groups (i.e., "what do they exist for?") rather than an *operational* one ("how do they *really* work?"). Business groups have basically been examined in their nature as concrete alternatives to the multidivisional enterprise (Colpan & Hikino, 2010). A relevant emphasis has been put on the country-specific attributes that determine the existence and survival of this organizational form, with inconclusive results (Whittington & Mayer, 2000). In particular, given the alleged superiority of the M (multidivisional)-form as an efficient organizational artifact, the persistence of business groups – otherwise sometimes labeled as H (holding)-form – in developed economies has been ascribed to residual imperfections. These imperfections could be in the capital markets (resulting in disproportionate incentives to leverage) and/or in the persistence of concentrated ownership structures (incentivizing leverage as well; Faccio & Lang, 2002). The ultimate perversity of business groups – in this perspective – was additionally that they basically coincided with an extractive attitude by dominant shareholders toward minority shareholders (Johnson, La Porta, Lopez-de-Silanes, & Shleifer, 2000). The (negative) view of

*Address for correspondence: Asli M. Colpan, Graduate School of Management, Kyoto University, Yoshida-Honmachi, Kyoto, Japan 606-8501. Tel/fax: +81 75 7533517; E-mail: colpan@gsm.kyoto-u.ac.jp

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12144

business groups as a bundle of control-enhancing mechanisms contrasts with the more positive one, which, as mentioned above, considers them as efficient solutions in the case of market imperfections (especially in the context of developing economies).

Notwithstanding the available evidence at the "micro-organizational" level derived from in-depth case studies, business historians were also not attentive in providing a governance-oriented theory of business groups. National cases in which they constituted (and still are) a persisting feature of the corporate landscape have been examined mainly from an instrumental perspective. Research about Italy, where business groups are a permanent feature of the corporate landscape in almost every sector (Colli, Rinaldi, & Vasta, 2015) has in fact emphasized how business groups brilliantly solve the problems linked to the need by founders and families to keep firm control over expanding businesses (Aganin & Volpin, 2005; Amatori, 1997). Other scholars have shown in detail how, particularly in the case of state-owned companies, the business group served as an effective way to flexibly expand the boundaries of the concern in order to achieve goals of political-economic nature (Amatori, 1997; Colli & Vasta, 2015). Japanese business historians have emphasized the continuity between pre- and post-war corporate structures of large firms showing how groups allowed balancing family interests with managerial control, at the same time avoiding the threat of hostile takeovers (Morikawa, 1992). Similar considerations have been put forward for other European (Barca & Becht, 2001) and Asian countries (Amsden, 2001), characterized by an overwhelming diffusion of business groups. The instrumental perspective has, in any case, been prevalent over the operational one.

A research perspective emphasizing the governance-related aspects internal to the organization can better highlight the operational nature of business groups. Further, the topic of group governance is important and deserves a systematic review for two reasons. First, governance of business groups is different from, and more complex than, the governance of stand-alone firms due to various multiplex ties among group firms (Holmes, Hoskisson, Wam, & Holcomb, 2015; Manikandan & Ramachandran, 2015; Yiu et al., 2013). The characteristic control and coordination mechanisms in business groups therefore necessitate a closer examination to understand their functioning and organizational/performance consequences. Second, and relatedly, it has been shown that these distinctive control mechanisms, especially the pyramidal structures, are used extensively by wealthy families who have been entrusted a critical degree of the large enterprises' corporate governance in many countries (outside the US and UK). As such, the characteristic governance of these groups that control large proportions of their countries' economies may have important consequences, such as *economic entrenchment* retarding economic growth (Morck, Wolfenzon, & Yeung, 2005). This potential influence of business groups in their economies makes the examination of their governance even more pressing. In particular, as we will further discuss below, a large bulk of the literature in the field of corporate finance has emphasized a peculiar set of potential threats to minority shareholders, which derive from the extractive attitudes of controlling owners in "tunneling out" of the companies belonging to the group in excess of their cash-flow rights.

In light of this background, the aim of this study is twofold: to review and integrate the previous research on corporate governance of business groups, and propose future research directions to study the governance of business groups through identifying weaknesses and limitations in the extant literature. We adopt a broad definition of corporate governance for the purpose of this paper as 'the way in which corporations are owned, controlled, and coordinated and set their goals.' In this perspective, as our focus of analysis is business groups, we concentrate on and disentangle the characteristic governance attributes of business groups based on group ownership and the intra-group control and coordination devices in a group; namely the equity ties, director interlocks, and other ties. Our perspective focuses on the relationship between corporate governance attributes (as defined above, and in their turn largely determined by the institutional and historical features of the environment), and on their impact on the strategic and structural behavior of companies and subsequently on their performance.

This paper differentiates itself from previous studies on the subject in three dimensions. First, we aim to synthesize the business group governance literature around an organizing framework. In doing so, we especially focus on the relationships between group-related aspects of governance, including group ownership and intra-group control and coordination devices, as well as organizational and performance outcomes of such governance mechanisms. Second, we conduct an extensive literature review by identifying all the published literature in 30 leading journals on the subject. This kind of extensive review is beneficial to build an exhaustive picture of the literature. It is also helpful to find the gaps in the existing research to direct us to future analysis. Finally, this paper incorporates the business history research on business groups, which examines their evolution over a long period of time to have a cross-national and longitudinal coverage. This research orientation affects the reference material we analyze for this paper, which has ranged from journal articles in different fields of governance, management, strategy, organization, and finance as well as business history, to volumes and handbooks published on the topic, with specific reference to governance issues as defined above.

We begin by examining the evolution of the business group research and the different perspectives in it, in order to identify the state of the literature. In the next section, we aim to identify the research themes in the governance literature that relate to business groups. An important purpose here is to provide a comprehensive framework of the governance of business group research. In this section, the literature is assessed and the empirical outcomes of the past research are laid out. This section incorporates the theoretical and empirical research related to the governance of business groups. Finally, we propose an agenda for future studies.

EVOLUTION OF THE BUSINESS GROUP RESEARCH AND CORPORATE GOVERNANCE

The roots of the theoretical and systematic examination of business groups go back to Nathaniel Leff (1976, 1978). Since then, the business group literature has evolved in emphasizing four

© 2015 John Wiley & Sons Ltd

different factors to explain the emergence and development of business groups. The first comes from the economics literature, where business groups are seen as a response to market imperfections (Ghemawat & Khanna, 1998; Leff, 1978). The second comes from political science, which emphasizes the industrial policy instruments and links between policymakers and local entrepreneurs to explain the formation of groups (Kim, 2010; Schneider, 2010). Third, the management literature looks at the specific resources and capabilities of the entrepreneurs and within business groups to describe their development (Colpan & Hikino, 2010; Guillén, 2010). Last but not least, the corporate finance literature looks at business groups of the pyramidal variety as examples of growth processes dominated by leverage strategies, put in place when dominant shareholders aim to expand their companies with a limited investment of internal capital. As mentioned above, this conduct is largely aiming at the exploitation of minority shareholders (Morck, 2010). While these theories aim to underpin the emergence and development of business groups in certain national settings, they have implications for the strategies, structures as well as governance of business groups.

Nonetheless, the systematic examination of the theoretical and empirical underpinnings on the governance of business groups still remains underdeveloped, as also stressed by Boyd and Hoskisson (2010) and more recently by Yiu, Chen, and Xu (2013).[1] The most prevalent theories in the field of corporate governance are thus to be adapted to the interpretation of business groups; probably some of them are to be dismissed, and new ones are to be proposed. Building on and extending the two works mentioned above, we highlight four main governance theoretical streams helpful in the interpretation of business groups, and emphasizing in particular the ownership structure and the role of boards. Those are agency theory, stewardship theory, resource dependence theory, and institutional theory, which we found commonly employed in the studies that we examined in this paper. Below we briefly identify the critical aspects of each theoretical stream as well as their relevance to business groups.

Agency Theory

Probably the most consolidated theory in the field of corporate governance, agency theory (Jensen & Meckling, 1976) holds some relevance in the case of business groups. However, since this theory has been basically crafted to explain the existence and behavior of corporate boards in Anglo-Saxon-like firms, conventionally characterized by diffuse and silent ownership, it has to be adapted to the different setting of business groups with concentrated ownership. This means that the standard agency has to be adapted to the new situation, far less common in Anglo-Saxon countries, but quite standard elsewhere, of an endemic conflict between majority and minority shareholders, which came to be known as the "principal-principal" perspective in the literature (Dharwadkar, George, & Brandes, 2000; Young, Peng, Ahlstrom, Bruton, & Jiang, 2008). A detailed example of the application of agency theory to business groups is provided in Cuervo-Cazurra, 2006.

Stewardship Theory

Another theory of principal-agent relationships in the corporate environment contests the "egotist" view characteristic of agency theory (Davis, Schoorman, & Donaldson, 1997; Donaldson & Davis, 1991). Not surprisingly, stewardship theory has gained acceptance in those capitalist environments characterized by a close identification between managers and owners. Stewardship theory has in fact gained a broad acceptance in family business studies. In the case of business groups, particularly the family-owned ones, this approach appears to be quite relevant. Assuming that the group's affiliated companies are frequently owned by a family holding, and managed by family members, it is possible to assume that they would behave as responsible "stewards" for the other family members not directly involved in the management of the affiliated companies.

Resource Dependence Theory

While both agency and stewardship theories tend to see the boards as a way to manage the relationship between managers and shareholders, another stream of research considers boards as the way in which "firms interact with, and are affected by, their external environments" (Boyd & Hoskisson, 2010: 673). This interaction is carried on through a dense web of board members that allow the firm to achieve strategic information from outside. This view is particularly relevant in the case of business groups, where executives multiply their relations, and information retrieval opportunities, for the *n* companies belonging to the group. At the same time, board members act as means of diffusion of this information *inside* the group itself through the contacts they have with other executives.

Institutional Theory

The other theoretical framework that deserves mention is institutional theory. Like other organizational forms, business groups are the product of, and the efficient response to, a specific institutional environment. This perspective, which has been emphasized by scholars of emerging market firms (Chang & Hong, 2002; Khanna & Palepu, 2000; Khanna & Yafeh, 2007), stresses basically how business groups tend to flourish in particular institutional environments. In terms of corporate governance research, the institutional perspective suggests that institutional environment and the changes in that environment influence the governance practices of business groups. An example of past research along this line, for instance, is the effects of institutional changes in the aftermath of the Asian financial crisis on the transparency and accountability of business groups (Chang, 2006; Kim, 2010).

ORGANIZING FRAMEWORK AND ANALYSIS OF PAST RESEARCH

We integrate the research themes with regard to corporate governance and business groups building on the analysis of the extant literature. We concentrate on the salient business group-related aspects of governance and examine group ownership and intra-group devices for control and coordination. We then examine how these attributes are linked to organizational and performance outcomes.

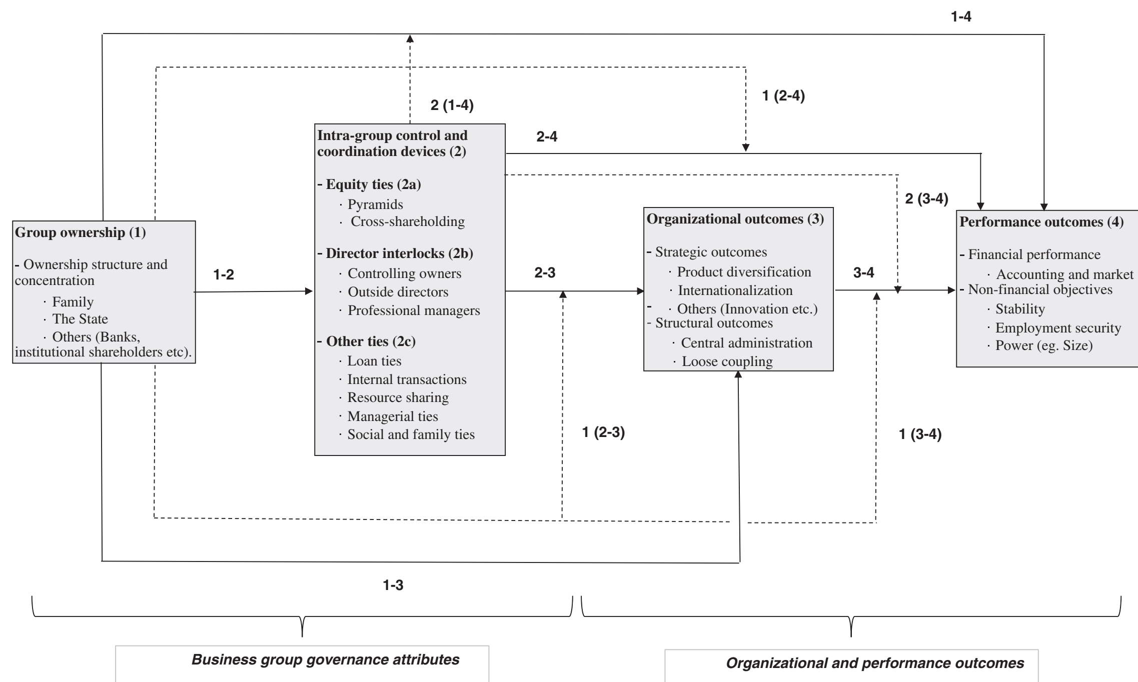
© 2015 John Wiley & Sons Ltd

We pay careful attention to the typology of business groups when we examine their corporate governance attributes. This is because, given the different research tracks and the literature's evolution, we see a variety of definitions and types of business groups in the literature. In a recent effort to understand what business groups are, Colpan and Hikino (2010) argued that business groups in their broadest sense characterize "an economic coordination mechanism in which legally independent companies utilize the collaborative arrangements to enhance their collective economic welfare." Under this definition, we find different types of business groups including hierarchical types with a central controlling unit (which may or may not be a formal and visible unit such as a holding company, as in the case of family-controlled groups in many emerging economies) and network types, which do not have a central controlling unit (e.g., the Japanese *kigyoshudan* formed after World War II, which does not contain an apex unit). The hierarchy type of business group has been argued to be the dominant form of large enterprise in emerging economies (Colpan & Hikino, 2010; Morck, 2010). The types most commonly analyzed in the literature have therefore been the two varieties of the hierarchy-type business groups from strategy and finance perspectives: diversified business groups that operate in a number of technologically or product-wise unrelated fields, and pyramidal business groups that contain a chain of publicly listed firms. Hence, for analytical focus and robustness, we will focus on this hierarchy variety of business groups for the examination of their corporate governance in this paper. (Our own research of the literature also shows the dominance of research in this variety of business group.)

In order to establish a complete picture of the relevant literature, we first conducted a search of the titles, abstracts, and keywords of articles published between Granovetter, 1995 (since when the term "business group" became established in the literature) and the end of 2014, for the term 'business group(s)' as well as related terms: 'pyramid,' 'keiretsu,' 'zaibatsu,' 'chaebol,' 'guanxi qiye,' 'grupos economicos,' and 'group affiliation'. We searched all the articles in the 30 main journals in business and management as well as finance, through EBSCO and the journals' own websites.[2] Reference to historical materials was made in particular to those in the list of the top business history journals. Second, we deleted those articles that appear more than once in different search terms. Third, we manually checked all identified articles and excluded ones that did not relate to corporate governance. Aside from this search of journal articles, we also examined influential work, especially books (chapters) and review articles, on the topic. This process resulted in a total of 119 publications.

We integrate the analysis of the existing literature by organizing our examination of the past research under five themes. Figure 1 illustrates our organizing conceptual framework around these research themes. We note that for simplicity and clarity of presentation, we show the causal relationships in a unilateral manner in the figure, although there may be bilateral relationships among the constructs implying reverse causality.[3] We will return and discuss the synthesizing of these distinct research themes in the section on future research directions. The literature review in our tables provide the main features as well as key findings of the studies' that we examined in our target journal articles in the order of their themes. This enables a general overview of what has been done on the governance of business groups up to the present and also helps us identify promising opportunities for future research.

FIGURE 1
Conceptual Framework for Governance of Business Group Research



Note: Straight lines denote direct relationships while dashed lines denote moderating relationships.

© 2015 John Wiley & Sons Ltd

Research on Group Ownership (1)

At the core of the governance of business groups literature is research related to group ownership. Common to most studies in this area is their emphasis on examining the different ownership structures in business groups, particularly focusing on the family-controlled ones. Further, and relatedly, they examine the extent of concentration in the ownership of business groups. Colpan and Hikino (2010) have shown that in 2007 (as well as in 1987) the large private enterprises in late-industrializing economies have been mostly organized as business groups and at the same time they predominantly have families as their controlling ownership. La Porta, Lopez-de-Silanes and Shleifer (1999), although not directly focusing on business groups, showed that widely-held firms are rare outside the US and UK and concentrated ownership is common elsewhere. By looking at the ownership structures of large firms in 27 wealthy countries, they find that families or the state have mostly controlled firms in those nations. In a more recent study, Morck (2010) shows that many countries' large business sectors are controlled by tiny handfuls of wealthy families that are organized as business groups. The national chapters of *The Oxford handbook of business groups* (Colpan et al., 2010) that examine 14 emerging economies illustrate a similar finding in that families are the major controlling owners of business groups in those nations.[4]

Several other influential scholars have also effectively addressed the ownership and control relationships in business groups. Cuervo-Cazurra (2006), in particular, classifies business groups into different types based on their ownership. He argues that each type of business group has different agency costs. In family-owned groups, the owners are either managers, or they have large control over managers, and therefore, there is no separation of ownership and control. In state-owned groups, on the other hand, there are substantial agency problems as it is the politicians who control the business groups, but in reality it is the citizenry who own the enterprises. In those run by technocrats – which has been, and still is, quite often the case among Western Europe's state-owned enterprises – additional specific agency-related issues arise, namely those between the top management and the politicians, who often appoint the board, and between top management in the apex company and that of the subsidiaries. These multiple conflicts often simultaneously take place with other conflicts arising between the government as majority shareholder and minority shareholders within the affiliated companies of a group (Colli, 2012a, 2012b). Notwithstanding its relevance, research on the corporate governance of groups of enterprises controlled by the state is still in its infancy (Musacchio & Lazzarini, 2014).

Empirical research on the ownership and control of non-family and non-state groups is even more scarce. Together with the families and the state, a third important constituency in terms of ownership are banks. Banks as ultimate controlling owners of business enterprises, and therefore also of business groups, can be found both especially in Asian and European business history. The banks of the former *zaibatsu* in pre-war Japan are credited with playing a pivotal role in the birth of the keiretsu system of horizontal business groups after World War II (Morikawa, 1992). In other cases, as in Italy during the interwar period, banks acted as financial holdings, leading the creation of business groups in order to diversify their investments (Colli & Vasta, 2015). Thanks to a system of cross-shareholdings between the bank itself and the companies belonging to the group, this could (and actually did) lead to a strong entrenchment of the banks' management. The declining influence, and grip, of German banks over the largest German industrial enterprises (Bradley & Sundaram, 2003) has also in some way reduced the incentives in studying the governance structures of bank-led business groups. Despite these remarkable examples, the presence of banks as controllers of business groups therefore stands as understudied. Table 1 illustrates the past research that has its prevalent focus in this stream.

Research on Intra-Group Devices for Control and Coordination (2)

An important stream of the literature is concerned with devices for control and coordination in business groups (see Table 2). We especially identify two critical and well-researched themes that focus on the formal devices of control and coordination, which are equity ties and director interlocks that have been argued to be strong delineators of group boundaries (Khanna & Rivkin, 2006). Other control and coordination mechanisms including loan ties, internal transactions, and resource sharing remain as much less researched areas. Although informal ties, especially among family members, have been a prominent theme, it has been argued that their sole presence may not be an adequate indicator in distinguishing group boundaries (Khanna & Rivkin, 2006). Below, we delve into the study of equity ties and director interlocks in more detail.

Equity Ties. A first relevant device is inherent to the very nature of business groups, which are formally characterized by the presence of ownership of equity stakes held by both the apex unit (usually organized as holding companies) and the operating companies in other companies belonging to the same group. As stressed above, research on these topics focuses especially on pyramidal structures, that is, "chains" aiming at preserving and amplifying the power of controlling shareholders. This holds in particular when some of the companies, which belong to the pyramid, are listed, thus implying the presence of large minority shareholders who are potentially in danger of exploitation by controlling shareholders.

The diffusion of pyramidal structures as devices, or mechanisms aiming at strengthening and enhancing the control power of blockholders (or the main shareholders), has been considered a typical feature of some capitalist environments, such as the late-industrializing nations and continental Europe in particular. This has serious political implications, particularly when the transparency and "proportionality" conditions among minority and majority shareholders are concerned. These political implications are also at the basis of regulation initiatives, some successful and some not. The European Commission, for instance, issued a number of Directives (627 Directives in 1988, 109 Directives in 2004), whose main purpose has been the disclosure of control-enhancing mechanisms, with particular reference to pyramidal structures.

Early comparative research on corporate ownership structures (La Porta et al., 1999) illustrates business groups as

© 2015 John Wiley & Sons Ltd

TABLE 1
Research Stream with Prevalent Focus on Group Ownership (1)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Chung, 2001	Taiwan	1972, 1974, 1976	Not explicit (based on official source)	Market-centered theories Institutional approach Culturalist perspective	1	Group formation is usually associated with firms that have coherent leadership. Those firms that lack a coherent leadership in ownership and management are unable to respond to institutional incentives promptly.
Tsui-Auch & Lee, 2003	Singaporean Chinese and Korean	1997	Hierarchy-type	Multiple theoretical lens	1	After the Asian currency crisis, Korean chaebol intensified family control, while Singaporean Chinese business groups absorbed more professional managers.
Young et al., 2008	Emerging economies	Not specified	Hierarchy-type Network-type	Principal-principal perspective Agency theory	1	Principal-principal conflict results from business group structures.
Colpan & Hikino, 2010	Late-industrializing economies	Not specified	Hierarchy-type	Multiple theoretical lens	1	Large private enterprises in late-industrializing economies are mostly organized as business groups and predominantly have families as controlling ownership.
Goldstein, 2010	South Africa	c.1910–2007	Hierarchy-type	No explicit theoretical lens	1	Six main business groups controlled economic activity (through pyramids) in South Africa. However, traditional family-centered groups decreased, while black-owned groups increased since 1994.
Tsui-Auch & Yoshikawa, 2010	Singapore	c.1950–2006	Hierarchy-type	No explicit theoretical lens	1	Family and state ownership of business groups are a common feature in Singapore. Both type of groups have maintained significant ownership of and control over their enterprises despite pressure for governance reforms.
Lee & Kang, 2010	China	c.1985–2007	Hierarchy-type	Agency theory	1	Dominance of state ownership is a distinguishing characteristic of Chinese business groups.
Wailerdsak & Suehiro, 2010	Thailand	c.1930–2008	Hierarchy-type	Separation of ownership and control	1	After the 1997 financial crisis, families managed to keep control of their groups while bank centered groups lost their power.
San Román, Fernández Pérez & Gil López, 2014	Spain	1942–2003	Hierarchy-type (pyramidal)	Institutional theory	1	Family business groups prove to be efficient alternatives to vertically integrated managerial corporations in environments characterized by situations enhancing the

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
						importance of network arrangements in dictatorships and regulated environments.
La Porta et al., 1999	Wealthy economies	1990s	Hierarchy-type	Agency theory	1, 2a, 1-2a	Concentrated ownership is the prevailing form of ownership among large companies in the world. This is achieved through an extensive use of control-enhancing mechanisms, particularly by wealthy individuals and families who in this way preserve their rights and wealth.
Khanna & Yafeh, 2007	Emerging markets	Not specified	Hierarchy-type Network-type	Multiple theoretical lens	1, 2	Business groups around the world share certain attributes but they are also differ from each other in terms of their ownership and other dimensions.
Aldrighi & Postali, 2010	Brazil	c.1960–2007	Hierarchy-type	Institutional framework	1, 2	Family ownership and pyramidal structures are common features of Brazilian groups. Families sit on the boards of companies, but do not usually serve as their CEO or chairperson.
Chung & Mahmood, 2010	Taiwan	c.1970–c.2000	Hierarchy-type	Institutional framework	1, 2a	While family ownership is declining, affiliate ownership has been increasing. Taiwanese groups often use a "pyramidal structure" to organize their ownership. The overall planning of the whole group is done via a set of socially related top executives.
Kim, 2010	South Korea	c.1960–2006	Hierarchy-type (chaebol)	Multiple theoretical lens	1, 2a	Family ownership and tight control through cross-shareholdings are features of the Korean chaebol. Corporate governance reforms were implemented to improve transparency and accountability after the Asian financial crisis.
Guriev, 2010	Russia	c.1980–2008	Hierarchy-type	Separation of ownership and control	1, 2a	Large private business groups are the major players in the Russian economy. Ownership concentration is very high when compared to other nations. Most groups are majority owners in their companies and the use of pyramids is minimal.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Kosenko & Yafeh, 2010	Israel	c.1950–2006	Hierarchy-type	Agency theory	1, 2a	Ten largest groups are all family owned. Israel is among the highest in terms of ownership concentration in the Western world. Eighty percent of all group-affiliated companies are part of pyramidal structures. Majority and minority shareholder conflicts are seen.
Miyajima & Kawamoto, 2010	Japan	Pre-World War II	Hierarchy-type (zaibatsu)	Agency theory	1, 2a, 2c	Family ownership and pyramidal structures were main features of pre-war zaibatsu. The main tools used to control first tier firms were personnel appointments, and the allocation of financial resources.
Üsdiken, 2010	Late-industrializing nations	Not specified	Hierarchy-type	Multiple theoretical lens	1, 2b	The mixture of family rule with increasing professionalized operational management seems persistent across a broad range of emerging economies.
Saxena, 2013	India	1983–2011	Hierarchy-type	Eclectic framework	1, 2b	This article proposes an eclectic and integrative framework to examine succession-related issues in business groups.
Solomon et al., 2002	South Korea	2000	Conglomerate groups (chaebol)	Agency theory	1, 1-2	It is necessary to improve the accountability of chaebol towards shareholders. The Korean Stock Exchange has required 25 percent outside directors on the board since 1999.
Chang, 2006	East Asian economies	Post-s	Mainly hierarchy-type	Multiple theoretical lens	1, 2, 1-2	Corporate governance reforms affecting business groups of East Asian nations after 1997 are examined.
Cuervo-Cazurra, 2006	Emerging and developed economies	Not specified	Common ownership Diversified	Agency theory	1, 1-3	Business groups are separated based on their ownership types. Each type has different agency costs and diversification logics.

Note: The numbers in the "focus" column stand for the numbers in Figure 1.
The papers are listed first by order of themes, and then chronologically within individual themes.

reservoirs of family control and concentrated ownership, as well as pyramids as control-enhancing devices. Pyramidal control, in sum, exerted a particular attraction on researchers examining issues related to the control modalities in business groups, in particular stressing how pyramids played a key role as devices for enhancing both financial and operational control over the whole group.

One additional, yet very relevant, aspect of equity ties in business groups concerns the presence of cross-shareholdings, or multiple mutual share-ownership of companies belonging both to horizontal and vertical business groups (Boyd & Hoskisson, 2010). Even in its simplest form, that is the exchange of relevant ownership stakes among companies belonging to the same group, cross-shareholdings may result

© 2015 John Wiley & Sons Ltd

TABLE 2
Research Stream with Prevalent Focus on Intra-Group Control and Coordination Devices (2)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Lincoln & Shimotani, 2010	Japan	Post-World War II	Network-type Hierarchy-type	Agency theory Transaction cost theory	2	Presidents' councils, partial cross-ownership, and personnel exchanges are the commonly employed governance mechanisms in the Japanese postwar keiretsu.
Boutin, Cestone, Fumagalli, Pica, & Serrano-Velarde, 2013	France	1995–2004	Hierarchy-type	Institutional theory Internal capital market theory	2	The paper explores the role of internal capital markets in determining the outcome of the competition between incumbent and entrant firms belonging to different groups with different internal capital markets.
Claessens, Djankov, & Lang, 2000	East Asia	1998–2000	Hierarchy-type (pyramidal)	Institutional theory	2a	The separation between ownership and control of companies is achieved through the presence of pyramidal structures.
Demirag & Serter, 2003	Turkey	1999	Hierarchy-type (pyramidal)	Separation of ownership and control	2a	Separation of ownership and control is achieved through pyramidal ownership and presence of business groups.
Kim, 2003	South Korea	1987–1992	Not explicit (chaebol)	Separation of ownership and control	2a	Chaebols exercise control through strategic interlocking ownership.
Urzua Infante, 2009	Chile	2000–2005	Hierarchy-type (pyramidal)	Agency theory, tunneling	2a	The paper shows that there is a negative correlation between boards' remuneration and cash flow rights in business groups showing a diffusion of tunneling practices.
Siegel & Choudhury, 2012	India	1989–1999	Hierarchy-type	Institutional theory	2a	The article shows how Indian business groups are implementing strategies aimed at good governance and that their behavior is far from tunneling and expropriation.
Bank & Cheffins, 2010	USA	1880–1930	Hierarchy-type (pyramidal)	Institutional theory	2a	Pyramidal business groups have scarce diffusion in the US not for institutional reasons but because of structural reasons due to the fact that capital markets were well developed.
Chernykh, 2008	Russia	2000–2002	Hierarchy-type (pyramidal)	Institutional theory	2a, 1	The paper analyzes the ultimate control patterns in listed Russian corporations, identifying the main owners and stressing the use they make of control-enhancing mechanisms, such as pyramids and golden shares, in order to keep control over the companies.
Lefort, 2010	Chile	c. 1930–2008	Hierarchy-type	Agency theory	2a, 2b	Pyramidal schemes are the most common way of achieving control in Chilean business groups. Groups are increasingly employing independent directors to sit on boards, indicating a trend toward the professionalization of Chilean boards of group firms.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Khanna & Rivkin, 2006	Chile	1997	Not explicit (based on official source)	Multiple theoretical lens	2a, 2c	Family connections and direct equity holdings do not serve as good indicators of group boundaries.
Masulis, Pham, & Zein, 2011	45 countries	2003–2006	Hierarchy-type (pyramidal)	Agency theory Internal capital market theory	2a, 2a-3	Group structures emerge not only to perpetuate control, but for necessities of financing both at the country and at the firm level. At the country level, pyramidal groups prevail in systems characterized by poor capital markets. At the firm level, intensity of investments increase for firms at the bottom of the pyramid.
Chizema & Kim, 2010	South Korea	2002–2006	Not explicit (chaebol)	Institutional theory	2a-2b	There is a significant and positive relationship between the proportion of outside directors and business group affiliation.
Ren, Au, & Birtch, 2009	China	1999	Diversified Network	Multiple theoretical lens	2b	Director interlocks occur in smaller business groups that tend to be regionally fragmented.
Boyd & Hoskisson, 2010	Emerging economies	Not specified	Hierarchy-type Network-type	Multiple theoretical lens	2b	Focus is primarily on the role of the board of directors as a governance mechanism in business groups.
Brookfield, 2010	Taiwan	1990–2000	Network-type	Multiple theoretical lens	2b	Business groups are important in understanding patterns of ownership ties. Director interlocks cross industry boundaries.
Yildirim-Öktem & Üsdiken, 2010	Turkey	2004	Hierarchy-type	Multiple theoretical lens	2b	Institutional pressures and joint venture partners' existence predict board professionalization better in business groups.
Lauterbach & Yafeh, 2011	Israel	1990s	Hierarchy-type (pyramidal)	Institutional theory	2b	In the case of the elimination of a relevant control-enhancing mechanism such as dual-class shares, business group affiliation does not replace it as a control-enhancing mechanism.
Fracchia, Mesquita, & Quiroga, 2010	Argentina	c.1930–2007	Hierarchy-type (grupos economicos)	Institutional framework	2b, 2a	Approximately 60 percent of boards of large business groups are family members. Control is achieved through direct equity holding, active family involvement, and interlocking directorates within business groups.
Sarkar, 2010	India	1947–2006	Hierarchy-type	Multiple theoretical lens	2b, 2a	A typical Indian business group is organized through pyramids with a controlling holding company at the helm. Director interlocks of family members are used extensively.
Chung, 2005	Taiwan	1972, 1974, 1976	(Guanxi) networks	Multiple theoretical lens	2c	The influences of guanxi for group relationship is evident in early stages of group formation.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Nakamura, 2011	Japan	1970–2008	Hierarchy-type Network-type	Selective adaptation theory	2c	Keiretsu will constrain more complete firm disclosure of intra-group transactions.
Yiu et al., 2013	Less-developed countries	Not specified	Hierarchy-type Network-type	Multiple theoretical lens	2, 1(2–4)	The chapter discusses vertical and horizontal governance mechanisms adapted by business groups.

Note: The numbers in the "focus" column stand for the numbers in Figure 1.
The papers are listed first by order of themes, and then chronologically within individual themes.

as a control and coordination mechanism of group firms. Nevertheless, on the negative side, such ties may also result in the protection, and entrenchment, of existing management. This happened, for instance, in the case of the early history of Japanese keiretsu after World War II when, deprived of the pivotal holding, the companies started a process of mutual protection from hostile takeovers through the multiple acquisition of small stakes among companies formerly belonging to the same zaibatsu (Morikawa, 1997).

Director Interlocks. A second (but less systematic and fragmented) research stream focuses instead on a control and coordination device inside business groups and the ways in which it is achieved. Interlocking directorates are commonly considered as the most common and efficient mechanism in place across companies belonging to the same corporate cluster and even across different industries (Brookfield, 2010), particularly evident in cases such as the Japanese keiretsu or the Korean chaebol (see Kikkawa, 1995; Kim, 2003). As a control and coordination device, director interlocks appear to be quite resilient in phases of economic stability and crisis – even if the available research largely deals with the evidence provided by East Asian countries such as Japan and Korea (Jang & Kim, 2002; McGuire & Dow, 2003). Boyd and Hoskisson (2010) stress the role of director interlocks as horizontal ties – particularly in what they define as N- (network)-form groups – activated inside the business groups. Furthermore, they emphasize how interlocks are active at the same level as social ties among board members. Yet, hierarchy-type groups also often use such ties besides the equity ties, as a means of effective control as well as coordination of group firms. Director interlocks in this instance become necessary when families would like to establish their firm presence in the whole group. In particular, this happens in operating companies that are listed and have outside shareholders and external board members, which necessitate the presence of the family on operating companies' boards to exert their influence. In Turkish family holdings, for instance, families dominate the boards of apex units (holding companies) as well as operating companies of the business groups employing board interlocks, while they increasingly leave the executive posts to salaried professionals and incorporate outside board members (Colpan, 2010).

A common research theme in this stream is therefore the domination of boards as well as board interlocks of family business groups by controlling family members. However the research on the actual functioning of these boards and interlocking directorates and the way the boards of the apex company and the operating companies work are almost non-existent. This is obviously central to an understanding of the real governance process that takes place within business groups. Further, only a relatively small strand of this literature explicitly looks at the role of the non-family board members, such as inside professional executives and outside members, and how they connect with other group as well as non-group firms. In Korea, for instance, studies show that since 1999, the Korean Stock Exchange has required listed companies, including chaebol-affiliated companies, to elect 25 percent outside directors on their boards and to be more attentive to protecting shareholders' interests (Solomon, Solomon & Park, 2002). Yet, overall, there are not many studies on understanding how these directors serving in group firms connect to other firms, and thus serve as mechanisms of group control and/or coordination.

Research on the Relationships between Group Ownership and Intra-Group Control and Coordination Devices (1-2)

Research on the relationship between the nature of controlling owners and the presence of devices for coordination and control inside the business group itself is not new. One of the seminal papers in the field of corporate governance (La Porta et al., 1999) points to the close relationship between the presence of concentrated ownership and the diffusion of pyramidal control. In this perspective, devices such as pyramids and cross-shareholdings, aiming at enhancing the power of controlling shareholders, allow the owners to exert a relatively strong control over the firm's decisions with a limited investment of their own resources. This literature also indicates that the main blockholders through such devices can exert a grip on group firms' administration and can significantly manipulate the group firms' investment, remuneration, and/or

© 2015 John Wiley & Sons Ltd

investment policies, in their own interest – and against the interests of minority shareholders. All of the relevant research examined in this paper indicates a direct relationship between the concentration of ownership and the potential exploitation of these devices, while we found very little evidence of research segmenting the introduction of specific devices according to the different types of ownership. Examining different typologies of business groups in Israel, for instance, Maman (1999) proposes a taxonomy of business groups according to differences in ownership structure which, in turn, influences the nature of the interlocking ties connecting the companies of the group.

What is possible to argue from the available evidence is that different control and coordination devices fulfill different purposes. Pyramidal control, as suggested above, allows an easier separation between control- and cash-flow rights, which is less the case for other devices that can efficiently carry on other purposes. Pyramidal structures are historically common both in private and state-owned business groups, even if with different purposes, since the latter are more inclined to employ such devices for leveraging purposes instead of tunneling – as is the case of many privately-held business groups (Sacristan-Navarro & Gomez-Anson, 2007; Sarkar, 2010).

Cross-shareholding ties, which often go hand in hand with interlocking directorships, tend to be more common in business groups that need to be closely coordinated by a "center" by means of personal connections, which can be enforced by loan ties, internal transactions, and other informal connections such as, for instance, resource exchanges. This is a typical situation, which has been historically concretized in the case of bank-controlled business groups in the Italian case, for instance (Colli & Vasta, 2015), but also in other types of horizontal control, as in the case of horizontal keiretsu-like groups (Lincoln & Shimotani, 2010).

Different ownership types also reside with a number of coordination mechanisms, which are more "informal," including, for instance, loan ties, managerial ties, social, and family ties (see Figure 1). Our review finds little or barely existing research trying to link ownership to the use of these coordination mechanisms. Some (almost intuitive) evidence suggests, for instance, that the use of these kinds of informal coordination mechanisms is more dependent on the cultural and institutional environment than the types of ownership itself. An effective example in provided by "guanxi" relations in China (Chung, 2005) or personal relations in the case of Japanese postwar keiretsu (Lincoln & Shimotani, 2010).

Of course, different typologies of control and coordination devices may reside within the same business group under a given ownership structure. For instance, in a family-owned business group, pyramidal control can exist with personal ties, while in bank-controlled business groups, coordination mechanisms such as loan ties and interlocking directorates may prevail. Research on these combinations barely exists, if not totally absent. Table 3 illustrates past research under this research stream.

Research on the Relationships between Group Ownership and Organizational/Performance Outcomes (1-3, 1-4)

Another promising, but under-studied, field of research concerns the relationships between group ownership and its organizational as well as performance outcomes. What, for instance, is the relationship between ownership structures in business groups, and their product and geographic diversification strategies? We examine this part by dividing it into two: organizational outcomes and performance outcomes (see Table 4 for relevant past research in this research stream).

Organizational Outcomes. Past research has especially examined the relationship between ownership structure and product diversification in business groups. A taxonomy of business groups according to their ownership and the varying motivations of those owners in increasing their groups' product diversification has been proposed by Cuervo-Cazurra (2006). According to this research, family-owned business groups are driven to diversify their product portfolio by the entrepreneurship of the family owners, who grasp opportunities in new businesses. According to some authors (and to a consolidated opinion among family business scholars), then, product diversification strategies are consistent with the willingness to diversify product-related risks (Gomez-Mejia, Makri, & Larraza Kintana, 2010), and also by the simultaneous necessity to create top managerial positions for the individual family members (Crespí-Cladera & Bru, 2006). Other research has also supported that family ownership has a positive influence on product diversification decisions in business groups (see, e.g., Chung, 2013, on the Taiwanese case, but also Binda, 2012 and Binda & Colli, 2011 in the cases of Spain and Italy, respectively).

In state-owned business groups, on the other hand, the motivation for entering into new businesses is often the provision of subsidized public goods or the development of a region, as well as the willingness to achieve new technology for instance through a joint venture with other enterprises, including foreign multinationals. These business groups have financial access to the governmental budgets and enjoy exclusive rights, such as monopoly, when government determines that necessary for national interest (Cuervo-Cazurra, 2006). A positive relationship between state ownership, diversification, and affiliates' performance has also been found in the case of Chinese firms (Lu & Yao, 2006).

Further research stresses how family and state ownership of business groups tend to positively affect the flexibility of firms in adopting coordinated strategies, for instance in terms of refocusing (Binda & Colli, 2011). However, to our knowledge no systematic effort has been made to connect structural characteristics of business groups (e.g., centrally and systematically administered organizational structures versus more loosely coupled organizational structures), to their ultimate ownership, leaving much room open for further research to identify regularities.

Performance Outcomes. One strand of research in this stream relates to the relationships between ownership and varying performance outcomes. Intuitively, a first relationship between ownership and performance takes place when the performance required and pursued changes according to the nature of the ownership itself. Different categories of potential owners such as families, the state, financial institutions, and minority shareholders have different perceptions and orientations in terms of the performance they expect and require from their investments. Cuervo-Cazurra (2006), for instance, has

© 2015 John Wiley & Sons Ltd

TABLE 3
Research Stream with Prevalent Focus on the Relationship between Ownership Structure and Intra-Group Control and Coordination Devices (1-2)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Maman, 1999	Israel	1974–1987	Hierarchy-type	Resource dependence theory	1-2b	This article discusses factors that lead to differences in interlocking ties within business groups, including patterns of ownership and management strategies.
Franks & Mayer, 2001	Germany	1990	Hierarchy-type (pyramidal)	Agency theory	1-2a	Concentrated ownership systems like the German one lead to pyramids and other control-enhancing mechanisms to be diffused.
Jang & Kim, 2002	South Korea	1998–2002	Conglomerate groups (chaebol)	Agency theory	1-2, 2-3	The actual corporate governance practices of Korean chaebols largely remain unchanged.
McGuire & Dow, 2003	Japan	1987–1997	Network-type	Multiple theoretical lens	1-2a	Keiretsu governance structure interlocks tend to persist in periods of crisis but foreign capital needs push toward an unwinding of interlocks.
Morck et al., 2005	Developed and emerging economies	Not specified	Hierarchy-type	Multiple theoretical lens	1-2a, 1, 2a	Large firms in most countries are basically organized as pyramidal groups controlled by a few wealthy families. This leads to governance problems between controlling and minority shareholders as well as to economic entrenchment.
Lee & Jin, 2009	China	1990–1994	Not explicit (hierarchy-type)	Multiple theoretical lens	1-2a	Business groups are the normal outcome of a process of dismantling of state-owned enterprises through a privatization process.
Hoshino, 2010	Mexico	c. 1970–2006	Hierarchy-type (grupos economicos)	No explicit theoretical lens	1-2a, 2a	Families preside over board of directors, chairperson and CEO roles of group companies. Pyramids are commonly used for control schemes.
Colpan, 2010	Turkey	c. 1920–2007	Hierarchy-type	Agency theory	1-2a, 1-2b	Families control business groups through pyramids, complex intercorporate shareholding structures, and interlocking directorates. Since the late 1990s there has been an increasing professionalization of top management.
Sacristan-Navarro & Gomez-Anson, 2007	Spain	2002	Hierarchy-type (pyramidal)	Institutional theory	1-2a, 2a	In Spanish family-controlled business groups, the presence of leverage mechanisms causes conflicts of interest between majority and minority shareholders.
Chung & Chan, 2012	Taiwan	1988–2004	Hierarchy-type (pyramidal)	Agency theory	1-2b	In ethnic Chinese family business groups in Taiwan, ownership structure of the affiliate affects the possibility of having family leadership.

Note: The numbers in the "focus" column stand for the numbers in Figure 1.
The papers are listed first by order of themes, and then chronologically within individual themes.

proposed a ranking among general categories of ownership in terms of their financial performance, with family-controlled groups showing better results than other types of group ownership. His argument is based on the idea that in family-owned business groups, efficiency is maximized by the reduction of agency costs due to the low level of conflict between

© 2015 John Wiley & Sons Ltd

TABLE 4
Research Stream with Prevalent Focus on the Relationship between Group Ownership and Organizational/Performance Outcomes (1-3, 1-4)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Chung & Luo, 2008b	Taiwan	1986–1998	Hierarchy-type	Agency theory Institutional theory	1-3	Family business groups are less likely to divest unrelated businesses. Institutional logics affect restructuring in these business groups.
Iacobucci & Rosa, 2010	Italy	1970–2000	Hierarchy-type	Resource-based view	1-3	"Portfolio entrepreneurs" create business groups through the involvement of capable managers involved by minority share packages in order to get control over their capabilities.
Binda & Colli, 2011	Italy and Spain	1973–2000	Hierarchy-type	Separation of ownership and control	1-3	Continental Europe countries characterized by high presence of family firms, and state-owned enterprises employ the business group form. This proves to be useful when refocusing strategies are necessary.
Chung, 2013	Taiwan	1998–2002	Family-owned entity Diversified, pyramidal	Agency theory	1-3	Family management and family ownership have critical roles in diversification decisions in family business groups.
Lodh et al., 2014	India	2001–2008	Hierarchy-type	Agency theory Institutional theory External resourcing perspective	1-3	Family-owned business group-affiliated firms innovate more than non-business group-affiliated firms.
Lynn & Rao, 1995	Japan	1874–1927	Hierarchy-type	Multiple theoretical lens	1-4	Failure of owners to correct managerial inadequacies led to failure in the Suzuki group.
Khanna & Palepu, 2000	India	1993–2000	Hierarchy-type	Institutional theory (market failures)	1-4	In developing markets, business groups play the role of substitutes for market imperfections. In diversified groups in the long run affiliated firms outperform the unaffiliated ones.
Bae, Kang, & Kim, 2002	Korea	1981–1997	Hierarchy-type	Agency theory, tunneling	1-4	In family-controlled business groups, when firms belonging to the group make an acquisition, minority shareholders suffer because controlling shareholders siphon resources from the acquired firm into other companies in the group that they control.
Campbell & Keys, 2002	South Korea	1993–1999	Hierarchy-type (chaebol)	Agency theory	1-4	In horizontal family-owned groups, corporate governance practices are particularly weak in terms of investor protection and are characterized by systematic underperformance, accentuated during the financial crisis of the 1990s.
Morck & Yeung, 2003	USA	1990s–2000s	Hierarchy-type	Agency theory	1-4	In family-controlled business groups, a series of agency problems arise in a different nature from those in managerial companies. Families may

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 4
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
						protect some companies in the group at the expense of the other shareholders.
Joh, 2003	Korea	1993–1997	Hierarchy-type (chaebol)	Agency theory	1-4	The paper examines how ownership structure impacts firm's performance through tunneling practices in subsidiaries.
Baek et al., 2004	South Korea	1997–2000	Hierarchy-type (chaebol)	Agency theory	1-4	During a period of financial crisis, companies belonging to family-owned concerns suffer more financially.
Baek et al., 2006	Korea	1989-2000	Hierarchy-type	Agency theory, tunneling	1-4	In horizontal groups characterized by weak governance structures, controlling shareholders benefit from opportunities for tunneling thanks to intra-group relations among firms in public offerings.
Lu & Yao, 2006	China	2001	Hierarchy-type (based on official source)	Multiple theoretical lens	1-4	State ownership increases the performance of group-affiliated firms, and this is higher when they have higher degrees of diversification.
Bertrand, Johnson, Samphantharak, & Schoar, 2008	Thailand	1990s	Hierarchy-type	Institutional theory Agency theory	1-4	The paper analyzes the relationship between family size, the modality of family involvement and the performances of the group, particularly in relation to tunneling practices damaging minority shareholders.
Almeida et al., 2011	Korea	1998–2004	Hierarchy-type	Agency theory	1-4	In business groups, evidence from Korea shows that the more a firm is central and functional to the acquisition strategy of the ownership, the more its market value has a discount.
Chung & Luo, 2013	Taiwan	1996–2005	Hierarchy-type	Social embeddedness and neoinstitutional perspectives	1-4	Outside successor premium is reduced in firms embedded in business group relationships.
Gonzalez, Guzman, Pombo, & Trujillo, 2014	Colombia	1996–2006	Hierarchy-type (pyramidal)	Agency theory	1-4	Minority shareholders in family-controlled groups press for dividends when they perceive that they are under threat of expropriation.
Inoue, Lazzarini, & Musacchio, 2013	Brazil	1995–2009	Hierarchy-type (pyramidal)	Agency theory Institution-based view Transaction cost economics	1-4, 1-3	When government minority stakes are allocated to business group affiliates, the positive effects of those stakes on ROA and capital expenditures are substantially reduced.
He, Mao, Rui, & Zha, 2013	China	2000–2010	Hierarchy-type (pyramidal)	Internal capital market theory	1-4	Business groups function as internal capital markets in cases of underdeveloped capital markets, depending also on the nature of controlling owners. For instance, in the case of China, state ownership plays a relevant role.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 4
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Chang, 2003	South Korea	1986–1996	Hierarchy-type (chaebol)	Agency theory	4-1	Performance determines ownership structure in business groups. Controlling shareholders employ insider information to take equity stakes in group-affiliated firms.
Gökşen & Üsdiken, 2001	Turkey	1994	Hierarchy-type	Macro-institutionalist theory Contingency theory	4-1	Family domination in ownership and management of business groups remain insensitive to size and time of founding of those groups.

Note: The numbers in the "focus" column stand for the numbers in Figure 1.
The papers are listed first by order of themes, and then chronologically within individual themes.

owners and managers. In family business groups, additionally, diversification strategies are more effective, due to the rapid decision making by the owners. This perspective is not unanimously accepted, however. Focusing again on family firms, Baek, Kang, and Park (2004) show, instead, that under specific framework conditions (e.g., a period of prolonged financial crisis), companies belonging to family-controlled business groups tend to perform financially worse than stand-alone companies. Of course, once the concept of performance is brought into the picture, problems may arise, due to, for instance, the multidimensional nature of the performance concept itself, which in our general scheme is summarized in the two broad categories of financial and non-financial performance (where the non-financial performance is connected to goals not related to profits, including the sustainability of the business, or even the welfare of different stakeholders such as the employees). Furthermore, there is little knowledge on the actual effectiveness of decision making under such governance. For instance, in the case of groups owned by families but managed by professional salaried managers, the information asymmetry between those salaried managers and family members (who usually serve as board directors) may result in ineffective decision making made by insufficiently informed family members that in turn leads to declining performance. This analytical perspective, overall, appears to be under-researched, and does not lead to any definite and quantitative conclusive results.

Based on the research evidence collected in this paper, a vsecond perspective investigates the issue of the relationship between ownership and performance under a more specific point of view; that is looking at how concentrated ownership affects the firm's financial outcomes in terms of their distribution among different shareholders. These aspects appear to be particularly relevant in the case of business groups. The presence of concentrated ownership associated with business group structures and extensive family ownership and control has been argued to cause the so-called "principal-principal" conflict between controlling and minority shareholders (Young et al., 2008). While there has often been no separation of ownership and control in those family-controlled groups, which has been the cause of the typical managerial agency problem seen in widely-held Anglo-Saxon firms, a new kind of conflict between different types of shareholders has become the core of the debate in the business group literature. An important strand of the literature therefore relates to the potential expropriation of minority shareholders as a source of trouble. This is particularly evident in finance journals we examined in this paper, in which agency theory is a prevalent theoretical lens for a number of contributions assessing the threat of expropriation as detrimental for minority shareholders and in particular for their financial welfare. Among the "usual suspects" are, of course, families, and their tendency to exploit minority shareholders. Morck and Yeung (2003) argue how in family-controlled business groups, owners may protect some companies in the group at the expense of the other shareholders. Baek, Kang, and Lee (2006) stress instead the (often researched) issue of tunneling, showing how in South Korean chaebols, characterized by weak governance structures, controlling shareholders benefit through tunneling opportunities that emerge from intra-group relations among firms in initial public offerings. We will return to this issue in the next section as we examine pyramids and their performance effects, but overall, empirical evidence on the presence of business group structures and minority shareholder exploitation has mostly been inconclusive.

Research on the Relationships between Intra-Group Control/Coordination Devices and Organizational/Performance Outcomes (2-3, 2-4)

A key component of governance in business groups, which is rather adequately covered by the prior literature, is the impact of the above-mentioned formal and informal coordination devices on organizational outcomes, and ultimately, on performance outcomes. Despite their drawbacks, the cumulative results of the prior research indicate that this particular research stream is in a relatively advanced stage and they have offered valuable insights. Table 5 provides the studies and their key findings under this research theme.

© 2015 John Wiley & Sons Ltd

TABLE 5
Research Stream with Prevalent Focus on the Relationships between Intra-Group Control and Coordination Devices and Organizational/Performance Outcomes (2-3, 2-4)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Chang & Hong, 2000	South Korea	1996	Hierarchy-type (chaebol)	Internal capital market theory	2-3	Affiliated firms to Korean business groups benefit from resource sharing.
Wei & Zhang, 2008	East Asia	1991–1996	Hierarchy-type (pyramidal)	Free cash-flow hypothesis	2-3	Evidence confirms that too much free cash flow in the hands of entrenched managers in groups characterized by an excessive separation between control and cash flow rights leads to overinvestment.
Lechner & Leyronas, 2009	France	1995–2005	Hierarchy-type	Resource-based view	2-3	In the case of SMEs, business groups are a device put in place in order to manage growth processes. Business groups are relevant to achieve capabilities, overcome limits, and set up cooperative agreements with competitors.
Belenzon & Berkovitz, 2010	European countries	1995–2004	Hierarchy-type (pyramidal)	Institutional theory	2-3	The paper analyzes the propensity of firms belonging to a business group to innovate and find a positive relationship between innovation and business group affiliation. Business groups are successful in providing resources in case of underdeveloped capital markets.
Kim et al., 2010	South Korea	1993–2003	Not explicit (hierarchy-type)	Institutional theory	2-3, 2a(3-4)	Business group affiliation affects the international diversification discount (negative relationship between international diversification and firm performance) during market-oriented institutional change.
Mahmood, Zhu, & Zajac, 2011	Taiwan	1981–1998	Not explicit (network ties in business groups)	Contingency model	2-3	Firms' multi-complex network ties in business groups are one critical source of capability acquisition.
Kikkawa, 1995	Japan	1945–1995	Network-type	Institutional theory	2a-3	Japanese business groups have been historically characterized by interlocking share ownership in order to increase the sense of security of top management.
Mahmood & Rufin, 2005	Developing countries	1990–2005	Network-type	Institutional theory	2a-3	Business groups substitute for governmental intervention in high-tech industries. Group membership allows the advantages of technological development to be enjoyed, which is previously provided by governmental intervention.
Almeida & Wolfenzon, 2006	n.a.	n.a.	Hierarchy-type (pyramidal)	Agency theory	2a-3	Pyramidal ownership in family firms allows the earnings of a firm within the group to be used to set up a new one.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 5
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Choe & Roell, 2007	South Korea	1997–1999	Hierarchy-type	Multiple theoretical lens	2a-3	Diversified business groups such as chaebols suffer risk of excessive diversification, but groups also have the flexibility to pursue rationalization in times of crisis.
Kim & Lee, 2001	South Korea	c. 1990–c. 2000	Hierarchy-type	Learning theory	2a-3	This paper discusses different learning processes in parent–subsidiary relations inside two Korean chaebols.
Kang, Lee & Na, 2010	South Korea	1994–1998	Hierarchy-type (chaebol)	Agency theory	2a-3	In pyramidal groups in a period of crisis, the separation between cash flow and control rights decreases the possibility of restructuring.
Binda, 2012	Italy, Spain	1950–2002	Hierarchy-type (pyramidal)	Institutional theory	2a-3	Business group structure in Italy and Spain delayed product diversification strategy until later in the twentieth century.
Paligorova & Xu, 2012	G7 countries	2003–2006	Hierarchy-type (pyramidal)	Internal capital market theory Agency theory	2a-3	Pyramids have a significantly higher debt leverage but the use of debt is also highly correlated to the risk of expropriation by controlling shareholders.
Chari, 2013	India	2000–2008	Hierarchy-type	Eclectic theory	2a-3	Business group affiliation has a direct impact on the propensity toward FDI in developing countries.
Byun, Choi, Hwang, & Kim, 2013	South Korea	2001–2007	Hierarchy-type (chaebol)	Internal capital market theory Co-insurance theory	2a-3	Evidence shows that in the case of Korea, companies belonging to the group experience a lower cost of public debt consistent with the co-insurance principle.
Ma et al., 2014	China	2007–2008	Not explicit	Multiple theoretical lens	2a-3	A firm's value in emerging markets is a U-shaped function of internationalization in terms of foreign sales intensity. Firms affiliated to a group show a higher propensity to internationalize in times of economic crisis.
Pattnaik, Chang, & Shin, 2013	India	1995–2003	Not explicit (based on prowess)	Agency theory Institution-based view Transaction cost economics	2a-3	Business group-affiliated firms are less transparent than unaffiliated firms. This increases the information asymmetry between group firms and their shareholders.
Belderbos & Heijltjes, 2005	Japan	1995	Hierarchy-type	Multiple theoretical lens	2c-3	Strategic dependence of affiliates from parent firms increases the probability of the appointment of expats.
Yiu, 2011	China	2007–2008	Not explicit (hierarchy-type)	Institutional theory Eclectic theory	2c-3	Business groups are devices for internalizing transactions. In doing so they create a favorable environment for developing ownership, location and internalization advantages.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 5
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Gaur et al., 2014	Emerging economies	1989–2005	Not explicit (hierarchy-type)	Resource-based view	2c-3	Companies belonging to a group are more likely to shift from export to FDI.
Zattoni et al., 2009	India	1990–2006	Hierarchy-type (based on prowess)	Institutional theory Transaction cost theory	2-4	Business groups outperform independent companies under market and institutional imperfections, but fail to show superior performance after markets become more efficient and institutions grow.
Gopalan, Nanda, & Seru, 2007	India	1989–2000	Hierarchy-type	Institutional theory Internal capital market theory	2-4	Business groups are a relevant device for creating internal credit markets and for transferring cash across different firms inside the group. However, this results in an increasing risk of failure propagation inside the group with effects on other firms and minority shareholders.
White et al., 2008	China	1998–1999	Hierarchy-type	Institutional theory	2-4	Belonging to a group provides many advantages, including the presence of control mechanisms which point to the reduction of administrative costs.
Bae, Cheon, & Kang, 2008	South Korea	1993–2001	Hierarchy-type (chaebol)	Internal capital market theory	2-4	Group structure can originate a sort of reverse-tunneling, or propping, when there are announcements of increased earnings by the group's firms, as they impact positively over the market value of other firms within the group.
Carney et al., 2011	28 countries	1998–2009	Hierarchy-type	Multiple theoretical lens	2-4	The article draws conclusions on the overall diffusion and relevance of business groups but also on the fact that they are not paragons or parasites per se, which depends on the specific institutional conditions in which they develop.
Lai, 1999	Japan	1945–1999	Network-type	Institutional theory	2a-4	Keiretsu business groups allow the security and the growth of each business.
Bertrand, Mehta, & Mullainathan, 2002	India	1989–1999	Hierarchy-type (pyramidal)	Agency theory, tunneling	2a-4	The authors propose a measure of the extent of tunneling in Indian business groups. They show how financial shocks propagate differently among firms depending on the extent of cash flow rights by controlling owners.
Carney & Gedajlovic, 2002	Hong Kong	1993	Not explicit	Separation of ownership and control	2a-4	Coupled ownership and control in business groups is positively related with dividend payout levels and financial liquidity, and negatively related with investments in capital expenditure.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 5
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Kim, 2003	Korea (but mostly theoretical)	1990	Hierarchy-type (chaebol)	Institutional theory	2a-4	In case of default, business groups reduce the amount of information for banks to select among firms to bail out or not to bail out.
Cheung, Rau, & Stouraitis, 2006	Hong Kong	1998–2000	Hierarchy-type (pyramidal)	Agency theory, tunneling	2a-4	On the basis of the evidence collected in the Hong Kong stock market, the paper assesses the tunneling propensity of controlling shareholders in pyramidal groups.
Villalonga & Amit, 2006	USA	1994–2000	Hierarchy-type (pyramidal)	Agency theory	2a-4	Families retain their control over companies through a multiple system of control-enhancing mechanisms, including pyramids, and this leads in general to a destruction of value.
Orbay & Yurtoglu, 2006	Turkey	2001	Hierarchy-type (pyramidal)	Agency theory	2a-4	In business group-affiliated firms, deviations from one share–one vote results in inferior investment performance and market valuation of firms, group membership improves the investment performance and market valuation of firms.
Chang, Cho, & Shin, 2007	South Korea	1993–2001	Hierarchy-type	Agency theory	2a-4	Chaebol firms have higher information asymmetry than non-chaebol firms. Corporate transparency improvement is not higher relative to non-chaebol firms in the post-financial crisis era.
Bena & Ortiz-Molina, 2013	Europe	1993–2006	Hierarchy-type (pyramidal)	Internal capital market theory	2a-4	Pyramidal ownership structures are of paramount importance in providing finance to the new firms when the possibility to get cash flow resources from external financiers is limited.
Gopalan, Nanda, & Seru, 2014	22 countries in Asia and Europe	2000–2010	Hierarchy-type (pyramidal)	Internal capital market theory	2a-4	Controlling owners encourage the distribution of dividends by cash-rich subsidiaries in order to use the pay-outs to reinvest in other firms.
Tabeta & Rahman, 1999	Japan	1973–1994	Subcontracting system	Transaction cost theory Principal-agent model	2a-4, 2b-4	Ownership of suppliers through minority shareholdings or sending directors to those firms affects the suppliers' risk-sharing behavior.
Lincoln et al., 1998	Japan	c. 1980–c. 1990	Network-type	Learning theory	2c-4	Purchase-supply relations in Japanese business groups have a direct effect on organizational learning, increasing efficiency.
Lee & Gaur, 2013	South Korea	1995–2009	Hierarchy-type	Capabilities theory	2c-4	Socio-cultural mechanisms of control common in business groups have significant effects on divisional performances differently from large diversified firms.
Buchuk, Larrain, Munoz, & Urzua, 2014	Chile	1990–2009	Hierarchy-type	Agency theory, tunneling	2c-4	In Chilean pyramidal business groups, intra-group lending and borrowing does not lead to expropriation of minority shareholders in borrowing firms because of protective legislation.

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 5
(Continued)

Author(s), year	Nation(s)	Sample period	Typology	Theoretical lens	Focus	Key findings related to corporate governance in business groups
Buysschaert et al., 2008	Belgium	2001	Companies affiliated with holding firms	Transaction cost, agency theory	2a-4, 1(2a-4)	The effect of group affiliation on profitability does not depend on group ownership.
Singh & Gaur, 2009	China and India	2007	Not explicit (diversified, pyramidal)	Agency theory Institutional perspective	2–4, 1(2-4)	Group affiliation and firm performance relationship is moderated by ownership concentration.

Note: The numbers in the "focus" column stand for the numbers in Figure 1.
The papers are listed first by order of themes, and then chronologically within individual themes.

Organizational Outcomes. The key question in this research stream is whether the way in which a business group is controlled and coordinated has an influence on the way in which the group crafts its strategies and structures. The fact that group membership is in some way affecting the strategic behavior of companies has been a relatively well-established research notion. It has been shown in a number of studies that business group membership, for instance, positively influences the propensity toward product diversification and internationalization (Chari, 2013; Gaur, Kumar & Singh, 2014; Kim, Kim & Hoskisson, 2010). It has also been shown that business group membership positively affects the propensity of innovation and organizational learning of their member companies (Lincoln, Ahmadjian & Mason, 1998; Lodh, Nandy & Chen, 2014; Ma, Yiu & Zhou, 2014). Nevertheless, what remains less researched is to connect the strategic behavior of group's affiliates to specific devices for control and coordination, including pyramids and/or board interlocks. There is, for instance, a fundamental difference between groups employing pyramidal control structures and those based on horizontal relations (between the holding apex and the affiliated companies) through interlocks. While in the first case we could expect a stricter, hierarchical control and channel of authority, which may result in more rigid, center-dependent strategies, in the second we can expect a loosely coupled relation which does not, up to a certain point, interfere with the autonomy of the single operating units.

The prior literature has suggested that pyramidal structures, whereby the family maintains effective control with a limited capital participation, are linked to the expansion of businesses in a business group (Cuervo-Cazurra, 2006). However, there has been little research on how pyramidal structures in business groups actually influence the growth strategies of groups and their affiliates. A rare study by Kali and Sarkar (2011) is a good starting point that shows that affiliates with wedge (between control and cash-flow rights of controlling owners) lower than the core firm of a group are more likely to be operating in unrelated activities. Hence, lower chains of a pyramid are used for diversification into various businesses, which makes it difficult for outside vinvestors to decipher the activities inside a group, and become in itself a tool to expropriate minority shareholders. Regarding the relationships between board characteristics of group firms and organizational outcomes, on the other hand, a good example of a research roadmap in this direction is provided by Boyd and Hoskisson (2010), who suggest introducing the analysis of board structures and their interlocks as drivers for understanding the basic strategic outcomes of business groups.

Performance Outcomes. The dominant strand of research in this stream relates to the relationships between pyramidal structures and their performance outcomes. Pyramids, as control/coordination mechanisms, have a relevant impact on performances both at the level of the individual operating companies belonging to a group and at the group level as a whole. The available literature in the field of finance has extensively examined one aspect of this "structure–performance" relationship, namely the fact that in the presence of pyramidal control, which derogates de facto at the so-called "proportionality principle," or one share–one vote, the market value of the companies belonging to the group is affected negatively (see, e.g., Core, Guay, & Rusticus, 2006). Some research has stressed the destruction of value taking place in pyramidal structures (Villalonga & Amit, 2006), while others convincingly demonstrate how pyramidal structures harm minority shareholders, and at the same time deviation from one share–one vote depresses the member firm's performance and its market value (Orbay & Yurtoglu, 2006). Several empirical works have shown evidence of tunneling and expropriation practices to have a clearly direct negative impact on the market value of companies belonging to a group (Almeida, Park, Subrahmanyam, & Wolfenzon, 2011). In turn, historical research has examined the diffusion of pyramidal structures in business groups, and argued that the scarcer they are, the higher is the level of transparency and efficiency of financial markets (Bank & Cheffins, 2010). Nevertheless, this research question is not entirely resolved. Some influential research has argued that not all business groups are associated with profit tunneling from minority shareholders, and such expropriation is not limited to business groups (Khanna & Yafeh, 2007). Further, Morck (2010) argues that as minority shareholders expect lower returns from firms in pyramidal structures, they discount the stock prices of their invested firms, and as such minority

© 2015 John Wiley & Sons Ltd

shareholders are not exploited and get a fair return from their investments.

The impact of pyramidal control on corporate performance in terms of *earnings* is even more controversial (Carney, Gedajlovic, Heugens, Van Essen, & Van Oosterhout, 2011). Some research, based on solid evidence, claims a negative effect. Observing a panel of Chinese private business groups, Tian, Zhao, and Zhu (2010) argue that affiliates in pyramidal groups tend to underperform due to "earnings management" by owners. The same perspective is shared by other researchers in different countries, such as Turkey (Yurtoglu, 2000), Taiwan (Shyu, 2013), and Malaysia (Malan, Salamudin, & Ahmad, 2014). Other authors, however, share a more cautious approach. As far as financial liquidity, access to internal capital markets, and the availability of intra-group resources is concerned, for instance, business group affiliation and pyramids seem to have a positive effect (Bena and Ortiz-Molina, 2013; Carney & Gedajlovic, 2002). In a meta-analysis, Carney et al. (2011) have argued that the cost of business group affiliation slightly outweighs its benefits in terms of the resulting accounting performance. Very few studies, or perhaps none, however, assess the relationship between pyramidal control and other kinds of performance, such as the longevity of affiliates, for instance.

On the other hand, the extent to which director interlocks as control and coordination mechanisms affect the efficiency of the group's members has been the subject of relatively limited research effort (see, e.g., White, Hoskisson, Yiu, & Bruton, 2008). Despite the fact that we were able to find a number of studies that looked at the roles of director interlocks and boards in business groups, overall evidence on the actual "functioning" of these devices and their performance outcomes is limited. For instance, how in reality do the interlocking family board members, professional managers, and outside directors interact, formulate, and execute strategies for the whole group? (Üsdiken, 2010). What is the best combination and use of such board ties to gain access to different resources and capabilities, and ultimately to achieve higher returns? Some studies (Colpan, 2010; Tsui-Auch & Yoshikawa, 2010) suggest that CEOs in these groups have only little power, and they stay as "eventual representative of the family," while outside board members are incorporated for "cosmetic" reasons. This may suggest that it is only the family members that are the key decision makers and only family interlocks matter. Overall, unfortunately, there are few attempts to understand the actual "functioning" and performance outcomes of director interlocks as well as boards in governing the business groups.

DIRECTIONS FOR FUTURE RESEARCH

As discussed above, there is a cumulative body of research on the governance of business groups, while there remains still much work to be done. Based on the gaps in the literature that we have identified in this paper, we propose four high-priority avenues for research that deserve particular attention: comprehensive and synthesized approach, ownership goals and performance consequences, functioning of the boards, and cross-national and longitudinal approaches. This section therefore offers a research agenda centered on these four topics and future research questions stemming out of our examination of the literature.

Direction 1: Comprehensive and Synthesized Approach

First is to draw on the research tracks identified above and investigate the relationship between prevailing business group governance and organizational and performance outcomes with a more comprehensive and synthesized approach (Desender, Aguilera, Crespi & García-Cestona, 2013). While we have some fragmented knowledge in the abovementioned dimensions, there is still a pressing need to examine the direct and moderating relationships between those dimensions to come up with a more complete and comprehensive picture. For instance, we have little evidence on whether there is any preference in terms of the use of equity ties, director interlocks, social ties, and other control and coordination mechanisms depending on the ownership composition (family, state, banks, and others) of business groups. There is also some potential to explore the relationship between ownership types (and concentration) and board characteristics and composition in groups' firms. Does increasing family concentration in business groups, for instance, mean less role for professional managers as well as outside directors in the group's apex firm and its operating units? In a related vein, there is still little knowledge on the relationships between different control and coordination mechanisms employed in business groups. Are they substitutes or complements? Which types of control mechanisms can complement, and which other types substitute each other?

A related and more pressing opportunity is to examine the effects of such governance attributes on the organizational and performance outcomes of business groups with a more dynamic and co-evolutionary context. This is because it is not only that certain governance attributes may end up in certain strategies, structures, and performance outcomes, but also depending on such outcomes, business groups may actually take different types of governance attributes. For instance, increased internationalization and innovation activities of a business group firm may attract more foreign shareholders (to that firm, or its apex firm), who may pressure the group to increase its transparency, dissolve some complex ties among group firms, and even incorporate outside directors.[5] Some research, then, has tested the moderating effects of different group ownership on the group affiliation and performance relationships. Singh and Gaur (2009), for instance, in their study of Indian firms, argue that the group affiliation–firm performance relationship is moderated by ownership concentration. Their study shows that the stronger negative effect of group affiliation was decreased in the case of a higher family ownership concentration. Unfortunately, the type of research that examines these types of moderating relationships is scarce; other examples include Buysschaert, Deloof, Jegens and Rommens (2008) and Kim et al. (2010). The lack of established knowledge about the interaction of these forces calls for future research to take an integrated and dynamic approach.

Finally, governance structures depend also on the institutional context that they are set in, and upcoming research

© 2015 John Wiley & Sons Ltd

should formulate testable concrete hypotheses in incorporating the changes and differences of governance attributes and their outcomes in such context (Belenzon & Berkovitz, 2008; Chittoor, Kale, & Puranam, 2015; Weimer & Pape, 1999). A number of studies have used the Asian financial crisis of 1997 as a natural testing environment for this type of analysis. Chang and Shin (2006), for instance, suggest that CEO turnover sensitivity to performance is greater in chaebol firms than in stand-alone ones after the Asian financial crisis. Tsui-Auch and Lee (2003) also show that after the Asian currency crisis, Singaporean Chinese business groups absorbed more professional managers, while Korean chaebol intensified family control. Robust hypothesis building and testing are necessary to ultimately understand the varying governance effects in different institutional contexts (see, e.g., Zattoni, Pedersen, & Kumar, 2009). This proposition also connects to our fourth research direction below that calls for more cross-national research.

Direction 2: Ownership Goals and Performance Consequences

One of the most promising opportunities for future research that we have discovered is related to the complex relationships between the ownership of business groups and the performance consequences under such ownership. As already suggested in the literature (e.g., Cuervo-Cazurra, 2006), the prevailing ownership characteristics of business groups have an effect on their overall strategies, structures, as well as performance outcomes.

If the nature of ownership and its influence on the strategies and structures of the group deserve more attention than is currently available in existing research (as we mentioned above), an equally relevant and pressing issue concerns the theme of *performance*. Differences in performance levels have been detected between business group-affiliated firms and independent firms (Khanna & Rivkin, 2001) and among different typologies of business groups (Cuervo-Cazurra, 2006). Available research, however, not only fails to adequately examine group-level performance (as opposed to affiliate performance), but it also fails in deepening the concept of performance itself, which is apparently identified with *financial performance* in terms of returns over, for instance, the investments or the assets. A more promising direction of research is thus the incorporation of different conceptual dimensions of performance in the analysis, including non-financial performance, which may be the primary goal of certain categories of owners.

It has been suggested in the literature that prevalent ownership categories are traditionally associated to goals toward which strategies can be directed (Cuervo-Cazurra, 2006; Mayer & Whittington, 1996): in the case of state ownership, groups are often used in order to enhance the stability of industries, to sustain employment, or stabilize supply. Families employ business groups in order to allow equilibrium in the exploitation of family resources and to grant an appropriate professional outcome (such as jobs) and personal benefit (such as prestige) for family members (Cuervo-Cazurra, 2006; Morck, 2010). Further, the case of family business groups, which pursue unrelated diversification in order to accommodate properly the needs of different family members to lead dissimilar business lines to avoid conflict among individual family members, is a clear example of how a specific governance dimension (ownership) is influencing the strategy of the group as well as the concept of performance used to assess the success (or failure) of that strategy (Colli, 2012a, 2012b).

Although less analyzed in the literature, other types of groups, such as widely-held groups and bank-centered groups, also illustrate different logics. Widely-held business groups expand both to cope with management's own willingness to enlarge influence and power, and also with the goal to keep high profitability levels through product diversification. In bank-centered groups, banks in charge of coordinating business groups through ownership stakes, as may be the case in several bank-centered systems both in Asia and Europe, are likely to influence the process of diversification in order to raise both profitability levels, but also to leverage on the group's internal credit market in order to minimize the risk inherent in the lender's position (Makino & Yiu, 2014: 570).

Informed by qualitative arguments in the abovementioned studies and drawing on multiple theoretical perspectives referred to earlier, we therefore encourage scholars to make more in-depth, qualitative as well as quantitative, examinations on the performance outcomes of business groups under different types of ownership. The "ultimate goals," financial and non-financial, that varying ownership aim to achieve should also contribute to our understanding of the role of the business group organization itself.

Direction 3: Functioning of the Boards

A third venue for future research, in the light of the assessment of the topic mentioned earlier, is the "functioning" of the boards and the roles assigned to the boards of directors in a business group. The investigation of the board's role and functions inside business groups is also a crucial step toward a theory of business groups' governance. Nevertheless, in-depth knowledge on the way the boards of the apex company and the operating companies work is almost non-existent. To start with, it is crucial for scholars to investigate how the boards of group firms are taking decisions and what roles individual directors are playing in that process.

A particularly promising area for research is therefore closely examining the "real" functions that boards of directors and top executives play in the group firms. This generally necessitates a close and deep investigation of business groups not only through statistical data but also through interviews and archival work (including board minutes, when available). To start with, however, researchers can consider some of the following questions: Are boards of the subsidiaries a replication of those in the parent company or are they actually independent? What are the relations of the members of a group firm's board with the other group firm's directors? Are subsidiaries' boards rubber-stamping the decisions taken at the central level or are they enjoying substantial decisional autonomy? Some research (Boyd & Hoskisson, 2010; Colpan, 2010), for instance, suggests that especially in case of family-controlled business groups, families often form another "invisible" institution like a family council in which all the critical decisions for the whole group are made. If this understanding of business group governance is correct, then the roles of

© 2015 John Wiley & Sons Ltd

individual operating companies' boards may become simple rubber-stamping at the extreme. Of course, the realization of such interference may depend on several factors like the direct and indirect equity stakes the family has in individual operating units, director interlocks they employ, and other mechanisms. This may also depend on the institutional context, with more professionalism taking place in more market-oriented economies (Chung & Luo, 2008a; Üsdiken, 2010). But eventually, unless the actual functioning of the boards are recognized, simplistic examinations on the composition and characteristics of board members may be misleading to comprehend the real governance of business groups.

Direction 4: Cross-National and Longitudinal Approaches

Finally, cross-national and longitudinal studies are urgently needed to understand the differences in governance mechanisms of business groups and their performance outcomes in different emerging economies and developed nations and over long periods of time. Our tables show that the dominant majority of business group governance research has been conducted on single national economies (particularly in Asia), rather than taking a comparative cross-national approach. To start with, therefore, systematic cross-national research is an immense opportunity to undertake in this literature. The necessity of international comparisons have been pointed out in the most recent research on business groups, which explicitly emphasizes a cross-national approach in order to understand similarities and differences of business groups across different institutional contexts (Colpan & Hikino, 2010, 2016).

The research on business groups has frequently highlighted the heterogeneous diffusion of business groups across different geographic locations depending on specific institutional and historical factors. Business groups have been, therefore, implicitly or explicitly, considered as a relevant dimension in assessing the variety of firms across different capitalistic systems and economic microstructures (Colpan & Hikino, 2016). In management research (Whittington & Mayer, 2000) and organizational sociology (Fligstein, 1990; Whitley, 1999), for instance, the diffusion of business groups has been interpreted as a sort of resilient "institutional perversity" in continental European countries, differentiating them from US big business – characterized by integrated multidivisional structures. This immediately places business groups, as alternative organizational structures, at the core of the literature related to the so-called "varieties of capitalism approach." They are a relevant feature of coordinated market economies in which the prevailing collaborative attitudes among firms find a concrete outcome in the structure of inter-firm group relations. The study of the resilience of business groups in developed economies as efficient governance structures suggests a key relevance in particular when they are compared with those in emerging markets. Assuming that they have different purposes and hence strategic orientations in the different contexts of emerging and mature economies, a comparative analysis of the governance mechanisms of business groups at different stages of economic development is a valuable field of research still to be explored.

Being a permanent feature in some corporate economies, the long-term analysis of the role played by business groups over time is another promising field of research in which management scholars as well as business historians can offer a relevant contribution. In this longitudinal approach, first we see a need to examine the change and continuity taking place in business group governance. Üsdiken (2010) suggests that despite all the economic and institutional transitions emerging markets have been going through, there is limited change in the governance of business groups with persistent family control despite greater incorporation of salaried managers. The available evidence is rather scant and scattered, however, suggesting future research opportunities in this direction (Üsdiken, 2010). Second, even longer-term and historical approaches to business groups in different phases of development of modern economies may be another fruitful direction. Colli and Vasta (2015) put forward, for instance, a good example offering a taxonomy of business group development in the course of over 100 years of Italian economic history, encompassing both ownership and strategic dimensions. In the long run (and in coincidence with economic and institutional transformations), business groups assume different forms, orientation, and purposes, passing from horizontal collusive purposes to vertical hierarchical structures centered on families and the state. This kind of investigation will likely require long-term qualitative and/or quantitative data, but it will surely be valuable in informing future theory and empirical studies on the governance of business groups in different phases of economic development.

CONCLUSION

The aim of the present research was to offer a review, synthesis, and extension of the literature on the governance of business groups. After having collected the most prominent work published in several scholarly journals and books addressing issues connected to corporate governance issues in business groups, we have proposed a conceptualization of the main research questions they address and classified them according to their research themes.

Our analysis shows that academic research on corporate governance in business groups has been increasing but is still a developing field. Available analyses make use of the main theoretical frameworks in use in general in corporate governance research. However, there are several areas of research, which still need stronger conceptualization and empirical work, leaving many opportunities for future studies. Given the increasing relevance of business groups in the corporate landscape of emerging and developed economies, there is surely a pressing need to substantiate and extend the findings of previous studies.

Our study identifies four avenues for future research on corporate governance in business groups. This includes the examination of the complex relationships and co-evolutionary processes among corporate governance attributes, and organization and performance outcomes of business groups; the effects of ownership goals on groups' performance outcomes; the role and the actual functioning of boards inside business groups; as well as analyses of cross-national comparisons and long-term development of business group governance. In summary, we hope that this article will create greater awareness on

© 2015 John Wiley & Sons Ltd

business groups and their governance, and encourage scholars to contribute to our understanding the "inside the black-box" of business groups.

ACKNOWLEDGEMENTS

We would like to thank the Special Issue Editor Ruth Aguilera, Journal Editor Alessandro Zattoni and three anonymous reviewers for their valuable comments and suggestions to improve this paper.

NOTES

1. The most recent work by Holmes et al. (2015), which reviews business group research in strategy-related fields, also makes a similar argument to these two previous studies.
2. We have selected journals that cover governance-related topics from the top 50 SSCI journals listed under "business", "management," and "finance" areas based on their impact factor in 2013. We have then added three major business history journals to that list.
3. We note that a predominant majority of the papers in this review examine the relationships in our specified unilateral relation, rather than examining reverse causality among constructs.
4. China, however, is an anomaly where state is the dominant controlling owner.
5. On the impact of internationalization on ownership and governance attributes, see, e.g., Sheng and Silva Pereira (2014).

APPENDIX: List of Journals Covered in this Review

Academy of Management Annals
Academy of Management Journal
Academy of Management Perspectives
Academy of Management Review
Administrative Science Quarterly
Asia Pacific Journal of Management
British Journal of Management
Business History
Business History Review
California Management Review
Corporate Governance: An International Review
Enterprise and Society
Entrepreneurship Theory and Practice
Family Business Review
Harvard Business Review
Journal of Corporate Finance
Journal of Finance
Journal of Financial Economics
Journal of International Business Studies
Journal of Management
Journal of Management Studies
Journal of World Business
Long Range Planning
Management and Organization Review
Management Science
Organization Science
Organization Studies
Review of Finance
Review of Financial Studies
Strategic Management Journal

REFERENCES

Aganin, A. & Volpin, P. 2005. The history of corporate ownership in Italy. In R. K. Morck (Ed.), ***The history of corporate governance around the world***: 325–361. Chicago, IL: University of Chicago Press.

Aldrighi, D. M. & Postali, A. S. 2010. Business groups in Brazil. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 353–386. Oxford: Oxford University Press.

Almeida, H., Park, S. Y., Subrahmanyam, M. G., & Wolfenzon, D. 2011. The structure and formation of business groups: Evidence from Korean *chaebols*, ***Journal of Financial Economics***, 99: 447–475.

Almeida, H. & Wolfenzon, D. 2006. A theory of pyramidal ownership and family business groups, ***The Journal of Finance***, 61: 2637–2680.

Amatori, F. 1997. Growth via politics: Business groups Italian style. In T. Shiba & M. Shimotani (Eds.), ***Beyond the firm: Business groups in international and historical perspective***. Oxford: Oxford University Press.

Amsden, A. 2001. ***The rise of the "rest": Challenges to the West from late-industrializing economies***. Oxford: Oxford University Press.

Bae, G. S., Cheon, Y. S., & Kang, J. K. 2008. Intragroup propping: Evidence from the stock-price effects of earnings announcements by Korean business groups, ***The Review of Financial Studies***, 21: 2015–2060.

Bae, K. H., Kang, J. K., & Kim, J. M. 2002. Tunneling or value added? Evidence from mergers by Korean business groups, ***The Journal of Finance***, 57: 2695–2740.

Baek, J., Kang, J., & Lee, I. 2006. Business groups and tunneling: Evidence from private securities offerings by Korean chaebols, ***The Journal of Finance***, 61: 2415–2449.

Baek, J., Kang, J., & Park, K. S. 2004. Corporate governance and firm value: Evidence from the Korean financial crisis, ***Journal of Financial Economics***, 71: 265–313.

Bank, S. A. & Cheffins, B. R. 2010. The corporate pyramid fable, ***Business History Review***, 84: 435–458.

Barbero, M. I. & Jacob, R. (Eds.). 2008. ***La neuva historia de empresas en Améica Latina y España***. Buenos Aires: Temas.

Barca, F. & Becht, M. 2001. ***The control of corporate Europe***. Oxford: Oxford University Press.

Belderbos, R. A. & Heijltjes, M. G. 2005. The determinants of expatriate staffing by Japanese multinationals in Asia: Control, learning and vertical business groups, ***Journal of International Business Studies***, 36: 341–354.

Belenzon, S. & Berkovitz, T. 2008. Business group affiliation, financial development and market structure: Evidence from Europe. Available at SSRN: http://ssrn.com/abstract=1086882.

Belenzon, S. & Berkovitz, T. 2010. Innovation in business groups, ***Management Science***, 56: 519–535.

Bena, J. & Ortiz-Molina, H. 2013. Pyramidal Ownership and the Creation of New Firms, ***Journal of Financial Economics***, 108: 798–821.

Bertrand, M., Johnson, S., Samphantharak, K., & Schoar, A. 2008. Mixing family with business: A study of Thai business groups and the families behind them, ***Journal of Financial Economics***, 88: 466–498.

Bertrand, M., Mehta, P., & Mullainathan, S. 2002. Ferreting out tunnelling: An application to Indian business groups, ***Quarterly Journal of Economics***, 117: 121–148.

Binda, V. 2012. Strategy and structure in large Italian and Spanish firms, 1950–2002, ***Business History Review***, 86: 503–525.

Binda, V. & Colli, A. 2011. Changing big business in Italy and Spain, 1973–2003: Strategic responses to a new context, ***Business History***, 53: 14–39.

Boutin, X., Cestone, G., Fumagalli, C., Pica, G., & Serrano-Velarde, N. 2013. The deep pocket effect of internal capital markets, ***Journal of Financial Economics***, 109: 122–145.

Boyd, B. & Hoskisson, R. E. 2010. Corporate governance of business groups. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford***

© 2015 John Wiley & Sons Ltd

handbook of business groups: 670–695. Oxford: Oxford University Press.
Bradley, M. H. & Sundaram, A. K. 2003. The emergence of shareholder value in the German corporation. EFA 2004 Maastricht Meetings Paper No. 1467.
Brookfield, J. 2010. The network structure of big business in Taiwan, ***Asia Pacific Journal of Management***, 27: 257–279.
Buchuk, D., Larrain, B., Munoz, F., & Urzua, F. 2014. The internal capital markets of business groups: Evidence from intra-group loans, ***Journal of Financial Economics***, 112: 190–212.
Buysschaert, A., Deloof, M., Jegens, M., & Rommens, A. 2008. Is group affiliation profitable in developed countries? Belgian evidence, ***Corporate Governance: An International Review***, 16: 504–518.
Byun, H., Choi, S., Hwang, L., & Kim, R. 2013. Business group affiliation, ownership structure and the cost of debt, ***Journal of Corporate Finance***, 23: 311–331.
Campbell, T. L. & Keys, P. Y. 2002. Corporate governance in South Korea: The chaebol experience, ***Journal of Corporate Finance***, 8: 373–391.
Carney, M. & Gedajlovic, E. 2002. The coupling of ownership and control and the allocation of financial resources: Evidence from Hong Kong, ***Journal of Management Studies***, 39: 123–146.
Carney, M., Gedajlovic, E. R., Heugens, P. P., Van Essen, M., & Van Oosterhout, J. H. 2011. Business group affiliation, performance, context, and strategy: A meta-analysis, ***Academy of Management Journal***, 54: 437–460.
Chang, J., Cho, Y. J., & Shin, H. H. 2007. The change in corporate transparency of Korean firms after the Asian financial crisis: An analysis using analysts' forecast data, ***Corporate Governance: An International Review***, 15: 1144–1167.
Chang, J. J. & Shin, H. H. 2006. Governance system effectiveness following the crisis: The case of Korean business group headquarters, ***Corporate Governance: An International Review***, 14: 85–97.
Chang, S. J. 2003. Ownership structure, expropriation, and performance of group affiliated companies in Korea, ***Academy of Management Journal***, 46: 238–253.
Chang, S. J. 2006. Introduction: Business groups in East Asia. In S. J. Chang (Ed.), ***Business groups in East Asia: Financial crisis, restructuring and new growth***: 1–26. Oxford: Oxford University Press.
Chang, S. J. & Hong, J. 2000. Economic performance of group-affiliated companies in Korea: Intragroup resource sharing and internal business transactions, ***Academy of Management Journal***, 43: 429–448.
Chang, S. J. & Hong, J. 2002. How much does the business group matter in Korea?, ***Strategic Management Journal***, 23: 265–274.
Chari, M. D. R. 2013. Business groups and foreign direct investments by developing country firms: An empirical test in India, ***Journal of World Business***, 48: 349–359.
Chernykh, L. 2008. Ultimate ownership and control in Russia, ***Journal of Financial Economics***, 88: 169–192.
Cheung, Y. L., Rau, P. R., & Stouraitis, A. 2006. Tunneling, propping, and expropriation: Evidence from connected party transactions in Hong Kong, ***Journal of Financial Economics***, 82: 343–386.
Chittoor, R., Kale, P., & Puranam, P. 2015. Business groups in developing capital markets: Towards a complementarity perspective, ***Strategic Management Journal***, 36: 1277–1296.
Chizema, A. & Kim, J. 2010. Outside directors on Korean boards: Governance and institutions, ***Journal of Management Studies***, 47: 109–129.
Choe, S. & Roell, T. W. 2007. What to shed and what to keep: Corporate transformation in Korean business groups, ***Long Range Planning***, 40: 465–487.
Chung, C.-N. 2001. Markets, culture and institutions: The emergence of large business groups in Taiwan, 1950s–1970s, ***Journal of Management Studies***, 38: 719–745.
Chung, C.-N. 2005. Beyond guanxi: Network contingencies in Taiwanese business groups, ***Organization Studies***, 27: 461–489.
Chung, C.-N. & Luo, X. 2008a. Human agents, contexts, and institutional change: The decline of family in the leadership of business groups, ***Organization Science***, 19: 124–142.
Chung, C.-N. & Luo, X. 2008b. Institutional logics or agency costs: The influence of corporate governance models on business group restructuring in emerging economies, ***Organization Science***, 19: 766–784.
Chung, C.-N. & Luo, X. R. 2013. Leadership succession and firm performance in an emerging economy: Successor origin, relational embeddedness, and legitimacy, ***Strategic Management Journal***, 34: 338–357.
Chung, C.-N. & Mahmood, I. P. 2010. Business groups in Taiwan. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 180–209. Oxford: Oxford University Press.
Chung, H. M. 2013. The role of family management and family ownership in diversification: The case of family business groups, ***Asia Pacific Journal of Management***, 30: 871–891.
Chung, H. M. & Chan, S. T. 2012. Ownership structure, family leadership, and performance of affiliate firms in large family business groups, ***Asia Pacific Journal of Management***, 29: 303–329.
Claessens, S., Djankov, S., & Lang, L. P. 2000. The separation of ownership and control in East Asian corporations, ***Journal of Financial Economics***, 88: 81–112.
Colli, A. 2012a. Coping with the Leviathan: Minority shareholders in state-owned enterprises – Evidence from Italy, ***Business History***, 55: 1–25.
Colli, A. 2012b. Contextualizing performances of family firms: The perspective of business history, ***Family Business Review***, 25: 243–277.
Colli, A. & Vasta, M. 2015. Large and entangled: Italian business groups in the long run, ***Business History***, 57: 64–96.
Colli, A., Rinaldi, A., & Vasta, M. 2015. The only way to grow? Italian Business groups in historical perspective, ***Business History***, doi: 10.1080/00076791.2015.1044518.
Colpan, A. M. 2010. Business groups in Turkey. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 486–525. Oxford: Oxford University Press.
Colpan, A. M. & Hikino, T. 2010. Foundations of business groups: Towards an integrated framework. In A. M. Colpan, T. Hikino, & J. R. Lincoln (Eds.), ***The Oxford handbook of business groups***: 15–66. Oxford: Oxford University Press.
Colpan, A. M. & Hikino, T. 2016. ***Business groups in the West***. Oxford: Oxford University Press.
Colpan, A. M., Hikino, T., & Lincoln, J. R. (Eds.). 2010. ***The Oxford handbook of business groups***. Oxford: Oxford University Press.
Core, J., Guay, W., & Rusticus, T. 2006. Does weak governance cause weak stock returns? An examination of firm operating performance and investors' expectations, ***The Journal of Finance***, 61: 655–687.
Crespí-Cladera, R. & Bru, L. 2006. Diversification of family business groups and board control. University of the Balearic Islands.
Cuervo-Cazurra, A. 2006. Business groups and their types, ***Asia Pacific Journal of Management***, 23: 419–437.
Davis, J. A., Schoorman, F. D., & Donaldson, L. 1997. Toward a stewardship theory of management, ***Academy of Management Review***, 22: 20–47.
Demirag, I. & Serter, M. 2003. Ownership patterns and control in Turkish listed companies, ***Corporate Governance: An International Review***, 11: 40–51.
Desender, K., Aguilera, R. V., Crespi, R., & García-Cestona, M. 2013. When does ownership matter? Board characteristics and behavior, ***Strategic Management Journal***, 34: 823–842.
Dharwadkar, R., George, G., & Brandes, P. 2000. Privatization in emerging economies: An agency theory perspective, ***Academy of Management Review***, 25: 650–669.
Donaldson, L. & Davis, J. A. 1991. Stewardship theory or agency theory: CEO governance and shareholder returns, ***Australian Journal of Management***, 16: 49–65.

© 2015 John Wiley & Sons Ltd

Faccio, M. & Lang, J. P. 2002. The ultimate ownership of Western European corporations, ***Journal of Financial Economics***, 65: 365–395.

Feenstra, R. & Hamilton, G. 2006. ***Emergent economies, divergent paths: Economic organization and international trade in South Korea and Taiwan***. Cambridge: Cambridge University Press.

Fligstein, N. 1990. ***The transformation of corporate control***. Cambridge, MA: Harvard University Press.

Fracchia, E., Mesquita, L., & Quiroga, J. 2010. Business groups in Argentina. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 325–352. Oxford: Oxford University Press.

Franks, J. & Mayer, C. 2001. Ownership and control of German corporations, ***The Review of Financial Studies***, 14: 943–977.

Gaur, A. S., Kumar, V., & Singh, D. 2014. Institutions, resources and internationalization of emerging economy firms, ***Journal of World Business***, 49: 12–20.

Ghemawat, P. & Khanna, T. 1998. The nature of diversified business groups: A research design and two case studies, ***Journal of Industrial Economics***, 46: 35–61.

Gökşen, N. S. & Üsdiken, B. 2001. Uniformity and diversity in Turkish business groups: Effects of scale and time of founding, ***British Journal of Management***, 12: 325–340.

Goldstein, A. 2010. Business groups in South Africa. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 547–574. Oxford: Oxford University Press.

Gomez-Mejia, L., Makri, M., & Larraza Kintana, M. 2010. Diversification decisions in family-controlled firms, ***Journal of Management Studies***, 2: 223–252.

Gonzalez, M., Guzman, A., Pombo, C., & Trujillo, M.-A. 2014. Family involvement and dividend policy in closely-held firms, ***Family Business Review***, 27: 365–385.

Gopalan, R., Nanda, V., & Seru, A. 2007. Affiliated firms and financial support: Evidence from Indian business groups, ***Journal of Financial Economics***, 86: 759–795.

Gopalan, R., Nanda, V., & Seru, A. 2014. Internal capital market and dividend policies: Evidence from business groups, ***The Review of Financial Studies***, 27: 1102–1142.

Granovetter, M. 1995. Coase revisited: Business groups in the modern economy, ***Industrial and Corporate Change***, 4: 93–130.

Granovetter, M. 2005. Business groups in social organization. In N. Smelser & R. Swedberg (Eds.), ***The handbook of economic sociology***: 429–450. Princeton University Press: Princeton, NJ.

Guillén, M. F. 2010. Capability building in business groups. In A. M. Colpan, T. Hikino, & J. R. Lincoln (Eds.), ***The Oxford handbook of business groups***: 743–762. Oxford: Oxford University Press.

Guriev, S. 2010. Business groups in Russia. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 526–546. Oxford: Oxford University Press.

He, J., Mao, X., Rui, O. M., & Zha, X. 2013. Business groups in China, ***Journal of Corporate Finance***, 22: 166–192.

Holmes, M., Hoskisson, R. E., Wam, W. P., & Holcomb, T. R. 2015. Business group research: a comprehensive review, theoretical framework, and future research agenda. Working Paper.

Hoshino, T. 2010. Business groups in Mexico. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 424–458. Oxford: Oxford University Press.

Iacobucci, D. & Rosa, P. 2010. The growth of business groups by habitual entrepreneurs: The role of entrepreneurial teams, ***Entrepreneurship: Theory and Practice***, 34: 345–377.

Inoue, C. F. K. V., Lazzarini, S. G., & Musacchio, A. 2013. Leviathan as a minority shareholder: Firm-level implications of state equity purchases, ***Academy of Management Journal***, 56: 1775–1801.

Jang, H. & Kim, J. 2002. Nascent stages of corporate governance in an emerging market: Regulatory change, shareholder activism and Samsung Electronics, ***Corporate Governance: An International Review***, 10: 94–105.

Jensen, M. C. & Meckling, W. H. 1976. Theory of the firm: Managerial behavior, agency costs, and ownership structure, ***Journal of Financial Economics***, 3: 305–360.

Joh, S. W. 2003. Corporate governance and firm profitability: Evidence from Korea before the economic crisis, ***Journal of Financial Economics***, 68: 287–322.

Johnson, S., La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. 2000. Tunnelling, ***American Economic Review***, 90: 22–27.

Jones, G. 2000. ***Merchants to multinationals***. Oxford: Oxford University Press.

Kang, J. K., Lee, I., & Na, H. S. 2010. Economic shock, owner-manager incentives, and corporate restructuring: Evidence from the financial crisis in Korea, ***Journal of Corporate Finance***, 16(3): 333–351.

Kali, R. & Sarkar, J. 2011. Diversification and tunneling: Evidence from Indian business groups, ***Journal of Comparative Economics***, 39: 349–367.

Khanna, T. & Palepu, K. 2000. Is group affiliation profitable in emerging markets? An analysis of diversified business groups, ***Journal of Finance***, 55: 867–891.

Khanna, T. & Palepu, K. 2010. ***Winning in emerging markets: A road map for strategy and execution***. Cambridge, MA: Harvard University Press.

Khanna, T. & Rivkin, J. W. 2001. Estimating the performance effects of business groups in emerging economies, ***Strategic Management Journal***, 22: 45–74.

Khanna, T. & Rivkin, J. W. 2006. Interorganizational ties and business group boundaries: Evidence from an emerging economy, ***Organization Science***, 17: 333–352.

Khanna, T. & Yafeh, Y. 2007. Business groups in emerging markets: Paragons or parasites?, ***Journal of Economic Literature***, 45: 331–372.

Kikkawa, T. 1995. Kigyo Shudan: The formation and functioning of enterprise groups, ***Business History***, 37: 44–53.

Kim, B. & Lee, Y. 2001. Global capacity expansion strategies: Lessons learned from two Korean carmakers, ***Long Range Planning***, 34: 309–333.

Kim, D.-W. 2003. Interlocking ownership in the Korean chaebol, ***Corporate Governance: An International Review***, 11: 132–142.

Kim, H. 2010. Business groups in South Korea. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 157–179. Oxford: Oxford University Press.

Kim, H., Kim, H., & Hoskisson, R. L. 2010. Does market-oriented institutional change in an emerging economy make business-group-affiliated multinationals perform better? An institution-based view, ***Journal of International Business Studies***, 41: 1141–1160.

Kock, C. & Guillén, M. F. 2001. Strategy and structure in developing countries: Business groups as an evolutionary response to opportunities for unrelated diversification, ***Industrial & Corporate Change***, 10: 1–37.

Kosenko, K. & Yafeh, Y. 2010. Business groups in Israel. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 459–487. Oxford: Oxford University Press.

La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. 1999. Corporate ownership around the world, ***The Journal of Finance***, 54: 471–517.

Lai, G. M.-H. 1999. Know who you are doing business with in Japan: A managerial view of keiretsu and keiretsu business groups, ***Journal of World Business***, 34: 423–448.

Lauterbach, B. & Yafeh, Y. 2011. Long-term changes in voting power and control structure following the unification of dual class shares, ***Journal of Corporate Finance***, 17: 215–228.

Lechner, C. & Leyronas, C. 2009. Small-business group formation as an entrepreneurial development model, ***Entrepreneurship: Theory and Practice***, 33: 645–667.

Lee, J.-H. & Gaur, A. S. 2013. Managing multi-business firms: A comparison between Korean chaebols and US diversified firms, ***Journal of World Business***, 48: 443–454.

Lee, K. & Jin, X. 2009. The origins of business groups in China: An empirical testing of the three paths and the three theories, ***Business History***, 51: 77–99.

© 2015 John Wiley & Sons Ltd

Lee, K. & Kang, Y. 2010. Business groups in China. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 210–236. Oxford: Oxford University Press.

Leff, N. H. 1976. Capital markets in less developed countries: The group principle. In R. McKinnon (Ed.), ***Money and finance in economic growth and development: Essays in honor of Edward S. Shaw***: 97–122. New York: Marcel Dekker.

Leff, N. H. 1978. Industrial organization and entrepreneurship in the developing countries: The economic groups, ***Economic Development and Cultural Change***, 26: 661–675.

Lefort, F. 2010. Business groups in Chile. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 387–423. Oxford: Oxford University Press.

Lincoln, J. R., Ahmadijan, C., & Mason, E. 1998. Organizational learning and purchase-supply relations in Japan: Hitachi, Matsushita and Toyota compared, ***California Management Review***, 40: 241–264.

Lincoln, J. R. & Shimotani, M. 2010. Business networks in postwar Japan: Whither the keiretsu?. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 127–156. Oxford: Oxford University Press.

Lodh, S., Nandy, M., & Chen, J. 2014. Innovation and family ownership: Empirical evidence from India, ***Corporate Governance: An International Review***, 22: 4–23.

Lu, Y. & Yao, J. 2006. Impact of state ownership and control mechanisms on the performance of group affiliated companies in China, ***Asia Pacific Journal of Management***, 23: 485–503.

Lynn, L. H. & Rao, H. 1995. Failures of intermediate forms: A study of the Suzuki Zaibatsu, ***Organization Studies***, 16: 55–80.

Ma, X., Yiu, D. W., & Zhou, N. 2014. Facing global economic crisis: Foreign sales, ownership groups and corporate value, ***Journal of World Business***, 49: 87–100.

Mahmood, I. P. & Rufin, C. 2005. Government's dilemma: The role of government in imitation and innovation, ***Academy of Management Review***, 30: 338–360.

Mahmood, I. P., Zhu, H., & Zajac, E. J. 2011. Where can capabilities come from? Network ties and capability acquisition in business groups, ***Strategic Management Journal***, 32: 820–848.

Makino, S. & Yiu, D. W. 2014. A survey of strategic behavior and firm's performance in Asia. In M. A. Witt & G. Redding (Eds.), ***The Oxford handbook of Asian business systems***: 561–588. Oxford: Oxford University Press.

Malan, I., Salamudin, N., & Ahmad, N. 2014. Empirical research on characterization of pyramid structure and firm performance, ***Middle-East Journal of Scientific Research***, 21: 2156–2168.

Maman, D. 1999. Research note: Interlocking ties within business groups in Israel – A longitudinal analysis, 1974–1987, ***Organization Studies***, 20: 323–339.

Manikandan, K. S. & Ramachandran, J. 2015. Beyond institutional voids: Business groups, incomplete markets, and organizational form, ***Strategic Management Journal***, 36: 598–617.

Masulis, R., Pham, P., & Zein, J. 2011. Business groups around the world: Financing advantages, control motivations, and organizational choices, ***Review of Financial Studies***, 24: 3556–3600.

Mayer, M. & Whittington, R. 1996. The survival of the European holding company. In R. Whitley & P. H. Kristensen (Eds.), ***The changing European firm: Limits to convergence***. London: Routledge.

McGuire, J. & Dow, S. 2003. The persistence and implications of Japanese keiretsu organization, ***Journal of International Business Studies***, 34: 374–388.

Miyajima, H. & Kawamoto, S. 2010. Business groups in prewar Japan: Historical formation or legacy. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 97–126. Oxford: Oxford University Press.

Morck, R. 2010. The riddle of the great pyramids. In A. M. Colpan, T. Hikino, & J. R. Lincoln (Eds.), ***The Oxford handbook of business groups***: 602–628. Oxford: Oxford University Press.

Morck, R., Wolfenzon, D., & Yeung, B. 2005. Corporate governance, economic entrenchment, and growth, ***Journal of Economic Literature***, 43: 655–720.

Morck, R. & Yeung, B. 2003. Agency problems in large family business groups, ***Entrepreneurship: Theory and Practice***, 27: 367–382.

Morikawa, H. 1992. ***Zaibatsu: The rise and fall of family enterprise groups in Japan***. Tokyo: University of Tokyo Press.

Morikawa, H. 1997. Increasing organizational capabilities of large industrial enterprises, 1880s–1980s. In A. D. Chandler, Jr., F. Amatori, & T. Hikino (Eds.), ***Big business and the wealth of nations***: 307–335. Cambridge: Cambridge University Press.

Musacchio, A. & Lazzarini, S. G. 2014. ***Reinventing state capitalism: Leviathan in business, Brazil and beyond***. Cambridge, MA: Harvard University Press.

Nakamura, M. 2011. Adoption and policy implications of Japan's new corporate governance practices after the reform, ***Asia Pacific Journal of Management***, 28: 187–213.

Orbay, H. & Yurtoglu, B. B. 2006. The impact of corporate governance structures on the corporate investment performance in Turkey, ***Corporate Governance: An International Review***, 14: 349–364.

Paligorova, T. & Xu, Z. 2012. Complex ownership and capital structure, ***Journal of Corporate Finance***, 18: 701–716.

Pattnaik, C., Chang, J. J., & Shin, H. H. 2013. Business groups and corporate transparency in emerging markets: Empirical evidence from India, ***Asia Pacific Journal of Management***, 30: 987–1004.

Ren, B., Au, K. Y., & Birtch, T. A. 2009. China's business network structure during institutional transitions, ***Asia Pacific Journal of Management***, 26: 219–240.

Sacristan-Navarro, M. & Gomez-Anson, S. 2007. Family ownership and pyramids in the Spanish market, ***Family Business Review***, 20: 247–265.

San Román, E., Fernández Pérez, P., & Gil López, Á. 2014. As old as history: Family-controlled business groups in transport services: The case of SEUR, ***Business History***, 56: 1201–1222.

Sarkar, J. 2010. Business groups in India. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 294–324. Oxford: Oxford University Press.

Saxena, A. 2013. Transgenerational succession in business groups in India, ***Asia Pacific Journal of Management***, 30: 769–789.

Schneider, B. R. 2010. Business groups and the state: The politics of expansion, restructuring and collapse. In A. M. Colpan, T. Hikino, & J. R. Lincoln (Eds.), ***The Oxford handbook of business groups***: 650–669. Oxford: Oxford University Press.

Sheng, H. H. & Silva Pereira, V. 2014. Effects of internationalization on ownership structure: Evidence from Latin American firms. Brazilian Administration Review, 3: 10.1590/1807-7692bar2014353.

Shiba, T. & Shimotani, M. (Eds.). 1997. ***Beyond the firm: Business groups in international and historical perspective***. New York: Oxford University Press.

Shyu, J. 2013. Ownership structure, capital structure, and performance of group affiliation: Evidence from Taiwanese group-affiliated firms, ***Managerial Finance***, 39: 404–420.

Siegel, J. & Choudhury, P. 2012. A reexamination of tunneling and business groups: New data and new methods, ***The Review of Financial Studies***, 39: 1763–1798.

Singh, D. A. & Gaur, A. S. 2009. Business group affiliation, firm governance, and firm performance: Evidence from China and India, ***Corporate Governance: An International Review***, 17: 411–425.

Solomon, J., Solomon, A., & Park, C.-Y. 2002. The evolving role of institutional investors in South Korean corporate governance: Some empirical evidence, ***Corporate Governance: An International Review***, 10: 211–224.

Tabeta, N. & Rahman, S. 1999. Risk sharing mechanism in Japan's auto industry, ***Asia Pacific Journal of Management***, 16: 311–330.

Tian, G. G., Zhao, S., & Zhu, Y. 2010. How does the separation of ownership and control affect corporate performance?: The impact of earnings management in China. The 23rd Australasian Finance and Banking Conference.

© 2015 John Wiley & Sons Ltd

Tripathi, D. 2004. ***The Oxford history of Indian business***. New Delhi: Oxford University Press.
Tsui-Auch, L. S. & Lee, Y.-J. 2003. The state matters: Management models of Singaporean Chinese and Korean business groups, ***Organization Studies***, 24: 507–534.
Tsui-Auch, L. S. & Yoshikawa, T. 2010. Business groups in Singapore. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 267–293. Oxford: Oxford University Press.
Urzua Infante, F. 2009. Too few dividends? Groups' tunneling through chair and board compensation, ***Journal of Corporate Finance***, 15: 245–256.
Üsdiken, B. 2010. The kin and the professional: Top leadership in family business groups. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 696–716. Oxford: Oxford University Press.
Villalonga, B. & Amit, R. 2006. How do family ownership, control and management affect firm value?, ***Journal of Financial Economics***, 85: 385–417.
Wailerdsak, N. & Suehiro, A. 2010. Business groups in Thailand. In A. M. Colpan, T. Hikino, & J. Lincoln (Eds.), ***The Oxford handbook of business groups***: 237–266. Oxford: Oxford University Press.
Wei, K. C. J. & Zhang, Y. 2008. Ownership structure, cash flow, and capital investment: Evidence from East Asian economies before the financial crisis, ***Journal of Corporate Finance***, 14: 118–132.
Weimer, J. & Pape, J. C. 1999. A taxonomy of systems of corporate governance, ***Corporate Governance: An International Review***, 7: 152–166.
White, R. E., Hoskisson, R. E., Yiu, D. W., & Bruton, G. D. 2008. Employment and market innovation in Chinese business groups affiliated firms: The role of group control systems, ***Management and Organization Review***, 4: 225–256.
Whitley, R. 1999. ***Divergent capitalisms: The social structuring and change of business systems***. Oxford: Oxford University Press.
Whittington, R. & Mayer, M. 2000. ***The European corporation: Strategy, structure and social science***. Oxford: Oxford University Press.
Yildirim-Öktem, Ö. & Üsdiken, B. 2010. Contingencies versus external pressure: Professionalization in boards of firms affiliated to family business groups in late-industrializing countries, ***British Journal of Management***, 21: 115–130.
Yiu, D. W. 2011. Multinational advantages of Chinese business groups: A theoretical exploration, ***Management and Organization Review***, 7: 249–277.
Yiu, D. W., Chen, X., & Xu, Y. 2013. Corporate governance in business groups. In M. Wright, D. S. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***The Oxford handbook of corporate governance***: 465–488. Oxford: Oxford University Press.
Young, M. N., Peng, M. W., Ahlstrom, D., Bruton, G. D., & Jiang, Y. 2008. Corporate governance in emerging economies: A review of the principal–principal perspective, ***Journal of Management Studies***, 45: 196–220.
Yurtoglu, B. B. 2000. Ownership, control and performance of Turkish listed firms, ***Empirica***, 27: 193–222.
Zattoni, A., Pedersen, T., & Kumar, V. 2009. The performance of group-affiliated firms during institutional transition: A longitudinal study of Indian firms, ***Corporate Governance: An International Review***, 17: 510–523.

Andrea Colli is Professor of Economic History at the Department of Policy Analysis and Public Management, Bocconi University, Milan, Italy. His research interests range from the history of family firms, to small and medium-sized enterprises to corporate governance in historical perspective. He has published several articles in the main business history journals, and in journals of family business research. He has been associate review editor of *Family Business Review* since October 2012, and co-editor of *Business History* since 2013. He has edited, with Paloma Fernandez Perez, *The Endurance of Family Business: a Global Overview* (Cambridge University Press, 2013).

Asli M. Colpan is Associate Professor of Corporate Strategy at the Graduate School of Management and The Hakubi Center for Advanced Research, Kyoto University, Japan. She is also a visiting professor at Koç University, College of Administrative Sciences and Economics, Turkey. Her work has been published in such journals as *Industrial and Corporate Change*, *Journal of Management Studies*, and *Strategic Management Journal*. She is the co-editor of the *Oxford Handbook of Business Groups* (Oxford: Oxford University Press, 2010). She is currently an Associate Editor of *Asian Business & Management* and Senior Editor of *Management and Organizational History*.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 303–321

Corporate Governance in Banks

Kose John, Sara De Masi* and Andrea Paci

ABSTRACT

Manuscript Type: Review
Research Question/Issue: We survey the literature on corporate governance in banks in the US and international settings. We discuss how the specialness of banks, deposit insurance, high bank leverage, and bank regulation interact with bank governance. We evaluate bank governance from three perspectives: (1) maximizing bank equity value, (2) maximizing total enterprise value, and (3) maximizing social objectives. Our survey includes evidence on how bank governance differs from that of manufacturing firms. We also survey studies on managerial incentives in banks and their implications for bank performance and risk taking before and during the 2007–2008 financial crisis.
Research Findings/Insights: The high leverage (usually above 90 percent) of banking institutions gives rise to a trade-off between strengthening equity governance and maximizing enterprise value. Aligning managers very closely with shareholders can give rise to strong incentives for risk shifting to the detriment of firm value. The bank risk choices might also go against the societal objectives of a stable financial system.
Theoretical/Academic Implications: We provide a framework for the optimal design of bank governance and bank regulation, considering the objectives of both depositors and society-at-large in addition to those of bank shareholders. This framework could be especially important in determining risk choices by banks and the effects of such on the stability of the financial system.
Practitioner/Policy Implications: Our analysis of the literature surveyed has policy implications for bank regulation, top-management compensation in banks, and directives for design of governance in banks. We discuss implications for direct regulation of banks and regulation of bank governance. The findings surveyed provide guidance for board independence, board size, board composition, and incentive features in top-management compensation.

Keywords: Corporate Governance, Board of Director Mechanisms, Board Composition, Executive Compensation, Ownership Mechanisms

INTRODUCTION

In recent years, no other set of firms has been as closely examined as banks and financial institutions. Many papers and policies have been proposed, discussed, and enacted on every aspect of banking, finance, and governance. In particular, scholars and policymakers aim to answer the question, "What is special about banks and how might it affect bank governance?"

Starting in the 1980s, Eugene Fama (1985) investigated the differences between banks and nonfinancial companies, underlying their governance issues. Since then, many researchers have studied issues of banks' corporate governance in several countries (for general issues on corporate governance, see Laeven, 2013 and Levine, 2004; for a US perspective, see Adams & Mehran, 2003 and Mehran, Morrison, & Shapiro, 2012; for a European perspective, see Ferrarini, 2015 and Hopt, 2013; for an international perspective, see Acharya et al., 2009; Macey & O'Hara, 2003; and Mullineux, 2006). Banks have unique features that influence and interact with corporate governance mechanisms. Conflicts of interest between shareholders and debtholders, bank regulation, opacity, and complexity of bank activities are the main features that make bank governance different from that of nonfinancial companies. In spite of the existing research, many questions remain unanswered. Our purpose is to summarize the recent literature on the corporate governance of banks. We also provide a new framework for thinking about the role of corporate governance in banks.

Our novel framework is to examine corporate governance in banks from three different perspectives. First, consistent with the traditional framework, we examine corporate governance in banks from the point of view of aligning managers with shareholders. This governance has been called "equity governance" in banks. Second, we study corporate governance from the point of view of maximizing the total value of the bank, i.e., the total market value of the equity and the debt. This viewpoint is an important perspective for banks, which are highly leveraged institutions with debt claims (deposits) constituting more than 90 percent of capital claims (see the next section for additional discussion of this

*Address for correspondence: Sara De Masi, Department of Economics and Management, University of Florence, via delle Pandette, 9, Florence, Italy. Phone: +39 (055) 2759684; Fax: +39 (055) 2759737; E-mail: sara.demasi@unifi.it

© 2016 John Wiley & Sons Ltd
doi:10.1111/corg.12161

perspective). Third, we examine bank governance from the point of view of society at large (including participants in the economy who might not hold equity or debt claims in the bank). We view bank governance from the perspective of the social planner who is focused on the role of banks in a safe and sound financial system. The social planner has the ability to put in place mechanisms of regulation that can restrict the bank's activities, its investments and its capital structure. Regulation can also interact with the mechanisms of corporate governance, which would affect managerial incentives and choices (Hubbard & Palia, 1995; Walter, 2004). This social planner's perspective helps us to understand the interaction between bank regulation and bank governance.

Although a significant proportion of the corporate governance literature focuses on the conflict between shareholders and managers, in banks, the divergence of interests between shareholders and debtholders is prominent. In our survey, we highlight the natural conflict that exists between equity governance (corporate governance from the equity point of view) and debt governance (corporate governance from the debtholders' perspective). Specifically, in banks, as in any highly leveraged firms, there is a hard-wired relationship between the strength of equity governance and the strength of debt governance. Corporate governance mechanisms that align managers' interests with those of shareholders also increase the costs of conflict between equity holders and debtholders. Similarly, the debt governance mechanism that aims to protect depositors and debtholders necessarily blunts the effectiveness of equity governance. By providing a general framework to understand equity governance and the debt governance in highly leveraged institutions, we hope to bring additional clarity to the results in the literature on corporate governance in banks. For our first research question, we study how strengthening equity governance in banks might aggravate the agency costs of debt and therefore reduce the enterprise value of banks. In addition to leverage, we also discuss the characteristics of banks that make them special and hence affect their corporate governance.

Stulz (2015) highlights the importance of optimal risk taking by banks in determining their success and the health of the financial system. A bank's ability to measure and manage risks creates value for shareholders. He stresses the importance of the right risk management, the right governance, the right incentives, and the right culture for risk taking to maximize shareholder wealth. Although recognizing the importance of the risk management system examined by Stulz (2015), we build a framework that recognizes an inherent conflict between maximizing shareholder wealth and maximizing total firm value with respect to risk taking in banks. Our framework also recognizes that equity value-maximizing risk choices by banks might not be consistent with socially optimal stability of the financial system. In other words, our framework examines corporate governance in banks from three perspectives: (1) share value maximization, (2) total value maximization, and (3) socially optimal financial system stability.

De Haan and Vlahu (2015) is a recent survey on corporate governance in banks. They examine different aspects of corporate governance mechanisms in banks primarily from the point of view of shareholder value maximization. We extend this work and use a novel framework, described above, to examine the effectiveness of bank governance. Our new framework yields several new insights and policy implications for the optimal design of bank governance and bank regulation.

Our second research question explores the different mechanisms of bank governance and how these mechanisms differ by country worldwide. Policymakers around the world have started to question the appropriateness of the current corporate governance in banks (in the UK, the Walker Report, 2009; in Europe, the European Commission Green paper, 2010; in the US, Federal Reserve Board, 2013; worldwide, Basel Committee on Banking Supervision, 2006, 2008, 2010, 2015). Here, we have four aims: (1) to investigate differences in the boards of banks and nonfinancial companies and how these differences affect the governance–performance relationship, (2) to survey the international studies about corporate boards and board effectiveness in banks, (3) to review the research about the ownership structure of banks, and (4) to study the role of incentive features in CEO compensation in bank performance and in inducing risk taking by banks.

This paper is organized as follows. Special attributes of banks and their implications for corporate governance are discussed in the first section. The empirical literature on corporate governance mechanisms is reviewed in the second section. These mechanisms include board structure and board quality, ownership structure, and incentives and compensation. The third section concludes, offering a critical review of the existing research and an agenda for further research.

WHAT IS SPECIAL ABOUT CORPORATE GOVERNANCE OF BANKS?

As with any other company, banks are affected by governance problems, typically associated with the separation of ownership and control. However, banks have special features that intensify governance problems and might reduce the effectiveness of standard governance mechanisms (Caprio & Levine, 2002; Laeven, 2013; Levine, 2004).

There is extensive literature that examines corporate governance in banks and how it differs from that in nonfinancial firms (Becht, Bolton, & Roell, 2012; Caprio & Levine, 2002; Devriese, Dewatripont, Heremans, & Nguyen, 2004; Hopt, 2013; Laeven, 2013; Levine, 2004; Macey & O'Hara, 2003; Mülbert, 2010; (Mehran & Mollineaux, 2012) Van der Elst, 2015).[1] These studies examine the special attributes of banks that have given rise to bank governance structures that differ from those of manufacturing firms.

The first attribute is the high leverage of banks. It is not uncommon for leverage in banks to exceed 90 percent (Adams & Mehran, 2003; Berger & Bouwman, 2013; DeAngelo & Stulz, 2015; Esty, 1997, 1998; Hopt, 2013; Laeven, 2013; Levine, 2004; Macey & O'Hara, 2003). Unlike nonfinancial companies, the major providers of capital to banks are depositors and other debtholders. Gornall and Strebulaev (2014) show that, typically, the average leverage of banks, measured as the ratio of debt to assets, is between 87 and 95 percent, whereas the average leverage of nonfinancial companies is in the range of 20–30 percent. This high leverage increases the probability of bank failures.

© 2016 John Wiley & Sons Ltd

The governance implications of high leverage are also of importance. The conflict of interest between shareholders and debtholders in the presence of high leverage interacts with the equity governance in banks. Macey and O'Hara (2003) argue that banks are susceptible to a higher degree of the moral hazard problem than are manufacturing firms. Laeven (2013) claims that the special attributes of banks imply that agency costs are likely to be more pronounced in such financial institutions than in other firms. Specifically, in banks, debtholders (depositors) are the primary claimholders (John & Qian, 2003), and their interests might diverge substantially from those of the shareholders. As in any other company, whereas shareholders maximize their wealth, debtholders are owed only a fixed payoff. When managers successfully invest in a risky project, the project produces large benefits for shareholders, whereas debtholders receive a fixed payment. Conversely, if the project fails, the value of collateral to debtholders decreases, with a decline in the value of outstanding debt. If the firm goes bankrupt, limited liability allows stockholders simply to walk away, shifting all the risk to creditors (John & Senbet, 1998). This risk-shifting incentive on the part of managers who act on behalf of shareholders has governance implications in terms of agency costs of debt, effective monitoring, and the efficiency of managerial incentives.

In their study, John and Qian (2003) argue that if top management in highly leveraged companies, such as banks, is very closely aligned with equity interests, they will have strong incentives to undertake high-risk investments, even investments that lack positive net present value (John & Qian, 2003: 109). Thus, standard managerial incentives that align shareholders' interests with managers' interests might increase shareholder–debtholder conflict in leveraged firms. Therefore, increasing the strength of equity governance has the potential to increase the agency cost of debt in banks, resulting in a loss in firm value. In other words, very strong equity governance might result in a reduction in firm value for these highly leveraged financial institutions. In this framework, regulation might serve to blunt the effectiveness of equity governance. Again, given the high leverage of banks, restricting extreme forms of equity governance can serve to reduce the agency costs of debt and hence increase firm value.

We also examine bank governance from the point of view of society at large and the financial system in which banks are important players. Here, agents in the economy, who might not hold equity or debt claims in the bank, might still derive benefits from a safe and sound financial system. A well-governed bank might be important to the stability of the overall financial system Adams, 2010. In this case, the social planner might regulate the banking sector in two ways. On the one hand, the regulator might restrict the investment choices of banks and impose capital requirements. On the other hand, the regulator might mandate features of bank governance, which in turn affect managerial incentives and risk choices. This framework will be used to study the interaction between bank regulation and bank governance in the next subsection.

Another bank attribute that makes bank governance important is the opacity and complexity of banking assets. Although some scholars question the opacity of banks, others argue that in the banking industry, informational asymmetries are more important than in manufacturing industries (Becht et al., 2012; Furfine, 2001; Laeven, 2013; Levine, 2004; Morgan, 2002). Some argue that loan quality might not be readily observable and can be hidden for long periods because the complexity of many financial instruments makes it more difficult to measure and verify risks (Ferrarini, 2015; Laeven, 2013; Morgan, 2002). During the financial crisis, for example, it came to light that many financial innovations, such as securitized products (obtained by pooling and tranching of original loans) and off-balance sheet activities implemented through special-purpose vehicles, increased risks. These risks were not fully understood or properly managed (Carlin, Kogan, & Lowery, 2013; Cebenoyan & Strahan, 2004; Dell'Ariccia, Igan, & Laeven, 2012; Purnanandam, 2011). Moreover, the risk composition of banks' assets can be altered more quickly than in manufacturing companies. This change in risk composition might not be immediately visible to directors or to outside investors. According to Levine (2004), the opacity of banks has important governance implications. First, the asymmetry of information in the context of banking makes it more difficult for diffuse equity holders to control managers and for debtholders to control banks from risk shifting from shareholders to debtholders. This difficulty of monitoring exacerbates agency costs. Second, opacity makes it more difficult to design effective incentive contracts. According to Levine (2004, "When outcomes are difficult to measure and easy to influence in the short run, managers will find it easier to manipulate pay-off from compensation packages." Managers of opaque banks can often design compensation packages that allow managers to benefit at the expense of the long-term success of the bank. However, other studies show that opacity might not affect banks so strongly. Banks are subject to many stringent disclosure requirements and balance regimes that make banks more transparent than nonfinancial companies (Flannery, Kwan, & Nimalendran, 2004; Hopt, 2013; John, Mehran, & Qian, 2010). Special bank auditors have particular information-related duties toward the bank supervisory authority and require special inquiries that increase the transparency of bank activities. Moreover, banks are followed by a large number of analysts who also possibly increase the degree of transparency (Flannery et al., 2004; John & Qian, 2003). In our survey, we will highlight features of bank governance that address the opacity of large, complex banking institutions (see, e.g., Adams & Mehran, 2012).

In addition to the firm-level features of banks, country-governance variables might also be relevant issues in the context of banks (Aggarwal, Erel, Ferreira, & Matos, 2011). Research on nonfinancial firms, for example, suggests that corporate governance is influenced by country-level variables such as domestic economic development (Chen, Li, & Shapiro, 2011), domestic institutions (Aguilera & Jackson, 2003; Aslan & Kumar, 2014; Kumar & Zattoni, 2013; (John, Litov, & Yeung, 2008) La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1998, 2000), and domestic financial system architectures (Renders & Gaeremynck, 2012; Renders, Gaeremynck, & Sercu, 2010). For the particular case of banks, Berglof (2011) proposes an excellent discussion on the interdependence between the "macro" governance system (i.e,, country-level governance variables) and "micro" governance mechanisms (i.e,, firm-level corporate governance variables) and on the importance of establishing a strong link. He underlines the differences among corporate governance systems and argues that the same rules

© 2016 John Wiley & Sons Ltd

could have very different effects in different countries. Conyon, Judge, and Useem (2011) discuss corporate governance mechanisms, at the firm level and macro level, during the 2007–2008 financial crisis. They note the importance and the interplay of "micro" and "macro" governance factors in contributing to the financial crisis and the importance of reforming them. Empirical research about the relationship between firm-level and country-level governance in the context of banks has been carried out. Caprio, Laeven, and Levine (2007) discuss the shareholder protection laws (country-level variable) that prevented expropriation from minority shareholders (firm-level variable) in 44 countries in 2001. Specifically, they assess whether governance mechanisms that reduce the ability of insiders to expropriate bank resources, such as investor protection laws, boost the market value of banks, which is considered a measure that indirectly evaluates the market's assessment of the governance of banks. They find that expropriation from minority shareholders is important in many countries and that investor protection laws can restrict this expropriation.[2] Erkens, Hunga, and Matos (2012) combine micro and macro governance factors during the financial crisis. They examine whether firm-level governance mechanisms or country-level governance mechanisms (such as the quality of legal institutions and the extent of laws protecting shareholder rights) are more important in determining firm performance during the crisis. Using a dataset of 296 financial firms from 30 countries during the financial crisis, they document that firm-level, but not country-level, governance mechanisms are important in explaining bank performance during the financial crisis. Their results are robust using alternative definitions of the crisis period and including the possible effect of government intervention. The relative importance of "macro" governance systems and "micro" governance mechanisms in bank governance demand additional research.

Bank Regulation and Bank Governance

Bank regulation is justified by the negative externalities that are associated with a bank failure. Specifically, an individual bank failure not only affects its shareholders but also poses serious consequences to depositors and other participants in the financial system and in the global economy. Bank regulation aims to protect depositors and promote stability of the financial system. To achieve these goals, the regulator can impose restrictions on the banking system (Caprio & Levine, 2012). These restrictions can be on bank capital, bank investments and loan choices, bank entry, and interstate banking (John & Qian, 2003; John, Saunders, & Senbet, 2000). In addition, the regulator might also establish mandatory standards for the quality and features of bank governance, for example, restrictions on the composition of the corporate board or restrictions on equity ownership concentration. In other words, bank regulation can modify traditional corporate governance mechanisms (Aguilera, Goyer, & Kabbach de Castro, 2013; Becher & Frye, 2011; Cambini, Rondi, & De Masi, 2015; Ellul & Yerramilli, 2013; John et al., 2010; Laeven & Levine, 2009; Saunders, Strock, & Travlos, 1990), indirectly inducing the manager toward achieving social objectives. This aspect of regulation can bring about interesting interactions with bank governance.

Why should regulators intervene to modify the corporate governance of banks? A primary reason could be that managerial incentives induced by strong equity governance might be misaligned with social objectives with respect to bank risk taking. The main rationale of bank regulation is the safety and the soundness of the financial sector, reducing systemic risks and protecting depositors. Conversely, strong equity governance mechanisms might induce risk-shifting incentives on the part of bank managers that, in turn, could lead to systemic risks. Excessive risk taking by banks can lead to instability of the banking system. Banks are critical components of any economy because they provide financing for firms and access to payment systems. The economic welfare of most stakeholders, such as employees, customers, suppliers, or citizens, depends upon the safety and soundness of the banking system. Bank regulation must address the social costs that bank risk taking creates, by weakening mechanisms of equity governance or reducing the incentive features of bank management compensation (Alexander, 2006). Therefore, socially optimal regulation might interact with bank governance to induce banks to make risk choices consistent with social goals. In addition, studying bank governance from the point of view of social objectives provides a novel framework to examine the interaction of regulation and bank governance.

Laeven (2013) and Levine (2004) discuss the interaction between bank governance and bank regulation. They identify three main corporate governance mechanisms that might be limited by bank regulation: (1) ownership concentration, (2) market for corporate control, and (3) monitoring by debtholders. Specifically, ownership concentration can be considered a governance mechanism that prevents managers from deviating too far from the interests of shareholders (Shleifer & Vishny, 1997). Large shareholders have a strong incentive to acquire information and monitor managers. Moreover, compared with the poorly informed small shareholder, they can be more effective at negotiating managerial incentive contracts that align shareholders' interests with managers' interests.[3] However, in many countries, bank regulation restricts the concentration of bank ownership and the ability of outsiders to purchase a substantial percentage of bank stocks (Caprio & Levine, 2002: 35). This limitation aims to prevent nonfinancial firms from exercising a controlling influence over banks that might distort banks' lending decisions or to avoid a high concentration of power in the economy. Barth, Caprio, and Levine (2004) show that out of the 107 countries, 79 limit the percentage of bank equity owned by a single entity. According to Levine (2004), this limitation might weaken the monitoring power exerted by large shareholders, providing managers with significant discretion over the control of corporate assets. Another governance mechanism that might be influenced by the ownership limitation is the market for corporate control. Hostile takeovers might discipline managers because these takeovers increase the threat of managers being removed for poor performance. Specifically, when a firm performs badly, it might receive a tender offer. If shareholders decide to accept the offer, the acquiring firm takes over the target firm, and, typically, the managers of the target firm are replaced (Hagendorff, Collins, & Keasey, 2010; Martin & McConnell, 1991). A threat of potential hostile takeovers creates incentives for managers to act in the best interests of the shareholders (Jensen, 1993; Jensen & Warner, 1988).

 © 2016 John Wiley & Sons Ltd

However, by limiting the purchase of shares, bank regulation makes hostile takeovers in banking extremely rare, reducing the efficiency of the market for corporate control (Levine, 2004).

Another governance mechanism that might be influenced by bank regulation is the monitoring role of debtholders. In addition to imposing restrictions on bank capital, ownership, bank investments, or entry, bank regulation also includes deposit insurance, which might limit the monitoring role of debtholders. Deposit insurance exists to avoid bank runs and liquidity problems associated with bank maturity transformation. Specifically, most of a bank's debt is short term, whereas bank assets tend to be of longer maturity. The aim of deposit insurance is to protect depositors from illiquid claims and bank runs. However, although deposit insurance is effective in protecting households' savings, it might substantively change corporate governance mechanisms. Specifically, deposit insurance reduces the incentives of depositors to monitor banks, directly hindering corporate governance. Because depositors are fully insured by a regulator, they do not suffer heavy losses in the event of bank insolvency (John et al., 2010). Consequently, they lack sufficient incentives to control the bank. Hence, deposit insurance as a form of regulation reduces the incentives of depositors to monitor banks and encourages shareholders to increase risks (Demirgüç-Kunt & Huizinga, 2004). Not surprisingly, countries with stronger deposit insurance tend to have a higher likelihood of suffering banking crises (Demirgüç-Kunt & Detragiache, 2002). Hence, the reduced monitoring role of debtholders suggests that the interaction between bank regulation and bank governance might also be studied from the point of view of total firm value. In other words, we should examine bank governance not only in terms of equity governance but also from the point of view of how equity governance interacts with debt governance. This interaction might provide an additional rationale why regulation might complement or substitute for equity governance. By limiting the effectiveness of equity governance, regulation indirectly reduces the agency costs of the conflict between debtholders and equity holders. In addition to curbing equity governance, regulation can directly increase debt governance by imposing equity capital requirements and restricting bank risk choices. In other words, regulation can act as a mechanism to weaken equity governance and to strengthen debt governance. Given the leverage of banks and the importance of debt claims in the capital structure of banks, optimally designed regulation should strike this balance in the interest of enterprise value.

Empirical research has tested the interaction between regulation and governance. Becher and Frye (2011) examine governance structures of regulated and unregulated firms at the time of their initial public offering (IPO), when governance might be argued to be optimal. For a sample of US banks during the years 1993–1998, they document that regulated firms have a significantly higher proportion of monitoring directors. Thus, regulation and governance are complements. Regulators seem to pressure firms to adopt effective monitoring structures. The evidence is also consistent with the regulators pressuring the banks to adopt governance structures that promote safety and soundness. Alexander (2006) and Mülbert and Citlau (2011) examine how bank regulation and reforms of bank governance relate to systemic risk. They argue that corporate governance can reduce firm-level risk, thereby reducing the probability of default and promoting financial stability.

In a cross-country study, Laeven and Levine (2009) study the effects of domestic regulation on banks' corporate governance structure for a sample of 279 banks across 48 countries in 2001. They show that, depending on banks' ownership structure, the same regulation policy can have different effects on bank risk taking. Controlling also for government intervention, they document that stricter regulation is associated with greater risks when the bank has a large shareholder and has lower risks in widely held banks. This result suggests that ignoring ownership structure leads to incomplete and occasionally erroneous conclusions about the effect of bank regulation on bank risk taking. Klomp and de Haan (2012) report that the effect of regulation on banking risks depends upon the bank risk profile. Using a sample of banks from 21 OECD countries for the years 2002–2008, they find that bank regulation significantly reduces risks in high-risk banks but has no effect on low-risk banks.

Li and Song (2013) study how cross-country bank regulation policy differences affect the internal governance arrangements of individual banks. Based on a sample of 277 listed banks across 55 countries over the period 2004–2010 and controlling for two-tier board structures, they find that empowering official supervisory agencies to discipline banks directly reduces board independence. In this study, the empirical evidence suggests that strengthening supervisory regulation leads to weakening the monitoring ability of equity governance. The evidence from this cross-country study is contrary to that of Becher and Frye (2011) in the US setting mentioned above. More research is needed to understand the interaction of regulation and equity governance.

GOVERNANCE MECHANISMS

In this section, we survey the literature on bank governance and discuss the prominent mechanisms individually, including corporate boards, ownership and managerial incentives. The discussion of corporate boards and their effectiveness is divided into several subsections on board structure (board independence, board size, board committees, and Chief Executive Officer [CEO] duality) and board quality. Ownership structure and incentive features in compensation contracts are surveyed in the following section.

In the context of manufacturing firms, the market for corporate control has also been viewed as an effective mechanism of corporate governance. Vulnerability to hostile takeovers is viewed as an important instrument of corporate governance (see, e.g., Hart, 1995; Gompers, Ishii, & Metrick, 2003). However, due to the structure of banking regulation in the United States and abroad, hostile takeovers have not played an important role in disciplining banks (see the excellent review by DeYoung, Evanoff, & Molyneux, 2009).

Board Structure

Why are bank corporate boards so important? How can a board of directors influence bank performance? As in any other company, the board of directors is a source of oversight

© 2016 John Wiley & Sons Ltd

and advice for managers (Adams & Ferreira, 2007; Adams, Hermalin & Weisbach, 2010). The monitoring function is more relevant in banks than in nonfinancial companies, in which debtholders, who are diffuse and mostly protected by deposit insurance, do not have strong incentives to control banks' decisions.

To evaluate board effectiveness in banks, it is important to understand how the banks are typically governed and whether there is a difference between boards of directors of banks and of nonfinancial companies. This issue is particularly important because many regulations have proposed a "one-size-fits-all approach," meaning governance regulations should be applied to every firm, regardless of the industry (Adams & Mehran, 2003; Van der Elst, 2015). The existing literature, which is largely empirical, grapples primarily with the following issues: How effective are boards in performing their monitoring function of banks? Do the banks' boards affect bank performance? Does board composition matter? (See, e.g., Muller-Kahle & Lewellyn, 2011.) The following section summarizes the literature and provides answers to the above questions.

Board Independence

Earlier studies on board independence compare the board composition of banks with that of nonfinancial firms. The aim is to evaluate the differences in governance structures. The main questions have been whether these differences are irrelevant or whether these differences indeed might constitute an industry specificity that should be considered by policymakers (Adams & Mehran, 2003; Belkhir, 2009; de Andres & Vallelado, 2008; Macey & O'Hara, 2003; Van der Elst, 2015).[4] In comparing board independence between banks and nonfinancial firms, empirical research shows consistent differences. On average, in the United States, the proportion of outsiders on bank boards is between 70 and 85 percent (Adams & Mehran, 2003; Belkhir, 2009; Booth, Cornett, & Tehranian, 2002), whereas the average proportion of outside directors on the board of nonfinancial companies is between 60 and 70 percent (Adams, 2012; Bhagat & Black, 2002). Similar results are obtained in non-US settings. De Andres and Vallelado (2008) show that, in a sample of 69 commercial banks from six OECD countries (the United Kingdom, Canada, the United States, Italy, Spain, and France) over the period 1995–2005, on average, outsiders account for 80 percent of directors. Kim, Kitsabunnarat-Chatjuthamard, and Nofsinger (2007) study board independence in a sample of financial and nonfinancial firms in 14 European countries (Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Spain, Sweden, Switzerland, and the United Kingdom) in 2000. They find that the percentage of outside directors in these countries ranges from 0 to 76 percent. Their main conclusion is that the degree of shareholder protection is associated with higher board independence. In their sample, there is a dominance of countries with the French civil law system; these countries have board independence ranging from 0 to 14.98 percent. The British common law countries are the United Kingdom with 76.05 percent and Ireland with 74.41 percent. Overall, board independence declines as one moves from British common law countries to French civil law countries.[5]

The difference between bank boards and nonfinancial boards, both in the United States and in Europe, is consistent with the argument that bank boards might optimally have more-independent directors because they must address complex instruments and trading activities. Country-level variables might amplify this difference. Using an international sample of commercial banks over the period 1996–2006, de Andres, Romero-Merino, Santamaría, and Vallelado (2012) show that more complex banks that also have low ownership concentration and are headquartered in a civil law country have more independent (and larger) boards.[6] However, Adams and Mehran (2012) argue that the status of outside directors in banks might be overstated because of the lending relationships with directors or directors' employers that are not individually disclosed.

Board independence, in particular its effect on bank performance, has been studied. Adams and Mehran (2012) use a random sample of the 35 largest publicly traded bank holding companies (BHCs) in the United States. They collected data from 1965 to 1999, and they found that board independence is not related to bank performance. The results are consistent with those of nonfinancial firms. Other empirical research shows a nonlinear relationship between independent directors and bank performance. De Andres and Vallelado (2008) analyze the board of directors of an international sample of banks over the period 1995–2005. All banks in the sample have a one-tier board structure. The authors show that outside directors and bank performance have an inverted U-shaped relationship. The authors claim that the inclusion of outsiders improves performance, but when a high proportion of the total board is reached, performance starts to decrease. Pathan and Skully (2010) further investigate the effect of independent directors. For a sample of 212 US bank holding companies from 1997 to 2004, the authors indicate that banks benefit from a higher number of independent directors when the cost of monitoring managers is low. In a later study, Pathan and Faff (2013) use generalized method of moments (GMM) estimations to address the heterogeneity and endogeneity that usually affect the governance–performance relationship. They find that both board size and the independence of directors decrease bank performance for a panel of large US bank holding companies over the period 1997–2011. This result holds during the crisis period. These findings are more evident for banks with low market power and for banks that are more protected from the threat of external takeover. Pathan and Faff (2013) claim that their results suggest that independent directors in banks might be chosen to conform to regulatory requirements or that the market for high-performing independent directors is limited. This result indicates that the dominant recommendations, suggesting a high number of independent directors, should be followed carefully. The negative board–independence–performance relationship is confirmed during the years of financial crisis. Minton, Taillard, and Williamson (2014) find that, for a sample of US banks during the financial crisis, the percentage of independent directors is negatively associated with bank performance.[7]

Turning to international evidence, Erkens et al. (2012) show that, during the crisis, banks with more-independent boards experienced worse stock returns. Specifically, they use a unique dataset of 296 large financial firms from 30 countries

© 2016 John Wiley & Sons Ltd

for the years 2007–2008. They argue that independent directors encouraged managers to raise equity capital during the crisis period to ensure capital adequacy and reduce bankruptcy risk (because the value of risky assets deteriorated during the crisis period). Therefore, financial institutions could no longer rely on rolling over short-term loans against these assets and were forced to raise capital. Because raising equity capital was very costly during that period, doing so led to worse stock returns during the crisis and caused a wealth transfer from existing equity holders to debtholders. This result implies that the equity governance (board independence) that traditionally has been used to reduce agency costs between managers and shareholders caused a wealth transfer during the crisis from shareholders to debtholders. The results might be influenced by differences in corporate governance systems and/or government intervention such as a government bailout.

Using a large data sample on US nonfinancial and US financial firms for the period 1996–2007, Adams (2012) shows that banks with TARP (Troubled Asset Relief Program) funds have a greater number of independent directors. She argues that, because bank activities are more complex and opaque than are those of nonfinancial firms and because the cost of monitoring can be high in the case of banks, greater independence might be counterproductive. Independent directors are not employed in the banks and, together with the opacity and complexity of bank activities, such directors are less likely to have an in-depth knowledge of the internal workings of the banks on whose boards they sit. These results challenge the policy formulation concerning the inclusion of a high number of independent directors. The effect of independent directors is influenced by the cost of monitoring and by the period of study (whether it was before, during, or after the financial crisis). Beyond a certain limit, the effect of independent directors might be detrimental for the bank, suggesting that the percentage of independent directors alone is not a sufficient metric of "good governance." In addition to the number, the "quality" of independent directors is also important. Developing new measures of the effectiveness of independent directors and their influence on governance will be a fruitful direction for future research.

Board Size

A large body of research examines board size in banks and compares board sizes in banks with those in nonfinancial firms. In the United States, banks have larger boards than nonfinancial firms (Adams, 2012; Adams & Mehran, 2003; Booth et al., 2002). De Andres and Vallelado (2008) document that the above result also holds for an international sample of banks with one-tier boards from six OECD countries (the United Kingdom, Canada, the United States, Italy, Spain, and France) over the years 1995–2005. These differences in board size between banks and nonfinancial firms might be due to the complexity of bank activities and the regulatory recommendations, which require more board committees, such as the lending committee and the credit-risk committee (Adams & Mehran, 2012).

The second interesting question that has been largely analyzed in the context of banks is whether board size affects bank performance. Several studies examine the relationship between board size and various measures of firm performance (such as Tobin's q, return on assets, or return on equity) for financial firms. In contrast to the findings for nonfinancial firms, most of the studies show that bank board size is positively related to bank performance. Specifically, Adams and Mehran (2012) show that the relationship between board size and firm performance (measured by Tobin's q) is statistically significantly positive for large US banks for the years 1965–1999. Similar results are reported by Aebi, Sabato, and Schmid (2012) for US banks during the financial crisis. The reason the research on banks finds a positive relationship between board size and bank performance might be because banks are complex firms and the benefits of larger boards overcome their costs. De Andres and Vallelado (2008) and Grove, Patelli, Victoravich, and Xu (2011) go further. They show an inverted-U relationship between board size and Tobin's q. They show that the inclusion of more directors should benefit the monitoring and advisory functions, improving bank performance. Specifically, de Andres and Vallelado (2008) find a limit (19 directors) beyond which the costs associated with a larger board (such as coordination problems, slow decision making, and control costs) dominate the benefits. Thus, the relevant finding that emerges in the literature is that the optimal board size is a trade-off between advantages (better monitoring and more competence to address problems) and disadvantages (control and coordination problems) (see Dalton, Daily, Johnson, & Ellstrand, 1999). This trade-off in the banking industry seems to indicate that larger boards are necessary to address all the functions that they serve in banks (see, e.g., de Andres & Vallelado, 2008).

Another topic that has received increasing attention in banking is the relationship between board size and risk taking. The role of the board of directors has been viewed as crucial in monitoring a bank's risks. Pathan (2009) examines the relationship between bank board structure and bank risk taking. Among the other governance variables, he shows that a small bank board is associated with higher risk taking for a sample of 212 large US banks for the years 1997–2004. Similar results are reported for a sample of US banks by Fernandes and Fich (2013) for the years 2003–2006 and by Minton et al. (2014) for the years 2004–2006. Wang and Hsu (2013) study a sample of financial institutions belonging to Standard & Poor's 1500 over the period 1996–2010. They find that board size is negatively and nonlinearly associated with the possibility of operational risk events. They find that when the board size exceeds 14, adding an incremental board member increases the likelihood of operational risk events. The implication is that beyond a board size of 14 directors, problems of communication and conflicts can outweigh the advantage of knowledge development by a large board.

More recent evidence finds that the negative relationship between board size and bank risk taking also holds during the financial crisis. Berger, Imbierowicz, and Rauch (2016) report that the relationship between the probability of bank default and board size of US commercial banks for the years 2007–2010 is negative in most of their results.

Board Committees

The effectiveness of the board is influenced by board committees. The regulatory recommendations and the complexity of

© 2016 John Wiley & Sons Ltd

bank activities place emphasis on the importance of board committees in banks. Sun and Liu (2014) study the relationship between the effectiveness of the audit committee and bank risk taking in the United States for the years 2008–2010. They find that banks with long board-tenure audit committees have lower total risk and idiosyncratic risk, whereas banks with busy directors on their audit committees have higher total risk and idiosyncratic risk. Barakat and Hussainey (2013) study the quality of audit committee and operational risk disclosure in European banks. Using a sample of 85 banks from 20 EU countries (Austria, Belgium, Bulgaria, Cyprus, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Lithuania, Malta, the Netherlands, Poland, Portugal, Spain, Sweden, and the United Kingdom) for the years 2008–2010, they find that banks with more active audit committees provide operational risk disclosure of higher quality and that this relationship is influenced by the ownership structure of the banks. Their results suggest that high audit committee effectiveness might constrain bank risk-taking activities.

In addition to the audit committee, the risk committee has also received attention. Aebi et al. (2012) examine whether the presence of the Chief Risk Officer (CRO) on the bank board is associated with better bank performance during the financial crisis. They show that banks in which the CRO reports directly to the board of directors and not to the CEO have significantly higher stock returns and return on equity (ROE) during the financial crisis period. Ellul and Yerramilli (2013) study the strength and independence of the risk committee at BHCs in the United States for the years 1995–2010. They document that in approximately 69.3 percent of BHCs' annual observations, not one independent director on the board's risk committee had any prior financial industry experience. They create a risk management index (RMI) by taking the first principle component of the following six risk management variables: the presence of a CRO, a dummy variable that identifies whether the CRO is an executive officer, a dummy variable that identifies whether the CRO is among the five highest-paid executives, the ratio of the CRO's total compensation to the CEO's total compensation, the risk committee experience (a dummy variable indicating whether at least one of the independent directors serving on the board's risk committee has prior banking and financial industry experience), and a dummy variable that indicates whether the risk committee is active. They document that banks with a high RMI in place before the onset of the financial crisis have lower tail risk, a smaller fraction of nonperforming loans, better operating performance, and higher annual returns in the crisis years, 2007–2008. Overall, these results suggest that a strong and independent risk management function can curtail tail risk exposures at banks and possibly enhance value, particularly in crisis years.

At the international level, Lingel and Sheedy (2012) study the quality of oversight of the board risk committee. They report evidence that the proportion of experienced bankers in the risk committee has increased significantly from 2004 to 2010. They show that stronger risk governance reduces risk and increases return on assets (ROA) in a sample that includes 60 banks representing 17 nations with different regulatory and business contexts. They suggest that decisions about risk governance matter regardless of specific local conditions. However, they document that this relationship does not hold during the financial crisis; at the international level, stronger risk governance does not have a significant effect on risk outcomes in the years 2007 and 2008. Al-Haidi, Hasan, and Habib (2015) investigate whether the existence of separate risk committee characteristics is associated with market risk disclosure for a sample of financial firms in Gulf Cooperation Council (GCC) countries (i.e,, Oman, Bahrain, Kuwait, Qatar, Saudi Arabia, and the United Arab Emirates) for the years 2007–2011. They find that firms with a separate risk committee, better risk committee qualification, and larger risk committee size are associated with greater market risk disclosure. Their findings suggest that the risk committee and its features can be a mechanism to improve the disclosure of risk-related information, making the firm more transparent to outside stakeholders and reducing agency problems between inside and outside investors.

Yeh, Chung, and Chih-Liang (2011) study the effect of independent directors on different committees in the 2007–2008 financial crisis. Using the 20 largest financial institutions from the G8 countries (Australia, Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States), they find that the independence of both the auditing and risk committees has a positive effect on performance during the crisis. Controlling for different governance environments, they find that the influence of committee independence on financial institution performance is particularly significant in civil law countries. They do not find a significant relationship between the independence of compensation and nomination committees and bank performance.

These results show that stronger audit and risk committees have a positive influence on the performance of banks and might constrain bank risk taking. More accurate and better risk governance avoids higher risks whose effects might harm the stability of the financial system and society at large. These findings might have policy implications on optimal regulation of banks. Regulation of bank governance from the point of view of social objectives should be guided by the above evidence.

CEO Duality

CEO duality is defined as the practice of a single individual serving as both CEO and board chair (Krause, Semadeni, & Cannella, 2014). The opacity of banks, the lack of market control, and the complexity of agency costs can weaken CEO discipline, making it more important to separate leadership roles in banks. Several studies on financial firms analyze the effect of CEO duality on bank risk taking. As risk-averse entrenched managers, bank CEOs have fewer incentives to take risks. Pathan (2009) shows that, for a sample of US banks over the period 1997–2004, CEO duality negatively affects bank risk taking. Simpson and Gleason (1999) find that CEO duality decreases the probability of financial distress in their sample of 287 US banks for the period 1989–1993. They state that a CEO who is also the chairman of the board is capable of pursuing his/her own interests and consuming private benefits. This potential behavior also implies less risk taking to protect their human capital and private benefits. This result holds in the case of the recent financial crisis. In a study of bank defaults for US commercial banks over the years 2007–2010,

© 2016 John Wiley & Sons Ltd

Berger et al. (2016) report that CEO duality reduces bank default probabilities one year and two years prior to default. They control for corporate governance variables, market competition, state economic indicators, and regulatory variables and whether the bank received funds from the government. They state that the board structure is not decisive for its stability, whereas managerial incentives have a highly significant and positive influence on a bank's probability of failure.

Other research focuses on the relationship between CEO duality and performance. Grove et al. (2011) use a sample of 236 US public commercial banks over the period 2005–2008. They find a negative relationship between CEO duality and bank financial performance. They show that CEO duality affects bank performance but does not influence loan quality.

These findings challenge the idea that CEO duality weakens corporate governance. Our interpretation of the evidence is that the feature of CEO duality might decrease the effectiveness of equity governance in banks, but it improves the performance of banks from the two additional perspectives that we have highlighted. The evidence that CEO duality reduces the probability of bank default and bank risk taking suggests that CEO duality might strengthen bank governance from the perspective of debtholders and from the perspective of society at large.[8]

Board Quality

Other components of effective governance are the ability and willingness of bank boards to challenge management and engage in good dialog to ensure that the company's decisions consider the wide range of factors that could affect stakeholders' interests (Mehran et al., 2012: 11). To accomplish this task, the board of directors should have the competence and expertise to grasp the complexity of the bank's assets and thus the associated risks. The main questions asked by scholars and regulators are: How many "financial experts" should a bank board have? Are financial experts able to assess the risks posed by the more complex products? Should nonfinancial experts be included on the board of a bank?

Research has documented the effect of the directors' experience on bank performance. Aebi et al. (2012) investigate whether experience and financial expertise influenced US bank performance during the crisis. Their results show that the presence of a CRO on the board of a bank positively influenced the bank's performance during the financial crisis. However, they report evidence that the relationship between the percentage of nonexecutive directors with a financial background or expertise and bank performance in the crisis was negative. This finding is consistent with the findings of Minton et al. (2014). For a sample of US banks, they show that the financial expertise of independent directors is negatively related to bank performance during the financial crisis and positively related to risk taking. These results are consistent with independent directors aligned more closely with management using their financial expertise to maximize shareholder value. Given the high leverage of banks, it is possible that stronger equity governance leads to more risk taking that might be detrimental for overall bank performance. Another explanation could be that external financial experts are more willing to let their bank participate in more risk-taking activities due to their familiarity with and understanding of complex financial instruments (Minton et al., 2014: 377). Both explanations are important considerations for policymakers in their examination of governance reforms of the financial sector.

In the case of European banks, Hau and Thum (2009) find evidence that, during the financial crisis, board members without financial experience in the largest German banks were positively related to losses by the banks. Similarly, Garicano and Cuñat (2010) show that Spanish cajas chairmen who had no previous banking experience (or postgraduate education) performed worse in the years 2007–2009. However, the nonprofit nature of the cajas and the political links of German banks make this result difficult to generalize to international banks (Mehran et al., 2012). The relationship between board expertise and bank performance might be influenced by the measures used as proxy for financial expertise or by the leadership and directors' networks. An interesting study by Johansen and Pettersson (2013) examines board interlocks as a mechanism to influence board-level decisions through the sharing of knowledge and experiences. Using a sample of Danish banks between 1998 and 2008, the authors show that board interlocks bring experience with incoming auditors to the auditor choice decision. This influence should be considered in the discussion of the effect of financial expertise. In a recent study, Elyasiani and Zhang (2015) find that, for a sample of US banks over the period 2011–2010, bank performance is positively associated with busyness of directors and risk measures are inversely related to busyness of directors. They report evidence that performance (risk) benefits of having busy directors strengthened (weakened) during the financial crisis of 2007–2009. These results challenge the effect of busy directors; in banks, in which activities are complex and opaque, directors with multiple directorships are capable of bringing extensive knowledge, information, and experience they have accumulated by sitting on multiple boards. In a review of corporate governance and bank risk taking, Srivastav and Hagendorff (2016) state that board attributes (i.e,, educational qualification and prior relevant experience of board members) can have an important bearing on bank risk-taking incentives. They suggest that future research should investigate the marginal effect of financial expertise on the likelihood that banks underestimate their risk exposures.

Other research has focused on the characteristics of executives. Using a sample of German banks for the years 1994–2010, Berger, Kick, and Schaeck (2014) investigate how age, gender, and educational composition of executive teams affect the portfolio risk of financial institutions. They remove from the sample all banks that were subject to regulatory interventions, capital support measures, and distress mergers to obtain a clean identification of the effect of changes in board composition on bank portfolio risk in a sample of banks that does not contain seriously troubled institutions. They show that banks take on more portfolio risk when managed by younger executives and less portfolio risk when managed by better educated executives. Nguyen, Hagendorff, and Eshraghi (2015) study how the characteristics of executive directors affect bank performance in a sample of US banks in the period from January 1999 to December 2011. They show that age, education, and prior work experience of executives create shareholder wealth, whereas gender is not linked to measurable value

© 2016 John Wiley & Sons Ltd

effects. They document that these effects decrease with a higher proportion of nonexecutive directors. These results suggest that increased board monitoring and involvement of nonexecutive directors in board decision making reduces the executive's influence.

Ownership Structure

The nature of a firm's agency problems is influenced by the structure of ownership. When a company is owned by numerous small shareholders, monitoring managers can be difficult and costly for the firm. In this context, managers have high discretion in allocating funds (John & Senbet, 1998). In the United States, for example, most companies have a dispersed ownership; CEOs in the largest corporations own, on average, only 0.3 percent of the shares. In many economies around the world, there is concentrated ownership by inside shareholders who are also the major decision makers in the firms. In this case, the large shareholder has an incentive to collect information and monitor managers. On the other hand, a large shareholder might consume private benefits at the expense of minority shareholders (Shleifer & Vishny, 1997).

This dichotomy of ownership (dispersed versus concentrated ownership) is valid for banking firms in the United States and abroad, and agency problems in banks are influenced by the banks' ownership structure. In their empirical study, Caprio et al. (2007) analyze the degree of ownership concentration for a sample of 244 banks across 44 countries in 2001. They find that the cross-country average for a widely held bank is 25 percent and that 75 percent of the largest listed banks have a controlling shareholder. Examining the differences across countries, they show that in Canada, Ireland, and the United States, 90 percent of the banks are widely held, whereas in 21 out of 44 countries, not a single bank is widely held. These differences might be explained by the legal investor protection and the regulatory environment. The authors show that countries with weak legal protection of shareholders have a significantly lower fraction of widely held banks than do countries with strong legal protection. Moreover, they report evidence that countries with strong official supervisory power and capital restrictions do not have a larger fraction of widely held banks. In another international study of 296 financial firms from 30 countries, Erkens et al. (2012) report evidence that, during the financial crisis, most of the financial firms had a large shareholder (e.g., 30 percent of US banks, 23 percent of Canadian banks, and 100 percent of the banks in Sweden, Belgium, and the Netherlands had at least one large shareholder). Caprio et al. (2007) focus on the particular type of controlling shareholder. Family ownership is very important in many countries. The government is the main controlling shareholder in some countries (Egypt, Greece, India, Indonesia, and Thailand), whereas in 29 out of 44 countries, the government is not a controlling owner in any bank.

The relationship between bank ownership and bank performance is interesting. Iannotta, Nocera, and Sironi (2007) compare the performance and risk of a sample of 181 large banks from 15 European countries for 1999–2004. They find that ownership concentration does not significantly affect a bank's profitability. However, a higher ownership concentration is associated with better loan quality, lower asset risk, and lower insolvency risk. Busta, Sinani, and Thomsen (2014) investigate the relationship between ownership concentration and market value of European banks over a 13-year period (1993–2005). They argue that this relationship is influenced by different institutional settings. They suggest that restrictions of shareholdings in banks could alleviate governance problems in some countries, but not in others.

Haw, Ho, Hu, and Wu (2010) focus on a sample of East Asian and Western European banks for the years 1990–1996. They find that banks with concentrated control exhibit poorer performance, lower cost efficiency, greater return volatility, and higher insolvency risk relative to widely held ones. The authors also study the effectiveness of direct regulation of banks versus the regulatory mechanisms that induce private monitoring and market discipline. Their metric of private monitoring is measured by the extent to which the regulatory regime promotes private monitoring and independent market discipline of banks. They document that private monitoring mechanisms are more effective than public rules and supervision. Controlling for legal institutions and private monitoring, their evidence shows that country-level institutions play important roles in constraining insider expropriation. Bouvatier, Lepetit, and Strobel (2014) examine whether differences in ownership concentration can explain differences in the level of earnings management and whether the regulatory environment plays a role in potentially disciplining such corporate behavior. Using a sample of European commercial banks over the period 2004–2009, they find that income-smoothing practices do depend on the degree of ownership concentration and the regulatory environment. They find that banks with highly concentrated ownership use discretionary loan-loss provisions to smooth their income. This behavior is less pronounced in countries with stronger supervisory regimes or higher external audit quality (see also Mülbert & Citlau, 2011).

Another stream of research studies the effects of the type of the main shareholder. Berger, Clarke, Cull, Klapper, and Udell (2005) test the effect of state ownership and foreign ownership on bank performance in Argentina in 1993–1994. They find that state-owned banks have poorer long-term performance than do domestically owned or foreign-owned banks. Micco, Panizza, and Yanez (2007) study the relationship between bank ownership and bank performance both in developing and industrial countries in the years 1995–2002. They find that state-owned banks located in developing countries tend to have lower profitability and higher costs than their private counterparts and that the opposite is true for foreign-owned banks. The paper finds no strong correlation between ownership and performance for state-owned banks located in industrial countries.

Cornett, Guo, Khaksari, and Tehranian (2010) examine performance differences between state-owned banks and privately owned banks before, during, and after the Asian financial crisis. They find that the differences in cash flow returns, core capital, and nonperforming loans between state-owned banks and privately owned banks were not significant during the post-crisis period from 2001 to 2004. They argue that this finding is consistent with the view that the increasing globalization of financial services competition has the effect of creating pressure to generate a substantially improved banking policy that disciplines inefficient regulators

© 2016 John Wiley & Sons Ltd

and substantially enhances the performance of state-owned banks (Cornett et al., 2010: 77). Borisova, Brockman, Salas, and Zagorchev (2012) examine the effect of government ownership on corporate governance in Europe. For a sample of financial and nonfinancial firms in the period from January 2003 to June 2009, they find that government ownership reduces the number of board committees and increases the power of the CEO. These results are affected by the legal environment; government ownership is detrimental in civil law countries but is beneficial in common law countries.

Interestingly, in a recent paper, Saghi-Zedek and Tarazi (2015) investigate the effect of the ultimate shareholders with excess control rights on bank profitability and risk during the financial crisis. For a sample of commercial banks in 17 Western European countries in 2002–2010 and controlling for government interventions, they find that the presence of excess control rights is associated with lower profitability, higher earnings volatility, and higher default risk before the crisis (2002–2006). They conclude that ownership structure does matter in explaining cross-variation in bank performance in the 2007–2008 financial crisis, suggesting that bank monitoring and supervision by regulators should closely account for shareholder behavior in complex ownership structures.

A long-debated topic is the ownership of insiders, such as CEOs and managers. The ownership of insiders is a corporate governance mechanism to reduce agency costs between managers and shareholders. Booth et al. (2002), and Adams and Mehran (2003) show a difference in CEO ownership between manufacturing firms and financial firms in the United States. They report evidence that CEOs and bank directors hold less equity than do CEOs and directors in manufacturing firms. Other studies document the relationship between CEO and insiders' ownership and bank performance, as a test of the effectiveness of insider ownership as a corporate governance mechanism to align the interests of managers with those of shareholders. Westman (2011) uses a sample of listed and unlisted bank holding companies, commercial banks, and investment banks from 37 European countries in the period from 2003 to 2006. He finds a positive relationship between the ownership of managers and directors and bank performance.[9] For their sample of 236 US public commercial banks, Grove et al. (2011) document that the level of block ownership is positively associated with financial performance (measured by ROA in 2007) and stock performance (measured by excess stock returns in 2008). However, they argue that large equity insiders only partially explain bank performance during the financial crisis.

Many papers have focused on insiders' (CEO, managers, and directors) ownership and risk taking. In a study of US banks for the years 1978–1985, Saunders et al. (1990) find a positive relationship between ownership by managers and risk taking. Examining only CEO and directors' ownership, Demsetz, Saidenberg, and Strahan (1997) find a positive relationship between insider ownership (CEO and directors) and risk taking for US banks in 1991–1995. Anderson and Fraser (2000) highlight that this relationship depends on the year considered. They show different relationships in two different periods, finding a positive relationship for the years 1997–1998 and a negative relationship for the years 1992–1994. This result is confirmed by Pathan (2009) and Aebi et al. (2012). Pathan (2009) finds a positive relationship between CEO ownership and total risks for 212 large US commercial banks for the years 1997–2004. Aebi et al. (2012) report that this relationship is not significant during the financial crisis. Lee (2002) focuses on larger banks with a low probability of failure in the United States over the period 1987–1996. The author shows a negative relationship between insider ownership and risks. In a recent study, Berger et al. (2016) analyze the role of ownership structure and management structure on the probability of default of US commercial banks in the years 2007–2010. They show that the percentage of shares held by the CEO and insiders is greater in default banks than in no-default banks. Specifically, their evidence shows that, during the financial crisis, CEOs' and independent directors' high shareholdings do not have a direct effect on the probability of default. In contrast, high shareholdings of lower-level management, such as a vice president, significantly increase default risk. They argue that lower-level managers with large shares might take more risk to increase the value of their shares.

Incentives and Compensation

In corporate governance, equity-based compensation contracts have been considered an effective mechanism for aligning the interests of managers with those of shareholders.[10] One of the early studies on CEO compensation in the banking industry is by Houston and James (1995). They show that, compared with CEOs in other industries, CEOs in US banks, on average, receive less cash compensation, hold fewer stock options, and receive a smaller percentage of their total compensation in the form of options and stocks (over the period 1980–1990). Studying a sample of Standard & Poor's (S&P) 500, the S&P Mid-Cap and the S&P Small-Cap firms for the years 1992–2012, Conyon (2014) documents that executive compensation in the US has grown significantly from 1992 to 2012 and that most CEO compensation is delivered in the form of variable pay (i.e,, bonuses, stock options, and restricted stock). Interestingly, he shows a slight correlation between executive compensation and affiliated directors on boards. Specifically, he finds no robust evidence that the level of executive compensation is higher in firms that have non-independent compensation committees and/or boards. In the context of banks, Adams and Mehran (2003) confirm this trend. They state that, in the last few years, the use of stock options in banking executive compensation packages has increased. Although this pattern has followed the pattern of other industries, the growth and level of stock options remain significantly lower in banks than in manufacturing firms. Similarly, other research shows a significant difference in the level and structures of executive compensation in banks compared with nonfinancial companies both in the US and abroad (Becher, Campbell, & Frye, 2005; Becher & Frye, 2011; Gregg, Jewell, & Tonks, 2012).

Most of the empirical research focuses on the consequences of high-powered incentive managerial contracts such as bonus pay and option contracts. Specifically, the idea of more closely aligning CEO pay with stockholder objectives through pay-performance sensitivity contracts has been one of the most popular governance practices (Becht et al., 2012; (Cuñat & Guadalupe, 2009) Zalewska, 2016). By making managers' compensation dependent on firm performance, shareholders can provide incentives, pushing managers to make decisions

© 2016 John Wiley & Sons Ltd

in the shareholders' best interest. However, this compensation practice might have less desirable effects (Hughes, Lang, Mester, Moon,& Pagano, 2003).

The first documented drawback is the problematic effect on bank performance. If pay-performance sensitivity were an effective tool to induce managers to make decisions that maximize shareholders' wealth, then banks with CEOs whose incentives were well aligned with those of shareholders would perform better. Fahlenbrach and Stulz (2011) analyze the influence of CEO incentives and share ownership on performance for a sample of US large banks in the period from 2006 to 2008. They find no evidence that better-performing banks have CEOs with better-aligned incentives. Specifically, they report that options and cash bonuses were unrelated to bank performance during the financial crisis, and they show that CEO ownership is negatively correlated with bank performance. Thus, banks provided stronger incentives to worse-performing CEOs during the crisis. The authors also find that the relationship between bank performance and CEO incentives does not differ between banks that have received funds from the government and banks that have not. A possible explanation for their results is that CEOs with better incentives to maximize shareholder wealth took risks that other CEOs did not. Ex ante, these risks appeared profitable for shareholders. Ex post, these risks had unexpectedly poor outcomes. Beltratti and Stulz (2012) reinforce this conclusion for a sample of international banks. They investigate the relationship between corporate governance and bank performance during the credit crisis. They find that banks with more shareholder-friendly boards performed worse during the crisis. The authors argue, "Banks that were pushed to maximize shareholder wealth before the crisis took risks that were understood to create shareholder wealth, but were costly ex post because of outcomes that were not expected when the risks were taken" (Beltratti & Stulz, 2012: 3). In an interesting paper, Keys, Mukherjee, Seru, and Vig (2009) find no relationship between the quality of loan originations and top-management incentives in the United States for the period January 2001–December 2006 (the years in which the securitization market for subprime mortgages grew to a meaningful size). In other words, they find that the level of total compensation of top management per se does not have an effect on the performance of loans. They document, instead, that the relative power of the risk manager (measured by the risk manager's share of pay given to the top five compensated executives in the company) has a negative effect on default rates. They suggest that stronger risk management departments inside the bank partially alleviate the moral hazard problem.

These papers have shown that high pay-performance sensitivity might induce managers to take higher risks. On the one hand, a possible explanation might be that CEOs focused on the interests of shareholders and took actions they believed the market would welcome. On the other hand, CEOs might have undertaken high-risk investments because they benefitted greatly from good performance, whereas losses associated with poor performance were limited (Allen & Gale, 2000 ,Chen, Steiner, & Whyte, 2006; Sullivan & Spong, 2007). In other words, if top-management compensation is very closely aligned with shareholders' interests, managers have strong incentives to undertake high-risk investments. This risk-taking issue is exacerbated in the banking industry because of banks' unique features, as discussed in the second section.

Bebchuk, Cohen, and Spamann (2010) document the negative consequences of incentive compensation. They show that incentive compensation at Bear Stearns and Lehman Brothers induced top management to take excessive risks from 2000 to 2008. In a more recent study, DeYoung, Peng, and Yan (2013) provide evidence for a sample of US banks for 1995–2006, showing that high wealth incentives in large banks induced risk taking. One of the most compelling studies of the link between compensation and risk taking in the financial industry is by Cheng, Hong, and Scheinkman (2015). The authors study how residual executive compensation (i.e,, the compensation that cannot be explained by firm size and by industry factors) is related to several measures of risks for a sample of US financial firms from 1992 to 2008. Their results show a strong positive correlation between residual compensation and risk taking and a negative relationship between insider ownership and risks. Brown, Jha, and Pacharn (2015) examine 533 CEO severance contracts for US financial services firms from 1997 to 2007 using metrics such as tail risk and asset quality and find that severance pay encourages excessive risk taking. This finding suggests that executives were rewarded or encouraged to take excessive risks (Thanassoulis, 2013). In an interesting conceptual paper, Zalewska (2016) argues that the traditional approach according to which remuneration can be a tool to reduce the principal-agent conflict is inadequate in the case of the banking sector. She states that remuneration can be a source of conflict between shareholders and other stakeholders. This conflict is very important in the banking sector because banks are fundamental providers of funding of economic and business activities. For this reason, she proposes an active involvement of regulators to balance short-term performance with the long-term needs of society. She notes the need for fundamental changes to national governance structure, cultures, and practices to address this issue.

Early evidence shows that the relationship between executive pay and performance and risk taking is different among Chinese banks. Luo (2015) examines the determinants of executive compensation in Chinese banking in 2005–2012 and finds no significant pay-for-performance relationship and no significant relationship between CEO power and executive compensation. Of course, the large Chinese banks included in this sample are state-owned. Government ownership of banks is a significant determinant of executive compensation and executive promotions in Chinese banks. Government priorities might also play a role in loan-making decisions. These factors might be important in explaining the low pay-for-performance sensitivity in Chinese banks. Additional research is needed to determine the role of state ownership in bank governance in China.

Increasing attention on compensation raises the question of whether bankers' pay should be regulated ex ante by an authority or should be freely set by the banks' boards of directors. Murphy (2013) argues that a compensation system characterized by a cap on variable compensation will create negative incentives for managers, resulting in reduced bank performance. This result occurs because, in the case of a failed risky project, bank managers' compensation will not suffer because their remuneration is largely fixed. Conversely, in the case of a successful risky project, bank managers will not

© 2016 John Wiley & Sons Ltd

obtain the reward, and they will not be compensated accordingly. The bonus cap makes compensation less sensitive to bank performance, which is the opposite of what is desirable in an incentive-compensation plan. In a recent study, Ferrarini (2015) discusses recent international rules concerning the mandatory structure of managerial compensation in banks. He questions the idea that managerial compensation has led banks to take excessive risks during the financial crisis. He discusses the role of middle managers and prudential regulation in risk taking and suggests an improvement in capital adequacy and organizational requirements rather than a direct intervention in bankers' incentives.

High pay-performance sensitivity also has implications in terms of agency costs between shareholders and debtholders. Banks are highly leveraged organizations; when managers are rewarded with stock grants, they experience a conflict of interest with debtholders, just as would any other bank shareholders (Becht et al., 2012). Specifically, in highly leveraged companies, high pay-performance sensitivity induces risk to shift from shareholders to debtholders (Becht et al., 2012; Bolton, Mehran, & Shapiro, 2015; John et al., 2010; John & John, 1993; John & Qian, 2003). John and Qian (2003) and John et al. (2010) argue that the optimal managerial compensation structure in highly leveraged firms such as banks should have low pay-performance sensitivity to offset the increased risk-shifting incentive toward debtholders. Bennett, Güntay, and Unal (2015) examine the relationship between CEO's inside debt holdings (pension benefits and deferred compensation) and the bank default risk and performance for a sample of US banks. They find that that in 2006, higher holdings of inside debt relative to inside equity by a CEO is associated with lower default risk and better performance during the crisis period. Bolton et al. (2015) develop a model that proposes linking executive compensation to both stock price and the credit default swap (CDS) spreads. Specifically, to offset the agency costs among different stakeholders, the authors propose linking executive compensation not only to stock price performance but also to a market estimate of the default risk of the bank (CDS). Srivastav and Hagendorff (2016) note that, although research has shown that inside debt reduces risk, future research should document the relationship between inside debt and risk components (i.e,, idiosyncratic risks and systemic risks).

Another aspect that has been highlighted recently is the importance of culture in risk taking and incentive compensation. Stulz (2015) argues that risk management is a function of corporate culture and its ability to shape the business environment. He states that it is impossible to set up an incentive plan that leads executives to take the right actions in every situation. In banks, not only the executives but also loan officers, who decide whether a loan is granted, make decisions about risks. Stulz argues that as a bank focuses on specific risks that can be quantified and accounted for in employees' incentive plans, employees have incentive to accept risks that are not quantified and monitored. Because of the limits of risk management and incentives, the ability of a firm to manage risk properly depends on its corporate culture.[11] Fahlenbrach, Prilmeier, and Stulz (2012) show that latent characteristics of banks, which can be explained by culture, are helpful in understanding how crises affect banks. Cultural differences between societies have a profound influence on the level of bank risk taking, and they partially explain bank financial troubles during the recent financial crisis (Kanagaretnam, Lim, & Lobo, 2011; (Li, Griffin, Yue & Zhao, 2012; Mihet, 2013.) Srivastav & Hagendorff, 2016). Resick, Gillian, Keating, Dickson, Kwan, and Peng (2011) discuss the different leadership styles and cultures across countries. Leadership might interact with risk-taking behavior. There is limited empirical work on the relationship between culture, compensation, incentives, and corporate outcomes, and the existing literature does not focus on the features that make banks unique. This stream of research deserves further investigation.

SUGGESTIONS AND CONCLUSIONS

Bank governance and top-management compensation in banks have been topics of intense policy discussions in recent years. Many policy documents have outlined recommendations about bank boards and governance structures. Common recommendations have been to focus on the board of directors, its independence, and its composition, and on how to structure managerial compensation to minimize risk-taking behavior (Basel Committee on Banking Supervision, 2008, 2010, 2015; Federal Reserve Bank, 2011; Walker Report, 2009).

In this paper, we have reviewed the literature on corporate governance in banks, in the US setting and in international settings. A novel feature of our survey is that we evaluate bank governance from three different perspectives. Our first perspective is to examine corporate governance in banks from the perspective of equity governance. Here, governance mechanisms are viewed in terms of how effective they are in aligning managers with the objective of share value maximization. Our second perspective is to view bank governance from the point of view of the objective of maximizing the total value of the bank. Incentivizing managers to maximize the total market value of the debt and equity is an important objective for banks, whose leverage often exceeds 90 percent. In designing bank governance or designing optimal regulation of governance features in banks, it is important to realize that strengthening equity governance can often be to the detriment of total firm value. Our third perspective examines bank governance from the point of view of society at large. We view bank governance from the perspective of a social objective that is focused on the role of banks in promoting a safe and sound financial system.

Although we have focused primarily on the internal mechanisms of corporate governance, we also survey the literature on the interaction of bank governance with bank regulation. We start with how corporate governance in banks is shaped by the special characteristics of banks and how bank governance differs from governance in manufacturing companies.

In the second section, we survey the main mechanisms of bank governance, including corporate boards in banks, board size, board composition, board independence, board committees, CEO duality, board expertise, ownership structure, and incentives and compensation. We also survey the cross-country evidence on these topics. We review managerial incentives and their effects on bank performance and bank risk taking. We argue that high-powered managerial incentives might lead to excessive risks and high agency costs of debt. In

© 2016 John Wiley & Sons Ltd

evaluating the efficacy of different mechanisms of bank governance, we use our new framework with its three perspectives. In particular, we view the relationship between different features of bank governance on bank risk taking before, during, and after the financial crisis. We consider bank performance not only from the perspective of equity value but also from that of debt value and the stability of the financial system. The social perspective provides us with a framework to understand the evidence on the interaction between bank regulation and bank governance.

We provide suggestions and directions for future research on corporate governance in banks. We suggest four main directions for future work. The current literature finds inconclusive results on the effect of financial expertise on bank performance and risk taking. Future research might consider additional variables, such as board interlocks and directors' networks, to obtain sharper predictions. This new focus could clarify the relationship between board expertise and performance and/or risk taking.

Second, the importance of board independence has been emphasized by both regulators and policymakers. Nevertheless, the empirical effect of independent directors on outcomes in banks is not well understood. We argue that future research should investigate the "quality" of independent directors. Increasing the number of independent directors on bank boards might not be an optimal mechanism for guaranteeing stability or good performance. Experience, network, age/tenure, or other personal characteristics of independent directors might influence their effectiveness. Experimenting with such dimensions of quality of directors might provide a more comprehensive understanding of the effect of independent directors (see, e.g., Forbes & Milliken, 1999).

Third, high-powered managerial incentives have been considered to induce managers to undertake high-risk investments. We argue that risk taking is a function of institutional factors, cultural factors, leadership style, and corporate culture. Empirical results on this issue are limited. We propose that future research consider the interactions between institutions, culture, risk taking, and the special features of banks. For example, institutional factors such as state ownership might interact with cultural factors to induce incentives in the Chinese banking context that are far from well understood.

Fourth, we propose a new framework to understand the conflict of interests between shareholders and debtholders and the relationship between equity governance mechanisms and debt governance mechanisms. Equity governance aligns the interests of managers with those of equity holders. Equity-aligned managers have risk-shifting incentives. Their risk taking lowers the value of debt and might reduce the value of the firm. Debt governance aims to protect the value of deposits and leads to a lower value of equity. We find it entirely natural that regulatory mechanisms have blunted the effectiveness of equity governance mechanisms. Most existing research has focused on traditional equity governance mechanisms, ignoring this interaction. Future research should study the interaction of equity governance and debt governance in the presence of high leverage. Theoretical models of bank governance that explore this interaction in the presence of regulation will provide additional insights. Empirical predictions of such models can also be tested using relevant data.

ACKNOWLEDGEMENTS

We are especially grateful to Associate Editor Chris Florakis, Editor Praveen Kumar, and two anonymous reviewers for their extensive and helpful comments. We are also thankful to Iftekhar Hasan, Qiao Jiang, Ronald Masulis, David Yermack, Xun Zhong, and Ming Ming Zhou for their comments.

NOTES

1. OECD (2009) and Devriese et al. (2004) identify three special factors of banks: systemic risk, high leverage, and dispersed non-experts as claim holders. Mülbert (2010) and Laeven (2013) count six differences between banks and nonbanks: leverage, opacity of the assets, diffuse depositors, maturity liquidity function, large creditors, and regulation.
2. They define broadly the expropriation from minority shareholders. They include "theft, transfer pricing, asset stripping, the preferential hiring of family members, the allocation of credit in a manner that enriches bank insiders but hurts the bank, and other perquisites that benefit bank insiders but hurt the bank" (Caprio et al., 2007: 585).
3. The corporate governance literature identifies problems related to concentrated ownership such as rent expropriation from minority shareholders, debtholders, or other stakeholders (Jensen & Meckling, 1976; Shleifer & Vishny, 1997).
4. For example, the Sarbanes-Oxley Act (SOX) and the New York Stock Exchange (NYSE) and NASDAQ exchange listing rules emphasize director independence for all listed firms. Adams and Mehran (2012) challenge the "one size-fits-all" approach. They say, "Bank directors often represent some of the best customers of the bank. But, such directors should most likely not be considered independent. Therefore, to comply with SOX, banks have to exclude them from audit committees and either increase board size to satisfy independence requirements or discontinue the practice of appointing customer representatives to their boards. While such changes could be beneficial, there are arguments why having bank customers on the board may be a good practice" (Adams & Mehran, 2012: 244).
5. The sample in this study includes several countries that have a two-tier board system in which normal functions and responsibilities are divided into the management board and the supervisory board (Hopt & Leyens, 2004). The authors use two methods to calculate board independence in two-tier boards: (1) they calculate the ratio of the independent directors from both tiers of the board to the total number of directors from both tiers of the board, and (2) they calculate the ratio of the independent directors on only the supervisory board to the total number of directors on the supervisory board. The authors conclude that the results are independent of the method used.
6. De Andres et al. (2012) include banks from Canada, the United Kingdom, the United States (common law countries), and France, Italy, the Netherlands, and Spain (civil law countries). All of the banks in the sample have one-tier boards.
7. The authors mention that they control for government bailout, but the results are not reported.

© 2016 John Wiley & Sons Ltd

8. To our knowledge, existing research has not examined the effect of CEO duality on bank risk taking in banks with two-tier boards.
9. More specifically, the author finds that board ownership has a positive effect on the profitability of traditional banks (that are financed by depositors and have mostly loan-making operations). However, management ownership has a positive effect on the profitability of non-traditional banks (that also have operations in securities trading, wealth management, and underwriting). The author argues that the positive effect of board ownership for traditional banks indicates that the safety net reduces the monitoring incentives of depositors, making it important to incentivize outside board members. Conversely, the greater opacity and complexity in the product portfolio of non-traditional banks make it important to incentivize top management, who have a higher expertise in their bank's products.
10. For a literature review on CEO compensation for nonfinancial companies, see Frydman and Jenter (2010).
11. There is a large organizational behavior literature on corporate culture. For a recent review, see Bouwman (2013).

REFERENCES

Acharya, V. V., Carpenter, J., Gabaix, X., John, K., Richardson, M., Subrahmanyam, M., Sundaram, R., & Zemel, E. 2009. Corporate governance in the modern financial sector. In V. Acharya & M. Richardson (Eds.), ***Restoring financial stability***. Hoboken, NJ: Wiley.

Adams, R. 2010. Governance of banking institutions. In H. K. Baker & R. Anderson (Eds.), ***Corporate governance***. Hoboken, NJ: Wiley.

Adams, R. 2012. Governance and financial crisis, ***International Review of Finance***, 12: 7–38.

Adams, R. & Ferreira, D. 2007. A theory of friendly board, ***The Journal of Finance***, 62: 217–250.

Adams, R., Hermalin, B. E., & Weisbach, M. S. 2010. The role of boards of directors in corporate governance: A conceptual framework and survey, ***Journal of Economic Literature***, 48: 58–107.

Adams, R. & Mehran, H. 2003. Is corporate governance different for bank holding companies? ***FRBNY Economic Policy Review***, 9: 123–142.

Adams, R. & Mehran, H. 2012. Bank board structure and performance: Evidence for large bank holding companies, ***Journal of Financial Intermediation***, 21: 243–267.

Aebi, V., Sabato, G., & Schmid, M. 2012. Risk management, corporate governance, and bank performance in the financial crisis, ***Journal of Banking & Finance***, 36: 3213–3226.

Aggarwal, R., Erel, I., Ferreira, M., & Matos, P. 2011. Does governance travel around the world? Evidence from institutional investors, ***Journal of Financial Economics***, 100: 154–181.

Aguilera, R., Goyer, M., & Kabbach de Castro, L. R. 2013. Regulation and comparative corporate governance. In M. Wright, D. S. Siegel, K. Keasey, & I. Filatotchev (Eds.), ***Handbook of corporate governance***. Oxford: Oxford University Press.

Aguilera, R. & Jackson, G. 2003. The cross-national diversity of corporate governance: Dimensions and determinants, ***Academy of Management Review***, 28: 447–465.

Al-Hadi, A., Hasan, M. M., & Habib, A. 2015. Risk committee, firm life cycle, and market risk disclosures, ***Corporate Governance: An International Review***, DOI: 10.1111/corg.12115.

Alexander, K. 2006. Corporate governance and banks: The role of regulation in reducing the principal-agent problem, ***Journal of Banking Regulation***, 7: 17–40.

Allen, F. & Gale, D. 2000. ***Comparing financial systems***. Cambridge, MA: MIT Press.

Anderson, R. & Fraser, D. 2000. Corporate control, bank risk taking, and the health of the banking industry, ***Journal of Banking & Finance***, 24: 1383–1398.

Aslan, H. & Kumar, P. 2014. National governance bundles and corporate governance agency costs: A cross-country analysis, ***Corporate Governance: An International Review***, 22: 230–251.

Barakat, A. & Hussainey, K. 2013. Bank governance, regulation, supervision, and risk reporting: Evidence from operational risk disclosures in European banks, ***International Review of Financial Analysis***, 30: 254–273.

Barth, J. R., Caprio, G., & Levine, R. 2004. Bank supervision and regulation: What works best? ***Journal of Financial Intermediation***, 13: 205–248.

Basel Committee on Banking Supervision. 2006. ***Enhancing corporate governance for banking organizations***. Basel: BIS.

Basel Committee on Banking Supervision. 2008. ***Principles for sound liquidity risk management and supervision***. Basel: BIS.

Basel Committee on Banking Supervision. 2010. ***Principles for enhancing corporate governance***. Basel: BIS.

Basel Committee on Banking Supervision. 2015. ***Corporate governance principles for banks***. Basel: BIS.

Bebchuk, L. A., Cohen, A., & Spamann, H. 2010. The wages of failure: Executive compensation at Bear Stearns and Lehman 2000–2008, ***Yale Journal on Regulation***, 27: 257–282.

Becher, D. A., Campbell, T. L., & Frye, M. B. 2005. Incentive compensation for bank directors: The impact of deregulation, ***Journal of Business***, 78: 1753–1777.

Becher, D. A. & Frye, M. B. 2011. Does regulation substitute or complement governance? ***Journal of Banking & Finance***, 35: 736–51.

Becht, M., Bolton, P., & Roell, A. 2012. Why bank governance is different, ***Oxford Review of Economic Policy***, 27: 437–463.

Belkhir, M. 2009. Board of directors' size and performance in the banking industry, ***International Journal of Managerial Finance***, 5: 201–221.

Beltratti, A. & Stulz, R. M. 2012. The credit crisis around the globe: Why did some banks perform better? ***Journal of Financial Economics***, 105: 1–17.

Bennett, R. L., Güntay, L., & Unal, H. 2015. Inside debt, bank default risk, and performance during the crisis, ***Journal of Financial Intermediation***, 24: 487–513.

Berger, A. & Bouwman, C. 2013. How does capital affect bank performance during financial crises? ***Journal of Financial Economics***, 109: 146–176.

Berger, A., Clarke, G., Cull, R., Klapper, L., & Udell, G. F. 2005. Corporate governance and bank performance: A joint analysis of the static, selection, and dynamic effects of domestic, foreign, and state ownership, ***Journal of Banking & Finance***, 29: 2179–2221.

Berger, A., Imbierowicz, B., & Rauch, C. 2016. The roles of corporate governance in bank failures during the recent financial crisis, ***Journal of Money, Credit and Banking***, forthcoming.

Berger, A., Kick, T., & Schaeck, K. 2014. Executive board composition and bank risk taking, ***Journal of Corporate Finance***, 28: 48–65.

Berglof, E. 2011. A European perspective on the global financial crisis, ***Corporate Governance: An International Review***, 19: 497–501.

Bhagat, S. & Black, B. 2002. The non-correlation between board independence and long term firm performance, ***Journal of Corporation Law***, 27: 231–273.

Bolton, P., Mehran, H., & Shapiro, J. 2015. Executive compensation and risk taking, ***Review of Finance***, 19: 2139–81.

Booth, J. R., Cornett, M. M., & Tehranian, H. 2002. Boards of directors, ownership, and regulation, ***Journal of Banking & Finance***, 26: 1973–1996.

© 2016 John Wiley & Sons Ltd

Borisova, G., Brockman, P., Salas, J. M., & Zagorchev, A. 2012. Government ownership and corporate governance: Evidence from the EU, ***Journal of Banking & Finance***, 36: 2917–2934.

Bouvatier, V., Lepetit, L., & Strobel, F. 2014. Bank income smoothing, ownership concentration and the regulatory environment, ***Journal of Banking & Finance***, 41: 253–270.

Bouwman, C. 2013. The role of corporate culture in mergers and acquisitions. In E. Perrault (Ed.), ***Mergers and acquisitions***. New York: Nova Science Publishers.

Brown, K., Jha, R., & Pacharn, P. 2015. Ex ante CEO severance pay and risk-taking in the financial services sector, ***Journal of Banking & Finance***, 59: 111–126.

Busta, I., Sinani, E., & Thomsen, S. 2014. Ownership concentration and market value of European banks, ***Journal of Management and Governance***, 18: 159–183.

Cambini, C., Rondi, L., & De Masi, S.. 2015. Incentive compensation: Does regulation matter? ***Corporate Governance: An International Review***, 3: 378–395.

Caprio, G., Laeven, L., & Levine, R. 2007. Governance and bank valuations, ***Journal of Financial Intermediation***, 16: 584–617.

Caprio, G. & Levine, R. 2002. Corporate governance in finance: Concepts and international observations. In R. E. Litan, M. Pomerleano, & V. Sundararajan (Eds.), ***Financial sector governance: The roles of the public and private sectors***. Washington, DC: The Brookings Institution.

Caprio, G. & Levine, R. 2012. Forward: The governance of banks and bank regulators. In J. R. Barth, C. Lin, & C. Wihlborg (Eds.), ***Research handbook on international banking and governance***. Northampton, MA: Edward Elgar.

Carlin, B., Kogan, S., & Lowery, R. 2013. Trading complex assets, ***The Journal of Finance***, 68: 1937–1960.

Cebenoyan, A. & Strahan, P. 2004. Risk management, capital structure and lending at banks, ***Journal of Banking & Finance***, 28: 19–43.

Chen, C., Steiner, T., & Whyte, A. M. 2006. Does stock option-based executive compensation induce risk-taking? An analysis of the banking industry, ***Journal of Banking & Finance***, 30: 915–945.

Chen, V. Z., Li, J., & Shapiro, D. 2011. Are OECD-prescribed "good corporate governance" practices really good in an emerging economy? ***Asia Pacific Journal of Management***, 26: 115–138.

Cheng, I., Hong, H., & Scheinkman, J. 2015. Yesterday's heroes: Compensation and creative risk-taking, ***The Journal of Finance***, 70: 839–879.

Conyon, M. J. 2014. Executive compensation and board governance in US firms, ***The Economic Journal***, 124: F60–F89.

Conyon, M. J., Judge, W. Q., & Useem, M. 2011. Corporate governance and the 2008–09 financial crisis, ***Corporate Governance: An International Review***, 19: 399–404.

Cornett, M. M., Guo, L., Khaksari, S., & Tehranian, H. 2010. The impact of state ownership on performance differences in privately-owned versus state-owned banks: An international comparison, ***Journal of Financial Intermediation***, 19: 74–94.

Cuñat, V. & Guadalupe, M. 2009. Executive compensation and competition in the banking and financial sectors, ***Journal of Banking & Finance***, 33: 495–504.

Dalton, D. R., Daily, C. M., Johnson, J. L., & Ellstrand, A. E. 1999. Number of directors and financial performance: A meta-analysis, ***Academy of Management Journal***, 42: 674–686.

de Andres, P. & Vallelado, E. 2008. Corporate governance in banking: The role of the board of directors, ***Journal of Banking & Finance***, 32: 2570–2580.

de Andres, P., Romero-Merino, M., Santamaría, M., & Vallelado, E. 2012. Board determinants in banking industry: An international perspective, ***Managerial and Decision Economics***, 33: 147–158.

de Haan, J. & Vlahu, R. 2015. Corporate governance of banks: A survey. ***Journal of Economic Surveys***, DOI: 10.1111/joes.12101.

DeAngelo, H. & Stulz, R. 2015. Liquid-claim production, risk management, and capital structure: Why high leverage is optimal for banks, ***Journal of Financial Economics***, 2: 219–236.

Dell'Ariccia, G., Igan, D., & Laeven, L. 2012. Credit booms and lending standards: Evidence from the subprime mortgage market, ***Journal of Money, Credit and Banking***, 44: 367–384.

Demirgüç-Kunt, A. & Detragiache, E. 2002. Does deposit insurance increase banking system stability? An empirical investigation, ***Journal of Monetary Economics***, 49: 1373–1406.

Demirgüç-Kunt, A. & Huizinga, H. 2004. Market discipline and deposit insurance, ***Journal of Monetary Economics***, 51: 375–399.

Demsetz, R., Saidenberg, M., & Strahan, P. 1997. ***Agency problems and risk taking at banks***. Working Paper no. 29, Federal Reserve Bank of New York Staff Report, New York.

Devriese, J., Dewatripont, M., Heremans, D., & Nguyen, G. 2004. Corporate governance, regulation and supervision of banks, ***Financial Stability Review***, 2: 95–120.

DeYoung, R., Evanoff, D. D., & Molyneux, P. 2009. Merger and acquisition of financial institutions: A review of the post-2000 literature, ***Journal of Financial Services Research***, 36: 87–110.

DeYoung, R., Peng, E., & Yan, M. 2013. Executive compensation and business policy choices at US commercial banks, ***Journal of Financial and Quantitative Analysis***, 48: 165–196.

Ellul, A. & Yerramilli, V. 2013. Stronger risk controls, lower risk: Evidence from US bank holding companies, ***The Journal of Finance***, 68: 1757–1803.

Elyasiani, E. & Zhang, L. 2015. Bank holding company performance, risk, and "busy" board of directors, ***Journal of Banking & Finance***, 60: 239–251.

Erkens, D. H., Hunga, M., & Matos, P. 2012. Corporate governance in the 2007–2008 financial crisis: Evidence from financial institutions worldwide, ***Journal of Corporate Finance***, 18: 389–411.

Esty, B. C. 1997. Organizational form and risk taking in the savings and loan industry, ***Journal of Financial Economics***, 44: 25–55.

Esty, B. C. 1998. The impact of contingent liability on commercial bank risk-taking, ***Journal of Financial Economics***, 47: 189–218.

European Commission. 2010. ***Corporate governance in financial institutions and remuneration policies***. Green paper. Brussels: European Commission.

Fahlenbrach, R. & Stulz, R. M. 2011. Bank CEO incentives and the credit crisis, ***Journal of Financial Economics***, 99: 11–26.

Fahlenbrach, R., Prilmeier, R., & Stulz, R. 2012. This time is the same: Using bank performance in 1998 to explain bank performance during the recent financial crisis, ***Journal of Finance***, 67: 2139–2185.

Fama, E. 1985. What's different about banks? ***Journal of Monetary Economics***, 15: 29–39.

Federal Reserve Board. 2011. ***Supervisory guidance on model risk management***. Washington, DC: Board of Governorns of the Federal Reserve System.

Federal Reserve Board. 2013. ***Capital planning at large bank holding companies: Supervisory expectations and range of current practice***. Washington, DC: Board of Governors of the Federal Reserve Board.

Fernandes, N. & Fich, E. 2013. Does financial experience help banks during credit crises? Unpublished paper.

Ferrarini, G. 2015. ***CRD IV and the mandatory structure of bankers' pay***. Working Paper Series in Law no. 289, European Corporate Governance Institute, Brussels.

Flannery, M. J., Kwan, S. H., & Nimalendran, M. 2004. Market evidence on the opaqueness of banking firms' assets, ***Journal of Financial Economics***, 71: 419–460.

Forbes, D. P. & Milliken, F. J. 1999. Cognition and corporate governance: Understanding boards of directors as strategic decision-making groups, ***Academy of Management Review***, 24: 489–505.

© 2016 John Wiley & Sons Ltd

Frydman, C. & Jenter, D. 2010. CEO compensation, ***Annual Review of Financial Economics***, 2: 75–102.

Furfine, C. H. 2001. Banks as monitors of other banks: Evidence from the overnight Federal Reserve fund market, ***Journal of Business***, 74: 33–57.

Garicano, L. & Cuñat, V. 2010. Did good Cajas extend bad loans? Governance, human capital, and loan portfolios. In S. Bentolila, M. Boldrin, J. Diaz-Gimenez, & J. J. Dolado (Eds.), ***The crisis of the Spanish economy*: *Economic analysis of the Great Recession***. Madrid: Fedea.

Gompers, P., Ishii, J., & Metrick, A. 2003. Corporate governance and equity prices, ***Quarterly Journal of Economics***, 118: 107–156.

Gornall, W. & Strebulaev, I. A. 2014. ***Financing as a supply chain*: *The capital structure of banks and borrowers***. Working Paper no. 166, Stanford University, Rock Center for Corporate Governance, Stanford, CA.

Gregg, P., Jewell, S., & Tonks, I. 2012. Executive pay and performance: Did bankers' bonuses cause the crisis? ***International Review of Finance***, 12: 89–122.

Grove, H., Patelli, L., Victoravich, L., & Xu, P. 2011. Corporate governance and performance in the wake of the financial crisis: Evidence from US commercial banks, ***Corporate Governance: An International Review***, 19: 418–436.

Hagendorff, J., Collins, M., & Keasey, K. 2010. Board monitoring, regulation, and performance in the banking industry: Evidence from the market for corporate control, ***Corporate Governance: An International Review***, 18: 381–395.

Hart, O. 1995. Corporate governance: Some theory and implications, ***Economic Journal***, 105: 678–689.

Hau, H. & Thum, M. P. 2009. Subprime crisis and board (in-)competence: Private vs. public banks in Germany, ***Economic Policy***, 24: 701–751.

Haw, I., Ho, S., Hu, B., & Wu, D. 2010. Concentrated control, institutions, and banking sector: An international study, ***Journal of Banking & Finance***, 34: 485–497.

Hopt, K. J. 2013. Corporate governance of banks and other financial institutions after the financial crisis: Regulation in the light of empire and theory, ***Journal of Corporate Law Studies***, 13: 219–253.

Hopt, K. J. & Leyens, P. 2004. Board models in Europe: Recent developments of internal corporate governance structures in Germany, the United Kingdom, France, and Italy, ***European Company and Financial Law Review***, 1: 135–168.

Houston, J. & James, C. 1995. CEO compensation and bank risk: Is compensation in banking structured to promote risk taking? ***Journal of Monetary Economics***, 36: 405–431.

Hubbard, G. R. & Palia, D. 1995. Executive pay and performance: Evidence from the US banking industry, ***Journal of Financial Economics***, 39: 105–130.

Hughes, J. P., Lang, W. W., Mester, L. J., Moon, C., & Pagano, M. 2003. Do bankers sacrifice value to build empires?: Managerial incentives, industry consolidation, and financial performance, ***Journal of Banking & Finance***, 27: 417–447.

Iannotta, G., Nocera, G., & Sironi, A. 2007. Ownership structure, risk and performance in the European banking industry, ***Journal of Banking & Finance***, 21: 2127–2149.

Jensen, M. 1993. The modern industrial revolution, exit, and the failure of internal control systems, ***The Journal of Finance***, 48: 831–80.

Jensen, M. & Meckling, W. 1976. Theory of the firm: Managerial behavior, agency costs, and ownership structure, ***Journal of Financial Economics***, 3: 305–360.

Jensen, M. & Warner, J. B. 1988. The distribution of power among corporate managers, shareholders, and directors, ***Journal of Financial Economics***, 20: 3–24.

Johansen, T. R. & Pettersson, K. 2013. The impact of board interlocks on auditor choice and audit fees, ***Corporate Governance: An International Review***, 21: 287–310.

John, K., Litov, L., & Yeung, B. 2008. Corporate governance and risk-taking, ***The Journal of Finance***, 63: 1679–1728.

John, K., Mehran, H., & Qian, Y. 2010. Outside monitoring and CEO compensation in the banking industry, ***Journal of Corporate Finance***, 16: 383–399.

John, K. & Qian, Y. 2003. Incentive features in CEO compensation in the banking industry, ***FRBNY Economic Policy Review***, 9: 109–121.

John, K., Saunders, A., & Senbet, L. W. 2000. A theory of bank regulation and management compensation, ***Review of Financial Studies***, 13: 95–125.

John, K. & Senbet, L. W. 1998. Corporate governance and board effectiveness, ***Journal of Banking & Finance***, 22: 371–403.

John, T. A. & John, K. 1993. Top-management compensation and capital structure, ***The Journal of Finance***, 48: 949–974.

Kanagaretnam, K., Lim, C. Y., & Lobo, J. 2011. Effects of national culture on earnings quality of banks, ***Journal of International Business Studies***, 42: 853–874.

Keys, K., Mukherjee, T., Seru, A., & Vig, V. 2009. Financial regulation and securitization: Evidence from subprime loans, ***Journal of Monetary Economics***, 56: 700–720.

Kim, K., Kitsabunnarat-Chatjuthamard, P., & Nofsinger, J. 2007. Large shareholders, board independence, and minority shareholder rights: Evidence from Europe, ***Journal of Corporate Finance***, 13: 859–880.

Klomp, J. & de Haan, J. 2012. Banking risk and regulation: Does one size fit all? ***Journal of Banking & Finance***, 36: 3197–3212.

Krause, R., Semadeni, M., & Cannella, A. 2014. CEO duality: A review and research agenda, ***Journal of Management***, 40: 256–286.

Kumar, P. & Zattoni, A. 2013. How much do country-level or firm-level variables matter in corporate governance studies? ***Corporate Governance: An International Review***, 21: 199–200.

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. W. 1998. Law and finance, ***Journal of Political Economy***, 106: 1113–1155.

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. W. 2000. Investor protection and corporate governance, ***Journal of Financial Economics***, 58: 3–27.

Laeven, L. 2013. Corporate governance: What's special about banks? ***Annual Review of Financial Economics***, 5: 63–92.

Laeven, L. & Levine, R. 2009. Bank governance, regulation, and risk-taking, ***Journal of Financial Economics***, 93: 259–275.

Lee, S. W. 2002. Insider ownership and risk-taking behaviour at bank holding companies, ***Journal of Business Finance & Accounting***, 29: 989–1005.

Levine, R. 2004. ***The corporate governance of banks*: *A concise discussion of concepts and evidence***. Working paper no. 3404, World Bank Research, Washington, DC.

Li, K., Griffin, D., Yue, H., & Zhao, L. 2012. How does culture influence corporate risk-taking? ***Journal of Corporate Finance***, 23: 1–22.

Li, L. & Song, F. M. 2013. Do bank regulations affect board independence? A cross-country analysis, ***Journal of Banking & Finance***, 37: 2714–2732.

Luo, Y. 2015. CEO power, ownership structure and pay-performance in Chinese banking, ***Journal of Economics and Business***, 82: 3–16.

Lingel, A. & Sheedy, E. 2012. ***The influence of risk governance on risk outcomes – international evidence***. Working paper no. 37, Applied Finance Centre Research Paper, Macquarie University, Sydney.

Macey, J. R. & O'Hara, M. 2003. The corporate governance of banks, ***FRBNY Economic Policy Review***, 9: 91–107.

Martin, K. J. & McConnell, J. J. 1991. Corporate performance, corporate takeovers, and management turnover, ***The Journal of Finance***, 46: 671–687.

© 2016 John Wiley & Sons Ltd

Mehran, H. & Mollineaux, L. 2012. ***Corporate governance of financial institutions***. Working paper no. 539, Federal Reserve Bank of New York.
Mehran, H., Morrison, A., & Shapiro, J. 2012. Corporate governance and banks: What have we learned from the financial crisis? In M. Dewatripont & X. Freixas (Eds.), ***The crisis aftermath: New regulatory paradigms***. London: Centre for Economic Policy Research.
Micco, A., Panizza, U., & Yanez, M. 2007. Bank ownership and performance: Does politics matter? ***Journal of Banking & Finance***, 31: 219–241.
Mihet, R. 2013. Effects of culture on firm risk-taking: A cross-country and cross-industry analysis, ***Journal of Cultural Economics***, 37: 109–151.
Minton, B. A., Taillard, J. P., & Williamson, R. 2014. Financial expertise of the board, risk taking, and performance: Evidence from bank holding companies, ***Journal of Financial and Quantitative Analysis***, 49: 351–380.
Morgan, D. P. 2002. Rating banks: Risks and uncertainty in an opaque industry, ***American Economic Review***, 92: 874–888.
Mülbert, P. O. 2010. ***Corporate governance of banks after the financial crisis – theory, evidence, reforms***. Working paper series in law no. 151, European Corporate Governance Institute, Brussels.
Mülbert, P. O. & Citlau, R. D. 2011. ***The uncertain role of banks' corporate governance in systemic risk regulation***. Working paper series in law no. 179, European Corporate Governance Institute, Brussels.
Muller-Kahle, M. I. & Lewellyn, K. B. 2011. Did board configuration matter? The case of US subprime lenders, ***Corporate Governance: An International Review***, 19: 405–417.
Mullineux, A. 2006. The corporate governance of banks, ***Journal of Financial Regulation and Compliance***, 14: 375–382.
Murphy, K. 2013. Regulating banking bonuses in the European Union: A case study in unintended consequences, ***European Financial Management***, 19: 631–657.
Nguyen, D. L., Hagendorff, J., & Eshraghi, A. 2015. Which executive characteristics create value in banking? Evidence from appointment announcements, ***Corporate Governance: An International Review***, 23: 112–128.
OECD 2009. ***Corporate governance and the financial crisis: Key findings and main messages***.
Pathan, S. 2009. Strong boards, CEO power and bank risk-taking, ***Journal of Banking & Finance***, 33: 1340–1350.
Pathan, S. & Faff, R. 2013. Does board structure in banks really affect their performance? ***Journal of Banking & Finance***, 37: 1573–1589.
Pathan, S. & Skully, M. 2010. Endogenously structured boards of directors in banks, ***Journal of Banking & Finance***, 34: 1590–1606.
Purnanandam, A. 2011. Originate-to-distribute model and the subprime mortgage crisis, ***Review of Financial Studies***, 24: 1881–1915.
Renders, A. & Gaeremynck, A. 2012. Corporate governance, principal-principal agency conflicts, and firm value in European listed companies, ***Corporate Governance: An International Review***, 20: 125–143.
Renders, A., Gaeremynck, A., & Sercu, P. 2010. Corporate governance ratings and company performance: Across-European study, ***Corporate Governance: An International Review***, 18: 87–106.
Resick, C., Gillian, M., Keating, M., Dickson, M., Kwan, H., & Peng, C. 2011. What ethical leadership means to me: Asian, American, and European perspectives, ***Journal of Business Ethics***, 101: 435–457.
Saghi-Zedek, N. & Tarazi, A. 2015. Excess control rights, financial crisis and bank profitability and risk, ***Journal of Banking & Finance***, 55: 361–379.
Saunders, A., Strock, E., & Travlos, N. 1990. Ownership structure, deregulation, and bank risk taking, ***The Journal of Finance***, 45: 643–654.
Shleifer, A. & Vishny, R. W. 1997. A survey of corporate governance, ***The Journal of Finance***, 52: 737–783.
Simpson, W. & Gleason, A. 1999. Board structure, ownership, and financial distress in banking firms, ***International Review of Economics and Finance***, 8: 281–292.
Srivastav, A. & Hagendorff, J. 2016. Corporate governance and bank risk-taking, ***Corporate Governance: An International Review***, DOI: 10.1111/corg.12133.
Stulz, R. M. 2015. Risk-taking and risk management by banks, ***Journal of Applied Corporate Finance***, 27: 8–19.
Sullivan, R. & Spong, K. 2007. Manager wealth concentration, ownership structure, and risk in commercial banks, ***Journal of Financial Intermediation***, 16: 229–248.
Sun, J. & Liu, G. 2014. Audit committees' oversight of bank risk-taking, ***Journal of Banking & Finance***, 40: 376–387.
Thanassoulis, J. 2013. Industry structure, executive pay, and short-termism, ***Management Science***, 59: 402–419.
Van der Elst, C. 2015. ***Corporate governance and banks: How justified is the match?*** Working paper series in law no. 284, European Corporate Governance Institute, Brussels.
Walker Report. 2009. ***A review of corporate governance in UK banks and other financial industry entities – Final Recommendations***. London.
Walter, I. 2004. Conflicts of interest and market discipline among financial service firms, ***European Management Journal***, 22: 361–76.
Wang, T. & Hsu, C. 2013. Board composition and operational risk events of financial institutions, ***Journal of Banking & Finance***, 37: 2042–2051.
Westman, H. 2011. The impact of management and board ownership on profitability in banks with different strategies, ***Journal of Banking & Finance***, 35: 3300–3318.
Yeh, Y., Chung, H., & Chih-Liang, L. 2011. Committee independence and financial institution performance during the 2007–08 credit crunch: Evidence from a multicountry study, ***Corporate Governance: An International Review***, 19: 437–458.
Zalewska, A. 2016. A new look at regulating bankers' remuneration. ***Corporate Governance: An International Review***, DOI: 10.1111/corg.12149.

Kose John is the Laura H. Carnell Professor of Finance at Fox School of Business, Temple University and Charles William Gerstenberg Professor of Banking and Finance at New York University, Stern School of Business. He has also taught at the University of Chicago, Columbia University and Institut d'Etudes Politiques de Paris (Sciences Po). He has won several awards, including the Jensen Prize for the best paper published in 2000. He is on the Nomination Committee for the Nobel Prize in Economics for 2016. He has authored/edited 24 books and published over 103 research articles in the major finance and economics journals. His recent research focuses on banking, the financial crisis, corporate governance, top-management compensation, valuation of distressed claims, and comparative bankruptcy and governance systems. He served as the president of the Financial Management Association International during 2014–15.

Sara De Masi is Lecturer at the University of Florence. She teaches Corporate Governance and Financial Institutions, in the MSc "Finance and Risk Management". Since 2011 she is also Lecturer at Kent State University where she teaches International Business. Recently, she has been a visiting researcher at New York University, Leonard N. Stern School of Business. She holds a PhD in Economics, Markets and Institutions from IMT – Institute for Advanced Studies. Her research interests

 © 2016 John Wiley & Sons Ltd

are in the areas of corporate governance, executive compensation, regulation, banking and financial institutions, innovation, and strategy.

Andrea Paci is Full Professor of Management at University of Florence – Department of Economics and Management. He is also Chairman of the MSc "Management and Business Administration" at the School of Economics and Management, University of Florence. His research interests are corporate governance, entrepreneurship, and banking and financial institutions. He is advisor for businesses and institutions. He served as independent director and as chairman of the Board of Statutory Auditors of many corporations, banks, and financial institutions. He was economic counselor to the Italian government.

© 2016 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 322–333

A New Look at Regulating Bankers' Remuneration

Anna Zalewska*

ABSTRACT

Manuscript Type: Conceptual
Research Questions/Issues: Executive remuneration, whether as a tool for resolving agency problems or as a sign of them, has been discussed in the literature for decades. The discussion, however, has been focused on non-financial firms, and bankers' remuneration, particularly in the context of corporate governance, has been overlooked until recently. However, following the financial crisis, regulators have begun intervening into banking boards' responsibilities, including remuneration. This raises numerous questions, in particular, how far the existing non-financial literature applies to banks, and if not, why and how this impacts on appropriate corporate governance in banking, and what challenges this brings?
Research Findings/Insights: The paper argues that due to numerous externalities, notably the interconnectivity and systemic risk of the banking sector, a traditional approach to remuneration based on resolving the principal-agent conflict is inappropriate. Active involvement of regulators is needed to balance the short-term performance of the banking sector with the long-term needs of society. This, however, means that remuneration and corporate governance of banks is no longer an individual bank issue but is a national and probably an international phenomenon. In some cases this may require fundamental changes to the national governance structure, culture, and practices.
Theoretical/Academic Implications: The analysis questions the suitability of the common idea of assessing corporate governance in banks in the same way as is done for non-financial institutions. Given that several traditional non-financial board responsibilities have been partially passed over to regulators in the banking sector, a new theoretical model of corporate governance is needed for banks. The paper examines relational contracts (echoed to some extent in stewardship, stakeholder, and network theories), and argues that these cannot be expected to be successful in the banking environment.
Practitioner/Policy Implications: The paper highlights the importance of tying the corporate governance of banks with other regulatory measures employed to restrict risk taking. It also stresses the need for harmonization of corporate governance metrics for the banking sector at a national/international level.

Keywords: Corporate Governance, Executive Remuneration, Banks, Regulation, Systemic Risk

INTRODUCTION

According to principal-agent theory, the separation of ownership and control is the starting point for the debate on how to mitigate the problems that arise because principals and agents hired by them may have different objectives, and that the principals do not fully observe the actions undertaken by agents. Consequently, how to minimize differences in objectives, how to limit asymmetries of information between agents and principals, and how to minimize their effects have become key strands of the corporate governance literature. The alignment of interests by making agents equity focused is one of most commonly postulated solutions. Consequently, a vast literature is devoted to discussing existing and optimal remuneration structures of top-tier management and CEOs. Many papers are written on whether remuneration practices ensure that shareholders' value has been maximized (for an overview, see Frydman & Jenter 2010). Similarly, executive, and in particular, CEO's remuneration has frequently been addressed by regulators and other policymaking bodies (e.g., US Congress, Securities and Exchange Commission (SEC), European Commission (EC), individual governments).

Whilst the majority of the literature has been focused on the corporate governance of non-financial companies, the 2008 financial crisis has brought the financial sector and, in particular, banks into the spotlight. It became apparent that there is a gap in the literature and potentially also in regulation, on who should structure remuneration in banks and what form this should take. Pre-financial crisis codes of good practice and regulation were cross-industrial and country-focused in nature. They also were not particularly interventionist when it came to influencing the size and form of remuneration. However, the financial crisis has revealed that, since banks and other financial institutions do not fit into the classic picture of agency theory, their remuneration practices may need more attention. Moreover, it is not only that tighter internal governance mechanisms may need to be in place (e.g., better risk-management practices) but also that leaving remuneration

*Address for correspondence: Anna Zalewska, School of Management, University of Bath, Bath BA2 7AY, UK. Tel: +44 01225 384354; E-mail: a.zalewska@bath.ac.uk

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12149

decisions in the hands of bankers' boards may be a mistake. For example, structuring bankers' remuneration to maximize shareholder value does not necessarily reduce the systemic risk of the banking sector. In the case of banks there are strong externalities and material risk-taking is often performed outside boardrooms. New regulations make an attempt to take these into account and ensure that bankers, and therefore banks, maintain investment strategies within predefined risk limits. This, however, may not be fully consistent with what shareholders would vote for and, therefore, the shareholder-centrism of the existing approaches to corporate governance and remuneration is insufficient and potentially harmful.

The aim of the paper is to discuss bankers' remuneration issues and recent regulatory policies in the field. The paper argues that given the banking sector's specifics (e.g., its asymmetries of information, interconnectivity, systemic risk, weak relational contracts) and the fact that bankers' remuneration may be a source of type III agency conflicts (i.e,, conflict arising between principals and broadly understood stakeholders) that contribute to substantial economic and social costs borne by the third parties, it is not appropriate to leave remuneration issues solely in the hands of shareholders. It provides arguments in support of regulators being actively involved in setting remuneration structures to balance the short-term incentives of principals with long-term financial/economic stability. Given that risk-management has already been monitored and overlooked by regulators, and there are good arguments to perceive remuneration as part of the risk-management practices, regulatory involvement in setting remuneration seems advisable to ensure consistency of policies and practices. Although the paper postulates that regulators should be involved in setting remuneration structures (as they already set risk metrics), it also provides a critical assessment of recent regulatory developments and highlights several complications arising from an introduction of potentially contradictory and potentially overzealous policies.

The contribution of this research reaches, however, far beyond remuneration issues. If regulators have a say-on-pay and risk-taking (hence influence banks' strategies) the question arises about the role and position of boards. This paper argues that the existing theories of corporate governance fall a long way short of providing a conceptual base for setting goals and performance metrics for the banking industry. Therefore, the paper casts doubt on the common idea of assessing corporate governance in banks in the same way as for non-financial institutions, especially given the cross-country character of banking sector regulation.

The paper starts by discussing the relevant concepts and findings of the literature concerning the use of remuneration as an incentive. Then, it examines the specific characteristics of the banking sector and identifies the shortcomings of the 'traditional' approach to remuneration for the banking sector. Next, it provides a discussion of the literature on regulation of bankers' remuneration and the current state of regulatory developments in the area, and analyses specific issues arising from current regulatory changes. The summary of the main arguments and discussion of implications of the analysis is provided in the closing section.

REMUNERATION AS INCENTIVES

A significant portion of the corporate governance literature has been devoted to studying the potential conflict between principals and agents stemming from asymmetries of information and high transaction costs. The principal-agent conflict is studied when the principal is typically narrowly defined as shareholders (e.g., the Anglo-Saxon approach) and also when a broader definition of the principal is applied, that is, when the principal is assumed to consist of shareholders and other stakeholders (e.g., in the Germanic approach these include employees, sponsoring bank representatives, etc.).

It is also well recognized in the literature that agency problems are not limited to discord between agents and their principals. The principals themselves are prone to generate conflicts. For instance, issues can arise when controlling shareholders try to take advantage of non-controlling shareholders (type II agency problems), or between shareholders and stakeholders (type III agency problems) (Thomsen & Conyon 2012).

Incentives and monitoring are important instruments used to reduce the consequences of the asymmetries of information between agents and principals, and to some extent can be thought of as substitutes (Zalewska 2014a). Monitoring decisions of senior management is often time consuming, expensive and slows decision making so, understandably, considerable attention has been paid to establishing good incentive structures. Thus, remuneration is seen as an important tool in fostering greater efficiency in situations where there are market failures.

Most commonly, remuneration issues are studied in the context of the principal-agent conflict (i.e., type 1 agency problems). In the world where principals find it difficult to assess the qualities of agents that they wish to appoint, cannot fully and completely observe the actions of the agents once appointed, and where transaction costs make it difficult for the principals to monitor the agents, remuneration appears to enter the picture in two distinct, but interlinked ways (for a review, see Frydman & Jenter 2010). One relates to the role of remuneration in reducing the consequences of separation of ownership and control and, in particular, how the structure of remuneration packages can be used to protect principals from powerful agents by aligning the interests of the agents with those of the principals. This implies that in addition to setting the pay level to attract the most talented and suitable agents, remuneration should be set to reward them for good performance. In other words, it should have an option-like nature. Granting options, therefore, seems like an obvious solution to the incentives issue if shareholder value is to be maximized. Indeed, numerous papers document the benefits of option grants (e.g., Core & Guay 2001; Core, Guay, & Larcker 2003; Core, Guay, & Thomas 2005; Core & Larcker 2002; Morck, Shleifer, & Vishny 1988). However, there always remained skepticism about this approach to incentives (e.g., Buck, Shahrim, & Winter 2004), although Hintz and Müller-Bloch (2015) report a negative reaction on the German market to the introduction of restrictions on executive remuneration.

However, another strand of the remuneration literature focuses on a potential 'dark-side' of remuneration. Here it is emphasized that remuneration is often excessive (remuneration is a symptom not the solution), that executives are able to

© 2015 John Wiley & Sons Ltd

undermine attempts at alignment, and that the alignment agenda actually encourages executives to engage in excessive risk-taking (this latter point is particularly a concern in the banking sector). In short, in this strand of the literature, there is significant skepticism regarding the use of equity-linked compensation as a tool for solving agency (type I) issues. Making agents shareholders in the firms where they are employed does not turn agents into '100% principals'. Their risk attitudes, ability to create diversified portfolios, time preferences, etc., may hamper the full alignment of interests. Indeed, granting equity-linked compensation can create severe problems and even magnify the agency conflict. First, there are numerous papers suggesting that executives engage in activities that dilute the incentives bestowed upon them (e.g., Lie 2005; Ofek & Yermack 2000). Second, it is not altogether clear that equity-linked compensation results in better firm performance. Bebchuk and Fried (2003, 2004) argue that US executive compensation practices fail to protect shareholders because the high compensation of CEOs does not increase incentives. Core, Holthausen, and Larcker (1999) conclude that greater remuneration reflects weak corporate governance rather than good performance. A similar conclusion is reached by Balafas & Florackis (2014), Chance, Kumar, & Todd (2000), Dow & Raposo (2005), Hall & Murphy (2003), Oyer (2004), Rajgopal, Shevlin, & Zamora (2006), and many others.

These two strands of the literature, i.e., the perception that remuneration practices are an effective corporate governance tool and the perception that remuneration practices are a manifestation of weak corporate governance, suggest that regulation (e.g., corporate governance codes, legal interventions, tax structures designed to incentivize particular forms of remuneration) has a role to play in removing or ameliorating market failures. Unfortunately, partly because of the politicization of many of the concerns surrounding the separation of ownership and control, arriving at the right regulation is not easy and the regulation itself can easily create problems and lead to more inefficiency.

The requirement to disclose remuneration is an obvious example of a policy with strong side effects. It may seem obvious that shareholders should know how much money goes from their pockets straight to the pockets of managers in the form of remuneration. Even if they are not owners, the similar argument could be applied to stakeholders, particularly if they were represented on advisory boards. Therefore, remuneration disclosure seems like good corporate governance practice. However, it is well documented in the literature that when the quality of workers is unknown, and remuneration paid observed by all workers, it is optimal to pay more rather than less to attract quality workers (Hayes & Shaefer 2009; Park, Nelson, & Huson 2001). However, neither regulators nor economic theory give a clear view as to where the "more" should stop. The UK Combined Code of Corporate Governance 2006 states that "levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose" (Main Principle (para. B1)). Unfortunately, it is not clear what the 'sufficient' but not 'unnecessary' high level of remuneration would be.

In the US remuneration disclosure has a long tradition (for a summary, see Murphy 2011). The US was the first country to set rules for disclosure of executive remuneration of publicly traded firms when in 1938 the SEC passed a Securities Act that requested companies to name directors, officers, and other persons whose remuneration exceeded $25,000. It was also the first and, in fact, the only country that over the following decades developed detailed regulations on the content and format of what should be reported.[1] The effects are quite clear, executive remuneration disclosure has had a spiraling effect on the size of remuneration (Conyon & Murphy 2000; Hayes & Shaefer 2009), and these days US executives are paid more than executives in other countries (e.g., Murphy 2013), although Fernandes, Ferreira, Matos, & Murphy (2013) suggest that differences in firm characteristics account for a significant proportion of this difference. In spite of this evidence, it has now become standard to request disclosure of remuneration in minutes of general meetings and/or annual reports in many countries around the world (Practical Law 2014).

Even if remuneration seems central in the principal-agent problem, one might question whether it is relevant for type II and type III agency problems as these do not directly result from, or involve, remuneration agreements between the parties involved. Although there may be no remuneration agreements among shareholders or between shareholders and stakeholders, remuneration may play a significant role in generating conflict. For instance, managers may be paid in such a way that they have clear incentives to be partial in a conflict between groups of shareholders, or between shareholders and stakeholders, or even substantially contribute to its creation. There are numerous cases of third parties paying a bill for reckless behavior of management (e.g., several environmental disasters fall in this category), yet the banking industry with its inherent systemic risk and interconnectivity (Liu, Quiet, & Roth 2015) makes it unique in this regard. Indeed, when negligence of safety standards by BP led to an oil spill in the Gulf of Mexico in 2010, BP had to pay a fine of $18.7bn to settle claims of the US government (Rushe 2015). But neither the event itself, nor the compensation fine, has resulted in a crisis in the oil industry in the UK, the US, or any other country. Obviously, it did not lead to economic turbulence on a global, or even national scale. However, in the case of the banking industry, reckless behavior in one bank can bring the whole banking industry down, and with it the whole economy. If remuneration practices in the banking industry create or exacerbate external costs that banks may inflict on third parties (i.e., taxpayers, debt holders), then remuneration practices in the sector need special attention. Before the evidence that remuneration practices affect banking risk-taking is discussed, the next section provides arguments for why the banking industry is different from other sectors.

WHY ARE BANKS AND BANKERS' REMUNERATION DIFFERENT?

Until recently there was little in the corporate governance literature that focused exclusively on banking and bankers' remuneration, although the almost unique features of market failure surrounding banking were commonly understood (e.g., Diamond 1984; Diamond & Dybvig 1983). In particular, it is well acknowledged that costs that banks may inflict on third parties, as a result of transaction costs and asymmetries

© 2015 John Wiley & Sons Ltd

of information, are particularly high. Hence, the specific features of banking mean that a remuneration debate solely based on the separation of ownership and control misses a great deal of the story and, therefore, may lead to incorrect conclusions and harmful solutions.[2]

When discussing remuneration structures as a mechanism to resolve the issues arising from the separation of ownership and control, it is implicitly assumed that a firm is equity financed and does not have any social or broad-economy links and obligations over and above those present for most corporations (e.g., environmental issues). As indicated at the end of the previous section, the banking sector does not fit into this standard approach. Two primary drivers for this are (i) banks' capital structure, and (ii) banks' interconnectivity and their systemic risk.

Starting with capital structure, Allen, Carletti, & Marquez (2014) document that the ratios of deposits to liabilities and deposits to GDP in the 2000–2007 period were 60–90 percent and 50–200 percent, respectively for the five countries they study (France, Germany, Italy, Japan, US). In contrast, the ratios of stock market capitalization of banks to GDP varied between 3 and 25 percent for the same period for the five countries studied by Allen et al. (2014).[3] Even though not all banks are listed on stock markets (e.g., small regional savings banks in Germany and the US) and, therefore, the statistics are potentially downward biased, the differences in the ratios are clear and illustrate that shareholders are a relatively minor group in comparison with depositors and other stakeholders.

The second driver (interconnectivity and systemic risk) suggests that it is not sufficient to consider corporate governance on a bank-by-bank basis. In any banking sector there is often a significant number of institutions that are very closely networked with each other. Hence, the failure of one bank can affect the stability of the whole financial sector (Liu et al. 2015). Moreover, banks' services are very deeply rooted into the economic activities of their countries. They provide financial services to ordinary citizens, firms of various sizes as well as governmental projects. Even in the most advanced economies with the most developed stock markets, such as the US, the UK, and Japan, banks are fundamental providers of financing of economic and business activities. Their role in supporting and ensuring the economic development of countries is fundamental. If the banking sector experiences difficulties, the whole of society bears the consequences. In the 2008 financial crisis, the rescuing packages cost taxpayers billions of dollars, pounds, euros, etc., and this is before all other economic and social costs of slow economic growth, declining level of household income, increased unemployment, etc., have been accounted for.[4] Therefore, banks' obligations stretch far beyond maximization of shareholder value, or even beyond those of stakeholders when stakeholders are perceived as those related to a single bank (e.g., employees). This magnifies agency type III conflicts.

These features of the banking industry make banks' risk-taking and remuneration a particular issue. It is well recognized in the literature that if any firm is highly levered, there is a conflict of interest between shareholders and debt holders. In good times shareholders scoop high returns (debt holders receive a fixed, predefined return), but in bad times shareholders' losses are bounded due to limited liability. That is, the firm's equity is itself a call option on the firm's assets. This means that risk-taking preferences of shareholders will be much higher than those of debt holders, and sub-optimal from the debt holder's perspective (e.g., Bebchuk & Spamann 2010; Boeri, Lucifora & Murphy 2013). Therefore, if shareholders design managerial remuneration, and succeed in resolving type I agency problems by aligning managers' interest with their own, this can be at the cost of debt holders if capital markets are distorted and inefficiencies induced (e.g., Stiglitz & Weiss 1981). This is because, by fulfilling their duties towards shareholders, managers would take more risk than it would be appropriate from the perspective of debt holders, and society, and potentially contribute to the creation of a financial crisis.

This simple example can easily be generalized to a situation where a body of shareholders is extended to include the stakeholders related to the bank (e.g., employees, debt holders). A narrowly defined group of stakeholders cannot be expected to align their interests with a broadly defined set of stakeholders which includes other banks and almost all, if not all, of society. Therefore, risk taking of an individual bank may be excessive enough to lead to distress and even collapse of the whole sector with national and even international consequences.

This is an issue in particular when banks are systemically important ('too big to fail') and also if they are heavily interconnected (e.g., failure of a bank can create payment problems throughout the economy and cause significant costs for individuals and companies that have no direct relationship with the bank). Given transaction costs and asymmetries of information, it is difficult for such stakeholders to protect themselves from undue risk taking by banks. Hence, it is possible that allowing principals to align remuneration with their risk preferences could leave taxpayers no alternative but to pour money in to rescue banks if business turns bad. Thus, whilst remuneration may be beneficial in minimizing the type I agency conflict between agents and principals in most of the corporate sector, in the case of the banking industry regulation of remuneration of some form is likely to be needed to address conflicts that arise between principals and broad economic and social agents affected by bank operations, policies, and performance, i.e., stakeholders in the broadest possible sense. In particular, regulation may be needed to ensure that the rights of both groups are protected.

SHAREHOLDER-SET BANKERS' REMUNERATION AND RISK-TAKING

Is there material evidence that alignment of banking executive incentives with shareholder interests should be a material concern?[5] If one reads the popular press and listens to politicians, one can easily come to the conclusion that bankers' remuneration was one of the main causes of the 2008 financial crisis. In 2009 the Financial Stability Forum (FSF) published a report that stated that "(m)ultiple surveys find that over 80 percent of market participants believe that compensation practices played a role in promoting the accumulation of risks that led to the 2008 crisis. Experts agree" (Financial Stability Forum 2009). Given the events of 2007 and of the following year, there is no doubt that excessive risk was accumulated, but is it exclusively the fault of bankers that they 'accumulated risk' if it was the case that their remuneration incentives were

© 2015 John Wiley & Sons Ltd

structured to do exactly that? It is clearly important to try to understand whether it was shareholders who took advantage of everyone else, in other words was remuneration set by shareholders to achieve selfish interests, despite the risk to the wider economy, or was it a manifestation of rent seeking and dominance of managers? Furthermore, if it is true that remuneration structures induced risk-taking, which parts of remuneration were most toxic for stakeholders' interests?

The question of whether executive remuneration practices are the effect or cause of agency problems has long been debated in the literature. The case of the banking industry refreshes the debate but does not deliver a clear answer. What we know is that executive remuneration in the banking industry grew enormously in recent decades. Suntheim (2010) reports that between 1997 and 2007 the average remuneration of CEOs grew from $2.3 m to nearly $5.4 m. The averaging was taken over 74 banks from 18 countries. However, this 230 percent growth over the 10 years is easily overshadowed by the growth of CEO pay in general. According to *Forbes*, the average annual compensation of CEOs of the top 500 companies was $5.8 m in 1997 and the equivalent statistic calculated for CEOs of top 800 companies was $16.6 m in 2007 (Forbes 2011). This means that the growth of the average US CEO remuneration was over 280 percent. Furthermore, Adams (2012) finds that, after controlling for size, the level of CEO pay prior to the financial crisis was lower in financial firms than in non-financial firms. Interestingly, she also documents that after controlling for size the proportion of equity-linked compensation was lower in financial firms than in non-financial firms prior to the financial crisis. This finding seems to suggest that shareholders of non-financial institutions aligned more their CEOs with their preferences than shareholders of financial institutions. Given that it is common to assume that CEOs are more risk averse than shareholders (e.g., because their wealth may be less diversified) and would prefer less rather than more equity-linked compensation, the finding may suggest that the scope for rent seeking by executives in financial institutions was higher than in non-financial institutions. However, the lower alignment of banking CEOs' remuneration packages indicates that, compared with other sectors, risk-taking remuneration-related incentives were potentially lower in the financial than in non-financial institutions. This does not mean that in total risk-taking incentives were lower. Bebchuk, Cohen, & Spamann (2010) argue that the structure of compensation in the top US financial institutions was particularly toxic when combined with the high levered capital structure of the financial institutions. DeYoung, Peng, & Yan (2013) show that following deregulation of the banking industry in the US, contractual risk-taking incentives for CEOs increased through the 2000s and that CEOs responded positively to these incentives. They document that this increase in risk-taking was particularly strong for the larger banks who were "best able to take advantage of these opportunities". Moreover, Fahlenbrach & Stulz (2011) find that the pre-crisis alignment of US CEOs' incentives with those of shareholders was positively associated with the subsequent bad performance of banks during the financial crisis. Beltratti & Stulz (2012) reinforce this conclusion using a sample of 32 countries. They find that the more "shareholder-friendly" boards were, the worse was the performance of banks during the first stages of the financial crisis. This evidence strengthens the argument that the alignment of incentives of shareholders and management has negative connotations. This also provides some evidence that, even though CEOs and top management may have had a significant role in adopting undue levels of risk-taking, shareholders' contribution to the process should not be underestimated.

When it comes to risk-taking, it is also important to bear in mind that risk-taking in the banking sector is not restricted to CEOs and executives who set business strategies. Even though, it is common for empirical studies to focus on the alignment of CEOs' incentives with those of shareholders, in practice, risk-taking is part of the daily operations of bankers at many levels of the hierarchy. Decisions made by single, low-rank individuals can bring banks to their knees. Stories of Howie Hubble of Morgan Stanley, or Jérôme Kerviel of Société Générale are well-publicized examples of reckless risk-taking by rogue traders, but the public eye seems to overlook the fact that many decisions (e.g., to provide mortgages to low-income borrowers without any assurance of repayment; e.g., Agarwal, Amromin, Ben-David, Chomsisengphet & Evanoff 2014) have been made at a much lower level, and that bank employees well below executive board level had incentives to exceed sound risk levels. This part of the alignment of the incentives of banking staff with the maximization of shareholder value is not properly addressed in the traditional literature even though regulators devote lots of attention to the issue (e.g., Bank of England's directives, European Central Bank's directives).

Bannier, Feess, & Packham (2013) study whether the competitive nature of the market for talent is related to risk-taking and, in particular, whether a bonus culture leads to excessive risk-taking. They construct a model in which bonuses introduced to separate high-ability from low-ability workers lead to excessive risk-taking which "does not only reduce social welfare but also reduces the bank's own profits". Therefore, they argue in favor of reduction of banking bonuses although point out that "any regulatory restrictions on compensation schemes would have to account for a multitude of different factors" which are not present in their theoretical model. Indeed, Thanassoulis (2012) points out that preventing any bonuses, i.e., "forcing banks to issue fix wages" increases the risks that banks must bear and can increase default risk. Murphy (2013) discusses pre-crisis banking bonus practices in the US and EU countries and presents a study of the regulation's "unintended consequences". He argues that the EU regulation to cap bankers' bonuses (Capital Requirement Directive 2013) will not resolve the growing level of remuneration, excess risk taking, and low performance. As Murphy (2013) documents, the ratio of variable-to-fixed compensation in leading EU banks before, during, and after the financial crisis was about ten-fold lower than the ratio observed for US banks, yet the scale of the banking crisis in numerous EU countries was comparable, if not greater, than the scale of the banking problems in the US. It is interesting to note that in spite of the imposition of a tight cap on executive bonuses, recent stress tests still showed substantial weakness of the banking sector across the EU (e.g., Treanor 2014). It should probably be taken as a positive sign that regulators and politicians have not responded to it with another wave of remuneration tightening policies. It is hard to speculate what is going

© 2015 John Wiley & Sons Ltd

wrong in restructuring of the banking industry but the fact that the French banks are weakest in Europe (Braithwaite 2014), while France did not experience a fully blown systemic banking crisis (Laeven & Valencia 2013) nor had particularly inflated executive remuneration (Murphy 2013) suggests that the reforms that have been undertaken may not be particularly effective.

REGULATING BANKERS' REMUNERATION

This section, initially covers the small but growing literature on the issue, and then discusses current developments in the regulation of bankers' remuneration.

The Academic Literature

A central focus of the literature is how to deal with excessive risk taking potentially induced by remuneration structures compatible with shareholder preferences. Edmans and Liu (2010) argue that tying the remuneration of CEOs to internal debt would reduce risk-taking incentives. They argue that pension plans are a natural form of exposing CEOs to "unsecured, unfunded obligations which, in nearly all cases, have priority with other creditors in bankruptcy," so they are a good tool to address stockholder-bondholder conflict. However, this may carry less applicability to banks that are too big to fail and, therefore, have little risk of bankruptcy. Bolton, Mehran & Shapiro (2015) further develop the idea of linking CEOs' remuneration to debt. They argue that the CEO's remuneration should be tied to the bank's credit default swaps. They also bring to the debate an important observation. They conclude that "shareholders may not be able to commit to design compensation contracts in this way."

This point is further enhanced by De Angelis & Ginstein (2014). They show that US firms structure CEO compensation packages to tie performance-based rewards to what is relevant for firms. In particular, growth firms tie CEO pay-performance metrics to stock market performance as accounting performance measures are less informative about long-term growth opportunities. This is yet another argument against allowing shareholders to structure bankers' remuneration. If the long-term growth of the banking industry is to be secured, allowing shareholders to link executive remuneration to stock market performance is not a good way forward. This point is further enhanced by the literature on shareholder activism. There is a strong evidence that shareholders are effective in promoting their own interests (Correa & Lel 2013; Cuñat, Giné, & Guadalupe, 2015; Illiev & Vitanova 2015; Stathopoulos & Voulgaris 2015).

Wei & Yermack (2011) show that equity (bond) prices rise (fall) when investors learn that CEOs of these companies have a relatively large exposure to the "inside debt" (via defined benefit pensions and deferred remuneration). Once more, this indicates that as much as debt-linked compensation may be beneficial, shareholders may have strong objections to introduce them. However, passing decision making to stakeholders is not a good alternative either. Illueca, Norden, & Udell (2014) study linkages between governance and deregulation on the risk-taking of Spanish savings banks. They find that following deregulation, savings banks that were subject to higher political influence lent money to firms with higher default risk, which consequently resulted in higher loan defaults. Although their research design is predominantly focused on documenting the negative impact of politicians on government-owned or -controlled banks, it sheds some light on governance issues and the effect of applying non-value-maximizing objectives. This adds to our argument that a third party is needed to negotiate strategic objectives of banks between shareholders and governments representing stakeholders.

Regulatory Developments

The Credit Crunch of 2007 has brought bankers' remuneration into the spotlight. Even though it was not the first time that the banking sector has been in turmoil, it was the first time that regulatory changes had been so broadly and internationally discussed, agreed, and implemented. Reforms of the banking sector, corporate governance law and practices, and (of most interest for this paper) bankers' remuneration were introduced in countries that suffered from major systemic banking crisis (e.g., the US and the UK), moderate systemic crisis (e.g., France, Switzerland, Italy) and those that did not experience a systemic banking crisis (e.g., Australia and Canada) (classification according to Laeven & Valencia 2013). It is beyond the scope of this article to discuss regulatory changes introduced in all countries, hence the focus will be on the US and the EU. The US is of interest because for decades it has been the country where most attention has been paid to executive remuneration. In EU countries, on the other hand, remuneration has not been perceived as such an important factor, and there have been fundamental differences between member states in the role and power of executive remuneration.[6]

As already discussed, executive remuneration holds a well-established position as a corporate governance mechanism in the US and attracts lots of public attention (e.g., Andersen 2002; Nocera 2009). Kuhnen & Niessen (2012) study the impact of public outrage on the remuneration paid to top executives in the period 1992–2008 and find that although the composition of remuneration changed (the proportion of salary increased while the proportion of option pay declined), there was no statistically significant impact on the size of remuneration paid. This suggests that some "external" intervention might be needed.

Given that the compensation packages of senior executive officers (SEOs), notably their size and direct link to short-term performance, have been perceived as one of the crucial factors in bringing the banking sector to the precipice, numerous policies that followed the Credit Crunch of 2007 have focused on restricting remuneration of SEOs. The Troubled Asset Relief Program (TARP), signed off by President George W. Bush in October 2008, clearly specified that recipients of financial support provided by TARP must establish (if they had none prior to entering TARP) and maintain a compensation committee during the remainder of the TARP period (Code for Federal Regulation 2008). Those compensation committees had multiple tasks relating to the form and size of remuneration offered and paid to SEOs and other employee compensation plans. For instance, a compensation committee was requested to "discuss, evaluate, and review at least every six months, with the TARP recipient's senior risk officers, the SEO

© 2015 John Wiley & Sons Ltd

compensation plans to ensure that the SEO compensation plans do not encourage SEOs to take unnecessary and excessive risks that threaten the value of the TARP recipient," and that they "do not encourage behavior focused on short-term results rather than long-term value creation, the risks posed by employee compensation plans and how these risks were limited, including how these employee compensation plans do not encourage behavior focused on short-term results rather than long-term value creation" (Code for Federal Regulation 2008).

Following on from the initial responses to the crisis, the regulatory intervention was further enhanced by the Dodd-Frank Act (DFA) of 2010 which applied to all listed companies and required that, in addition to information about the remuneration of executive directors and the assessment of performance justifying the financial rewards, companies will also disclose the median annual total compensation of all employees and the ratio of this median to the total compensation of the CEO. It also required companies to disclose whether any directors or employees were permitted to purchase financial instruments designed to hedge or offset potential decline in the value of the company's securities that were held by them as part of their compensation.

The DFA required that the federal agencies regulating financial institutions (including the Federal Reserve, and the SEC) jointly adopt rules addressing remuneration practices. In 2010, the Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation adopted guidance for banks under their supervision, and in 2011, together with the National Credit Union Association, the Federal Housing Finance Agency, and the SEC, they proposed rules on incentive compensation. The rules were of a rather generic nature. For instance, with regard to the balance between fixed and variable remuneration components, the proposal states that "incentive-based remuneration arrangements … should balance risk and financial rewards in a manner that does not provide covered persons with incentives to take inappropriate risks that could lead to material financial loss at the covered financial institution." Whether the remuneration schemes that were adopted were appropriate would be assessed by the agencies proposing the rule. In particular, an incentive-based compensation package would be approved as being "balanced when the amounts paid to a covered person appropriately take into account the risks, as well as the financial benefits, from the covered person's activities and the impact of those activities on the covered financial institution" (Securities and Exchange Commission, 2011). However, the work on such policies has been slow and no rules have been adopted so far.

The DFA also empowered shareholders to have a "say on pay" of executive directors named in annual proxy statements. This is a non-binding vote that can be cast at least once every three years. Companies are required to hold a "frequency" shareholder vote no less than once every six years on whether the shareholder vote on 'say on pay' should be every year, two years, or three years. Although, these are non-binding votes, the potential role of shareholders in setting bankers' remuneration is stronger than it was before the financial crisis. This is a potential ignition point for further problems given all the evidence on the negative effects of shareholders' influence on remuneration incentives for top bankers.

Outside the US the view that compensation practices at large financial institutions were a leading cause of the financial crisis was also widely held. In 2009 the Financial Stability Forum (FSF) published a report advising on prudential remuneration practices. It postulated that "compensation must be adjusted for risk" and that "compensation outcomes must be symmetric with risk outcomes" (Financial Stability Forum 2009). Moreover, it should be disclosed in a "clear, comprehensive and timely" manner to "facilitate constructive engagement with shareholders" (Financial Stability Forum 2009). In April 2009 at the London Summit of the G20, the leaders agreed "to endorse and implement the FSF's tough new principles on pay and compensation" (G20 London Summit 2009). In September 2009 at the G20 Summit in Pittsburgh, heads of 19 countries and the Presidents of the EC and of the European Council agreed to the proposal put forward by the Financial Stability Board, the successor of the FSF, to "regulate compensation practices to support financial stability" (G20 Pittsburgh Summit 2009). In particular, they requested financial firms to immediately limit "variable compensation as a percentage of total net revenues when it is inconsistent with the maintenance of a sound capital base," restrain from granting multi-year guaranteed bonuses, and defer, tie to performance, impose appropriate claw-back, and vest in the form of stock or stock-like instruments a significant part of variable compensation, as long as these create incentives aligned with long-term value creation and the time horizon of risk. They also called for "making firms' compensation policies and structures transparent through disclosure requirements." The following summits did not directly regulate the SEO compensation, but the debate on its form and size did not cease.

Over the next few years the EU moved from "'pay governance' to pay design" (Dijkhuizen 2014). The Capital Requirement Directive (CRD III) published in 2010 contained clear requirements on how much of variable pay should be equity-linked and how much deferrable, as well as the length of the deferral period. These directives were not for CEOs or executives only but applied to "categories of staff whose professional activities have a material impact on their risk profile, remuneration policies and practices that are consistent with effective risk management" (Capital Requirement Directive 2010). These are commonly known as material risk takers (MRTs).

The concept of MRTs is not uniform and the details vary from country to country (in some it is restricted to the banking sector, while others expand it to the whole financial sector), yet there are some important commonalities. MRTs are not just CEOs and members of the executive board, but also employees responsible for control functions, risk takers, that is, those who have a material impact on the risk profile and financial soundness (e.g., propriety traders, dealers, loan officers, risk managers), as well as those whose total remuneration is comparable to the top managers, executives, and risk takers.

The desire to structure the remuneration of MRTs such that it is risk sensitive and aligned with the long-term incentives of their institutions is at the center of the regulatory debate. It is common that these new regulations include deferral and 'claw-back' policies but there are substantial differences across countries in the details of these policies. In Sweden, for instance, there is relatively little intervention in individual institutions' policies. It is the board of directors that decides about

© 2015 John Wiley & Sons Ltd

remuneration policies, and it is left to the board of directors of individual institutions to decide how much fixed and performance-based remuneration should be paid, although it is expected that boards set appropriate maximum ratios of variable to fixed pay. In the case of MRTs, variable remuneration must be based on profit (not revenue/turnover) and adjusted for "all types of current and potential risk" (Ashurst 2012). However, for firms with more than SEK500bn ($60bn) on the balance sheet date for the previous financial year, at least 50 percent of the variable remuneration of senior management must be in non-cash form. In France, variable remuneration must represent a material part of the total remuneration, and at least 40 or 60 percent of it (depending on level of remuneration) must be performance-based that is assessed on an individual and collective basis. If losses occur, the deferred part of the variable remuneration must be reduced or not paid. In contrast, in Germany there is no provision in respect to equity-linked remuneration over and above the recommendation that fixed and variable pay should be determined on a proportionate basis (Ashurst 2012). There are also big changes in the EU with regard to when and what proportion of remuneration can be paid. Even though the details of deferrals differ, it is common that the deferral period is between three and five years.

The policies adopted by the UK are interesting given that the UK has a system that to some extent resembles that of the US (a stock market-oriented financial system with a strong presence of commercial banks) but, on the other hand, it is part of the EU system and has to comply with regulations set by the EU. In general, the approach of the UK regulators (the Financial Services Authority (FSA) until 2013, replaced by the Financial Conduct Authority and the Prudential Regulation Authority) has been more efficient in passing and implementing new regulations than the American counterparts. In January 2010 the Remuneration Code became operational and covered the 26 largest banks, building societies, and big broker dealers. By January 2011 the Remuneration Code was revised and extended to over 2,000 financial institutions (i.e,, all banks, building societies, and investment firms under the Capital Adequacy Directive).

The European Parliament took a stand that requirements adopted by individual member states were insufficient and after lengthy public debate and with top politicians expressing their support for the public discontent with the size of bonuses paid, or to be paid, to senior executive officers of banks which received financial support and governmental guarantees, in June 2013 the European Council of Ministers approved the fourth Capital Requirement Directive (Capital Requirement Directive 2013) which regulates bankers' variable pay.[7] In particular, it specifies that "the variable component shall not exceed 100% of the fixed component of the total remuneration for each individual" (Article 94 g(i), Capital Requirement Directive 2013). Tougher or lighter restrictions could be imposed by individual member states, but the upper limit of the variable component had not to exceed 200 percent (Article 94 g(ii), Capital Requirement Directive 2013) unless approved through a specific EU procedure.

So far there is rather limited evidence of the success of this requirement. But press reports seem to support some of the concerns expressed by Murphy (2013) (e.g., Schäfer 2014; Vander Weyer 2014).

ISSUES ARISING FROM CURRENT REGULATORY CHANGES

Setting internationally agreed risk requirements and standards for the banking industry has a long tradition, yet in recent years there have been big changes in the issues that are being addressed. Setting standards for corporate governance of individual institutions and, in particular, for remuneration incentives at a bank level is a new phenomenon. It reflects the recognition that remuneration incentives need to be coordinated with the other risk-taking mechanisms and standards. It also reflects the view that it may be beneficial to perceive the corporate governance of banks as a national, or even international, phenomenon rather than an individual bank issue. Although it is now recognized that regulation of remuneration should have a cross-border character if risk-taking by banks is to be controlled, it is not clear that all the changes that have been imposed on remuneration practices, or are under consideration, are potentially positive.[8]

The difficulties with finding the appropriate breadth and depth of regulatory intervention at an international level should not be ignored, however. Given cross-country differences in corporate governance architecture and in the role and form of pre-crisis remuneration practices, it is not clear how, and indeed whether, the cross-country alignment of remuneration practices can be achieved without, in some cases, fundament changes to the national governance structure, culture, practices, etc. Given that the role of shareholders in setting remuneration incentives should be reduced (not increased through 'say-on-pay'), and the focus on shareholder value maximization needs to be dampened, a new paradigm of coexistence of corporate governance and regulation needs to be found. Setting remuneration to lower risk-taking and, hence, potentially lowering expected short-term returns, may not to be consistent with shareholders' wishes. It will then be left to regulators to oversee solutions that will balance shareholders' short-term desires with the long-term interests of the banking sector. "Rationally" speaking, shareholders are also taxpayers and ordinary citizens who, if banks go bust and a financial crisis strikes, may lose their jobs and a significant part of their life savings.

It is also important to recognize that the regulatory intervention will require the development of new metrics of good corporate governance practices for boards. Hence, as the enhanced power of the regulatory agencies emerges and infiltrates into decision making throughout banks, it is important to understand what corporate governance characteristics might be considered as good in this context and how they can be implemented. More research in this direction is necessary.

The current regulation goes far beyond controlling the remuneration of the CEO and at boardroom level. This contrasts with the academic literature which has predominantly focused on the top executives. The importance of individual MRTs in the currently developing regulatory regimes is captured both by specifying MRTs' remuneration structures and by making individual MRTs' remuneration dependent on collective performance. However, care needs to be taken to ensure that this fits well into the overall regulatory framework rather than overzealously dealing with the problem. For example, the regulation of MRT remuneration is only one part of the regulatory structure that is designed to reduce the risks

© 2015 John Wiley & Sons Ltd

arising from MRT actions. The Basel II and III framework has three pillars. Pillar 1 sets minimum capital requirements for banks, Pillar 2 sets specific requirements following supervision of banks on an individual basis, and Pillar 3 mandates disclosure. If supervisors of a bank feel that an MRT is following an overly risky strategy, then the bank will be required to hold what is called a Pillar 2 add-on, i.e., bank-specific extra capital requirement to offset the risk of the activity. Although the bank as a whole will be holding the additional capital required, the additional capital is solely driven by the specific activity that is worrying the supervisors. Therefore, one can make a case that the same problem is being regulated twice, hence it is essential that the two approaches are dealt with in tandem.

The remuneration structure is set to dampen incentives for MRTs to adopt risky strategies and the Pillar 2 add-ons are also designed to reduce the risk. Since the remuneration rules are applied to all MRTs in a jurisdiction whereas the Pillar 2 add-on is based on a specific action in a specific bank, one could argue that factoring in the role of the Pillar 2 add-on, as opposed to setting the two forms of regulation independently, is the proportionate response. It would be helpful to know much more about this interaction and it ought to be a focus of future research. Indeed, this is an example of a broader concern, namely how does the regulation of remuneration interact with the new regulatory framework. Whereas the interaction of other tools in the banking regulation "toolkit" (e.g., capital, liquidity, resolution, etc.) seems to be analyzed and is a constant source of discussion, the precise interaction of the regulation of remuneration with the broader framework is far less clear.

Another issue is related to remuneration deferrals. Making managers accountable appears to be a desirable outcome, yet even if one wishes to tie the manager to long-term projects, it is impossible to postpone the payment of remuneration until the project is completed. Managers will have to be paid periodically before the long-term project ends to secure their personal consumption. However, allowing for intermediate payments brings moral hazard back to the game as a manager's incentives to work hard get diluted, especially if the job market is liquid and the manager can move job before the current project is completed (and full information about the performance is revealed). Even if in real-life situations deferring remuneration does not eliminate moral hazard, some deferral of remuneration seems a sensible component of regulation of remuneration. In current recommendations, deferrals of remuneration are commonly imposed for a period of three to five years, which in light of the above discussion of Pillar 2 add-on may be excessive.

The above discussion and the regulatory changes themselves have been focused on individuals, i.e., CEOs, top executives, MRTs. However, remuneration of boards and teams is a complex issue that also needs attention. The classic governance literature is built on the idea of a tournament, which is associated with rivalry and, therefore, risk-taking. As regulators try to reduce risk-taking, and relate remuneration of individuals to team performance, it is important to understand what the optimal remuneration structures for bankers as teams would be. Zalewska (2014b) shows that, for non-financial firms, big disparities in remuneration can be negatively associated with performance and suggests that these effects may be country-dependent. This may also be true in banking; big disparities in remuneration may be harmful to team spirit and joint responsibility in some countries.

As has been indicated in this paper, the asymmetries of information between the parties that create the scope for excessive risk-taking and short-term gains are not unique to banking, although the scale and precise interactions between the parties may be. There is a large literature discussing and documenting how relational contracts between employees and senior management, and between contracting companies, can mitigate many of the asymmetries, incompleteness of contracts, and incentives to seize short-term gains at the expense of long-term relationships. The ideas and examples appear in a broad sphere of academic study – across management, organizational science, sociology, anthropology, political science, and economics. Unfortunately, there is no universally accepted definition of a relational contract, but loosely, parties have a relational contract when many of the relevant events affecting long-term interactions cannot be defined in advance and the parties fill this gap by building a relationship of trust, and resolve the matters when they arise rather than attempt to specify as much as possible in the contract or protect themselves by underinvesting in the relationship. To some extent stewardship, stakeholder, and network theories echo some of these notions. Relational contracts can be very effective and self-fulfilling but are hard to establish, particularly in an environment where parties have been prone to taking a short-term view (e.g., Gibbons & Henderson, 2012, who suggest that relational contracts are probably the best explanation for persistent differences in performance between firms that display little sign of convergence).

Anecdotally, there seems little evidence of relational contracts in banking, yet the benefits could be enormous given the problems that arise from short-term decision making. This raises the question whether there is scope for such contracts or is there something about banking that creates a poor environment for the development of relational contracting. The analysis presented in the paper suggests that the latter is most likely to be the case. Relational contracts require parties to have low discount rates so that they are willing to value the long-term benefits of a relationship (be it between bank and customer or between counterparties) over the short-term gains that can be achieved by taking advantage of current circumstances. The complex interconnectivity of the banking system means that a relationship between counterparties can be disrupted by the actions of, and/or shocks to, others in the financial community. This reduces the stability of any relationship and hence tends to place a bias for short-term gains over long-term relationships compared to many other sectors. Furthermore, as we have emphasized endlessly, the banking model is based around balancing risks and has an inherent risk structure at its heart (Diamond & Dybvig 1983). Although not absolutely essential, in general, those that are comfortable operating in risky environments are less likely to have discount rates as low as those working in inherently safer environments. Hence the individuals in the industry are probably not best placed to focus on relational contractual structures.

Finally, as a note of caution, it is important to point out that regulation of banks and regulation of remuneration will not be a perfect solution to all the problems. For example, Besley &

© 2015 John Wiley & Sons Ltd

Ghatak (2013) point out that "it seems improbable to believe that the financial sector can be regulated to completely remove excess risk taking" and suggest that specific bonus taxation can be beneficial (albeit in a world where the regulation of financial enterprises that they consider does not have any specific regulation of remuneration). Dittmann, Maug & Zhang (2011) warn against the unintended consequences of remuneration restrictions. They suggest that if restricting (ex-post) total pay is associated with lower risk-taking incentives, it will increase the level of total pay and give higher relative rewards for mediocre performance. They also point out that restricting ex-ante remuneration weakens the bargaining power of a firm in attracting talented and hard-working CEOs.

CONCLUSIONS AND IMPLICATIONS

This paper provides a new look at the banking sector's remuneration issues and regulation. It focuses on recent regulatory attempts to regulate remuneration in order to reduce risk taking, and issues arising from these regulatory changes. Given the specifics of the banking sector and, in particular, its exceptionally large asymmetries of information, interconnectivity and systemic risk, the paper argues that the traditional approach to remuneration as a solution to the agency type I conflict, i.e., the principal-agent conflict, is inadequate. The paper argues that in the case of the banking sector, remuneration may be a source of type III agency conflict, i.e., the conflict between shareholders and other stakeholders, and as such cannot be left in the hands of shareholders or even financial institution-related stakeholders (e.g., employees). The paper also provides theoretical arguments why other institutional relationships (e.g., relational contracting) fail in the banking sector. Therefore, the paper argues that regulation of remuneration is unavoidable to ensure that both the short-term industry performance and the long-term economic interests of society are balanced. In short, regulators have an overview of the banking sector as a whole, and are already in charge of setting safety and soundness rules (including risk-taking restrictions). To ensure a consistent and holistic approach to these policies, regulators should also be actively involved in determining remuneration as remuneration ought to be perceived as part of a broader agenda of monitoring and restricting banks' risk taking. This, however, impacts on the position of boards (both unitary and dual) and their role in setting strategic objectives, calling for the development of a new paradigm of corporate governance suitable for the banking sector. Given the global nature of interconnections in the banking industry and the current cross-country differences in corporate governance architecture (and in the role and form of pre-crisis remuneration practices), fundamental changes to national governance structures, cultures, practices, etc., need to be acknowledged and addressed.

Numerous regulatory steps have been taken in recent years to strengthen the banking sector in individual countries and regions. Not all these regulatory changes can, however, be fully supported by the current state of research. Indeed, some of the new policies can be perceived as controversial and seem more like "knee-jerk" reactions driven by political desire to calm an agitated public rather than rational and well-informed decisions. Increasing shareholders' say-on-pay rights and stringent caps on executive bonuses are examples of regulatory changes that may not necessarily strengthen the banking sector. The sheer scale and complexity of the reforms further add to the need for more research on the subject.

ACKNOWLEDGEMENTS

I would like to thank the Editor, Professor Praveen Kumar, Associate Editor, Professor Chris Florackis, and two anonymous reviewers for their useful comments and suggestions. I would also like to thank Professor Paul Grout for helpful comments.

NOTES

1. The remuneration disclosure requirements have not changed in a linear way over time, e.g., there have been periods of higher and lower disclosure. See Dew-Becker (2009) for details.
2. It is important to note that a conflict between shareholders and stakeholders (commonly referred to as type III conflict in corporate governance literature) can emerge even when there is no separation of ownership and control (type I conflict). For as long as an owner, or owners, of a bank are disjoined with stakeholders (e.g., society, taxpayers) and, therefore, do not represent the interests of stakeholders, there is an externality that forms the core of this analysis. One could speculate that if a bank was state owned and the state represented the interests of the society, then the conflict would not exist. However, this argument is not correct either as there is numerous evidence that state ownership is not optimal (e.g., Cornett, Guo, Khaksari & Tehranian 2010).
3. These statistics are based on the author's own calculations using WB statistics of stock market capitalisation to GDP ratios and banking sector capitalisation to stock market capitalisation calculated using statistics provided by DataStream.
4. For instance, the Government Accountability Office's estimates show that the cost of the 2008 financial crisis to the US economy reached $22trillion ('GAO report: Financial crisis cost $22 trillion', *Bank Credit News*, 18 February 2013. Available at http://bankcreditnews.com/news/gao-report-financial-crisis-cost-22-trillion/ (accessed December 6, 2015).
5. In this section shareholders are the focus but it should be kept in mind that in many countries that experienced systemic banking crisis (e.g., Germany, Finland, the Netherlands) there are dual boards. Therefore, it can be expected that some stakeholders were also involved in setting strategies, risk-taking and remuneration.
6. In many countries around the world the role of the executive remuneration receives limited emphasis.
7. 'Say on pay' is not a novelty in the EU. In many EU countries 'say on pay' is part of the established governance routine. In some countries it is binding (e.g., Sweden, Norway), in some just advisory (e.g., the UK).
8. It is documented that regulators can be particularly tough when representing public interests (Garside, Grout & Zalewska 2014; Grout, Jenkins & Zalewska 2014). However, even if the public support a tough stance, it does not necessarily mean that this has economic justification (Masciandaro & Passarelli 2013).

REFERENCES

Adams, R. 2012. Governance and the financial crisis, ***International Review of Finance***, 12: 7–38.

Agarwal, S., Amromin, G., Ben-David, I., Chomsisengphet, S., & Evanoff, D. D. 2014. Predatory lending and the subprime crisis, ***Journal of Financial Economics***, 113: 29–52.

© 2015 John Wiley & Sons Ltd

Allen, F., Carletti, E., & Marquez, R. 2014. Deposits and bank capital structure. Working Paper. Available at http://fic.wharton.upenn.edu/fic/papers/14/14-08.pdf (accessed November 23, 2015).

Andersen, K. 2002. City of shame. The New York Times, 6 October. Available at https://global.nytimes.com/2002/10/06/magazine/06BLAME.html?pagewanted=print&position=top (accessed December 6, 2015).

Ashurst. 2012. Remuneration in the financial services industry: A global view 2012. London: Ashurst LLP.

Balafas, N. & Florackis, C. 2014. CEO compensation and future shareholder returns: Evidence from the London Stock Exchange, ***Journal of Empirical Finance***, 27: 97–115.

Bannier, C. E., Feess, E., & Packham, N. 2013. Competition, bonuses, and risk-taking in the banking industry, ***Review of Finance***, 17: 653–690.

Bebchuk, L. A., Cohen, A., & Spamann, H. 2010. The wages of failure: Executive compensation at Bear Stearns and Lehman 2000–2008, ***Yale Journal on Regulation***, 27: 257–282.

Bebchuk, L. A. & Fried, J. 2003. Executive compensation as an agency problem, ***Journal of Economic Perspectives***, 17: 71–92.

Bebchuk, L. A. & Fried, J. 2004. ***Pay without performance***. Cambridge, MA: Harvard University Press.

Bebchuk, L. A. & Spamann, H. 2010. Regulating bankers' pay, ***Georgetown Law Journal***, 98: 247–287.

Beltratti, A. & Stulz, R. M. 2012. The credit crisis around the globe: Why did some banks perform better?, ***Journal of Financial Economics***, 105: 1–17.

Besley, T. & Ghatak, M. 2013. Bailouts and the optimal taxation of bonus pay, ***American Economic Review: Papers & Proceedings***, 103: 163–167.

Boeri, T., Lucifora, C., & Murphy, K. 2013. ***Executive remuneration and employee performance-related pay***. Oxford: Oxford University Press.

Bolton, P., Mehran, H., & Shapiro, J. 2015. Executive compensation and risk taking, ***Review of Finance***, 19: 2139–2181.

Braithwaite, T. 2014. Alternative stress tests find French banks are weakest in Europe. Financial Times, 27 October. Available at http://www.ft.com/cms/s/0/fad2c772-5dd7-11e4-b7a2-00144feabdc0.html#axzz3RuTY2pD1 (accessed December 6, 2015).

Buck, T., Shahrim, A., & Winter, S. 2004. Executive stock options in Germany: The diffusion or translation of the US-style corporate governance, ***Journal of Management and Governance***, 8: 173–186.

Capital Requirement Directive 2010/76/EU of the European Parliament and of the Council (CRD-III). 2010. ***Official Journal of the European Union*** L 329/3.

Capital Requirement Directive 2013/36/EU of the European Parliament and of the Council (CRD-IV). 2013. ***Official Journal of the European Union*** L 176/338.

Chance, D. M., Kumar, R., & Todd, R. B. 2000. The 'repricing' of executive stock options, ***Journal of Financial Economics***, 57: 129–154.

Code for Federal Regulation (CFR). 2008. §30.4 Q-4: What actions are necessary for a TARP recipient to comply with the standards established under sections 111(b)(3)(A), 111(b)(3)(E), 111(b)(3)(F) and 111(c) of EESA (evaluation of employee plans and potential to encourage excessive risk or manipulation of earnings)? Available at http://www.law.cornell.edu/cfr/text/31/30.4 (accessed November 23, 2015).

Conyon, M. J. & Murphy, K. J. 2000. The prince and the pauper? CEO pay in the United States and the United Kingdom, ***Economic Journal***, 110: F640–F671.

Core, J. E. & Guay, W. 2001. Stock option plans for non-executive employees, ***Journal of Financial Economics***, 61: 253–287.

Core, J. E., Guay, W., & Larcker, D. F. 2003. Executive equity compensation and incentives: A survey, ***Economic Policy Review***, 9: 27–50.

Core, J. E., Guay, W., & Thomas, R. S. 2005. Is US compensation inefficient pay without performance?, ***Michigan Law Review***, 103: 1142–1185.

Core, J. E., Holthausen, R. W., & Larcker, D. F. 1999. Corporate governance, chief executive officer compensation, and firm performance, ***Journal of Financial Economics***, 51: 371–406.

Core, J. E. & Larcker, D. F. 2002. Performance consequences of mandatory increases in executive stock ownership, ***Journal of Financial Economics***, 64: 317–340.

Cornett, M. M., Guo, L., Khaksari, S., & Tehranian, H. 2010. The impact of state ownership on performance differences in privately-owned versus state-owned banks: An international comparison, ***Journal of Financial Intermediation***, 19: 74–94.

Correa, R. & Lel, U. 2013. Say on pay laws, executive compensation, CEO pay slice, and firm value around the world. Board of Governors of the Federal Reserve System International Finance Discussion Papers No. 1084.

Cuñat, V., Giné, M., & Guadalupe, M. 2015. Say pays! Shareholder voice and firm performance, ***Review of Finance*** forthcoming. DOI: 10.1093/rof/rfv056.

De Angelis, D. & Ginstein, Y. 2014. Performance terms in CEO compensation contracts, ***Review of Finance***, 19: 619–651.

DeYoung, R., Peng, E. Y., & Yan, M. 2013. Executive compensation and business policy choices at US commercial banks, ***Journal of Financial and Quantitative Analysis***, 48: 165–196.

Dew-Becker, I. 2009. How much sunlight does it take to disinfect a boardroom? A short history of executive compensation regulation in America, ***CESifo Economic Studies***, 5: 434–457.

Diamond, D. 1984. Financial intermediation and delegated monitoring, ***Review of Economic Studies***, 51: 393–414.

Diamond, D. & Dybvig, P. 1983. Bank runs, deposit insurance, and liquidity, ***Journal of Political Economy***, 91: 401–419.

Dijkhuizen, T. 2014. The EU's regulatory approach to banks' executive pay: From "pay governance" to pay design, ***European Company Law***, 11: 30–37.

Dittmann, I., Maug, E., & Zhang, D. 2011. Restructuring CEO pay, ***Journal of Corporate Finance***, 17: 1200–1220.

Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA). 2010. Public Law 111-203. Washington, DC: US Government Publishing Office.

Dow, J. & Raposo, C. C. 2005. CEO compensation, change, and corporate strategy, ***The Journal of Finance***, 60: 2701–2727.

Edmans, A. & Liu, Q. 2010. Inside debt, ***Review of Finance***, 15: 75–102.

Fahlenbrach, R. & Stulz, R. M. 2011. Bank CEO incentives and the credit crisis, ***Journal of Financial Economics***, 99: 11–26.

Fernandes, N., Ferreira, M., Matos, P., & Murphy, K. J. 2013. Are US CEOs paid more? New international evidence, ***Review of Financial Studies***, 26: 323–367.

Financial Stability Forum (FSF). 2009. FSF principles for sound compensation practices. Available at http://www.financialstabilityboard.org/publications/r_0904b.pdf (accessed November 23, 2015).

Forbes. 2011. Historical chart: Two decades of CEO pay. Available at http://www.forbes.com/lists/2011/12/ceo-pay-20-year-historical-chart.html (accessed December 6, 2015).

Frydman, C. & Jenter, D. 2010. CEO compensation, ***Annual Review of Financial Economics***, 2: 75–102.

G20 London Summit. 2009. London Summit – Leaders' statement. Available at https://www.imf.org/external/np/sec/pr/2009/pdf/g20_040209.pdf (accessed November 23, 2015).

G20 Pittsburgh Summit. 2009. Leaders' statement: The Pittsburgh Summit 2009. Available at https://g20.org/wp-content/uploads/2014/12/Pittsburgh_Declaration_0.pdf (accessed November 23, 2015).

Garside, L., Grout, P. A., & Zalewska, A. 2014. Does experience make you "tougher"? Evidence from competition law, ***Economic Journal***, 123: 474–490.

Gibbons, R. & Henderson, R. 2012. Relational contracts and organizational capabilities, ***Organization Science***, 23: 1350–1364.

© 2015 John Wiley & Sons Ltd

Grout, P. A., Jenkins, A., & Zalewska, A. 2014. Regulatory valuation of public utilities: A case study of the twentieth century, ***Business History***, 56: 936–955.
Hall, B. & Murphy, K. 2003. The trouble with stock options, ***Journal of Economic Perspectives***, 17: 49–70.
Hayes, R. H. & Shaefer, S. 2009. CEO pay and the Lake Wobegon effect, ***Journal of Financial Economics***, 94: 280–290.
Hintz, J.-M. & Müller-Bloch, S. 2015. Market reactions to the regulation of executive compensation, ***European Accounting Review***, 24: 659–684.
Illiev, P. & Vitanova, S. 2015. The effect of the say-on-pay vote in the US. Available at http://www.rhsmith.umd.edu/files/IlievPeter.pdf (accessed November 23, 2015).
Illueca, M., Norden, L., & Udell, G. F. 2014. Liberalization and risk-taking: Evidence from government-controlled banks, ***Review of Finance***, 18: 1217–1257.
Kuhnen, C. M. & Niessen, A. 2012. Public opinion and executive compensation, ***Management Science***, 58: 1249–1272.
Laeven, L. & Valencia, F. 2013. ***Systemic banking crisis database***, vol. 61, : 225–270. IMF Economic Review.
Lie, E. 2005. On the timing of CEO stock option awards, ***Management Science***, 51: 802–812.
Liu, Z., Quiet, S., & Roth B. 2015. Banking sector interconnectedness: What is it, how can we measure it and why does it matter? ***Bank of England Quarterly Bulletin***, 55: 130–138.
Masciandaro, D. & Passarelli, F. 2013. Financial systemic risk: Taxation or regulation?, ***Journal of Banking & Finance***, 37: 587–596.
Morck, R., Shleifer, A., & Vishny, R. W. 1988. Management ownership and market valuation: An empirical analysis, ***Journal of Financial Economics***, 20: 293–315.
Murphy, K. J. 2011. The politics of pay: A legislative history of executive compensation. Marshall School of Business Working Paper FBE 01.11.
Murphy, K. J. 2013. Regulating banking bonuses in the European Union: A case study in unintended consequences, ***European Financial Management***, 19: 631–657.
Nocera, J. 2009. The problem with flogging A.I.G. The New York Times, 20 March. Available at http://www.nytimes.com/2009/03/21/business/21nocera.html?pagewanted=all (accessed December 6, 2015).
Ofek, E. & Yermack, D. 2000. Taking stock: Equity-based compensation and the evolution of managerial ownership, ***The Journal of Finance***, 55: 1367–1384.
Oyer, P. 2004. Why do firms use incentives that have no incentive effects?, ***The Journal of Finance***, 59: 1619–1649.
Park, Y. W., Nelson, T., & Huson, M. R. 2001. Executive pay and the disclosure environment: Canadian evidence, ***Journal of Financial Research***, 24: 347–365.
Practical Law. 2014. Executive remuneration: international comparison of required approvals and disclosure. Available at http://uk.practicallaw.com/9-522-6320?q=&qp=&qo=&qe= (accessed November 23, 2015).
Rajgopal, S., Shevlin, T., & Zamora, V. 2006. CEO's outside employment opportunities and the lack of relative performance evaluation in compensation contracts, ***The Journal of Finance***, 59: 1813–1844.
Rushe, D. 2015. BP set to pay the largest environmental fine in US history for Gulf oil spill. The Guardian, 2 July. Available at http://www.theguardian.com/environment/2015/jul/02/bp-will-pay-largest-environmental-fine-in-us-history-for-gulf-oil-spill (accessed December 6, 2015).
Schäfer, D. 2014. EU banks beat bonus cap with cash allowances. Financial Times, 20 July 2014. Available at http://www.ft.com/cms/s/0/4da46ef0-0e92-11e4-a1ae-00144feabdc0.html#axzz3tZRcsTPx (accessed December 6, 2015).
Securities and Exchange Commission (SEC). 2011. Incentive-based compensation arrangements. Available at www.sec.gov/spotlight/dodd-frank/956-proposedrule-draft.pdf (accessed November 23, 2015).
Stathopoulos, K. & Voulgaris, G. 2015. The importance of shareholder activism: The case for say-on-pay, ***Corporate Governance: An International Review***. DOI:10.1111/corg.12147.
Stiglitz, J. & Weiss, A. 1981. Credit rationing in markets with imperfect information, ***American Economic Review***, 71: 393–410.
Suntheim, F. 2010. Managerial compensation in the financial service industry. Available at https://www.cass.city.ac.uk/__data/assets/pdf_file/0018/41544/Suntheim.pdf (accessed November 23, 2015)
Thanassoulis, J. 2012. The case for intervening in bankers' pay, ***The Journal of Finance***, 67: 849–895.
Thomsen, S. & Conyon, M. 2012. ***Corporate governance: Mechanisms and systems***. New York: McGraw-Hill.
Treanor, J. 2014. Twenty-four European banks fail financial stress tests. ***The Guardian***, 26 October. Available at http://www.theguardian.com/business/2014/oct/26/european-banks-fail-financial-stress-tests (accessed December 6, 2015).
Vander Weyer, M. 2014. Over half of Europe's bankers bypass the EU bonus cap. ***Newsweek***, 24 October. Available at http://www.newsweek.com/2014/10/31/over-half-europes-bankers-bypass-eu-bonus-cap-279577.html (accessed December 6, 2015).
Wei, C. & Yermack, D. 2011. Investor reactions to CEOs' inside debt incentives, ***Review of Financial Studies***, 24: 3813–3840.
Zalewska, A. 2014a. Challenges of corporate governance: Twenty years after Cadbury, ten years after Sarbanes-Oxley Act, ***Journal of Empirical Finance***, 27: 1–9.
Zalewska, A. 2014b. Gentlemen do not talk about money: The case of British boards, ***Journal of Empirical Finance***, 27: 40–57.

Anna Zalewska is Professor of Finance and the Founding Director of the Centre for Governance and Regulation at the School of Management, University of Bath, UK. Given her background in both mathematics and economics (in 1998 she received a PhD in Mathematics at the Polish Academy of Sciences, Warsaw, and a PhD in Economics at the London Business School), her research covers a broad range of topics in financial economics. She publishes in corporate governance (remuneration and board issues), regulatory and stock market valuation of regulated companies, the pension industry (performance and impact on the development of financial markets), and emerging markets.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 334–345

Corporate Governance and Bank Risk-taking

Abhishek Srivastav* and Jens Hagendorff

ABSTRACT

Manuscript type: Review
Research Question/Issue: Bank governance has become the focus of a flurry of recent research and heated policy debates. However, the literature presents seemingly conflicting evidence on the implications of governance for bank risk-taking. The purpose of this paper is to review prior work and propose directions for future research on the role of governance on bank stability.
Research Findings/Insights: We highlight a number of key governance devices and how these shape bank risk-taking: the effectiveness of bank boards, the structure of CEO compensation, and the risk management systems and practices employed by banks.
Theoretical/Academic Implications: Prior work primarily views bank governance as a mechanism to protect the interests of bank shareholders only. However, given that taxpayer-funded guarantees protect a substantial share of banks' liabilities and that banks are highly leveraged, shareholder-focused governance may well subordinate the interests of other stakeholders and exacerbate risk-taking concerns in the banking industry. Our review highlights the need for internal governance mechanisms to mitigate such behavior by reflecting the needs of shareholders, creditors, and the taxpayer.
Practitioner/Policy Implications: Our review argues that the relationship between governance and risk is central from a financial stability perspective. Future research on issues highlighted in the review offer a footing for reforming bank governance to constrain potentially undesirable risk-taking by banks.

Keywords: Corporate Governance, Banks, Board of Directors, CEO Pay, Risk Management

INTRODUCTION

There has been considerable academic and regulatory interest in how to mitigate bank risk-taking behavior in recent years. Undue risk-taking by banks jeopardizes the safety and soundness of individual institutions as well as the stability of the entire financial sector when contagion causes risks to spill over to other financial institutions.

A case in point is the financial crisis that started in 2008. It is by now a widely held view that the vulnerability of the banking sector during the crisis was at least in part caused by a build-up of excessive risk by some banks before the crisis (Brunnermeier, 2009; DeYoung, Peng, & Yan, 2013). Further, there is significant discussion over the extent to which governance failures have contributed to the risk exposures of banks. In particular, there are questions over whether bank boards were unable to effectively monitor and control bank risk, whether executive pay was excessively structured to promote risk-taking, and whether banks' risk management systems were adequate (Bebchuk & Spamann, 2009; Kashyap, Rajan & Stein, 2008; Kirkpatrick, 2009).[1] The purpose of this paper is to focus on these issues by reviewing existing research on bank governance and risk with a view to formulate empirical questions for future research.

Our review is set against the background of recent regulatory reforms that have placed great emphasis on reforming governance in order to control bank risk-taking (Basel Committee on Banking Supervision, 2014; Federal Reserve, Office of the Comptroller of the Currency, Office of Thrift Supervision, Federal Deposit Insurance Corporation, 2010; Liikanen Report, 2012). To date, policymakers and regulators have focused on specific governance shortcomings. In the UK, the Walker Review (Walker, 2009) focused on making recommendations on board arrangements and the qualifications of board members as well as on the compensation arrangements of UK banks and financial firms. Similarly, the Netherlands has had a Banking Code in place since 2010 that contains guidelines on the make-up of bank boards, including the qualification and training of board members and their remuneration. Additionally, compensation guidelines for CEOs and other senior executives at large banks have raised the need for pay instruments to align managerial interests with ensuring bank stability (Federal Reserve et al., 2010).

However, Kashyap et al. (2008) argue that existing reforms tend to address only specific governance shortcomings, such as those related to pay or board composition, but do not address more fundamental governance flaws. Equally, Becht, Bolton, and Röell (2011) note that ongoing reforms tend to follow pre-crisis traditions, whereby governance mechanisms

*Address for correspondence: Abhishek Srivastav, University of Leeds, Maurice Keyworth Building, Leeds LS2 9JT, UK. Tel: +44 (0)11 3343 6321; E-mail: A.Srivastav@leeds.ac.uk

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12133

put shareholders firmly in control. This has resulted in considerable academic interest in identifying alternative approaches to reforming bank governance. For instance, the International Monetary Fund (2014) conducted a review of the extant literature on bank governance and assessed the impact of various governance measures on bank risk and performance. Specifically, the report argues that extant research has largely looked at the impact of governance on bank risk by looking at a select few governance mechanisms in isolation.

Further, Stulz (2015) argues that governance plays an important role in helping banks pursue an 'optimal' level of risk that allows managers to maximize shareholder value while also taking into account the social costs of bank failures. To achieve this objective, Stulz discusses the role of an effective risk management framework in identifying, measuring, and controlling bank risk exposures. Similarly, de Haan and Vlahu (2015) also review the corporate governance literature on banks, but their focus is primarily on the link between governance and bank performance (rather than governance and risk).

Our study builds upon the International Monetary Fund (2014) study and other existing work by taking a slightly different approach. We focus on reviewing the extant literature to identify 'blind spots' or policy-relevant research topics that have received limited research attention to date. In particular, this review differs from prior work in that we argue that bank governance should not be limited to appeasing shareholder interests, but also account for the interests of creditors and taxpayers – two stakeholder groups that play an important role in the banking industry. To this end, we examine the current state of research on internal bank governance by focusing on three broad themes and their impact on bank risk: the effectiveness of bank boards, the risk management systems and practices employed by banks, and the structure of CEO compensation (see Table 1 for a brief summary of prior research on different elements of bank governance and risk-taking). Ultimately, the purpose of this paper is to formulate questions for future empirical research.

Bank boards are the apex of the internal governance system. Boards hold overall responsibility for providing oversight into the monitoring of bank management, setting executive compensation contracts, and implementing an effective system of risk governance. To this end, our review first looks into the role of the board in terms of monitoring and advising senior bank executives. Next, our review looks into the role of executive compensation. Prior empirical literature has argued that bank boards structured executive pay to reward executives for excessive risk-taking through the use of stock options and short-term pay (DeYoung et al., 2013; Federal Reserve et al., 2010). Our review presents valuable insights on alternate pay mechanisms that can motivate bank managers to take into account the interests of other stakeholders. Finally, a board's ability to offer effective risk oversight is also conditional on accurate risk assessment and timely communication by the risk committee. To this end, our review highlights various research avenues that can further our understanding on the impact of risk management practices (e.g., the presence of a risk committee and Chief Risk Officer, and risk culture) on risk-taking.

Research on topical issues highlighted in this review may help inform policy research in developing sound and balanced governance structures. This can help in developing a more textured understanding of how each governance dimension operates. For instance, the review highlights how director skills and expertise affect risk monitoring and how the use of debt-based pay instruments for senior executives results in less risky bank policies.

This review article is organized as follows. The next section presents the theoretical foundations of governance and risk for banks. We then review past and ongoing research on the monitoring role of the board of directors, the impact of CEO compensation instruments on risk-taking, and the role of risk governance in banks. The final section concludes.

BACKGROUND

We start this section by surveying existing measures of bank risk-taking that have been adopted by prior research. We then outline the theoretical foundations for why risk-taking behavior by banks is of particular significance and how banks differ from non-banking institutions in important ways. In particular, we argue that banks' core activities are information-based and highly opaque, their capital structure is geared toward debt much more than any other major industry, and that the government is an important stakeholder in banks as an underwriter of guarantees. Finally, we highlight how 'traditional' governance frameworks (i.e,, those that align manager and shareholder interests) may result in heightened risk-taking concerns in the banking industry.

Bank Risk-taking

For the purposes of this review, we define bank risk-taking as policies that increase risk through any of various channels. We discuss some of the commonly used proxies for bank risk below.

Market risk captures losses incurred due to the impact of adverse market movements on the value of banks' on- and off-balance sheet positions. Recent regulatory reforms have focused on the framework used by banks to assess market risk as losses incurred on banks' trading books during the recent crisis had depleted bank capital and heightened financial stability concerns (Basel Committee on Banking Supervision, 2013). Prior work has measured market risk through tail risk measures, such as value-at-risk (VaR) and expected shortfall to estimate expected losses in the case of tail events (Ellul & Yerramilli, 2013; van Bekkum, 2015). Another common measure is stock volatility (Anderson & Fraser, 2000; Chen, Steiner, & Whyte, 2006; Konishi & Yasuda, 2004).

Further, *default risk* is a composite measure of bank risk that combines risks arising from investment and financing activities. Prior work has focused on measuring default risk through either an accounting-based measure Z-score (Houston, Lin, Lin, & Ma, 2010; Laeven & Levine, 2009; Pathan, 2009) or a market-based measure based on Merton's structural distance-to-default model (Gropp, Vesala, & Vulpes, 2006; Hagendorff & Vallascas, 2011).

Relatedly, banks can also pursue policies that result in shifting the costs of default to the taxpayer. To measure risk shifting, studies have sought to estimate the value of the government's financial safety net to shareholders as the value

© 2015 John Wiley & Sons Ltd

TABLE 1

Summary of Prior Literature on Bank Governance and Risk-Taking. This Table Presents a Brief Overview of Prior Literature Focusing on the Impact of Bank Governance on Risk-Taking Incentives.

Study	Governance measure	Summary
Board attributes		
Beltratti and Stulz (2012)	Shareholder-friendly board index collected by Institutional Shareholder Services (ISS)	• **Risk measures**: Default risk (Z-score); Equity risk (idiosyncratic component of stock volatility); Leverage risk (equity minus tangible assets scaled by assets); Portfolio risk (fraction of loan write downs to assets) • **Key findings**: Shareholder-friendly boards are positively associated with default risk, although this relationship is not entirely robust to different risk measures
Erkens et al. (2012)	Independent directors	• **Risk measures**: Default risk (expected default frequency); Equity risk (stock volatility); Leverage risk (amount of equity capital raised) • **Key findings**: No significant relationship between independent directors and default risk or equity risk. Banks with a higher fraction of independent directors reduced leverage risk by raising equity during the financial crisis.
Berger et al. (2014)	Demographics of executive directors (age, educational qualification, and gender)	• **Risk measures**: Portfolio risk (asset density, loan portfolio concentration) • **Key findings**: Portfolio risk is positively associated with younger executives and female directors. Portfolio risk is negatively associated with the fraction of directors with doctorate.
Minton et al. (2014)	Financial expertise of independent directors	• **Risk measures**: Equity risk (stock volatility); Leverage risk (risk-weighted capital ratio); Portfolio risk (fraction of loans secured by real estate) • **Key findings**: Boards consisting of higher amount of financial experts were positively associated with bank risk
International Monetary Fund (2014)	Board size Independent directors	• **Risk measures**: Default risk (Z-score and distance-to-default); Equity risk (systematic component of stock volatility); Tail risk (expected shortfall, marginal expected shortfall, and systemic risk) • **Key findings**: Higher fraction of independent directors is associated with lower bank risk, although boards that have more financial experts are associated with higher risk.
Executive pay		
Hagendorff and Vallascas (2011)	CEO pay-risk sensitivity or vega	• **Risk measures**: Default risk (Merton's distance-to-default) • **Key findings**: High vega banks pursue acquisitions that result in increasing default risk
DeYoung et al. (2013)	CEO pay-risk sensitivity or Vega CEO pay-performance sensitivity or Delta	• **Risk measures**: Equity risk (stock volatility) • **Key findings**: Higher vega is associated with an increase in equity risk. Higher vega results in shifting the business model of banks to non-traditional activities, i.e. a greater fraction of income from non-interest-bearing activities and derivatives investment.
International Monetary Fund (2014)	Fraction of equity-based pay	• **Risk measures**: Default risk (Z-score and distance-to-default); Equity risk (systematic component of stock volatility); Tail risk (expected shortfall, marginal expected shortfall, and systemic risk) • **Key findings**: Higher equity-based pay is associated with lower bank risk
Bennett et al. (2015)	CEO debt-based compensation	• **Risk measures**: Default risk (expected default frequency) • **Key findings**: Higher inside debt is associated with lower default risk during the crisis
van Bekkum (2015)	Fraction of CEO debt-based compensation	• **Risk measures**: Tail risk (value-at-risk, expected shortfall, covariance); Equity risk (stock volatility) • **Key findings**: Inside debt is negatively associated with different measures of bank risk
Bolton et al. (2015)	CEO inside debt to equity-based compensation	• **Risk measures**: Announcement effect on CDS spreads • **Key findings**: Announcement of CEO inside debt holdings is associated with lower CDS spreads
Cheng et al. (2015)	Residual compensation	• **Risk measures**: Equity risk (stock volatility)

© 2015 John Wiley & Sons Ltd

TABLE 1
Continued

Study	Governance measure	Summary
		• **Key findings**: Residual compensation is positively associated with equity risk
Risk management		
Keys et al. (2009)	Risk manager power: Fraction of risk managers pay to top-5 executive pay	• **Risk measures**: Portfolio risk (default rates on subprime loans) • **Key findings**: Stronger risk management is associated with less risky subprime loan securitizations
Fahlenbrach et al. (2012)	Risk culture, as proxied by bank performance during the 1998 Russian crisis	• **Risk measures**: Default risk (bank failures during the 2007–08 period) • **Key findings**: Banks with persistent risk-taking culture performed poorly and were more likely to fail during the 2007–08 financial crisis
Ellul and Yerramilli (2013)	Strength and independence of risk management function	• **Risk measures**: Tail risk (expected shortfall); Credit risk (fraction of non-performing loans) • **Key findings**: Stronger Risk Management Index (RMI) is associated with lower tail risk exposure and better loan quality. RMI is also a strong predictor of bank tail risk exposures during the financial crisis
International Monetary Fund (2014)	Presence of risk committee	• **Risk measures**: Default risk (Z-score and distance-to-default); Equity risk (systematic component of stock volatility); Tail risk (expected shortfall, marginal expected shortfall, and systemic risk) • **Key findings**: Banks with risk committee are associated with lower risk-taking

of a put option underwritten by taxpayers (Hovakimian & Kane, 2000; Merton, 1977; Ronn & Verma, 1986).

Leverage risk is defined as the risk arising from banks holding low amounts of capital to support their operations. Leverage risk is commonly measured using book capital ratios, such as high-quality (Tier-1) capital or risk-adjusted capital ratios (Flannery & Rangan, 2008; Gropp & Heider, 2010; Nier & Baumann, 2006). Finally, *portfolio risk* is defined as the volatility of asset returns arising from a bank's investment activities. Prior work has measured the portfolio risk of banks using the ratio of risk-weighted assets to assets or either book-based or market-based measures of asset volatility (Flannery & Rangan, 2008; Shrieves & Dahl, 1992; Vallascas & Hagendorff, 2013).

Theory: Are Banks Different?

Banking theory outlines various characteristics that differentiate banks from non-financial firms (Bhattacharya & Thakor, 1993; Diamond & Dybvig, 1983; Merton, 1977). This section focuses on the implications of these characteristics on bank risk-taking.

At its core, banking involves institutions accepting short-term liquid deposits and transforming them into long-term illiquid loans. During this intermediation process, banks privately monitor and collect information about the quality of their loan portfolio. Since bank loans are informationally opaque, external stakeholders cannot possess all relevant information to assess the true value of bank assets (Diamond, 1989, 1991; Morgan, 2002). As a result, managers may pursue policies that increase bank risk, without this being reflected on backward-looking balance sheets (Becht et al., 2011; Mehran, Morrison, & Shapiro, 2011).

Further, banks are unique because they benefit from explicit deposit insurance guarantees and more implicit guarantees in the form of emergency liquidity and the possibility of capital assistance (i.e,, bailouts) in times of distress (Bhattacharya & Thakor, 1993). Government guarantees act as a put option on a bank's assets and the value of this put is increasing in bank risk (Kareken & Wallace, 1978; Merton, 1977). Banks seek to maximize the value of the put by pursuing policies that increase overall risk. Consistent with this view, the extant literature has provided evidence of increased risk-taking in the presence of government guarantees (Dam & Koetter, 2012; Hovakimian & Kane, 2000).

Finally, banks are highly leveraged financial institutions where leverage exists as a factor of production.[2] Leverage results in exacerbating risk-taking concerns because the option value of government guarantees to shareholders is increasing with firm leverage, which leads to magnified benefits of increasing bank risk for highly leveraged banks (Bebchuk & Spamann, 2009; John, Mehran, & Qian, 2010; Keeley, 1990).

Shareholder-oriented v Stakeholder-oriented Bank Governance

Governance mechanisms deal with the ways in which outside investors and other stakeholders, such as government and employees, exercise control over senior management and other corporate insiders in order to protect their interests. Prior work has interpreted this from an agency-theoretic

© 2015 John Wiley & Sons Ltd

framework where utility-maximizing managers are risk-averse and lack the incentives to pursue risky but positive net present value (NPV) projects (Jensen & Meckling, 1976). To mitigate the agency costs of equity, key governance structures focus on protecting and promoting shareholder interests. Examples of this are the presence of independent directors on bank boards, the widespread use of equity instruments in executive remuneration, and a general assessment of executive performance on the basis of meeting shareholder interests (Holmstrom, 1982; Jensen & Meckling, 1976; Smith & Stulz, 1985; Weisbach, 1988).

However, there are conflicts between the risk preferences of shareholders and bank creditors. Shareholders hold convex claims over firm assets which cause their expected payoffs to rise exponentially with bank risk (Jensen & Meckling, 1976). By contrast, creditor payoffs are concave due to limited upside potential on the value of their claims. For creditors, excessive risk-taking therefore implies a higher probability of losses without the same potential for gains that shareholders benefit from. Such conflicts between bank shareholders and creditors are further exacerbated by bank bailout guarantees. There is a real prospect that highly leveraged banks take on undue risks in ways that benefit bank shareholders at the expense of creditors and the taxpayer (Bhattacharya & Thakor, 1993; John, John, & Senbet, 1991).

This risk-shifting problem in banking (when banks force taxpayers to finance their risk exposures) is widely recognized. For instance, John, Saunders, and Senbet (2001) show that aligning the interests between managers and shareholders results in banks taking risks that benefit bank shareholders at the expense of creditors and the taxpayer. Bolton, Mehran, and Shapiro (2015) also develop a theoretical model to show that shareholders lack appropriate incentives to control risk-taking by banks in order to take advantage of government guarantees and inability of external stakeholders to accurately measure bank risk.

In response to this issue, various scholars have proposed the need for bank governance to represent the interests of shareholders, creditors, and taxpayers (Adams & Mehran, 2003; Berger, Kick, & Schaeck, 2014; Bolton et al., 2015; Macey & O'Hara, 2003). Prior research provides some supporting evidence on the role of creditors and depositors in disciplining bank risk-taking. This stream shows that risky banks are charged higher interest rates in the interbank borrowing market (Furfine, 2001; King, 2008) and the subordinated debt market (Flannery & Sorescu, 1996). Depositors can also discipline risk-taking by demanding higher interest rates (Berger & Turk-Ariss, 2014; Martinez Peria & Schmukler, 2001). However, this research has focused on the role of creditors in externally monitoring bank risk-taking. Aligning manager and creditor interests through internal governance mechanisms (e.g., through executive pay that reflects creditor wealth) is likely to be more effective and the foundation of a governance mechanism that balances the interests of shareholders and creditors.

The next section focuses on the role of bank boards in controlling bank risk-taking and meeting creditor interests. We highlight a range of board characteristics that moderate a board's ability to monitor executives and can, therefore, help to protect creditor interests and maintain bank stability more generally.

THE ROLE OF THE BOARD IN MONITORING AND CONTROLLING RISK

The board of directors is widely regarded as the cornerstone of an effective internal governance framework (Fama & Jensen, 1983). It has ultimate responsibility for risk management and setting the tone for a bank's risk-taking culture at the top. The board ensures bank stability by monitoring executives over the impact of firm policies on bank risk, evaluating whether current and future risk-exposure is consistent with risk appetite, and designing executive incentives to promote prudent risk-taking.

Despite the key role that boards play in ensuring an effective system of governance, academic research on the impact of board characteristics on bank risk-taking is strikingly sparse. Most of the research in this area has been derived from non-financial firms (e.g., Adams & Ferreira, 2008; Almazan & Suarez, 2003; Harris & Raviv, 2008; Hermalin & Weisbach, 1998; Raheja, 2005).

Overall, the extant empirical research on the impact of boards on bank risk-taking presents ambiguous evidence. Akhigbe and Martin (2006) study the impact of the Sarbanes-Oxley (SOX) Act on financial institutions. The authors show that firms with independent boards see a decline in their stock volatility over the long term. Erkens, Hung, and Matos (2012) do not find any impact of board independence on bank risk during the financial crisis for a sample of large international banks. By contrast, Pathan (2009) reports that stronger boards, that is, boards which are smaller and exhibit stronger shareholder rights, are positively related to bank risk-taking. However, the author reports that boards characterized by a higher fraction of independent directors pursue less risky policies. Beltratti and Stulz (2012) also present evidence to show that banks with a shareholder-friendly board were more risky, although the results do not hold when the authors use different measures of risk.

Previous research suffers from the issue that the advisory and monitoring roles of the board are not directly observable. This has caused researchers to look instead at the impact of boards on observable outcomes such as bank policies or performance (Adams, Hermalin, & Weisbach, 2010). Moreover, board independence is a broad measure that fails to account for more nuanced board dynamics. The following two subsections examine more fine-grained aspects of board functions by highlighting the role of various board attributes in effective monitoring of senior management and the impact of powerful CEOs in undermining board effectiveness.

Board Attributes

We employ a broad definition of board attributes to encompass various competencies and skills that board members possess and the role that these attributes play in influencing bank policies. For instance, a diverse board may well be able to represent the interests of various stakeholders and, more importantly, solve complex issues faced by a firm in its day-to-day operations (Forbes & Milliken, 1999). Similarly, board competence in terms of prior banking experience and financial expertise may allow board members to better assess the impact of bank policies on risk (Kirkpatrick, 2009; Walker, 2009).

© 2015 John Wiley & Sons Ltd

While recent research has started to examine the effects of different board attributes, a majority of this stream has focused on assessing its impact on bank performance (e.g., Erkens et al., 2012; Hagendorff & Keasey, 2012; Nguyen, Hagendorff & Eshraghi, 2015). Berger et al. (2014) are among the first to look at board demographics and bank risk-taking. They find that executive teams composed of younger members and more women increase bank risk, while boards with a higher representation of individuals with a doctorate degree are negatively related to bank risk.

Ongoing policy debates have proposed the need for stakeholder representation on bank boards (Basel Committee on Banking Supervision, 2014; Kirkpatrick, 2009; Walker, 2009). For instance, the International Monetary Fund (2014) recommends that some board members should be creditor representatives. This is consistent with extant theoretical and empirical evidence that unsecured creditors (e.g., investors in convertible debt [Hilscher & Raviv, 2014], or interbank borrowers]Furfine, 2001; King, 2008]) are effective in terms of controlling risk-taking. In this context, Hilscher and Şişli-Ciamarra (2013) show that the presence of creditor representatives on boards is associated with creditor-friendly policies. The authors show that mergers announced by non-financials with a higher fraction of creditor-directors are associated with an increase in bondholder wealth and a fall in shareholder wealth.

Board competence in terms of the educational qualifications and prior relevant experience can also have an important bearing on bank risk-taking incentives. Given that banks are highly opaque and complex organizations, better education may influence the ability of directors to understand and interpret sophisticated risk measurement techniques and the impact of bank policies on risk. Consistent with this, Berger et al. (2014) show that banks where a higher fraction of executive officers held doctorate degrees were associated with lower risk.

Harris and Raviv (2008) posit that financial expertise is essential to understand the complex workings of the firm and the risks associated with firm policies. Various researchers (Hau & Thum, 2009; Minton, Taillard, & Williamson, 2014) and policy reviews (Kirkpatrick, 2009; Walker, 2009) have argued that many bank boards lacked sufficient financial expertise to identify and control bank risk exposures in the years preceding the crisis. Hau and Thum (2009) show that German banks where supervisory boards lacked financial expertise suffered from larger losses during the recent financial crisis. By contrast, Minton et al. (2014) report a positive relationship between financial expertise and bank risk in their sample of US banks. The authors attribute this to the fact that financial expertise allows board members to evaluate risky policies that may favor shareholders.

Future research should evaluate the marginal impact of financial expertise on the likelihood that banks engage in regulatory arbitrage and underestimate their risk exposures. An interesting avenue on which to base this research could be countries which employ a dual-tier structure (e.g., Germany, Japan, etc.), where supervisory boards consist of creditors and employees, thereby representing stakeholder interests. While Berger et al. (2014) also study the implications of board characteristics, such as, age, gender, and educational background, on risk-taking, the focus of their research is on executive board members. Future research should investigate if non-executive directors on the supervisory boards have the power and influence to shape bank policies. This issue is particularly important given the heightened expectations that US bank regulators have of bank boards in terms of providing effective risk oversight.

Board Process

Another important dimension that may affect bank risk-taking is board process. Board process refers to the behavior and the involvement of directors in a bank's decision-making process, such as director attendance, conduct during board meetings, and the relationship between executive directors and non-executive directors (Forbes & Milliken, 1999; McNulty, Florackis, & Ormrod, 2013; Roberts, McNulty, & Stiles, 2005). These and similar aspects of director behavior are also laid out in regulatory expectations of bank boards. For instance, the Office of the Comptroller of the Currency (1997) in the US lays down key director responsibilities which include staying informed about bank policies through regular attendance at meetings, preparation for meetings, and active involvement during board meetings.

Forbes and Milliken (1999) develop a theoretical framework that explains the internal workings of the board. The authors identify key processes that help explain how boards function. Pettigrew and McNulty (1995) categorize board involvement in firm-related matters into minimalist and maximalist boards. Firms where boards of directors are actively involved in shaping and influencing the choice of firm policies are classified as maximalist boards, and boards which wield little influence are classified as minimalist.

McNulty et al. (2013) show that board process is a key determinant of financial risk for non-financial firms. However, the authors note that board process does not influence business risk and partly attribute this finding to passive board behavior. In the context of banks, Adams and Ferreira (2012) argue that attendance is a key responsibility for directors as it helps in obtaining firm-specific information. However, the authors show that bank boards have poor attendance records compared to non-financials and that regulatory pressure is not sufficient to boost attendance, although meeting fees and total compensation have an economically significant influence.

However, there is little research on the implications of board process on risk-taking in banks. Internal board dynamics in terms of greater involvement of the board in key bank decisions can be one of the ways to improve bank governance. For instance, future research should assess how boards function when making important decisions. Another interesting issue may be to explore the importance that each bank assigns to developing director knowledge and skills through internal training programs and to explore whether such practices can improve the monitoring of executives.

CEO Power

Another important element that moderates the effectiveness of boards of directors is CEO power (Adams, Almeida, & Ferreira, 2005; Hermalin & Weisbach, 1998). In empirical studies, the power of a CEO is often captured using the number of positions held by a CEO (in particular, whether or not

© 2015 John Wiley & Sons Ltd

the CEO also acts as chairman), a CEO's tenure, or his/her performance relative to peers (Adams et al., 2005; Hermalin & Weisbach, 1998).

Powerful CEOs are likely to undermine board independence if they are able to influence board decisions and prevent boards from effective monitoring. Adams et al. (2005) show that firms with more powerful CEOs are characterized by higher performance variability, implying that powerful CEOs pursue policies which result in riskier outcomes. Therefore, powerful CEOs are more likely to influence board decisions toward pursuing risky policies.

Therefore, future work should assess the joint impact of bank boards and CEO power on bank policies. One potential line of enquiry could try to explain how board governance and CEO power interact. CEO power may increase with tenure and hence its effect on board oversight should be stronger as tenure increases. Another potential line of enquiry could focus on the role of CEO power in capturing the board in the period leading up to the financial crisis.

Taken together, this section argues that various board attributes can play a critical role in providing effective oversight into the functioning of bank executives. Another key mechanism through which bank boards can influence managerial behavior and their risk-taking incentives is through the structure of executive remuneration contracts. We focus on this issue in the next section.

STRUCTURING CEO PAY TO MITIGATE RISK-TAKING

Senior executives are responsible for the day-to-day management of the bank. The traditional setting in which CEO remuneration decisions are taken is laid out in Holmstrom (1982), where the board represents the interests of shareholders and evaluates the performance of the manager. Boards influence executive behavior by overseeing, monitoring, and structuring compensation policies. Consistent with this, DeYoung et al. (2013) show that US bank boards responded to expanded business opportunities after the US deregulation by embedding option-based equity incentives to encourage risk-taking. Another potential mechanism to embed contractual risk-taking incentives is by use of performance-based equity awards that induce managers to pursue risky policies that yield short-term payoffs (Bebchuk & Spamann, 2009; Federal Reserve et al., 2010).

The implications of such incentives on bank behavior and risk-taking preferences have come under increasing scrutiny (Bebchuk & Spamann, 2009; DeYoung et al., 2013; Thanassoulis, 2012). This is because compensating managers with instruments that induce risk-taking may well subordinate the interests of other stakeholder groups (Jensen & Meckling, 1976; John & John, 1993). Consistent with this view, Chen et al. (2006) show that there is a positive association between the percentage of option-based CEO wealth in total compensation and market-based measures of bank risk (e.g., systematic risk, idiosyncratic risk). Cheng, Hong, and Scheinkman (2015) show that banks where CEOs held excess CEO pay, calculated as the regression residual of total CEO pay on firm size, had higher risk exposure into subprime mortgage securities and higher return volatility. Bai and Elyasiani (2013) find that higher option incentives result in reduced bank stability and greater default risk. This association is also reflected in the choice of bank policies, with higher option-induced incentives resulting in riskier acquisitions (Hagendorff & Vallascas, 2011) and riskier investment policies (DeYoung et al., 2013; Mehran & Rosenberg, 2007).

However, over three decades of research on compensation has primarily focused on the link between equity-based compensation and risk-taking with little attention to other important components of CEO pay. Assessing alternate pay components is particularly important because ongoing policy reforms and emerging academic research have raised the need for compensating executives with instruments that promote long-term stability (Bolton et al., 2015; Federal Reserve et al., 2010).

In the following subsections, we shed some light on debt-based pay as well as the vesting schedule of equity awards which could affect firm risk-taking. Empirical research on these issues will enrich our knowledge on different characteristics of CEO pay to arrive at a holistic picture of the incentives arising from CEO compensation.

Recalibrating CEO Pay to Creditor Wealth and Longer Time Horizons

Inside Debt. One way to align the interests of CEOs with firm creditors involves debt-like instruments. A growing literature has shown that CEO pay consists of debt-like instruments, in the form of pension benefits and deferred compensation, and compensating CEOs with this so-called 'inside debt' can mitigate risk-taking (Cassell, Huang, Sanchez, & Stuart, 2012; Edmans & Liu, 2011; Sundaram & Yermack, 2007). The underlying rationale behind this is that CEOs with inside debt have a claim on bank cash flows because inside debt only becomes payable upon retirement. Crucially, these claims are unfunded and unsecured firm obligations, thereby putting the value of inside debt at risk if the firm defaults, and exposing CEOs to the same default risk concerns faced by external creditors (Edmans & Liu, 2011). As a result, when paid with inside debt, the risk preferences of CEOs should converge with those of external creditors, implying that higher inside debt may mitigate risk-taking concerns in the banking industry.

The use of inside debt is widespread and, most executives hold large amounts of inside debt. Sundaram and Yermack (2007) show that 78 percent of large S&P firms in their sample had some form of inside debt arrangements, with an average CEO holding $4.2 million in pensions. In the banking industry, Bennett, Guntay, and Unal (2015) show that 72 percent of banks held some form of inside debt in 2006, with an average CEO holding nearly $3.1 million.

Despite the widespread use of inside debt amongst banks, only a limited amount of applied research has assessed the impact of inside debt on bank policies. DeYoung et al. (2013) point out that bank CEO incentives are more heavily geared toward the interests of shareholders than in other industries, even though equity makes up only a small proportion of a bank's balance sheet. It is therefore particularly important to understand whether aligning managerial interests with the interests of external creditors dampens risk-taking.

© 2015 John Wiley & Sons Ltd

More recently, Bennett et al. (2015) show a negative association between inside debt and a market-based measure of default risk. Bolton et al. (2015) also show that the mandatory disclosure of inside debt holdings of bank CEOs in 2006 was perceived positively by creditors, with higher inside debt associated with lower credit default swap (CDS) spreads. Similarly, van Bekkum (2015) reports a negative relation between CEO and Chief Financial Officer (CFO) inside debt and measures of subsequent market volatility and tail risk. Srivastav, Armitage, and Hagendorff (2014) show that bank CEOs with higher inside debt are associated with more conservative bank payout policies.

Although research has shown that inside debt helps to reduce risk, we know little about how inside debt affects the separate risk components (idiosyncratic risk and systemic risk) and, by extension, incentives to shift the risk of default onto the safety net. Future research can also aid ongoing policy discussions over CEO pay by establishing how any risk reductions are realized.

Finally, existing measures of inside debt have been developed for non-financial firms. For instance, Jensen and Meckling (1976) proposed that CEOs face no risk-taking incentives if the ratio of inside debt to inside equity (i.e,, a CEO's personal leverage) resembles the ratio of a firm's outside debt to outside equity (i.e,, firm leverage). More recently, Wei and Yermack (2011) suggest measuring the strength of inside debt incentives as the sensitivity of a CEO's personal leverage to firm leverage. While such measures may be suitable for non-financial firms, their applicability to banks is questionable. This is because banks are highly leveraged, making it nearly impossible for a CEO's personal leverage to match anything resembling the leverage of the bank they are leading.

Further, key bank liabilities such as deposits benefit from explicit guarantees. Therefore, the components of inside debt ratios do not compare like for like: in banks, inside debt ratios contain both insured debt in the form of deposits as well as more junior (and unsecured) bank debt. Therefore, future research will need to more accurately measure the incentives originating from inside debt for banks to gain a better understanding of how these incentives impact the risk-taking behavior of senior bank managers.

Characteristics of CEO Compensation Contracts. Beside inside debt, an alternative way to mitigate the risk-taking incentives inherent in bank CEO pay is to discourage the adoption of equity awards that motivate executives to focus on meeting short-term targets. Equity awards granted to firm executives are subject to vesting criteria, wherein executives receive their awards gradually over the next one to five years. Therefore, executives with a long vesting schedule are more sensitive to long-term stability as they may not receive awards if the firm defaults.

Mehran et al. (2011) note that around 49 percent of bank CEOs in their sample held option awards which vested within one year. If equity awards vest within a short time, the payoffs to bank CEOs are no longer sensitive to the much longer time horizon over which economic risks are realized. This may incentivize CEOs to pursue bank policies that maximize current equity payoffs at the expense of long-term stability.

However, Fahlenbrach and Stulz (2011) note that there is a lack of evidence to show that bank CEO pay resulted in short-termism. The authors find that bank CEOs held on to vested equity and option grants before the crisis and subsequently bore huge wealth losses. This is in conflict with the widespread notion of pervasive short-termism inherent in CEO pay and it warrants further empirical research. A starting point for such an investigation could be the work of Gopalan, Milbourn, Song, and Thakor (2014) who devise a novel measure of CEO pay duration to reflect the level of short-termism underlying CEO pay. The authors define pay duration as the weighted average of the vesting schedule of options, stocks, and cash, with weights assigned according to the percentage contribution of each component to total pay.

Future research into CEO pay should also explore if the vesting schedule of equity awards can affect risk-taking. Most critically, there is a need to assess whether CEO pay in banking is more short-term in nature and causes higher levels of risk-taking than in other industries. Another challenge is to assess the mechanisms, such as the use of long-term deferred equity, through which CEO pay duration may be extended in order to promote long-term stability.

Relatedly, various equity awards are conditional on performance-based vesting criteria, wherein CEOs can accelerate the rate at which their equity awards vest if they meet certain performance criteria (e.g., share price increases). This tends to significantly increase the value of the existing equity portfolio of CEOs and may result in giving CEOs stronger incentives to increase firm risk (Bettis, Bizjak, Coles, & Kalpathy, 2010; Brisley, 2006). Future work should therefore account for both the time- and performance-based vesting criteria of CEO pay and assess whether certain features of equity awards can exacerbate risk-taking concerns.

Taken together, our review highlights the need for widening the scope of the literature by assessing the role of alternate pay components in remuneration contracts. Specifically, boards can align managerial incentives with bank stability by using pay components that offer payoffs over an extended horizon such as the use of inside debt and long-term vesting conditions on equity awards.

The next and final section of this review examines the role of corporate governance arrangements in improving the role of effectiveness of risk oversight.

BANK RISK MANAGEMENT AND RISK EXPOSURES

The role of risk management is to evaluate the impact of a firm's current and future policies on its risk exposure. A review of risk governance at major banks by the Senior Supervisors Group (2009), an international forum of senior representatives from various supervisory authorities, highlighted inadequate risk management practices behind the failure of banks to identify and control for their exposures to extreme events. Emerging literature on risk governance has also shown its importance for ensuring bank stability. For instance, Keys, Mukherjee, Seru, and Vig (2009) show that stronger risk management departments (measured by the share of top risk manager's compensation relative to the top five executives) originate less risky mortgage portfolios.

Aebi, Sabato, and Schmid (2012) show that banks where the Chief Risk Officer (CRO) directly reports to the board had

© 2015 John Wiley & Sons Ltd

stronger performance during the financial crisis of 2007–08. Ellul and Yerramilli (2013) provide evidence on the relationship between risk management and bank risk. The authors develop a Risk Management Index which consolidates different dimensions of the risk management function (e.g., the presence of a CRO on the board, experience on the risk committee, etc.) to show that banks with a higher risk management score in 2006 were less risky during the crisis. Lingel and Sheedy (2012) extend Ellul & Yerramilli's study by developing a risk management index in an international setting and show that banks with stronger risk management had lower risk over the period 2004–10. The authors focus on a sample of large international banks in order to include the dynamics of different legal, cultural, and regulatory environments.

While prior literature has shown some evidence on the effectiveness of risk governance, some important questions on the topic remain unanswered. For instance, there is limited research that analyzes whether risk management functions should be rigid, that is, based on compliance, or more focused on involving risk managers in key decisions without a formal system of compliance (Stulz, 2015). In this regard, Hall, Mikes, and Millo (2013) conducted a field study of two UK banks and showed that the bank where risk management followed a rigid 'box-ticking' approach failed to control its risk exposure.

More empirical and theoretical research along these lines will help to identify the antecedents of effective risk management. For instance, banks with effective risk management should be more likely to proactively monitor risk exposures and change practice in response to crisis episodes during or after periods of poor performance. Relatedly, little is known about the determinants of the composition of risk management committees and how its composition affects bank risk-taking.

Another aspect of risk management that deserves more attention is a bank's risk culture. Mehran et al. (2011) and Stulz (2015) argue that risk management practices are shaped by the risk-taking culture within a firm. Ellul and Yerramilli (2013) posit that the risk culture and risk management function may be jointly endogenous, that is, banks which have a more pronounced culture for risk-taking may also be less likely to install an effective system of risk management. Thus, it is not risk management but corporate culture that determines risk (Stulz, 2015). Consistent with this, Fahlenbrach, Prilmeier, and Stulz (2012) show that risk culture is a strong determinant of bank risk-taking. The authors document that bank risk and performance during the recent financial crisis are positively related to their performance during the 1998 crisis (sparked by Russia's default on some of its debt), thereby suggesting that banks with persistent risk culture take more risks. More recently, Bouwman and Malmendier (2015) also show that banks that have experienced macroeconomic and bank-specific shocks in the past are more likely to engage in safe lending practices and higher capitalization. One potential reason could be that a bank's culture is shaped by its history of experiencing and surviving such shocks, which further influences its future risk-taking behavior.

While quantifying the risk culture of a particular bank is difficult to incorporate into empirical analysis, future work should attempt to identify various dimensions of risk culture and account for its role in influencing risk management practices in banks. Another important issue is to assess how different governance mechanisms interact with each other. For example, banks with a culture that promotes risk-taking may be more likely to have weak risk management systems and this could have an important bearing on the type of executives and directors this type of institution hires. By contrast, an effective system of risk management may be undermined if the board lacks expertise to conduct meaningful risk assessments. Future research therefore needs to jointly take into account the dynamics of board effectiveness and risk management in order to develop a holistic understanding of how different governance mechanisms interact with each other.

CONCLUSIONS

The purpose of this paper is to review the literature on the corporate governance of banks with a particular focus on the implications of governance for bank risk-taking. Current governance practices are based on the principle that corporate governance mechanisms are designed to protect shareholder interests, with shareholders exercising control over bank operations and policies via the board of directors (Becht et al., 2011; Mehran et al., 2011). However, one of the lessons drawn from the recent crisis is the need to understand better how to design governance mechanisms that represent the interests of creditors and taxpayers, in addition to bank shareholders, with the aim of controlling bank risk-taking more effectively (Basel Committee on Banking Supervision, 2014; Federal Reserve et al., 2010; Kashyap, Rajan & Stein, 2008; Kirkpatrick, 2009).

Banks differ from non-banking firms in important ways that are relevant for risk-taking. Excessive leverage and the presence of government guarantees may exacerbate risk-taking incentives in the banking industry. Further, risk-taking will be beneficial for shareholders but detrimental for bank creditors and taxpayers who underwrite the type of guarantees that protect many bank liability holders from loss (Bhattacharya & Thakor, 1993; Merton, 1977). This literature review offers insights into how corporate governance can mitigate the risk-taking incentives which banks face.

In particular, we highlight three future strands of research on the internal governance of banks. First, there is a need to assess the impact of different board attributes on risk-taking. While prior research has largely focused on broad board measures (e.g., board size and board independence), our review encourages future research to focus on the more fine-grained aspects of how boards function, including the educational qualifications of directors and other personal characteristics. Second, empirical work has only recently begun to examine pay instruments that incentivize managers to focus on the long-term stability of banks. This review highlights the role of debt-based forms of compensation as a device to mitigate bank risk-taking. Finally, research needs to explore the risk management culture and risk management practices inside banks.

Future research should also address some of the fundamental governance issues for banks that remain unanswered to date. For instance, it will be interesting to explore the risk implications if banks represent the interests of creditors, taxpayers, and shareholders on boards. In this regard, our study supports the conclusions of de Haan and Vlahu (2015)

© 2015 John Wiley & Sons Ltd

who posit that future research on bank governance should take into account regulatory distortions and the role of large creditors within a broader governance framework. Moreover, we know very little about the inner workings of bank boards in terms of group dynamics and whether such board processes can influence the choice of bank policies. More empirical evidence on the issues highlighted in this review will help develop a deeper understanding of bank behavior within governance systems and serve as an empirical basis for ongoing governance recommendations for sustainable bank risk-taking.

ACKNOWLEDGEMENTS

The authors are indebted to Chris Florackis (the Associate Editor) as well as to two anonymous referees for very helpful comments and suggestions.

NOTES

1. Arguably, there exist various other dimensions that resulted in bank fragility during the global financial crisis of 2007–09, such as inadequate bank capital (Hanson, Kashyap, & Stein, 2011; Kashyap et al., 2008), unregulated shadow banking system (Gennaioli, Shleifer, & Vishny, 2013), and the too-big-to-fail problem (Freixas & Rochet, 2013). However, the focus of our paper is on one such channel: governance failures.
2. While leveraged buyouts (LBOs) are also highly leveraged, LBOs control agency costs of debt (e.g., risk-shifting) through various strategies such as the use of loan covenants, presence of LBO specialist sponsors who represent both equity holder and debt holder interests, and use of strip financing, where investors hold both equity-like and debt-like instruments (Jensen, 1989; Opler, 1993).

REFERENCES

Adams, R. B., Almeida, H., & Ferreira, D. 2005. Powerful CEOs and their impact on corporate performance, ***Review of Financial Studies***, 18: 1403–1432.

Adams, R. B. & Ferreira, D. 2008. One share-one vote: The empirical evidence, ***Review of Finance***, 12: 51–91.

Adams, R. B. & Ferreira, D. 2012. Regulatory pressure and bank directors' incentives to attend board meetings, ***International Review of Finance***, 12: 227–248.

Adams, R. B., Hermalin, B. E., & Weisbach, M. S. 2010. The role of boards of directors in corporate governance: A conceptual framework and survey, ***Journal of Economic Literature***, 48: 58–107.

Adams, R. B. & Mehran, H. 2003. Is corporate governance different for bank holding companies?, ***Economic Policy Review***, 9: 123–142.

Aebi, V., Sabato, G., & Schmid, M. 2012. Risk management, corporate governance, and bank performance in the financial crisis, ***Journal of Banking & Finance***, 36: 3213–3226.

Akhigbe, A. & Martin, A. D. 2006. Valuation impact of Sarbanes-Oxley: Evidence from disclosure and governance within the financial services industry, ***Journal of Banking & Finance***, 30: 989–1006.

Almazan, A. & Suarez, J. 2003. Entrenchment and severance pay in optimal governance structures, ***The Journal of Finance***, 58: 519–548.

Anderson, R. C. & Fraser, D. R. 2000. Corporate control, bank risk taking, and the health of the banking industry, ***Journal of Banking & Finance***, 24: 1383–1398.

Bai, G. & Elyasiani, E. 2013. Bank stability and managerial compensation, ***Journal of Banking & Finance***, 37: 799–813.

Basel Committee on Banking Supervision. 2013. Fundamental review of the trading book: A revised market risk framework. Basel: Bank for International Settlements.

Basel Committee on Banking Supervision. 2014. Corporate governance principles for banks. Basel: Bank for International Settlements.

Bebchuk, L. A. & Spamann, H. 2009. Regulating bankers' pay, ***Georgetown Law Journal***, 98: 247–287.

Becht, M., Bolton, P., & Röell, A. 2011. Why bank governance is different, ***Oxford Review of Economic Policy***, 27: 437–463.

Beltratti, A. & Stulz, R. M. 2012. The credit crisis around the globe: Why did some banks perform better?, ***Journal of Financial Economics***, 105: 1–17.

Bennett, R. L., Guntay, L., & Unal, H. 2015. Inside debt, bank default risk and performance during the crisis, ***Journal of Financial Intermediation*** In Press. doi: 10.1016/j.jfi.2014.11.006.

Berger, A. N., Kick, T., & Schaeck, K. 2014. Executive board composition and bank risk taking, ***Journal of Corporate Finance***, 28: 48–65.

Berger, A. N. & Turk-Ariss, R. 2014. Do depositors discipline banks and did government actions during the recent crisis reduce this discipline? An international perspective, ***Journal of Financial Services Research***, doi: 10.1007/s10693-014-0205-7.

Bettis, C., Bizjak, J., Coles, J., & Kalpathy, S. 2010. Stock and option grants with performance-based vesting provisions, ***Review of Financial Studies***, 23: 3849–3888.

Bhattacharya, S. & Thakor, A. V. 1993. Contemporary banking theory, ***Journal of Financial Intermediation***, 3: 2–50.

Bolton, P., Mehran, H., & Shapiro, J. 2015. Executive compensation and risk taking, ***Review of Finance***, doi: 10.1093/rof/rfu049.

Bouwman, C. & Malmendier, U. 2015. Does a bank's history affect its risk-taking?, ***American Economic Review***, 105: 321–325.

Brisley, N. 2006. Executive stock options: Early exercise provisions and risk-taking incentives, ***The Journal of Finance***, 61: 2487–2509.

Brunnermeier, M. K. 2009. Deciphering the liquidity and credit crunch 2007–08. ***Journal of Economic Perspectives***, 23: 77–100.

Cassell, C. A., Huang, S. X., Sanchez, J. M., & Stuart, M. D. 2012. Seeking safety: The relation between CEO inside debt holdings and the riskiness of firm investment and financial policies, ***Journal of Financial Economics***, 103: 588–610.

Chen, C. R., Steiner, T. L., & Whyte, A. M. 2006. Does stock option-based executive compensation induce risk-taking? An analysis of the banking industry, ***Journal of Banking & Finance***, 30: 915–945.

Cheng, I. H., Hong, H., & Scheinkman, J. A. 2015. Yesterday's heroes: Compensation and risk at financial firms, ***The Journal of Finance***, 70: 839–879.

Dam, L. & Koetter, M. 2012. Bank bailouts and moral hazard: Empirical evidence from Germany, ***Review of Financial Studies***, 25: 2343–2380.

DeYoung, R., Peng, E. Y., & Yan, M. 2013. Executive compensation and business policy choices at US commercial banks, ***Journal of Financial and Quantitative Analysis***, 48: 165–196.

de Haan, J. & Vlahu, R. 2015. Corporate governance of banks: A survey. ***Journal of Economic Surveys***, doi: 10.1111/joes.12101.

Diamond, D. W. 1989. Reputation acquisition in debt markets, ***Journal of Political Economy***, 97: 828–862.

Diamond, D. W. 1991. Monitoring and reputation: The choice between bank loans and directly placed debt, ***Journal of Political Economy***, 99: 689–721.

Diamond, D. W. & Dybvig, P. H. 1983. Bank runs, deposit insurance, and liquidity, ***Journal of Political Economy***, 91: 401–419.

Edmans, A. & Liu, Q. 2011. Inside debt, ***Review of Finance***, 15: 75–102.

Ellul, A. & Yerramilli, V. 2013. Stronger risk controls, lower risk: Evidence from US bank holding companies, ***The Journal of Finance***, 68: 1757–1803.

© 2015 John Wiley & Sons Ltd

Erkens, D. H., Hung, M., & Matos, P. 2012. Corporate governance in the 2007–2008 financial crisis: Evidence from financial institutions worldwide, ***Journal of Corporate Finance***, 18: 389–411.

Fahlenbrach, R., Prilmeier, R., & Stulz, R. M. 2012. This time is the same: Using bank performance in 1998 to explain bank performance during the recent financial crisis, ***The Journal of Finance***, 67: 2139–2185.

Fahlenbrach, R. & Stulz, R. M. 2011. Bank CEO incentives and the credit crisis, ***Journal of Financial Economics***, 99: 11–26.

Fama, E. F. & Jensen, M. C. 1983. Separation of ownership and control, ***Journal of Law and Economics***, 26: 301–325.

Federal Reserve, Office of the Comptroller of the Currency, Office of Thrift Supervision, Federal Deposit Insurance Corporation. 2010. Guidance on sound incentive compensation policies. June.

Flannery, M. J. & Rangan, K. P. 2008. What caused the bank capital build-up of the 1990s?, ***Review of Finance***, 12: 391–429.

Flannery, M. J. & Sorescu, S. M. 1996. Evidence of bank market discipline in subordinated debenture yields: 1983–1991, ***The Journal of Finance***, 51: 1347–1377.

Forbes, D. P. & Milliken, F. J. 1999. Cognition and corporate governance: Understanding boards of directors as strategic decision-making groups, ***Academy of Management Review***, 24: 489–505.

Freixas, X. & Rochet, J. C. 2013. Taming systemically important financial institutions, ***Journal of Money, Credit, and Banking***, 45: 37–58.

Furfine, C. H. 2001. Banks as monitors of other banks: Evidence from the overnight federal funds market, ***The Journal of Business***, 74: 33–57.

Gennaioli, N., Shleifer, A., & Vishny, R. W. 2013. A model of shadow banking, ***The Journal of Finance***, 68: 1331–1363.

Gopalan, R., Milbourn, T., Song, F., & Thakor, A. V. 2014. Duration of executive compensation, ***The Journal of Finance***, 69: 2777–2817.

Gropp, R. & Heider, F. 2010. The determinants of bank capital structure, ***Review of Finance***, 14: 587–622.

Gropp, R., Vesala, J., & Vulpes, V. 2006. Equity and bond market signals as leading indicators of bank fragility, ***Journal of Money, Credit, and Banking***, 38: 399–428.

Hagendorff, J. & Keasey, K. 2012. The value of board diversity in banking: Evidence from the market for corporate control, ***European Journal of Finance***, 18: 41–58.

Hagendorff, J. & Vallascas, F. 2011. CEO pay incentives and risk-taking: Evidence from bank acquisitions, ***Journal of Corporate Finance***, 17: 1078–1095.

Hall, M., Mikes, A., & Millo, Y. 2013. How do risk managers become influential? A field study in two financial institutions. Harvard Business School Working Paper.

Hanson, S. G., Kashyap, A., & Stein, J. C. 2011. A macroprudential approach to financial regulation, ***Journal of Economic Perspectives***, 25: 3–28.

Harris, M. & Raviv, A. 2008. A theory of board control and size, ***Review of Financial Studies***, 21: 1797–1832.

Hau, H. & Thum, M. 2009. Subprime crisis and board (in-)competence: Private vs. public banks in Germany, ***Economic Policy***, 24: 701–751.

Hermalin, B. E. & Weisbach, M. S. 1998. Endogenously chosen boards of directors and their monitoring of the CEO, ***American Economic Review***, 88: 96–118.

Hilscher, J. & Raviv, A. 2014. Bank stability and market discipline: The effect of contingent capital on risk taking and default probability, ***Journal of Corporate Finance***, 29: 542–560.

Hilscher, J. & Şişli-Ciamarra, E. 2013. Conflicts of interest on corporate boards: The effect of creditor-directors on acquisitions, ***Journal of Corporate Finance***, 19: 140–158.

Holmstrom, B. 1982. Moral hazard in teams, ***Bell Journal of Economics***, 13: 324–340.

Houston, J. F., Lin, C., Lin, P., & Ma, Y. 2010. Creditor rights, information sharing, and bank risk taking, ***Journal of Financial Economics***, 96: 485–512.

Hovakimian, A. & Kane, E. J. 2000. Effectiveness of capital regulation at US commercial banks, 1985 to 1994, ***The Journal of Finance***, 55: 451–468.

International Monetary Fund. 2014. Risk-taking by banks: The role of governance and executive pay. In ***Global Financial Stability Report: Risk-taking, liquidity, and shadow banking: Curbing excess while promoting growth***. Washington, DC: IMF.

Jensen, M. C. 1989. Active investors, LBOs, and the privatization of bankruptcy, ***Journal of Applied Corporate Finance***, 2: 35–44.

Jensen, M. C. & Meckling, W. H. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure, ***Journal of Financial Economics***, 3: 305–360.

John, K., John, T. A., & Senbet, L. W. 1991. Risk-shifting incentives of depository institutions: A new perspective on federal deposit insurance reform, ***Journal of Banking & Finance***, 15: 895–915.

John, K., Mehran, H., & Qian, Y. 2010. Outside monitoring and CEO compensation in the banking industry, ***Journal of Corporate Finance***, 16: 383–399.

John, K., Saunders, A., & Senbet, L. W. 2001. A theory of bank regulation and management compensation, ***Review of Financial Studies***, 13: 95–125.

John, T. A. & John, K. 1993. Top-management compensation and capital structure, ***Journal of Finance***, 48: 949–974.

Kareken, J. H. & Wallace, N. 1978. Deposit insurance and bank regulation: A partial-equilibrium exposition, ***The Journal of Business***, 51: 413–438.

Kashyap, A. K., Rajan, R. R., Stein, J. C. 2008. Rethinking capital regulation. Working Paper.

Keeley, M. C. 1990. Deposit insurance, risk, and market power in banking, ***American Economic Review***, 80: 1183–1200.

Keys, B. J., Mukherjee, T., Seru, A., & Vig, V. 2009. Financial regulation and securitization: Evidence from subprime loans, ***Journal of Monetary Economics***, 56: 700–720.

King, T. B. 2008. Discipline and liquidity in the interbank market, ***Journal of Money, Credit, and Banking***, 40: 295–317.

Kirkpatrick, G. 2009. The corporate governance lessons from the financial crisis, ***Financial Market Trends***, 2009: 61–87.

Konishi, M. & Yasuda, Y. 2004. Factors affecting bank risk taking: Evidence from Japan, ***Journal of Banking & Finance***, 28: 215–232.

Laeven, L. & Levine, R. 2009. Bank governance, regulation and risk taking, ***Journal of Financial Economics***, 93: 259–275.

Liikanen Report. 2012. High-level expert group on reforming the structure of the EU banking sector. Brussels, October.

Lingel, A. & Sheedy, E. 2012. The influence of risk governance on risk outcomes – International evidence. Macquarie Applied Finance Centre Research Paper No. 37.

Macey, J. R. & O'Hara, M. 2003. The corporate governance of banks, ***Economic Policy Review***, 9: 91–108.

Martinez Peria, M. S. & Schmukler, S. L. 2001. Do depositors punish banks for bad behavior? Market discipline, deposit insurance, and banking crises, ***The Journal of Finance***, 56: 1029–1051.

McNulty, T., Florackis, C., & Ormrod, T. 2013. Boards of directors and financial risk during the credit crisis, ***Corporate Governance: An International Review***, 21: 58–78.

Mehran, H., Morrison, A., & Shapiro, J. 2011. Corporate governance and banks: What have we learned from the financial crisis? Federal Reserve Bank of New York Working Paper no. 502.

Mehran, H. & Rosenberg, J. 2007. The effect of employee stock options on bank investment choice, borrowing, and capital. Federal Reserve Bank of New York Staff Report no. 305.

Merton, R. C. 1977. An analytic derivation of the cost of deposit insurance and loan guarantees: An application of modern option pricing theory, ***Journal of Banking & Finance***, 1: 3–11.

Minton, B. A., Taillard, J. P., & Williamson, R. 2014. Financial expertise of the board, risk taking, and performance: Evidence from bank

© 2015 John Wiley & Sons Ltd

holding companies, ***Journal of Financial and Quantitative Analysis***, 49: 351–380.
Morgan, D. P. 2002. Rating banks: Risk and uncertainty in an opaque industry, ***American Economic Review***, 92: 874–888.
Nguyen, D. D., Hagendorff, J., & Eshraghi, A. 2015. Which executive characteristics create value in banking? Evidence from appointment announcements, ***Corporate Governance: An International Review***, 23: 112–128.
Nier, E. & Baumann, U. 2006. Market discipline, disclosure and moral hazard in banking, ***Journal of Financial Intermediation***, 15: 332–361.
Office of the Comptroller of the Currency. 1997. ***The Director's book: The role of a national bank director***. Washington, DC: Office of the Comptroller of the Currency.
Opler, T. C. 1993. Controlling financial distress costs in leveraged buyouts with financial innovations, ***Financial Management***, 22: 79–90.
Pathan, S. 2009. Strong boards, CEO power and bank risk-taking, ***Journal of Banking & Finance***, 33: 1340–1350.
Pettigrew, A. M. & McNulty, T. 1995. Power and influence in and around the boardroom, ***Human Relations***, 48: 845–873.
Raheja, C. G. 2005. Determinants of board size and composition: A theory of corporate boards, ***Journal of Financial and Quantitative Analysis***, 40: 283–306.
Roberts, J., McNulty, T., & Stiles, P. 2005. Beyond agency conceptualisations of the work of the non-executive director: Creating accountability in the boardroom, ***British Journal of Management***, 16: 1–22.
Ronn, E. I. & Verma, A. K. 1986. Pricing risk-adjusted deposit insurance: An option-based model, ***The Journal of Finance***, 41: 871–896.
Senior Supervisors Group. 2009. Risk management lessons from the global banking crisis of 2008. October.
Shrieves, R. E. & Dahl, D. 1992. The relationship between risk and capital in commercial banks, ***Journal of Banking & Finance***, 16: 439–457.
Smith, C. W. & Stulz, R. M. 1985. The determinants of firms' hedging policies, ***Journal of Financial and Quantitative Analysis***, 20: 391–405.
Srivastav, A., Armitage, S., & Hagendorff, J. 2014. CEO inside debt holdings and risk-shifting: Evidence from bank payout policies, ***Journal of Banking & Finance***, 47: 41–53.
Stulz, R. 2015. Risk-taking and risk management by banks, ***Journal of Applied Corporate Finance***, 27: 8–19.
Sundaram, R. K. & Yermack, D. L. 2007. Pay me later: Inside debt and its role in managerial compensation, ***The Journal of Finance***, 62: 1551–1588.
Thanassoulis, J. 2012. The case for intervening in bankers' pay, ***The Journal of Finance***, 67: 849–895.
Vallascas, F. & Hagendorff, J. 2013. The risk sensitivity of capital requirements: Evidence from an international sample of large banks, ***Review of Finance***, 17: 1947–1988.
van Bekkum, S. 2015. Inside debt and bank risk, ***Journal of Financial and Quantitative Analysis*** Forthcoming.
Walker, D. 2009. A review of corporate governance in UK banks and other financial industry entities, Consultative Document, November.
Wei, C. & Yermack, D. 2011. Investor reactions to CEOs' inside debt incentives, ***Review of Financial Studies***, 24: 3813–3840.
Weisbach, M. S. 1988. Outside directors and CEO turnover, ***Journal of Financial Economics***, 20: 431–460.

Abhishek Srivastav is a teaching fellow in Banking & Finance at Leeds University Business School. He earned a PhD from The University of Edinburgh. His research focuses on CEO compensation and bank risk-taking, especially debt-based forms of compensation.

Jens Hagendorff is a professor of finance at Cardiff University. His research focuses on the drivers behind bank risk-taking and systemic risk as well as the corporate governance and risk-return profile of banks. He was recently a visiting fellow at The Federal Reserve Bank of Atlanta and the Bank of Spain in Madrid.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 346–358

Ownership, Activism and Engagement: Institutional Investors as Active Owners

Terry McNulty* and Donald Nordberg

ABSTRACT

Manuscript Type: Conceptual
Research Question/Issue: We research two questions: First, why do some institutional investors operate at a distance from organizations seemingly acting only to "exit" and "trade" shares, while others actively engage through various means of "voice"? Second, what processes and behaviour are associated with active ownership?
Research Findings/Insights: We develop the concept of active ownership by drawing on contrasting theories and images of ownership, identifying antecedents of active ownership and distinguishing between alternative processes of active ownership.
Theoretical/Academic Implications: Alternative pathways to active ownership contrast the distant, sometimes adversarial nature of shareholder activism with an engaged, collaborative relationship between investors and corporations. Few studies examine active ownership as a process of engagement and mutual exchange between parties taking a generally longer-term perspective toward investment in the firm and its affairs. After modeling active ownership, we develop a research agenda of substantive issues ranging from market and institutional conditions, through investment organization and practice, to board and investor relations.
Practitioner/Policy Implications: Opening up the multidimensionality of engagement and relations between investors and corporations is crucial to promoting good corporate governance. Policymakers and practitioners require such knowledge when anticipating and developing adjustments to institutions of corporate governance.

Keywords: Corporate Governance, Institutional Investors, Ownership, Activism, Engagement

INTRODUCTION

The global financial crisis of 2007–09 raised questions about many aspects of the economic system. After decades of concern about how corporations govern themselves, more attention is turning to other aspects of the complex web of connections that make up the system of capital. This article examines one aspect of that system, shareholders – in particular institutional investors and their engagement with the companies in which they invest. We review a broad body of literature crossing several disciplines to develop a model of active ownership by institutional shareholders and a related research agenda. Using the model, we address the following questions: First, why do some institutional investors operate at a distance from organizations seemingly acting only to "exit" and "trade" shares while others actively engage through various means of "voice"? Second, what processes and behavior are associated with active ownership?

The literature on shareholder activism[1] addresses these questions according to the characteristics of activists, target firms, and the environment (Goranova & Ryan, 2014). However, while shareholder activism is sometimes described as a broad phenomenon (Chung & Wynn, 2014), our reflection on the literature suggests it has been treated in quite a narrow way conceptually, methodologically, and empirically. More can be done to understand institutional investor heterogeneity and related motivations, processes, and effects involved in what we term "active ownership."

Our concept of active ownership includes shareholder activism, defined as "actions taken by shareholders with the explicit intention of influencing corporations' policies and practices" (Goranova & Ryan, 2014: 1232) but extends to a wider range of institutional investor behavior, that incorporates developing relations with corporations through different influence processes and intent. This type of on-going active ownership is likely to involve mutual exchanges aimed at understanding more than change, and taking a generally longer-term perspective toward investment in the firm and its affairs. Continuing engagement of this sort does not preclude change-seeking, but it is part of the process, rather than the process itself. Defined in this way, active ownership also contrasts with passive ownership, which involves holding the shares; collecting dividends and perhaps voting, but in an undeliberated way;[2] and trading.

This article thus augments recent work on shareholder activism (Goranova & Ryan, 2014) by considering alternative

*Address for correspondence: Terry McNulty, University of Liverpool Management School, Chatham Street, Liverpool L69 7ZH, UK. Email: t.h.mcnulty@liverpool.ac.uk

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12143

pathways of investor–firm interaction. Through greater attention to processes and plurality in relationships between investors and corporations, it infuses a debate dominated by agency theory and the financial incentives of shareholders with alternative theories of shareholder motivation and action. Prime among these are stewardship theory (Davis, Schoorman, & Donaldson, 1997) and ideas of psychological ownership (Pierce, Kostova, & Dirks, 2001). Both are typically used to analyze employee relationships with the firm (Hernandez, 2012) and thus far rarely applied to the domain of institutional investors and corporate governance (for a notable exception, see Sikavica & Hillman, 2008). Hirschman's (1970) theory of exit, voice, and loyalty is also used, taking account of a recent review of work on voice within organizations (Bashshur & Oc, 2015). Drawing on Greenwood and Hinings (1996), these theoretical dimensions are set within the contemporary market and institutional context of corporate governance.

Normatively, the growing significance of shareholder engagement is emphasized by a longstanding debate about the merits and mechanisms of shareholder empowerment. It is seen as well in recent practitioner attention to investor engagement and "stewardship" post-financial crisis (Davis, Lukomnik, & Pitt-Watson, 2009; Wong, 2010) and in public policy development (Eumedion, 2011; European Commission, 2014; FRC, 2010, 2012; ORSE, 2011).

Our contributions lie, first, in clarifying contrasting views and images of ownership; second, in portraying the antecedents of active ownership; and third, in building a model of how those antecedents create pathways to diverse processes of active ownership. We then identify suggestions for future research, drawing attention to substantive issues that range from market and institutional conditions, through investment organization and practice, to board and investor relations.

IMAGES OF OWNERSHIP

What does it mean to "own" a corporation? While parts of the corporate governance literature view owners as a simple construct of value-maximizing agents, recent scholarly work and policy documents have acknowledged the heterogeneity of investors (Isaksson & Çelik, 2013; Wang, 2014; Westphal & Zajac, 2013). Ownership has special resonance in law, psychology, sociology, and organization studies, invoking contesting conceptual framings.

Ownership as Rights

In legal scholarship on property, ownership is discussed as consisting of a bundle of rights. Demsetz (1967: 348) argues: "A primary function of property rights is that of guiding incentives to achieve a greater internalization of externalities."

Owners' rights open important controversies in the corporate governance literature. Control over assets is conferred upon managers, who act as agents of the principals, that is, the legal holders of equity in the company,[3] creating an agency problem when managers work in their own rather than in shareholders' interest. The agency problem operates on the assumption that shareholders hold residual rights; that is, they face the greatest risk when a company is in insolvency, justifying a privilege of primacy in decision making.

Shareholder primacy is much disputed (Mukwiri, 2013; Stout, 2013), by drawing upon the limited nature of shareholder rights in company law, and by challenging the argument concerning residual rights. The latter point leads to a dispute concerning the residual rights of employees (and indeed other stakeholders) that arise in view of their firm-specific investments in acquiring non-transferable knowledge and skills or from social bonds developed by their commitment to the company's business. These ideas argue against shareholder primacy and the latter points us toward another conceptualization of ownership.

Ownership as Commitment

Etzioni (1991) argues that property exists on two levels of meaning, the real and the symbolic, with objective and subjective properties. The real/objective level corresponds closely to notions both of legal and equitable ownership in law and of a view of the firm based in transaction cost economics. The symbolic/subjective level, however, involves rather different assumptions, one in which the person invests emotionally and identifies with the thing "owned."

Pierce et al. (2001: 299) develop this latter idea, identifying affective and cognitive dimensions: "The core of psychological ownership is the feeling of possessiveness and of being psychologically tied to an object." Ownership has its "roots" in satisfying a need, in building an identity, and in having a sense of place (Pierce et al., 2001).[4] As we discuss later, Sikavica and Hillman (2008) invoke psychological ownership in their analysis of shareholder activism.

Owner Versus Trader

These two conceptualizations contrast with a third and increasingly common view of the ways that shareholders "own" the corporation. Ownership confers specific rights – importantly, electing directors and approving major changes in capital – to shareholders, that is, to the persons (real or legal) who hold the shares when votes are cast.[5] For large, listed corporations, shareholders change all the time, as trading in equity markets occurs and investors shift between different shares or switch asset classes (e.g., from equities to real estate). Major capital markets pride themselves on their liquidity, making trading easier. Trading-focused rights-holders are often perceived as having short-term interests, more interested in the size of capital gains possible by churning investments than in the fundamentals of the businesses in which they invest.

Universal Ownership

This "trading" stance presents a sharp contrast to "universal ownership," a concept developed by two investment managers, Monks and Minow (1995), whose investment approach agitated for change at investee companies but with larger social and economic purposes in mind. They saw logical allies in pension funds and other investors whose interests lie in long-term performance of the economy for the benefit of vsociety as a whole. With fiduciary duties to large numbers

© 2015 John Wiley & Sons Ltd

of investors over long time horizons, these "universal" investors should be interested in being more than the "trader," whose concerns end with the relative performance of one company's shares versus another. This idea was developed by Hawley and Williams (2000), who see the structure and processes in the market context separating beneficiaries from the operationalization of ownership rights. Lydenberg (2007) then sees this as justification for a greater unity of interests and action among universal owners and social investors. More recently, Lydenberg (2014) advocated seeing the fiduciary duty of such investors to engage in long-term investment for the benefit of society as a whole. Such investors form the archetype of another image of ownership: the steward.

Owner as Steward

Drawing upon ideas of a commitment-focused approach to ownership and universal ownership, policymakers encourage investors to engage with the corporations and to look at the long term. A significant move of this nature was the UK Stewardship Code (FRC, 2010; revised 2012), subsequently reflected in policy in other countries and organizations, with echoes of stewardship theory in corporate management (Davis et al., 1997). Hernandez (2012: 174) defines stewardship as the "extent to which an individual willingly subjugates his or her personal interests to act in protection of others' long-term welfare." It is pro-social action, involving cognitive and affective mechanisms as antecedents to stewardship actions.

The concept of stewardship in corporate governance posits that most managers subordinate personal interests to the good of the organization and have intrinsic rather than just extrinsic (i.e,, financial) motivations (Davis et al., 1997). It points normatively to conclusions diametrically opposed to those in agency theory, namely that managers should be trusted more than controlled, supported more than monitored. While regulators, since the financial crisis, have promoted images of stewardship, others are more skeptical, viewing the market context as one that works against steward-like behavior from investors (Reisberg, 2015), creating an "Achilles' Heel" for the project (Cheffins, 2010).

These images of ownership and the shift in the policy context raise important questions of investor and owner psychology and behavior. Set against them and the empirical heterogeneity of investors noted by Goranova and Ryan (2014), Figure 1 identifies different approaches to ownership and what this means for corporate ownership and governance. This is now explored in detail via two distinct pathways of owner behavior.

VARIETIES AND PATHWAYS OF OWNERSHIP

The distinction between "financial" and "socially motivated" activism (Aguilera, Desender, Bednar, & Lee, 2015; Goranova & Ryan, 2014; Judge, Gaur, & Muller-Kahle, 2010) encourages examination of different motivations of shareholders and how they translate into active ownership behavior. In their historical account of three overlapping social movements in the US – socially responsible investment (SRI), shareholder value, and responsible investment – Welker and Wood (2011) illustrate a variety of shareholder interests and identities. SRI emerged in the 1960s and 1970s as activists sought to pluralize "both the category of shareholders and their moral beliefs"; shareholder value "folded shareholders into a singular homogeneous category and endowed them with a singular purpose: profit" (Welker & Wood, 2011: S61). The responsible investment movement is a synthesis, emphasizing regard for economic and governance as well as social concerns under the rubric ESG. This view "converts moral into economic reason such that responsible investing will conform to the shareholder value imperative" (Welker & Wood, 2011: S58). Responsible investors take a long-term view, drawing a link between financial returns and socially and environmentally beneficial outcomes. Responsible investing translates the goals of one into the values of the other, thus revitalizing the shareholder as a fuller "person."

That typology adds greater variety, human texture and context to distinctions such as "financial" and "social" activism. Our model of active ownership explores this variation and its expression in investor behavior, distinguishing two different approaches.

The first is signified by the path labeled as (a) in the model, which splits to show that institutional shareholders, as legal owners, can exercise rights to "exit" and "voice." Investors pursuing path (a) may do so with purely financial interests and incentives in mind, as seen in cases of corporate raiders and much hedge fund activism, as Goranova and Ryan (2014) discuss. But they also include ideologically driven activists, who use their legal rights as shareholders to advance causes with limited regard for the impact on the company. Other investor behavior along path (a) can include passively following the index, trading by mathematical models, or exits made out of disapproval with current business policy, sometimes called the "Wall Street Walk" (Admati & Pfleiderer, 2009). This is displayed in the model as path (a) passes through legal ownership to "exit."

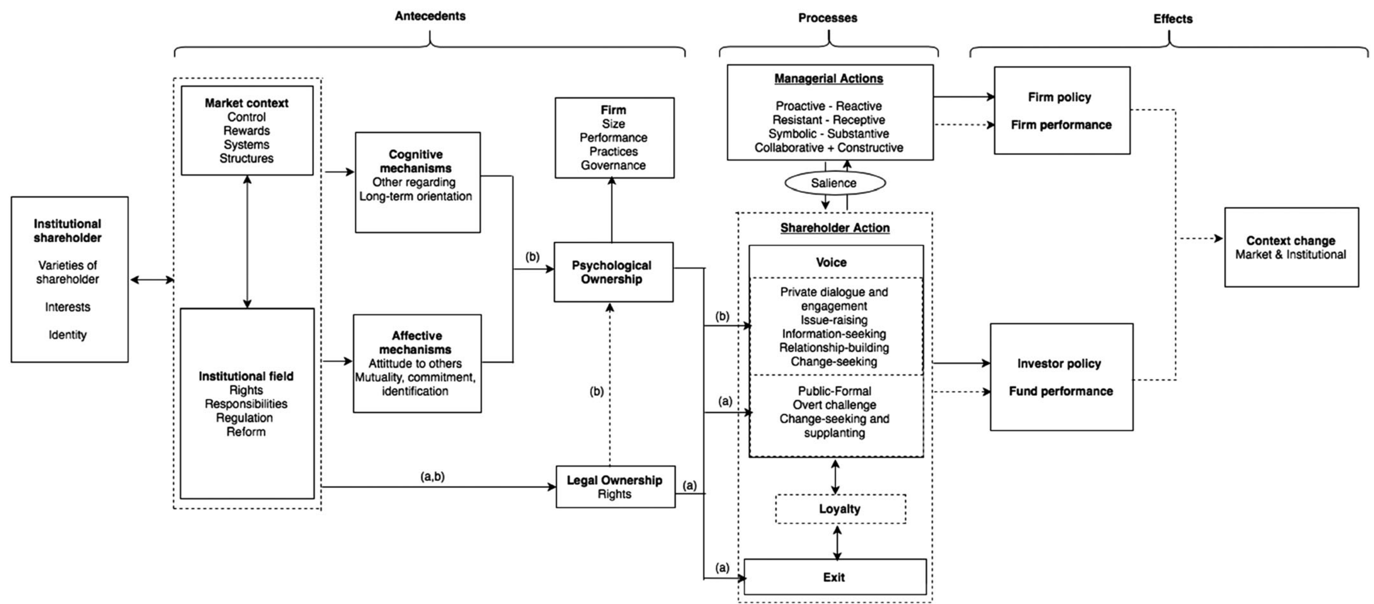
The range of behavior represented by path (a) covers a lot of investor action. In a commentary published alongside the article by Welker and Wood (2011: S67), Monks estimated that only 20 per cent of shares are held by investors who "might be thought of as real proprietors or even activist investors." However, even if it is the behavior of the majority in the market, path (a) is partial and inadequate for understanding motivations and behavior involved in active ownership, signified by path (b) in the model. Central to the difference between paths (a) and (b) is the phenomenon of psychological ownership. Considerations (cognitive mechanisms) and attitudes (affective mechanisms) make path (b) qualitatively different from path (a) in terms of investor engagement. This second approach, path (b), is our primary focus. The following discussion considers each element of the model, starting with antecedents of active ownership related to "market context," "institutional field," the "firm," and "mechanisms of psychological ownership."

ANTECEDENTS OF ACTIVE OWNERSHIP

The financial crisis provoked a reconsideration of the role of markets in corporate governance, in particular the

© 2015 John Wiley & Sons Ltd

FIGURE 1
A Model of Active Ownership



financialization of the economy (Fichtner, 2013; Mizruchi, 2010). Concerns voiced before the crisis, in particular among environmental and social activists but also corporations, about the short-term focus of investors (Aspen Institute, 2009; Bushee, 1998; Tonello, 2006) became a pressing matter of public policy work (Group of 30, 2012; Kay, 2012) and empirical analysis (Hutchinson, Seamer, & Chapple, 2015; Wang, 2014), leading to a normative debate (OECD, 2011; Pozen, 2014) and institutional changes. This section examines how changes in the market context and institutional arrangements put large investors under conflicting pressures with respect to engagement with corporations.

Market Context (Controls, Rewards, and Power)

Financial markets provide structures that shape the rewards of institutional investors as market actors, exert certain controls on their behavior, and inform development of active ownership. For reasons discussed below, it is a market context more oriented to institutional investor behavior described in path (a) rather than path (b).

Historically, equity markets developed to enhance capital formation. They did so ironically by increasing liquidity and making it easier for investors to withdraw from their investment, thus reducing the risk associated with owning company shares. Hirschman (1970) therefore saw equity markets giving emphasis to exit over voice. The more liquid the market, the more shareholders prefer exit to voice. Cox and Wicks (2011) find that reduced market liquidity is associated with greater engagement. Investors more likely to use exit rather than voice shun illiquid investments, making those companies more likely to experience investor engagement. However, like founders and family members, holders of large blocks of shares are less able to sell without adverse consequences on price, so they would prefer voice over exit (Marler & Faugère, 2010). Moreover, their inability to sell gives them a greater residual risk, helping to legitimate that voice.

By creating a way to take over and transform listed companies, equity markets also provide a vehicle to facilitate exercise of legal ownership rights, making voice more effective. Theorizing a market for corporate control, Manne (1965, 1984) set the stage for a first wave of large-scale shareholder activism, through the actions of "corporate raiders," in which control created rewards for activists (Croci, 2007). Empirical studies question the effectiveness of this method of control (e.g., Walsh & Kosnik, 1993), and the critique has intensified since the financial crisis (e.g., Widmer, 2011).

The period from the late 1990s through the financial crisis saw development of new investment vehicles, in particular hedge funds and sovereign wealth funds (Aguilera, Capapé, & Santiso, ; Bebchuk, Brav, & Jiang, 2015), able to channel large investments into equity markets. In addition, finance became an increasingly global market. Continental European exchanges emulated US practices to attract new company listings and investment funds.

Contributing to the evolving backdrop are changes in equity market structures that have increased liquidity and changed practices of investors. One is the consolidation of exchanges, bringing small orders together in one place and facilitating cross-border trading. Another is the development of off-exchange platforms creating "dark pools" of liquidity in which large shareholders could enter or exit positions more easily without adverse price implications (Kwan, Masulis, & McInish, 2015).

Another structural change is the growth of index-tracking. Index-tracking began long before the financial crisis, but the crisis accelerated demand for asset diversification at a low cost. Seeing their strategic direction in cost leadership, index-trackers have incentives that argue against engagement, a phenomenon decried by one of the industry's founders (Bogle, 2011). Practice changes, including use of

© 2015 John Wiley & Sons Ltd

derivative instruments, laid the groundwork for investment strategies offering abnormally positive and notionally riskless returns that some hedge funds promised. Short-selling and share lending, often by passive, index-tracking investors looking for extra yield, have become a central part of equity trading. Bans on short-selling enacted in 2008, early in the financial crisis, may have brought little reduction volatility and only served to reduce liquidity and thereby price discovery (Curtis & Fargher, 2014).

Rewards in investment can also shape the propensity to engage. Most investment managers are rewarded on a combination of fees levied on portfolio size and on the capital gains achieved, creating incentives for fund growth (e.g., winning new mandates) and investment performance. The balance between these two types of rewards reflects the fund's investment style and function. Those with specific fiduciary duties (e.g., pension funds) may have other responsibilities, which will affect how they choose their investments and what attitude they adopt towards engagement.[6]

Some changes, including the market for corporate control, derivatives, short-selling and other moves to increase liquidity, arose from enabling legislation or regulatory developments. They have diminished these justifications for engagement, creating disincentives for long-term investing and active ownership (Isaksson & Çelik, 2013). These forces are in contrast to non-market institutional forces more inclined post crisis to emphasize active ownership.

Institutional Field

Institutional arrangements shape investor engagement. These arrangements include the formal rights and responsibilities accruing from share ownership; semi-formal, voluntary codes; and informal, taken-for-granted assumptions about the purposes of investment management.

Company law establishes the basis of share ownership and associated rights. While rights vary in detail by jurisdiction, in general share ownership entitles the holder to elect directors, approve material changes in the capital, and decide on major changes in direction. It does not give the holder rights over the assets of the business, while limited liability puts a ceiling on shareholders' responsibility for debt.

Policy in the US since the 1970s has favored the market for corporate control over direct regulation of investor engagement. Elsewhere, semi-formal institutions played a formative role, and developments in the UK often gave a lead to other jurisdictions. While the Cadbury Report (1992) focused mainly on corporate boards, it also called for enhanced interaction with shareholders, and in particular with institutional investors, which were deemed best able to monitor corporate management and prevent excess. Subsequently, the Hampel Report (1998) and a government review of institutional investment (Myners, 2001) articulated investor–corporate interaction.

After protracted debate, the European Union adopted a Shareholder Rights Directive in 2007, enhancing the ability of shareholders to vote on a cross-border basis, solidifying ownership rights, encouraging engagement, and bolstering legal ownership (Eckbo, Paone, & Urheim, 2010; Rose, 2012). The EU has also moved to give investors a right to vote on corporate remuneration policies (European Commission, 2014). Another institutional change, in pension reform, led to changes in market structure, not least the reduced importance of defined-benefit, final-salary pension arrangements at many companies and their replacement with defined-contribution pensions based in part on life insurance contracts (Holzmann & Palmer, 2006).

These shifts led to greater shareholder entitlement to engage. Conversely, they encouraged a relative flow of investable funds toward the new investment vehicles and away from the archetypal long-term investors in pension funds. Pension funds themselves have diversified into newer, "alternative" investments. The institutional context thus favored shareholder challenge to management (activism) while diminishing the role of investors that might be identified as having long-term investment horizons.

With the onset of the financial crisis came a policy shift to promote shareholder engagement. The UK Stewardship Code for investors (FRC, 2010) called attention to the fiduciary duties of institutional investors to their beneficiaries. A review for the UK government of short-termism in markets (Kay, 2012) highlighted the lengthening supply chain in investment, and that institutional investors were one of a series of intermediaries at some distance from the end-investor and therefore the ultimate principal in the principal–agent relationship.

Countries, including Germany, France, Japan, the Netherlands, and Italy, followed suit, and EU green papers (European Commission, 2011, 2013) raised similar questions, which were incorporated in a proposal to revise the Shareholder Rights Directive (European Commission, 2014). In the US, regulation arising from the Dodd-Frank Wall Street Reform and Consumer Protection Act gave shareholders voice over executive pay ("Say on Pay") and revived attempts to make it easier for them to present resolutions to the annual meeting ("proxy access").

These policy moves (though less directly those in the US) envisage what we see as path (b) ownership, that is, ongoing engagement by institutional investors with investee companies. The revised UK Stewardship Code (FRC, 2012) calls for "purposeful dialogue" to promote "understanding," alongside their monitoring of corporate performance. This approach continues to legitimate shareholder primacy but it also encourages ongoing engagement and stewardship, rather than just relying on episodic activism and ultimately the market for corporate control.

Policy moves differ in detail but they embody assumptions about ownership and its rights and encourage institutional investors to act in ways similar to the "universal owner." This view is at considerable distance from the image and practice of the self-regarding, value-maximizing trader in path (a), with financial preferences for capital gains sooner rather than dividends later.

Thus, while developments in policy and institutions have sought to pull investors toward engagement, pressure from markets seems to push them toward trading (Aguilera & Jackson, 2003; Davis, 2008, 2010). The heterogeneity of investors and their motivations mean they may respond in different ways to these pressures, whether through voice or exit. To understand better the processes and prospects of engagement, we need to understand the link between

© 2015 John Wiley & Sons Ltd

shareholders' legal ownership and what makes them more deeply engaged.

Mechanisms of Psychological Ownership

Having established a relatively clear route, path (a), from the market and institutional context to legal ownership to exit or activism, we turn now to the more complex path (b), which leads through psychological ownership to different investor behavior. The policy moves outlined above seek to alter the behavior of investors in the direction of path (b) using incentives and invective. To understand what may be involved in a more engaged approach to ownership, the next section examines stewardship theory, beginning with the cognitive and affective mechanisms that underlay stewardship behavior (Hernandez, 2012). At this point, the model broadens beyond agency theory and assumptions of shareholder activism to offer a very different potential for institutional investor behavior.

Examining employee stewardship, Hernandez (2012: 181, 183, 185) identifies cognitive and affective mechanisms that develop "other-regarding" behavior, a "long-term communal welfare" and "affective commitment through mutual social exchange." These mechanisms create an "internal drive" in individuals to psychological ownership. In contrast to agency theory, which focuses on ownership and control as a source of power expressed through legal ownership supported by residual rights, psychological ownership is a cognitive-affective construct creating "a personal motivation to protect the object of ownership" (Hernandez, 2012: 182).

Cognitive. In portfolio theory and practitioner accounts (cf. Bogle, 2011; Hutchinson et al., 2015), the motivations in institutional investment are often described in financial terms, following a rational perspective, dominated by self-interest and reinforced by financial analysis, asset allocation, and risk-reward calculations. This chimes with the priority given to profit in the shareholder value movement (Welker & Wood, 2011). While such cognitive mechanisms may be calculative, focused on short-term goals, and self-serving, there are alternatives. Hernandez (2012: 183) proposes that stewardship cognition depends on defining one's self in relation to others, engaging in "pro-organization" behaviors for the long-term benefits of others.

Affective. Affect is "sense of connection with others" arising through mutual social exchange and prompting stewards to influence the collective in a positive way (Hernandez, 2012: 175). Stewards have an emotional tie to the beneficiaries of their actions as well as a deliberative one. Stewards show a sense of commitment, again for the long term. Affective mechanisms build connections and emotional attachment to the organization. Such regard for others and long-term orientation chime with the ideas of responsible investment, as shareholders seek to encourage companies not to "externalize their costs onto society" while "promoting the interests of the long-term shareholder" (Welker & Wood, 2011: S65).

Structural factors such as control processes and reward systems influence development of cognitive and affective mechanisms. This suggests the interaction and balance of cognitive and affective is dependent on the market and institutional context, the incentives and controls they create, and on the business policy choices and processes of the investors.

In our model, the dotted line from legal to psychological ownership indicates the potential for investors to evolve in their behavior as they develop some of the cognition and attitudes associated with psychological ownership. This can occur as institutional investors adapt their investment principles, their portfolios, and their practices of voice to mix principles of shareholder value with principles of responsible investment.

From Legal to Psychological Ownership and Stewardship

In Hernandez (2012) and Pierce et al. (2001), psychological ownership is seen among employees when they are not in any sense legal owners. Hernandez (2012) sees psychological ownership arising as an other-regarding, long-term perspective from the cognitive side combined with the affective commitment arising from mutual social exchange. Both arise from control systems that foster collaboration and personal responsibility and reward systems providing intrinsic motivations.

Sikavica and Hillman (2008) extend this concept into the world of shareholders, arguing that psychological ownership is "the natural complement to legal ownership." Their discussion stops short of accounting for the complexity and varieties of internal dynamics of institutional investors or how the market and institutional dynamics interact with them.

In the case of investment institutions, and with reference to the model, their legal ownership is not disputed; what differentiates activism along path (a) from the ongoing relationship of path (b) is that investors possess psychological as well as legal ownership. Exploring difference between paths (a) and (b) as reflected in processes and behavior of investors is the subject of the next part of the model and section of the paper.

FROM ANTECEDENTS TO PROCESSES OF ACTIVE OWNERSHIP: SHAREHOLDER VOICE, EXIT, AND LOYALTY

The progression from "antecedents" to "processes" of active ownership is framed by Hirschman's (1970) theoretical framework of exit, voice, and loyalty. It suggests that investors have a limited range of actions open to them, often interpreted as exit through selling shares, loyalty through holding shares, and voice through shareholder activism (Goranova & Ryan, 2014).

The model identifies two distinct pathways to institutional investor "voice" distinguished by different relationships between corporate managers and institutional investors, different investor motivations, and serving different functions. While path (a) in our model may proceed directly to "exit," it may also lead to shareholder activism, an episodic approach in which investors voice specific change-led intent. Activism so conceived is primarily self-interested, may be financially or ideologically motivated, and with short-term objectives. By contrast, path (b) involves interaction underpinned by concerns and attitudes that privilege the welfare and benefits beyond the self in favor of a wider group of "others." This stewardship orientation can underpin ongoing relationships

© 2015 John Wiley & Sons Ltd

and purposeful dialogue aimed at promoting mutual understanding for aims that are other-regarding and embodying a long-term orientation. As the paths are defined by processes not social and financial ideologies *per se*, either path could be taken by a wide range of investment organizations.

Within the distinction between paths (a) and (b), different conceptual and empirical relationships between loyalty, exit, and voice become more apparent. Hirschman's discussion of the framework in a corporate context implies that the more liquid the market in shares, the more likely exit will be preferred to voice. Voice requires effort, can be costly, and may require coordination with others. Exit can be an individual decision and accordingly: "The presence of the exit alternative can … tend to *atrophy the development of the art of voice*" (Hirschman, 1970: 43, original emphasis). But Admati and Pfleiderer (2009) show how exit can be a form a voice and have disciplinary effects on corporate management, especially when pay is tied to the share price.

Active ownership, in particular along path (b), involves loyalty, which is positioned centrally in the model and with a permeable boundary to exit on the one hand and voice on the other. Following Bootsma (2013), loyalty contributes to the "interplay" or "balance between exit and voice." Voice "means that shareholders exchange their views with the corporation. It involves interaction, a dialogue with the management of the corporation" (Bootsma, 2013: 117). Voice and loyalty interact through thoughtful hold decisions, employed by engaged institutional investors not through the "blind loyalty" in the passive holding of shares, as in low-cost index-tracking, but through reasons to be loyal in preference to exercising exit. Loyalty reinforces the predisposition to exercise voice and counteracts the presumed preference for exit in liquid markets. Echoing the preceding discussion of psychological ownership, loyalty involves some form of attachment to the corporation. Bootsma (2013) connects stewardship behavior and voice by distinguishing between "true" and "faux voice." "Faux voice" is self-interested, superficial engagement, while true voice is calculated behavior with some long-term considerations.

These conceptual developments and nuances highlight the diverse behavior and implications implied by paths (a) and (b). Path (a) allows for voice to be expressed as shareholder activism that is targeted at incumbent managers and boards, problem-focused and change-oriented. Much of the shareholder activism literature is cast in this image of self-interested shareholders bringing pressure to bear on companies in light of their interests, power, and identities (Goranova & Ryan, 2014). Along path (b) voice has a different tenor and behavioral expression, underpinned by a contrasting approach to self-interest, identification with the interests of others, and active engagement over time. To explore this distinction further, it is necessary to probe behavior involved in shareholder action.

PROCESSES OF INVESTOR–FIRM INTERACTION

Our model of active ownership involves the interaction of corporate managers and institutional investors. Central to our concerns is shareholder voice as expressed along paths (a) and (b).

Shareholder Actions

Empirical analyses tend to focus on voice that reaches public attention, whether through the voting records of institutional investors (Conyon & Sadler, 2010), shareholder resolutions proposed to company annual meetings (Rehbein, Logsdon & Van Buren, 2013), or hostile actions taken by disgruntled hedge funds that gain media attention (Katelouzou, 2013). These forms of shareholder voice are evident in path (a) and what we term activism, an investor-led, episodic approach with specific change-led intent. Cases in which investors confront firm managements or boards with specific change requests are the least ambiguous exercise of voice. The investor may be following path (a) directly, seeing immediate benefits from the firm's agreement to increase the dividend, change the chief executive, or abandon a planned acquisition. The investor's intent would then be guided by self-regarding, short-term considerations. Such actions are not necessarily detrimental to the company and its long-term prospects. Studies provide equivocal evidence that the short-termism of investors is incompatible with long-term benefits for the firm (Bebchuk et al., 2015; Brav, Jiang, Partnoy & Thomas, 2008a; Buchanan, Chai & Deakin, 2014; Katelouzou, 2013) and analyses (Coffee & Palia, 2014; Schneider & Ryan, 2011; Sharfman, 2015; Venkiteshwaran, Iyer & Rao, 2010).

Investors may also work together to increase their salience when confronting management. Crespi and Renneboog (2010) and Sauerwald and Peng (2013) show how coalitions of shareholders can effect changes in corporate management in confrontations with investors seeking change, what we have called path (a) interventions.

By contrast, along path (b), the exercise of shareholder voice unfolds in a very different manner, whereby voice is expressed through engagement between shareholders and managers over time. Such engagement accommodates plural actors pursuing a mix of principles, logics, and ideologies. As an expression of active ownership, path (b) describes shareholders engaging directly with management in a process that involves challenge and change of mutual benefit or at least accommodation. The process can involve, even begin with, mechanisms of shareholder voice, such as voting and resolutions, but it also involves private dialogue, often over a considerable time.

Such corporate–investor engagement is attributed to various systems of corporate governance around the world as a *modus operandi*, but it is not as well recognized in the literature because its private nature prevents much empirical study. Martin, Casson, and Nisar (2007) describe different forms of interactions and how umbrella organizations of investors orchestrate interactions with companies in the UK, paying particular attention to traditional investors in insurance, pensions, and collective investment. Martin et al. (2007: 81) categorize such meetings as "routine" and "extraordinary," where the latter tends to be issue-led and the former information exchanges and maintaining relationships. A current expression of the desire to foster a return to more of this "routine" approach to ownership can be seen in the Stewardship Code, a cause that has been criticized as harking back to the past (Cheffins, 2010; Reisberg, 2011).

Engagement of the sort practiced in path (b) is also evident in the strategic approach to advocacy by shareholders who follow a social agenda. Logsdon and Van Buren (2009) and

© 2015 John Wiley & Sons Ltd

Rehbein et al. (2013) use data from the Interfaith Center on Corporate Responsibility (ICCR), a coalition of shareholder activist groups in the US, to focus on dialogue. This occurs "when corporations and shareholder activist groups mutually agree to engage in ongoing communications to deal with a serious social issue as an alternative to the formal vote on a shareholder resolution" (Logsdon & Van Buren, 2009: 354). Both studies depict dialogue as a process that occurs in private and affords investors and corporation an opportunity for a relationship of mutual understanding and benefit over time. Such a relationship involves both parties being committed to negotiated solutions and coming to agreement on common principles of corporate practices and policies.

Goodman, Louche, van Cranenburgh, and Arenas (2014) go beyond Logsdon and Van Buren (2009) to examine the dynamics of voice and exit. For their study Goodman et al. (2014) eschew a focus on certain methods and outcomes in favor of an analysis of the engagement process as a whole including the "dynamics of the voice and exit options." Through an inductive case study approach of seven engagements on social, environmental, and ethical issues by three religious organizations, they model shareholder engagement as occurring in four procedural stages: issue-raising; information search and commencement of communication with the company; change-seeking using a range of methods; and outcomes, which may be satisfactory or unsatisfactory. Goodman et al. (2014) conclude that the dynamics of voice and exit differ in such processes of engagement: shareholders did not base their exit and voice decisions on economic considerations but political ones, using voice to further their beliefs and mission in society. They did not use the "silent exit" option, as being a comparatively small shareholder. If exit is used at all, divestment is combined with public statements (voice) that serve political argument. In contrast to Hirschman (1970), for Goodman et al. (2014: 208), voice and exit are "dynamic, mutually reinforcing and not necessarily sequential." Divestment may indeed be accompanied by continuing external engagement.

Managerial Actions

The preceding discussion approaches the issue from the point of view of shareholders. Of course, paths (a) and (b) imply very different situations for corporate management. It is important to also examine how managers behave in processes of shareholder voice and active ownership.

Goranova and Ryan (2014) suggest that management may be proactive or reactive, resistant or receptive. If receptive, the management response may be symbolic or substantive. Firms may decide not to listen, that is, not to engage with shareholders, or engage in an insincere, symbolic way (Westphal & Zajac, 1998) that does not allow a change in firm direction and signals rejection to the observant investor.

These categorizations depict the variety of responses to voice along path (a). We expand these categories, especially in the light of path (b), with dialogue as a form of managerial response that can open up a collaborative *and* constructive dynamic between investors and managers seeking to develop mutual understanding and benefits.

How firms react will depend on the salience of the voice. Drawing on the three attributes of stakeholder salience in Mitchell, Agle, and Wood (1997), Gifford (2010) studies the legitimacy, power, and urgency of shareholder engagement practices within three sizeable institutional investor organizations, Hermes and Insight Investment in the UK and the US-based Calvert. Gifford (2010) identifies that a strong business case and the values of the managers of investee companies are likely to be the most important contributors to shareholder salience. Similarly, Rehbein et al. (2013) find that corporate managers are more likely to engage in dialogue with shareholder activists when the firm is larger and more responsive to stakeholders, when the CEO is the board chair, and when the firm has a relatively low percentage of institutional investors. Set within resource dependency theory, the study draws attention to a positive relationship between managerial uncertainty and shareholder salience.

These findings and theoretical explanations remind us that paths (a) and (b) imply very different situations for corporate management. In terms of process, a public conflict backed by ownership size, path (a) may provoke a managerial response that is reactive and resistant. The process is an overt conflict and power-play likely to end up with winners and losers. By contrast, along path (b), processes of dialogue and engagement suggest a different basis of salience, one that is less rooted in power and more in the legitimacy of the issue and the unfolding mutuality. By acknowledging the challenge of activists or the information-seeking and dialogue, the firm legitimates investor voice; indeed, reasons for declining suggestions may be sufficiently compelling that they persuade the investor to alter its view and policy. However, in acknowledging and accepting an investor's position, the firm alters its stance and enacts change. Through the interaction, and through iterated interactions, both cognitive and affective mechanisms may come into play, deepening the bond of psychological ownership. The process of dialogue and engagement opens up space for a response and relationship that is more collaborative and constructive.

Such processes are dynamic and informed by the outcomes. As Goodman et al. (2014) observe, investors will not necessarily engage in ongoing dialogue without some sense of progress. In conditions of psychological ownership but an unresponsive firm, the investor may choose to exit, though with regret, or hold the shares either through blind loyalty or with loyalty diminished by the lack of acknowledgement. The investor with diminished loyalty may also postpone the exit decision while searching for alternatives, as cognitive processes dominate over affect. In our model, loyalty meditates the movement from voice to exit, as Bootsma (2013) proposes. We signify this in the model by the dotted line around loyalty.

FROM PROCESSES TO EFFECTS AND A WIDER RESEARCH AGENDA

The Goranova and Ryan (2014) review identifies "outcomes" of shareholder activism at firm, investor, and societal levels. Their review and our search identify studies each with interesting findings that allude to effects of financially oriented shareholder activism on corporate policy, corporate performance, and investment performance (Becht, Franks, Grant, & Wagner, 2015; Brav et al., 2008a; Brav, Jiang, Partnoy &

© 2015 John Wiley & Sons Ltd

Thomas, 2008b; Filatotchev & Dotsenko, 2015; Gantchev, 2013).

Welker and Wood (2011) argue that financially motivated activism of US corporate raiders in the 1970s and 1980s unleashed radical changes at firm level and business logics and structures worldwide. Other studies suggest social activists can influence corporate policy on social or environmental affairs (Rehbein et al., 2013). Voice acknowledged and accepted can lead to changes in firms, their performance (financial, reputational, social, etc.), practices, governance arrangements, and reputation. However, these are fragments of insight, providing a partial, equivocal view of significant "outcomes" of the relationship between shareholding and corporate governance. We propose our model of active ownership to stimulate further research into processes, outcomes, and effects of active ownership in ways that relate to fundamental questions of why, for whom, and how corporate governance matters.

Aguilera et al. (2015: 487) suggest four objectives for effective corporate governance concerning: (1) protection and enforcement of shareholder rights through managerial accountability; (2) mediation of different interests and demands of internal and external stakeholders; (3) transparent disclosure; and (4) provision of strategic and ethical guidance. Our model of active ownership, especially the process whereby shareholders engage directly with management in a process of dialogue for mutual benefit, path (b), seems pertinent to the first, second, and fourth of those objectives. Concerning the third, close, interpersonal relationships would seem to involve deeper transparency than those seen in the formalities of public disclosure. If the processes and behavior associated with path (a), which include trading shares or the episodic form of activism, are actually the dominant mode of action by shareholders, then a host of questions arise. They concern the meta-theme of corporate governance change throughout the breadth and depth of relations that make up the system of corporate governance. By way of indication, a substantive research agenda and related questions are raised below covering the interplay of markets and institutions, plural actors, their relations, resources, and expression of interests and power.

Market and Institutional Context

Has the financial crisis signaled a turning point in equity capital markets, in policy, practice, or purpose? Does the investment industry serve or subjugate financial and social goals? Do more liquid markets protect investors but also point them toward self-regarding behavior and a short-term orientation? If concepts of shareholder value and primacy have become institutionalized in the neoliberal market economies of the UK and US (Lok, 2010; Lounsbury, 2008) and encouraged short-termism (Barton & Wiseman, 2015), are these major obstacles to psychological ownership affecting movement along path (b)?

Active ownership has, since the financial crisis, become embodied in policy initiatives in many countries. That does not mean that such a stance is common among investors or easy to achieve. Current institutional arrangements embed assumptions of shareholder primacy and agency theory even as they advocate stewardship, with its purposeful dialogue and mutual understanding. Through its model, this paper has sought to theorize what is involved in stewardship, and illustrates that in using path (b). By doing so, we show the challenge facing policy. Path (a) is the dominant behavior in the market, and any change to path (b) is a complex process that will need to evolve over time. It faces hurdles imposed by a market context created in part by technologies and encouraged by policy and other institutional forces striving for valuable outcomes in domains other than corporate governance. The suggestion of funds evolving to cover financial and responsible investment imperatives and preparing and taking long-term investment is a sign of some progress in that evolution, but it remains to be seen how far and fast that process will go. Market dynamics suggest that ownership will continue to have many different expressions, so the question is more about tendencies and what this means for who benefits and what this means for the long and short term. An empirical agenda directed at identifying emergent practices and policies that encourage investors along the path of active ownership (path (b)) is important for future research in corporate governance.

Universal Owners and Funds of Funds

The pension funds run by the giant corporations of the 1950s and 1960s, or by giant trade unions of the same period, are now largely closed to new members. The market context we describe suggests considerable pressure for disengaged share ownership, even among the pension funds whose liabilities call out for assets with a long-term horizon (Tilba & McNulty, 2013). The patient capital of Warren Buffett is a model few if any have followed, or could. Much of the new money from those end-investors flows not into such funds, but into the funds-of-funds, detaching ownership even further from control by the end-beneficiary, with the consequence of greater intermediation. It may be a laudable goal to set policy to persuade institutional investors to serve the whole economy as a universal owner would. But are such prescriptions impractical in drawing on an idea associated with what seems to be a dying class of investor? Is policy also putting shareholders on a pedestal at a time when many voices within the policy framework are questioning unintended effects of the pursuit of shareholder value and whether the primary purpose of corporations is to serve investor interest?

Asset Firm Management

How do asset management organization and specialization relate to paths (a) and (b)? Some asset management firms organize themselves internally with investment selection (that is, the buy-sell-hold decision) conducted by one category of employees (the fund manager), while the proxy voting decision is done by another (the governance) department. These correspond to the exercise of exit and voice, but crudely so. Both representatives of the investor may meet corporate managers, sometimes separately, while others use processes to coordinate or collaborate concerning such contact. Corporate officers tell stories frequently of contradictory conversations with the two contact types. How do these combinations affect understanding on both sides?

© 2015 John Wiley & Sons Ltd

Shareholder Coalitions

In cases of concerted action, how do inter-organizational processes help or hinder development of active ownership? What happens when other-regarding, long-term oriented investors with strong psychological ownership collaborate with self-regarding, short-term focused legal owners? What effects does each have on the other?

Shareholder–Company Interaction

More formal interactions (e.g., shareholder resolutions, voting) are often supplemented with semi-formal ones (e.g., roadshows) and informal ones (dinners, one-on-one meetings), with increasing intimacy (Marston, 2008). The corporate governance literature is suspicious of close ties, as Roberts, McNulty, and Stiles (2005) observe. But intimacy may nurture affective responses in the face of calculative, rational, and procedural investment decision making. Research could help to identify the feedback loops between methods of voice and development of psychological ownership.

Board–Shareholder Interaction

How do boards relate to shareholders and how does that relationship affect the transition from path (a) to path (b)? The pathways of active ownership primarily accord to processes and related patterns of behavior. Inherent within the contrast between the distant or sometimes adversarial vnature of path (a) and the engaged, collaborative nature of path (b), are questions about relationships and, in particular, spirals of relationship building and decline. There are few studies of this yet, but it is an important area for development.

CONCLUSIONS

The financial crisis of 2007–09 and the role that corporate governance played in it make clear that we still have much to learn (Ahrens, Filatotchev, & Thomsen, 2011). Investors and corporations sit at the centre of the corporate governance system and we need to better understand how these two sets of actors work with and against each other. There is much more to be done to understand cognitive, affective, and behavioral aspects underlying relations of distance and closeness implied by pathways which constitute the model of active ownership in this article. For scholars to prise open the multidimensionality of engagement and relations of trust and distrust between key institutions and actors is crucial if the field is to engage with the concerns of good corporate governance. Relationships need also relate to formal institutional arrangements, for example, the proxy access reform in the United States – giving long-term shareholders greater ability to nominate directors – is a counterpoint for Swedish law, in which nomination committees are external to the board and comprise directors and representatives of blockholders (cf. Dent, 2012). The former is confrontational and impersonal; the latter is collaborative and personal but privileges one class of investor over others. Such developments open possibilities for new approaches to illuminate the paths to active ownership.

Practitioners need to understand those relationships empirically and theoretically if they are to make informed choices about how they should work together. Policymakers require such knowledge, too, to anticipate how any adjustments to the formal institutions of corporate governance may work, and to realize they will have limitations as well as possibilities.

ACKNOWLEDGEMENTS

We thank Eleanor McNulty for her technical assistance in preparing this paper and CGIR Associate Editor Ruth Aguilera and the reviewers for helpful comments.

NOTES

1. For a brief discussion of the methods used in the review, see Appendix A.
2. These are different from, though similar in a way to, active and passive portfolio management, where the former means deliberate selection of investment and the latter investing according to an *a priori* rule, as in index-tracking.
3. Legal scholarship sometimes draws a distinction between "legal" and "equitable" ownership based on whether the owner is afforded rights over the assets or rights only over the proceeds of the assets (Glackin, 2011; Hohfeld, 2014). In common use in corporate governance the two concepts are often conflated. In this article, "legal ownership" means legal rights over the equity, and the bundle of rights is limited in company law.
4. A similar mix of cognitive and affective mechanisms appears in scholarship concerning the "engagement" of consumers with brands (Brodie, Hollebeek, Jurić, & Ilić, 1917).
5. This is a slight simplification: In many countries shares are voted by the holder on a "record" date some time before the shareholders' meeting.
6. Since the financial crisis, the once-ubiquitous 2-and-20 formula used by hedge funds (two per cent of assets under management and 20 percent of capital gains) has come under pressure, mainly through changes in the percentages rather than the structure. In banking, regulators have sought to move director-level remuneration to a longer time horizon and include "clawbacks." Such moves featured less prominently in asset management.

APPENDIX A: Methods

This article was developed on the basis of a number of distinct but related strands of literature review and analysis using the Web of Science database involving a focused search for peer-reviewed articles using institutional investor* or shareholder* with engage*, activis* or steward* in their topics or titles. The search was restricted to shareholder actions, rather than activist groups in general. We looked specifically for empirical studies, major reviews, seminal theoretical contributions and conceptual frameworks across the range of disciplines in corporate governance studies.

The search for "institutional investor" generated the largest group of papers (topic = 2,441) and (title = 522). "Shareholder activism" generated 430 references while "shareholder engagement" generated 128 references. Combining the "topics" "institutional investor" and "activism" generated 237 references. All these were reviewed, along with an additional 16 references generated when "engagement" was included as a topic in the search. Further articles added when the "financial crisis" and shareholder activism were combined in the

© 2015 John Wiley & Sons Ltd

search, bringing the total to 292 papers. After filtering for duplicates, 188 articles were identified for more detailed examination.

REFERENCES

Admati, A. R. & Pfleiderer, P. C. 2009. The 'Wall Street Walk' and shareholder activism: Exit as a form of voice, ***Review of Financial Studies***, 22: 2645–2685.

Aguilera, R. V., Capapé, J., & Santiso, J. forthcoming. Sovereign wealth funds: A strategic governance view, ***Academy of Management Perspectives*** in-press.

Aguilera, R. V., Desender, K., Bednar, M. K., & Lee, J. H. 2015. Connecting the dots: Bringing external corporate governance into the corporate governance puzzle, ***The Academy of Management Annals***, 9: 483–573.

Aguilera, R. V. & Jackson, G. 2003. The cross-national diversity of corporate governance: Dimensions and determinants, ***Academy of Management Review***, 28: 447–465.

Ahrens, T., Filatotchev, I., & Thomsen, S. 2011. The research frontier in corporate governance, ***Journal of Management and Governance***, 15: 311–325.

Aspen Institute. 2009. ***Overcoming short-termism: A call for a more responsible approach to investment and business management***. Available at: http://www.aspeninstitute.org/sites/default/files/content/images/BSPonlineBroch.pdf (accessed 9 October 2015).

Barton, D. & Wiseman, M. 2015. Perspectives on the long term: What will it take to shift markets and companies away from a short-term way of thinking? ***McKinsey Quarterly***. Available at: http://www.mckinsey.com/insights/leading_in_the_21st_century/perspectives_on_the_long_term (accessed 9 October 2015).

Bashshur, M. R. & Oc, B. 2015. When voice matters: A multilevel review of the impact of voice in organizations, ***Journal of Management***, 41: 1530–1554.

Bebchuk, L. A., Brav, A., & Jiang, W. 2015. The long-term effects of hedge fund activism, ***Columbia Law Review***, 115: 1085–1156.

Becht, M., Franks, J., Grant, J., & Wagner, H. F. 2015. ***The returns to hedge fund activism: An international study***. European Corporate Governance Institute (ECGI) Finance Working Paper No. 402/2014.

Bogle, J. C. 2011. The clash of the cultures, ***Journal of Portfolio Management***, 37: 14–28.

Bootsma, B. 2013. An eclectic approach to loyalty-promoting instruments in corporate law: Revisiting Hirschman's model of exit, voice, and loyalty, ***Erasmus Law Review***, 6: 111–130.

Brav, A., Jiang, W., Partnoy, F., & Thomas, R. S. 2008a. Hedge fund activism, corporate governance, and firm performance, ***The Journal of Finance***, 63: 1729–1775.

Brav, A., Jiang, W., Partnoy, F., & Thomas, R. S. 2008b. The returns to hedge fund activism, ***Financial Analysts Journal***, 64: 45–61.

Brodie, R. J., Hollebeek, L. D., Jurić, B., & Ilić, A. 2011. Customer engagement: Conceptual domain, fundamental propositions, and implications for research, ***Journal of Service Research***, 14: 252–271.

Buchanan, J., Chai, D. H., & Deakin, S. 2014. Agency theory in practice: A qualitative study of hedge fund activism in Japan, ***Corporate Governance: An International Review***, 22: 296–311.

Bushee, B. J. 1998. The influence of institutional investors on myopic R&D investment behavior, ***The Accounting Review***, 73: 305–333.

Cadbury, A. 1992. ***Report of the Committee on the financial aspects of corporate governance***. London: Gee.

Cheffins, B. R. 2010. The Stewardship Code's Achilles' heel, ***Modern Law Review***, 73: 1004–1025.

Chung, H. H. & Wynn, J. P. 2014. Corporate governance, directors' and officers' insurance premiums and audit fees, ***Managerial Auditing Journal***, 29: 173–195.

Coffee, J. C., Jr. & Palia, D. 2014. ***The impact of hedge fund activism: Evidence and implications***. European Corporate Governance Institute Law Working Paper No. 266/2014.

Conyon, M. & Sadler, G. 2010. Shareholder voting and directors' remuneration report legislation: Say on pay in the UK, ***Corporate Governance: An International Review***, 18: 296–312.

Cox, P. & Wicks, P. 2011. Institutional interest in corporate responsibility: Portfolio evidence and ethical explanation, ***Journal of Business Ethics***, 103: 143–165.

Crespi, R. & Renneboog, L. 2010. Is (institutional) shareholder activism new? Evidence from UK shareholder coalitions in the pre-Cadbury era, ***Corporate Governance: An International Review***, 18: 274–295.

Croci, E. 2007. Corporate raiders, performance and governance in Europe, ***European Financial Management***, 13: 949–978.

Curtis, A. & Fargher, N. L. 2014. Does short selling amplify price declines or align stocks with their fundamental values?, ***Management Science***, 60: 2324–2340.

Davis, G. F. 2008. A new finance capitalism? Mutual funds and ownership re-concentration in the United States, ***European Management Review***, 5: 11–21.

Davis, G. F. 2010. Is shareholder capitalism a defunct model for financing development?, ***Review of Market Integration***, 2: 317–331.

Davis, J. H., Schoorman, F. D., & Donaldson, L. 1997. Toward a stewardship theory of management, ***Academy of Management Review***, 22: 20–47.

Davis, S. M., Lukomnik, J., & Pitt-Watson, D. 2009. Active shareowner stewardship: A new paradigm for capitalism, ***Rotman International Journal of Pension Management***, 2: 10–17.

Demsetz, H. 1967. Toward a theory of property rights, ***The American Economic Review***, 57: 347–359.

Dent, G. W., Jr.. 2012. Corporate governance: The Swedish solution, ***Florida Law Review***, 64: 1633–1668.

Eckbo, B. E., Paone, G., & Urheim, R. 2010. ***Efficiency of share-voting systems: Report on Sweden***. Tuck School Working Paper 2010-79.

Etzioni, A. 1991. The socio-economics of property, ***Journal of Social Behavior and Personality***, 6: 465–468.

Eumedion. 2011. ***Best practices for engaged share-ownership***. Resolution of the members of Eumedion. Available at: http://www.eumedion.nl/en/public/knowledgenetwork/best-practices/best_practices-engaged-share-ownership.pdf (accessed 9 October 2015).

European Commission. 2011. ***Green Paper: The EU corporate governance framework***. Available at: http://ec.europa.eu/internal_market/company/docs/modern/com2011-164_en.pdf (accessed 9 October 2015).

European Commission. 2013. ***Long-term financing of the European economy***. European Commission Green Paper COM(2013) 150/2. Available at: http://eur-lex.europa.eu/resource.html?uri=cellar:9df9914f-6c89-48da-9c53-d9d6be7099fb.0009.03/DOC_1&format=PDF (accessed 9 October 2015).

European Commission. 2014. ***Proposal for a Directive of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement***. European Commission legislative proposal. Available at: http://eur-lex.europa.eu/resource.html?uri=cellar:59fccf6c-c094-11e3-86f9-01aa75ed71a1.0003.01/DOC_1&format=PDF (accessed 9 October 2015).

Fichtner, J. 2013. Hedge funds: Agents of change for financialization, ***Critical Perspectives on International Business***, 9: 358–376.

Filatotchev, I. & Dotsenko, O. 2015. Shareholder activism in the UK: Types of activists, forms of activism, and their impact on a target's performance, ***Journal of Management & Governance***, 19: 5–24.

FRC. 2010. ***The UK Stewardship Code***. UK Financial Reporting Council. Available at: https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/The-UK-Stewardship-Code.pdf (accessed 9 October 2015).

© 2015 John Wiley & Sons Ltd

FRC. 2012. ***The UK Stewardship Code***. UK Financial Reporting Council. Available at: https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/UK-Stewardship-Code-September-2012.pdf (accessed 9 October 2015).

Gantchev, N. 2013. The costs of shareholder activism: Evidence from a sequential decision model, ***Journal of Financial Economics***, 107: 610–631.

Gifford, E. J. M. 2010. Effective shareholder engagement: The factors that contribute to shareholder salience, ***Journal of Business Ethics***, 92: 79–97.

Glackin, S. N. 2014. Back to bundles: Deflating property rights, again, ***Legal Theory***, 20: 1–24.

Goodman, J., Louche, C., van Cranenburgh, K. C., & Arenas, D. 2014. Social shareholder engagement: The dynamics of voice and exit, ***Journal of Business Ethics***, 125: 193–210.

Goranova, M. & Ryan, L. V. 2014. Shareholder activism: A multidisciplinary review, ***Journal of Management***, 40: 1230–1268.

Greenwood, R. & Hinings, C. R. 1996. Understanding radical organizational change: Bringing together the old and the new institutionalism, ***Academy of Management Review***, 21: 1022–1054.

Group of 30. 2012. ***Toward effective governance of financial institutions***. Available at: http://www.group30.org/images/PDF/TowardEffGov.pdf (accessed 9 October 2015).

Hampel, R. 1998. ***Committee of Corporate Governance – Final Report***. Available at: http://www.ecgi.org/codes/documents/hampel.pdf (accessed 9 October 2015).

Hawley, J. P. & Williams, A. T. 2000. The emergence of universal owners: Some implications of institutional equity ownership, ***Challenge***, 43: 43–61.

Hernandez, M. 2012. Toward an understanding of the psychology of stewardship, ***Academy of Management Review***, 37: 172–193.

Hirschman, A. O. 1970. ***Exit, voice, and loyalty: Responses to decline in firms, organizations, and states***. Cambridge, MA: Harvard University Press.

Hohfeld, W. N. 1917. Fundamental legal conceptions as applied in judicial reasoning, ***The Yale Law Journal***, 26: 710–770.

Holzmann, R. & Palmer, E. (Eds.). 2006. ***Pension reform: Issues and prospect for non-financial defined contribution (NDC) schemes***. Herndon, VA: World Bank Publications.

Hutchinson, M., Seamer, M., & Chapple, L. 2015. Institutional investors, risk/performance and corporate governance, ***The International Journal of Accounting***, 50: 31–52.

Isaksson, M. & Çelik, S. 2013. Equity markets, corporate governance and value creation, ***OECD Journal: Financial Market Trends***, 2013: 53–84.

Judge, W. Q., Gaur, A., & Muller-Kahle, M. I. 2010. Antecedents of shareholder activism in target firms: Evidence from a multi-country study, ***Corporate Governance: An International Review***, 18: 258–273.

Katelouzou, D. 2013. Myths and realities of hedge fund activism: Some empirical evidence, ***Virginia Law & Business Review***, 7: 459–511.

Kay, J. 2012. ***The Kay review of UK equity markets and long-term decision making – Final report***. Consultation of the UK Department of Business, Innovation and Skills. Available at: http://www.bis.gov.uk/assets/biscore/business-law/docs/k/12-917-kay-review-of-equity-markets-final-report.pdf (accessed 9 October 2015).

Kwan, A., Masulis, R., & McInish, T. H. 2015. Trading rules, competition for order flow and market fragmentation, ***Journal of Financial Economics***, 115: 330–348.

Logsdon, J. M. & Van Buren, H. J., III. 2009. Beyond the proxy vote: Dialogues between shareholder activists and corporations, ***Journal of Business Ethics***, 87: 353–365.

Lok, J. 2010. Institutional logics as identity projects, ***Academy of Management Journal***, 53: 1305–1335.

Lounsbury, M. 2008. Institutional rationality and practice variation: New directions in the institutional analysis of practice, ***Accounting, Organizations and Society***, 33: 349–361.

Lydenberg, S. 2007. Universal investors and socially responsible investors: A tale of emerging affinities, ***Corporate Governance: An International Review***, 15: 467–477.

Lydenberg, S. 2014. Reason, rationality, and fiduciary duty, ***Journal of Business Ethics***, 119: 365–380.

Manne, H. G. 1965. Mergers and the market for corporate control, ***Journal of Political Economy***, 73: 110–120.

Manne, H. G. 1984. In defense of the corporate coup, ***Northern Kentucky Law Review***, 11: 513–518.

Marler, J. H. & Faugère, C. 2010. Shareholder activism and middle management equity incentives, ***Corporate Governance: An International Review***, 18: 313–328.

Marston, C. 2008. Investor relations meetings: Evidence from the top 500 UK companies, ***Accounting & Business Research***, 38: 21–48.

Martin, R., Casson, P. D., & Nisar, T. M. 2007. ***Investor engagement: Investors and management practice under shareholder value***. Oxford: Oxford University Press.

Mitchell, R. K., Agle, B. R., & Wood, D. J. 1997. Toward a theory of stakeholder identification and salience: Defining the principle of who and what really counts, ***Academy of Management Review***, 22: 853–886.

Mizruchi, M. S. 2010. The American corporate elite and the historical roots of the financial crisis of 2008. In P. Hirsch & M. Lounsbury (Eds.), ***Markets on trial: The economic sociology of the US financial crisis – Research in the sociology of organizations***: 103–139. Bingley, UK: Emerald.

Monks, R. A. G. & Minow, N. 1995. ***Corporate governance***. Cambridge, MA: Blackwell.

Mukwiri, J. 2013. Myth of shareholder primacy in English law, ***European Business Law Review***, 24: 217–242.

Myners, P. 2001. ***Institutional investment in the United Kingdom: A review***. London: HM Treasury.

OECD. 2011. ***The role of institutional investors in promoting good corporate governance***. OECD Series on Corporate Governance. Available at: http://www.oecd.org/daf/ca/49081553.pdf (accessed 9 October 2015).

ORSE. 2011. ***L'engagement en France et à l'étranger: exercice du droit de vote et dialogue – Montée en puissance des critères extra financiers***. Report of the Observatoire de la Responsabilité Sociétale des Entreprises. Available at: http://www.orse.org/force_document.php?fichier=document_316.pdf&fichier_old=fr__exercice_du_droit_de_vote_et_dialogue.pdf (accessed 9 October 2015).

Pierce, J. L., Kostova, T., & Dirks, K. T. 2001. Toward a theory of psychological ownership in organizations, ***Academy of Management Review***, 26: 298–310.

Pozen, R. C. 2014. ***Curbing short-termism in corporate America: Focus on executive compensation***. Available at: http://www.brookings.edu/~/media/research/files/papers/2014/05/06%20pozen/brookings_shorttermismfinal_may2014.pdf (accessed 9 October 2015).

Rehbein, K., Logsdon, J. M., & Van Buren, H. J., III. 2013. Corporate responses to shareholder activists: Considering the dialogue alternative, ***Journal of Business Ethics***, 112: 137–154.

Reisberg, A. 2011. The notion of stewardship from a company law perspective, ***Journal of Financial Crime***, 18: 126–147.

Reisberg, A. 2015. The UK Stewardship Code: On a road to nowhere, ***The Journal of Corpororate Law Studies***, 15: 217–253.

Roberts, J., McNulty, T., & Stiles, P. 2005. Beyond agency conceptions of the work of the non-executive director: Creating accountability in the boardroom, ***British Journal of Management***, 16: S5–S26.

Rose, C. 2012. The new European shareholder rights directive: Removing barriers and creating opportunities for more shareholder

© 2015 John Wiley & Sons Ltd

activism and democracy, ***Journal of Management and Governance***, 16: 269–284.
Sauerwald, S. & Peng, M. 2013. Informal institutions, shareholder coalitions, and principal-principal conflicts, ***Asia Pacific Journal of Management***, 30: 853–870.
Schneider, M. & Ryan, L. 2011. A review of hedge funds and their investor activism: Do they help or hurt other equity investors?, ***Journal of Management & Governance***, 15: 349–374.
Sharfman, B. S. 2015. A theory of shareholder activism and its place in corporate law, ***Tennessee Law Review***, 82: 101–143.
Sikavica, K. & Hillman, A. 2008. Towards a behavioral theory of corporate ownership and shareholder activism, ***Academy of Management Annual Meeting Proceedings***: 1–6.
Stout, L. A. 2013. The toxic side effects of shareholder primacy, ***University of Pennsylvania Law Review***, 161: 2003–2023.
Tilba, A. & McNulty, T. 2013. Engaged versus disengaged ownership: The case of pension funds in the UK, ***Corporate Governance: An International Review***, 21: 165–182.
Tonello, M. 2006. ***Revisiting stock market short-termism***. The Conference Board Research Report No. R-1386-06-RR.
Venkiteshwaran, V., Iyer, S. R., & Rao, R. P. 2010. Is Carl Icahn good for long-term shareholders? A case study in shareholder activism, ***Journal of Applied Corporate Finance***, 22: 45–57.
Walsh, J. P. & Kosnik, R. D. 1993. Corporate raiders and their disciplinary role in the market for corporate control, ***Academy of Management Journal***, 36: 671–700.
Wang, M. 2014. Which types of institutional investors constrain abnormal accruals?, ***Corporate Governance: An International Review***, 22: 43–67.
Welker, M. & Wood, D. 2011. Shareholder activism and alienation: With CA comment by Robert A. G. Monks, ***Current Anthropology***, 52: S57–S69.
Westphal, J. D. & Zajac, E. J. 1998. The symbolic management of stockholders: Corporate governance reforms and shareholder reactions, ***Administrative Science Quarterly***, 43: 127–153.
Westphal, J. D. & Zajac, E. J. 2013. A behavioral theory of corporate governance: Explicating the mechanisms of socially situated and socially constituted agency, ***The Academy of Management Annals***, 7: 605–659.
Widmer, F. 2011. Institutional investors, corporate elites and the building of a market for corporate control, ***Socio-Economic Review***, 9: 671–697.
Wong, S. C. Y. 2010. Why stewardship is proving elusive for institutional investors, ***Butterworths Journal of International Banking and Financial Law***, 25: 406–412.

Terry McNulty is Professor of Management and Corporate Governance at the University of Liverpool. Over two decades he has published a body of research about processes of power, influence, accountability, and engagement by boards, institutional investors, pensions funds, and company secretaries. The impact of his research in policy and practitioner realms is evidenced by work that informed the UK Code of Corporate Governance, and governance-related activity of the Law Commission, the Association of Chartered Certified Accountants, the Institute of Company Secretaries and Administrators, and the Institute of Directors.

Donald Nordberg is Associate Professor at Bournemouth University Business School. After careers in financial journalism and investor communications in the US, UK and continental Europe, he became an academic, concentrating on strategy, boards and institutional analysis. He has published in journals including *Business History*, *Review of Political Economy*, and *Business Ethics*: *A European Review*, and his book *Corporate Governance*: *Principles and Issues* was published by Sage in 2011. A native of Chicago, he has two degrees from the University of Illinois, an MBA from the University of Warwick, and a PhD from the University of Liverpool.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 359–370

The Importance of Shareholder Activism: The Case of Say-on-Pay

Konstantinos Stathopoulos and Georgios Voulgaris*

ABSTRACT

Manuscript Type: Review
Research Question/Issue: This study focuses on the role of Say-on-Pay as a mechanism that aims to promote the efficiency of corporate governance by providing an additional channel for the expression of shareholder "voice." Initially introduced in the UK, Say-on-Pay has subsequently been adopted in a large number of countries and it has recently received significant attention from regulators, media, and the general public. The purpose of this study is to review prior literature related to Say-on-Pay and its impact on firm value and corporate decision making.
Research Findings/Insights: Our study highlights the interdisciplinary nature of research on Say-on-Pay. We also shed light on conceptual gaps and empirical discrepancies in prior studies, indicating that many questions linked to Say-on-Pay and its importance for the executive pay-setting process remain largely unanswered.
Theoretical/Academic Implications: At a theoretical level, we highlight potential areas for development of the existing theoretical framework for Say-on-Pay, which is at present rather limited and primarily influenced by agency theory. At an empirical level, we propose a substantial number of avenues for fruitful future research on this topic.
Practitioner/Policy Implications: In the light of recent proposals for extending the role of Say-on-Pay within the corporate governance framework, our findings are particularly relevant to regulators. More thought is needed about changing its nature from advisory to binding, as the degree of its effectiveness and the dynamics of the voting process are still unclear. Our study could also be informative for the media and the general public, especially given the increasing attention afforded to Say-on-Pay.

Keywords: Corporate Governance, Say-on-Pay, Shareholder Activism, Shareholder Voting

INTRODUCTION

Shareholder activism has played a key role in changing corporate decision making over recent years (Goranova & Ryan, 2014; Smith, 1996). The increased shareholder scrutiny of corporate practices has been significant and is evident in a number of countries. As a result, media organizations talk about a "shareholder spring" (Burgess & McCrum, 2012). Shareholder concerns regarding corporate policies are predominantly focused on the efficiency of corporate governance practices within a firm (Gillan & Starks, 2000). In particular, proposals by boards of directors regarding executive pay arrangements have attracted shareholder voting revolts on a number of occasions (Ertimur, Ferri, & Muslu, 2011; Thomas & Martin, 1999).

Our focus in this paper is on shareholder voting on executive pay and, more precisely, on a corporate governance mechanism commonly known as Say-on-Pay. Say-on-Pay was initially introduced in the UK in 2002 and mandates an advisory shareholder vote on executive remuneration proposed by the board of directors. A number of countries have followed the UK with the introduction of similar legislation, including the US, Australia, the Netherlands, Norway, Switzerland, and Sweden. The purpose of this mechanism is to promote transparency by providing a new means of expression of shareholder voice, and hence to improve corporate governance efficiency (Conyon & Sadler, 2010). This study discusses and critically evaluates existing research on Say-on-Pay and also provides suggestions for future research.

We find that research so far focuses on what we call the "intended" consequences of Say-on-Pay and follows two main paths. First, a number of studies examine the market reaction to the introduction of Say-on-Pay across different countries. We find evidence that the direction and degree of this reaction varies under different settings, a result which raises doubts about shareholders' perceptions regarding the effectiveness of Say-on-Pay. Second, several papers focus on the impact of Say-on-Pay-related voting outcomes on executive pay arrangements and firm decision making in general. Our review indicates that prior research fails to provide conclusive evidence that there is a strong impact of shareholder dissatisfaction, manifested by high voting dissent, on firm policies. We argue that these conflicting results can be attributed mainly to research design issues that invoke bias

*Address for correspondence: Georgios Voulgaris, Warwick Business School, The University of Warwick, Coventry CV4 7AL, UK. Tel: +44 24 765 73132; E-mail: Georgios.Voulgaris@wbs.ac.uk

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12147

in the relevant findings. In particular, the majority of these studies fail to incorporate in their analysis the dynamic nature of shareholder voting and the potential drivers or forces of resistance to Say-on-Pay and to corporate governance changes in general. Moreover, in many cases, we cannot exclude the possibility of confounding effects as well as selection bias issues driving the observed outcomes.

This study makes a number of contributions to the corporate governance literature. First, to our knowledge, this is the first systematic review of research on Say-on-Pay, which now forms a growing part of the wider shareholder activism literature. We highlight the increased research focus on shareholder empowerment and its impact on firm decision-making processes. Second, our analysis shows that the existing research on Say-on-Pay is rather one-dimensional and narrow, focused toward the intended consequences of Say-on-Pay on firm outcomes. We make a number of suggestions as to how this stream of research can be further extended by incorporating the role of key players, such as proxy advisors, in the Say-on-Pay voting process and also by taking into account the incentives of different firm stakeholders in relation to Say-on-Pay. Moreover, we highlight that the "unintended" consequences of Say-on-Pay largely remain unexplored and hence can be another interesting avenue for research. For example, the implications of Say-on-Pay for the managerial labor market and for agency costs of debt are unresolved issues that could enhance our understanding of this key corporate governance mechanism.

Third, an important contribution of this review is that we show there is scope for further multidisciplinary research related to Say-on-Pay that incorporates diverse research backgrounds and combines different research techniques. In the same spirit, we also highlight the transnational aspect of the subject and advocate international comparative research. We show that the extant literature is largely focused on the Anglo-Saxon environment; however, recent developments have opened fruitful directions for research incorporating a range of settings.

Overall, our review contributes to the ongoing debate on the usefulness of Say-on-Pay for corporate governance. Since its introduction, Say-on-Pay's effectiveness in promoting shareholder engagement has attracted much attention from academics, the media, and the general public in several countries. This has become more evident following recently introduced or proposed legislation in the UK and across the European Union that aims to further promote Say-on-Pay for firm governance (Department for Business Innovation & Skills, 2013; European Commission, 2012, 2014). The recent implementation of Say-on-Pay provisions within the Dodd-Frank Act has also intensified the debate in the US. Our analysis is thus relevant to a number of countries and could prove helpful for regulators and academics alike.

We present our findings in the following format: Initially, we provide a general overview of the shareholder activism literature and the positioning of Say-on-Pay studies in this literature. In the following section, we discuss the prevalent theoretical framework for Say-on-Pay. We then review empirical studies on the market reaction to the introduction on Say-on-Pay and the impact of this mechanism on firm outcomes. Subsequently, we provide suggestions for future research. We discuss the implications of our findings and draw conclusions in the final section.

BACKGROUND

Shareholder Activism

The importance of shareholder activism for corporate outcomes has attracted great attention from both the public and academia. A large number of studies have examined the factors leading to shareholder activism-related events, the different forms such activism can take and its impact on firm practices. We provide a brief overview of these studies and demonstrate how Say-on-Pay studies are positioned within the broad shareholder activism literature, of which Goranova and Ryan (2014) provide a detailed multidisciplinary review.

Firm size and performance are among the most important firm-related determinants of shareholder initiatives linked with activism (Cai & Walkling, 2011; Cziraki, Renneboog, & Szilagyi, 2010; Karpoff, Malatesta, & Walkling, 1996; Smith, 1996). Large firms are the focus of attention for activist shareholders, partly because they are more likely to attract attention and hence shareholders can expect to have greater public support for their proposals (Rehbein, Waddock, & Graves, 2004; Rowley & Moldoveanu, 2003). Large firms are also more subject to corporate governance issues, which means that activism can create more value for the shareholders (Del Guercio & Hawkins, 1999; John & Klein, 1995). The fact that firms with poor operating or market performance are also more likely to be the focus of shareholder activists (Bradley, Brav, Goldstein, & Jiang, 2010; Cziraki et al., 2010; Ertimur et al., 2011) highlights the role shareholder activism plays in monitoring the managers of underperforming firms. In addition, recent studies emphasize the importance of stock liquidity for shareholder activism (Edmans, Fang, & Zur, 2013; Norli, Ostergaard, & Schindele, 2015). Increased stock liquidity can facilitate the creation of blockholders and hence empower shareholders wishing to engage in activism. It is clear in the extant literature that the focus of shareholder activists is directed primarily toward ineffective corporate governance mechanisms as well as suboptimal executive pay arrangements (Davis & Thompson, 1994; Ferri & Sandino, 2009; Gillan & Starks, 2000).

Prior academic research identifies two main avenues for shareholder intervention in firm governance. The first channel ("exit") is linked with the threat of selling company shares, a decision which would impact negatively on the firm's stock price; this price drop will have direct wealth implications for the managers (related to equity-based compensation) as well as indirect ones (related to reputation) (Admati & Pfleiderer, 2009; Edmans, 2009). Exit threat hence gives managers the incentive to act in the interests of the firm and take decisions that will not destroy firm value (Edmans, 2009). Shareholders can also "vote with their feet" by selling all or part of their stake in the firm as a signal of dissatisfaction with the management team (Bhide, 1993; Parrino, Sias, & Starks, 2003; Roe, 1990). This form of activism decreases agency costs and can work in combination with other forms of shareholder intervention (Admati & Pfleiderer, 2009).

The second channel of activism ("voice") is expressed by taking direct action and getting involved in firm decision making. Shareholders can vote against the management or specific directors of the firm or become advocates of "just vote no" campaigns (Ashraf, Jayaraman, & Ryan, 2012; Conyon & Sadler, 2010; Davis & Kim, 2007; Del Guercio, Seery, & Woidtke,

© 2015 John Wiley & Sons Ltd

2008). Moreover, blockholders (i.e,, investors with over 5 percent ownership) can submit a 13D filing, demonstrating their intention to actively engage with the firm (Edmans et al., 2013; Klein & Zur, 2011). Shareholders can also initiate public campaigns and publicize letters directed to the management of the firm (Chowdhury & Wang, 2009; Hillman, Shropshire, Certo, Dalton, & Dalton, 2011). In such cases, shareholders bear the costs of monitoring the management of the firm by providing guidance or intervening in order to increase firm value or protect the firm from loss-making decisions. Shleifer and Vishny (1986) highlight the threat of the free-rider problem in such cases, whereby a shareholder bears all the monitoring costs but only a fraction of the perceived benefits. Evidently, the introduction of Say-on-Pay should be considered as an additional channel for shareholder voice and the expression of dissatisfaction with corporate decision making.

The impact of shareholder activism on firm outcomes has been widely studied in the relevant literature. A large number of papers examine the market reaction to different types of shareholder activism-related events and activist shareholders; overall, the findings in these studies are mixed (Agrawal, 2012; Cuñat, Gine, & Guadalupe, 2012; Del Guercio & Hawkins, 1999; Klein & Zur, 2011). Factors such as activist shareholder type, the objectives of the intervention and firm characteristics (e.g., level of institutional ownership) can impact on the direction and size of the market reaction. Del Guercio and Hawkins (1999) point out the difficulty of identifying the exact announcement dates of shareholder proposals; this poses an additional challenge to the researcher in terms of identifying the impact of activism on firm value, as most studies of this type follow an event study methodology.

Apart from market-related effects, studies have also focused on the impact of shareholder activism on firm performance, where again the findings are equivocal and primarily conditional upon the success of activism in addressing corporate governance issues within the firm (Del Guercio et al., 2008; Karpoff et al., 1996; Prevost & Rao, 2000). Studies have also examined the impact of shareholder activism on various firm outcomes and the firm's decision-making process. For example, David, Hitt, and Gimeno (2001) show that shareholder activism leads to an increase in R&D investment, both in the short and long term. Shareholder activism can also have a positive impact on corporate environmental (Clark & Crawford, 2012) and social (David, Bloom, & Hillman, 2007; Guay, Doh, & Sinclair, 2004) performance. Overall, shareholder activism appears to act as an effective monitoring mechanism that can improve corporate governance efficiency within the firm and can, in many instances, have a positive impact on firm value, performance, and decision making.[1]

SAY-ON-PAY

Theoretical Background

Say-on-Pay studies have so far mainly utilized agency-based theoretical models to build their framework and predictions. In modern corporations, the separation between ownership and control creates agency problems (Berle & Means, 1932; Jensen & Meckling, 1976). For this reason, shareholders need specific mechanisms to be in place to monitor managerial behavior and to ensure it is in the company's interests (Alchian & Demsetz, 1972; Jensen & Meckling, 1976). As part of this monitoring process, shareholders are likely to wish to intervene when they believe managerial actions are not in line with the company's interests and would destroy shareholder value (Edmans, 2014).

As mentioned above, prior research identifies two channels for shareholder intervention in firm governance, namely the threat of "exit" and the use of "voice." Say-on-Pay provides an additional tool for shareholder governance via the "voice" channel. A number of studies have provided models of different strategies that large shareholders can adopt to exert influence over governance issues using their "voice." More particularly, in their theoretical models, Shleifer and Vishny (1986) examine the circumstances under which shareholders, instead of choosing to become a free-rider, will incur monitoring costs and use their influence over firm decision making. Depending on the size of the initial stake in the firm, the shareholder can intervene in firm decision making in a number of ways, namely via a tender offer, a proxy fight, or negotiations with the management. Maug (1998) adds the role of liquidity, which gives a higher incentive to a shareholder to hold a large block of stocks and engage in active monitoring. *Ceteris paribus*, greater liquidity decreases the potential profits from frequent trading for smaller shareholders who are willing to sell their stocks at a discount, and thus encourages blockholding. This finding counters prior studies by Bhide (1993) and Coffee (1991), who argue that increased liquidity discourages the use of "voice" as a shareholder governance mechanism.

Mangen and Magnan (2012) highlight a potential problem with Say-on-Pay's role as a voice-related governance mechanism: Supporters of Say-on-Pay argue that it can embolden effective monitoring of firm management by large shareholders and hence promote corporate transparency; however, entrenchment problems can potentially lead to the collusion of large shareholders with the management team, and thus to blockholder support for suboptimal pay arrangements. This can lead to conflicts with other shareholders and firm stakeholders, thus increasing agency costs. Moreover, the board of directors might try to avoid significant negative reactions and potential dissent from voting shareholders by managing the disclosure of compensation plans. This could have a long-term negative impact on the quality of pay-related disclosure within the firm.

By integrating an additional theoretical perspective into their arguments, Krause, Whitler, and Semadeni (2014) provide a different Say-on-Pay theoretical framework to the prevalent one based on agency theory. They use prospect theory to claim that shareholders are more likely to vote negatively on high levels of CEO pay when the firm is performing poorly. This is due to the fact that decision makers view profits and losses asymmetrically (Kahneman & Tversky, 1979); hence shareholders are more likely to express their dissent about proposed executive pay arrangements when voting from a loss position. The authors confirm their arguments in an experimental setting and show that shareholders' loss aversion can have an impact on pay-related voting patterns.

Global Introduction and its Determinants

The UK government was the first, in 2002, to introduce the new legislation that became known as the Say-on-Pay initiative

© 2015 John Wiley & Sons Ltd

(Directors Remuneration Report (DRR) Regulations (2002)). According to this regulation, shareholders should express their approval or disapproval of executive pay proposals put forward by the board of directors using a voting process. The declared objective of this legislation was to promote corporate governance efficiency within the firm and increase the accountability of the board of directors toward its shareholders (Ferri & Maber, 2013). The DRR Regulations mandated that, from the fiscal year ending on December 31, 2002 onwards, the board of directors must prepare a detailed remuneration report and submit it to the Annual General Meeting (AGM) for approval. The shareholders are then required to cast non-binding votes on the proposed remuneration arrangements; apart from approving or rejecting the remuneration report, shareholders can also cast an abstaining vote. The 2013 Enterprise and Regulatory Reform Act (Department for Business Innovation & Skills, 2013) made Say-on-Pay voting binding, rather than advisory, thus providing shareholders with the ability to block a proposed executive pay package.

Following the UK, and after a series of cases of self-serving behavior by managers, the Netherlands introduced a new corporate governance code (Tabaksblat Code) in 2004, which included a provision for the introduction of Say-on-Pay voting. The main difference between the UK and Dutch legislation is that in the Dutch legislation the vote is not on the actual remuneration report but on the general principles adopted by the board for determining executive pay. Also, the vote is binding, not advisory, and only necessary when a board recommends changes to these principles. Sweden, Norway, and Denmark have adopted similar Say-on-Pay provisions as part of their corporate legislation (Thomas & Van der Elst, 2013). We observe that the frequency and nature of the voting differ across countries. Thomas and Van der Elst (2013) attribute these dissimilarities to the degree of concentration of ownership, differences in institutional ownership levels, the degree of social tolerance toward income inequality, and certain political influences in different countries. Table 1 provides information on the adoption of Say-on-Pay voting across countries.

TABLE 1
Say-on-Pay Adoption by country

Country	Adoption Year	Type of Firms	Type of Vote	Other Information
Australia	2005	Listed	Mandatory & advisory	Boards are required to explain their response to voting dissent higher than 25%. There is also a "two-strike" clause, where the board has to stand for re-election if dissent is higher than 25% for two consecutive years.
Belgium	2012	Listed	Mandatory & advisory	
Canada	2012	Listed	Voluntary & advisory	Companies have the option to ask for an advisory vote on the remuneration package and policy
Denmark	2007	Listed	Mandatory & binding	
Finland	2007	Listed	Mandatory & binding	
France	2014	Listed	Mandatory & advisory	
Germany	2010	Listed	Mandatory & advisory	Proposals for a binding vote were rejected by the German parliament in 2013
Italy	2011	Listed & banks	Mandatory & advisory (binding for banks)	
Japan	2005	Listed	Mandatory & binding	
Netherlands	2004	Listed	Mandatory & binding	Voting is required only when there are changes in the remuneration policy
Norway	2007	Listed	Mandatory & binding	
South Africa	2009	Listed	Mandatory & advisory	
Spain	2011	Listed	Mandatory & advisory	
Sweden	2005	Listed	Mandatory & binding	
Switzerland	2007	Listed	Mandatory & binding	Switzerland introduced voluntary and advisory Say-on-Pay regulation in 2007. Following a referendum in 2013, the nature of the vote changed in 2015
UK	2002	Listed	Mandatory & binding	The nature of the vote was mandatory & advisory until October 2013
USA	2011	Listed	Mandatory & advisory	Introduced as part of the Dodd-Frank Act 2010

© 2015 John Wiley & Sons Ltd

In a comparative study between the US and the UK on the rules and practices of shareholder proposals, Buchanan, Netter, Poulsen, and Yang (2012) show that UK shareholders have substantially greater powers than their US counterparts to express their opinions and impose changes to firm decision making. This could explain why the US authorities have recently introduced regulation, similar to that of the UK, on advisory shareholder voting on executive pay arrangements as part of the Dodd-Frank Act (2010). The regulation was passed despite opposing voices from a number of academics and business leaders claiming that Say-on-Pay voting can exacerbate rather than resolve agency problems in firms. Bainbridge (2009) claimed that the introduction of Say-on-Pay in the US would lead to a "federalization" of corporate governance legislation, which could have negative implications for the way the capital market operates; also, Say-on-Pay would be a solution to a non-existent problem with executive pay, as evidence of excessive managerial power within firms is rather weak. Hemphill and Lillevik (2009) claimed that the introduction of Say-on-Pay would constitute a major overreach of corporate legislation for reasons not associated with federalism but with the fact that, as existing legislation made the board of directors responsible for the pay-setting process, it already addressed the issue of the determination of executive pay contracts.

Due to activism-related events initiated by several institutional shareholders, a number of large Swiss companies agreed to adopt a voluntary Say-on-Pay advisory vote (Wagner & Wenk, 2015). However, following a 2013 referendum, which attracted significant attention from the media, the Swiss federal government is in the final stages of introducing mandatory voting on the election of the board of directors as well as the proposed executive pay arrangements. These changes will significantly affect corporate governance arrangements for Swiss firms and will lead to a power transfer from the boardroom to shareholders (Nyukorong, 2013). Hausmann and Bechtold-Orth (2013) express concerns that obliging the shareholders of Swiss firms to actively monitor and engage with their firms significantly increases shareholder responsibility, with important legal consequences.

Finally, following recent developments in a number of countries, there are also proposals in the EU to adopt a common policy on the determination of executive pay, including a Say-on-Pay vote on proposed executive pay arrangements (European Commission, 2012, 2014). The purpose of introducing such a regulation would be to increase shareholder responsibility and engagement with the firm. Although the voting process is expected to be mandatory, whether the outcome of the voting would have a mandatory or advisory nature is expected to be decided by each member state separately (Hausmann & Bechtold-Orth, 2013).

MARKET REACTION

Since the initial introduction of Say-on-Pay regulation in the UK in 2002, a growing literature has emerged focusing on market reactions to this regulatory change across a number of settings and taking into account different firm characteristics. Ferri and Maber (2013) report positive market reactions on the date of the announcement that the Say-on-Pay regulation would be introduced in the UK. This implies that shareholders view this new governance mechanism as a positive step towards fairer executive pay. More importantly, the authors find higher abnormal returns for firms with excessive CEO pay, generous severance contracts and weak penalties for poor performance. This indicates that shareholders consider Say-on-Pay to be an effective monitoring mechanism for firms with weak governance.

Cai and Walkling (2011) examine the effect of the introduction of Say-on-Pay on firm value in a US setting. Similarly to Ferri and Maber (2013), they find that the introduction creates value in firms with weak governance and dubious executive pay arrangements. However, it can also destroy value in other firms. More precisely, larger firms are more likely to be targeted by shareholder revolts over executive pay even when pay arrangements are not considered to be excessive. This indicates that the introduction of mandatory shareholder voting on pay might not be beneficial for all firms. The conflicting results of the aforementioned studies can be due to research design issues that we discuss at the end of this section.

In the same spirit, Cuñat et al. (2012) document an increase in firm value after the marginal approval of a shareholder proposal (including executive-pay-related proposals) that leads to improvements in corporate governance. They also show systematic differences in market reactions for firms with different ownership characteristics and levels of shareholder activism, and for different types of proposals. In a setting that alleviates endogeneity concerns, their study highlights the fact that enhancements in corporate governance create firm value.

Iliev and Vitanova (2013) examine the impact of the new Say-on-Pay regulation on firm value, for US firms, using a quasi-experimental setting. Using the fact that the Securities and Exchange Commission (SEC) offers firms with a public float lower than $75m the option of being exempt from mandatory Say-on-Pay, they demonstrate that these firms exhibited negative market returns upon the announcement of the Say-on-Pay regulation. This indicates that the mandatory nature of Say-on-Pay is value-relevant and that shareholders wish to vote regularly and express their opinions on executive pay proposals.

Wagner and Wenk (2015) examine the impact of the announcement of the introduction of binding Say-on-Pay on the value of Swiss firms. Interestingly, they find negative market reactions to the announcement for the majority of firms. This negative reaction is due to the additional monitoring costs that the shareholders will bear due to the proposed legislation. In effect, such a significant increase in shareholder power might initially sound like a positive step toward improved corporate governance, but the findings of this paper indicate that the costs linked with a binding Say-on-Pay vote could outweigh any potential benefits from an increase in corporate transparency.

Based on the aforementioned studies, we observe a number of conflicting findings related to Say-on-Pay and shareholders' perceptions of its usefulness for corporate governance. There is some evidence that the introduction of Say-on-Pay is perceived as beneficial, to a degree, for firms with weak governance structures and suboptimal executive pay arrangements in place. However, we observe systematic differences across different settings relative to the size and direction of the market reaction to the announcement of the introduction of Say-on-Pay for different types of firms.

© 2015 John Wiley & Sons Ltd

We believe that there can be a number of reasons for this. First, several of the above studies fail to incorporate a number of factors that could affect market reactions to Say-on-Pay, such as shareholder heterogeneity. Different types of shareholders have dissimilar firm-related incentives; hence the observed market reaction to the introduction of Say-on-Pay can be driven by shareholders' self-serving behavior and should not be considered as a signal of the usefulness of Say-on-Pay for corporate governance and shareholder empowerment. For example, we cannot exclude the possibility that the observed findings are driven by confounding effects, related to free-riding behavior by a number of investors who do not engage with the firm but expect to benefit from the Say-on-Pay-related monitoring activities of other shareholders. This is particularly relevant in this type of studies, as prior research has shown systematic differences in institutional ownership characteristics across different countries (Ferreira & Matos, 2008). Second, at a country level, there are differences in the "perceived value" of corporate governance (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 2000), so comparisons of market reactions between different environments may not be informative. Moreover, the well-documented cultural differences across countries regarding executive pay and its importance for corporate governance (Conyon & Murphy, 2000) can also impact on market reactions in relation to Say-on-Pay. Finally, institutional inertia, resistance or push for corporate governance-related improvements can act as moderators to market reactions to the introduction of Say-on-Pay and significantly affect the findings of the above studies.

OUTCOMES

Mandatory Voting on Pay

In addition to the impact of the introduction of Say-on-Pay on firm value, a large number of studies examine the effect of outcomes of mandatory voting on the level and structure of executive pay and on overall firm decision making. Alissa (2015) finds evidence that, in the UK, shareholder voting dissent increases with excessive executive pay. This implies that shareholders express their dissatisfaction with excessive pay practices through voting. Firms also respond to shareholder dissent by reducing excessive CEO pay practices or forcing the CEO out of office. The former happens only for firms with above-mean excessive compensation. These findings suggest that company boards seem to respond to shareholder dissatisfaction by adjusting, to a certain degree, their decisions.

Carter and Zamora (2008) examine which specific aspects of executive pay arrangements attract shareholder voting dissent. The study shows that negative voting is positively associated with high salaries, low pay-performance sensitivity for short-term bonus payments, and a high likelihood of dilution of equity-based pay. These findings suggest that shareholders are more likely to vote against executive pay arrangements associated with excessive pay. In line with Alissa (2015), boards try to respond to this dissatisfaction by making adjustments to suboptimal arrangements. Both of the above studies indicate that Say-on-Pay can act as an effective means of improving executive pay arrangements; however, they do not make any attempt to examine the underlying drivers of shareholder voting on pay or to explain the observed low levels of voting dissent.

Gregory-Smith, Thompson, and Wright (2014) report a positive association between negative voting and total pay levels for a large sample of UK firms over the period 2003 to 2012. There are also moderate changes in executive pay arrangements, but only in cases with high percentages of negative voting. Interestingly, these changes do not become more pronounced in the period following the 2007/08 financial crisis despite the expectation that Say-on-Pay voting would provide a straightforward avenue for shareholders to express dissatisfaction with losses suffered during that period. This finding contradicts prior studies on the role of Say-on-Pay as a channel of expression of shareholder dissatisfaction (Alissa, 2015; Carter & Zamora, 2008).

Ferri and Maber (2013) focus on UK firms with high percentages of voter dissent (higher than 20 percent) and examine board reactions to this strong shareholder dissatisfaction. These firms make significant changes to generous severance arrangements, remove or shorten the time period allowed for retesting the vesting provisions of equity-based pay, and increase pay-for-performance sensitivity for CEO pay. This implies that shareholders view Say-on-Pay as an effective way of expressing their dissatisfaction with ineffective pay arrangements and use it to push for their removal. Overall, the findings of this study suggest that high voter dissent can eventually lead to the removal of controversial CEO pay practices.

In contrast, Conyon and Sadler (2010) find limited evidence that a large amount of dissent among voting shareholders has any material impact on the subsequent level and structure of CEO pay for UK firms. They also find no significant changes in the structure of executive compensation following high levels of negative voting; in particular, there is no move toward higher proportions of performance-related, e.g. equity-based, pay. However, executive pay-related resolutions are more likely to attract negative voting from shareholders than other forms of resolution submitted for voting. This is consistent with the view that shareholders consider executive pay arrangements of great importance for firm value and an avenue for expressing their dissatisfaction with management decisions, as cases of high pay attract the highest levels of voter dissent. As we discuss later, we believe that the contrasting findings of these studies can be explained by further examining the dynamic nature of shareholder voting and its underlying drivers.

Cotter, Palmiter, and Thomas (2013) provide one of the first studies to examine voting patterns and the impact of the introduction of mandatory Say-on-Pay voting in the US on executive pay practices. The study identifies a positive relation between shareholder voting dissent and excessive pay practices, poor performance, and negative recommendations from proxy advisors. Interestingly, proxy advisors' recommendations have the greatest explanatory power for negative voting; hence, their role in this process requires further attention. Overall, they find that the introduction of mandatory voting on pay does not instigate a shareholder revolt against pay proposals, as some parties have suggested. In addition, they identify a positive impact on company management's responsiveness to shareholders' concerns about executive pay, especially in firms with excessive pay arrangements in place.

© 2015 John Wiley & Sons Ltd

Voluntary Voting on Pay[2]

In the US setting, a number of studies have examined the impact of voluntary shareholder voting proposals before its recent introduction as a mandatory corporate governance mechanism through the Dodd-Frank Act. Ertimur et al. (2011) focus on US-based shareholder activism events related to pay. In particular, they examine cases of shareholder Act. Ertimur etproposals and "vote no" campaigns directed against controversial executive pay arrangements. Activist shareholders target firms with high levels of CEO pay, regardless of whether these levels are considered excessive or not. Also, proposals aimed mainly at the pay-setting process are most likely to receive high levels of support. Meanwhile, those aimed at the design and structure of the pay package seem to receive less support. Overall, Ertimur et al. (2011) find that shareholder proposals are more effective in cases where the companies have excessive pay arrangements in place. These firms respond to shareholder dissatisfaction by significantly reducing the excessive levels of CEO compensation (by more than 35 percent on average).

Del Guercio et al. (2008) examine the "just vote no" form of shareholder activism. The organizers of these campaigns are typically activist shareholders trying to achieve a public vote of no confidence in one or more of the directors. A large number of them are driven by cases of excessive pay not associated with firm performance; hence, they are indirectly linked to Say-on-Pay voting. The study shows an increase in operating performance following the activism-related events and reports a positive association between these campaigns and CEO turnover decisions; the expression of shareholder dissatisfaction forces boards to take actions that protect shareholders' interests.

Burns and Minnick (2013) examine the specific impact of voluntary Say-on-Pay proposals on executive pay arrangements in the US. They report insignificant differences in the total level of CEO pay between firms that receive Say-on-Pay proposals and those that do not. However, they report a change in executive pay structure toward a higher proportion of incentive-based compensation compared to salary-based for firms that receive proposals. This increase is achieved through greater option-based pay, which also leads to an increase in pay-for-performance sensitivity. Interestingly, firms with high levels of cash-based CEO pay are more likely to receive Say-on-Pay proposals from their shareholders.

In contrast, a recent study by Armstrong, Gow, and Larcker (2013) provides little evidence that shareholder dissent leads to changes in the level or composition of incentive-based CEO pay for US firms. They find that, in firms where a compensation plan is rejected by shareholders, the shareholders are more likely to approve the plan in the succeeding year. The findings of this study suggest a weak effect of shareholder dissatisfaction, expressed through negative voting, on future CEO compensation arrangements. For this reason, any potential increase in shareholder power provided by mandatory Say-on-Pay voting will not have the anticipated outcomes on the pay-setting process.

Iliev and Vitanova (2013) find that the voluntary adoption of Say-on-Pay voting by firms has led to an increase in the overall levels of CEO pay and pay-for-performance sensitivity. They claim that higher pay is used by boards as a way of compensating managers for the higher sensitivity of pay to performance and the higher risk that a Say-on-Pay vote entails. Moreover, the directors of companies that voluntarily adopt Say-on-Pay receive greater support in the shareholder vote. Overall, the majority of the companies in their study had not attempted to avoid implementing the new regulation, and had decided to submit executive pay voting proposals; in other words, the boards of directors had shared the responsibility for the executive pay-setting process with the company shareholders.

Our above analysis suggests that evidence is still inconclusive as to whether Say-on-Pay is an effective channel for the expression of shareholder voice leading to improvements in corporate governance. There is conflicting evidence on the effect of voting results on future executive pay arrangements, CEO employment, and corporate policies in general. Also, research so far has not provided a plausible explanation for the observed low levels of shareholder voting dissent on executive pay discussed in the following section.

We suggest a number of explanations for this. First, the existing research fails to incorporate the dynamic nature and the underlying drivers of Say-on-Pay voting. The role of intermediaries, such as proxy advisors, and also the importance of shareholder heterogeneity and of conflicts of interest between different firm stakeholders in this process are all factors that could explain prior conflicting evidence on the impact of Say-on-Pay voting outcomes on firm decision making. As we analyze in the following section, these are all factors that future studies could incorporate to help us further understand the Say-on-Pay voting process. Second, selection bias issues can be prevalent in a number of studies, especially in the cases of the adoption of voluntary voting on executive pay. Since firms choose to solicit shareholder voting on an ad-hoc basis, the above studies can only observe the specific proposals submitted for voting; hence the firm's choice to request a vote on pay can be a source of self-selection bias for the findings of these studies. It is still unclear whether this choice is a sign of efficient corporate governance structures within the firm or whether it can be due to other reasons, such as managerial entrenchment. Therefore, the ways that shareholders choose to cast their votes or generally engage with Say on Pay in such a setting need further analysis.

SUGGESTIONS AND IMPLICATIONS FOR FUTURE RESEARCH

The previous sections provide an overview of the theories underpinning Say-on-Pay research, empirical evidence on the impact of the introduction of Say-on-Pay on firm value and the effect of voting results on corporate outcomes. The purpose of this section is to discuss the theoretical and empirical implications of prior Say-on-Pay-related research and suggest potential avenues for future research at a theoretical and empirical level. At a theoretical level we suggest a number of potential developments of the existing Say-on-Pay framework. At an empirical level, we argue there is scope for extending existing Say-on-Pay-related research on what we call its "intended" consequences on firm value and corporate governance. We also contend that the "unintended" consequences

© 2015 John Wiley & Sons Ltd

of Say-on-Pay remain under-explored and can provide fruitful avenues for future research.

Theoretical Advances

As mentioned previously, at a theoretical level, the majority of the extant literature takes an agency theory perspective in explaining Say-on-Pay-related phenomena. Evidently, there is merit in viewing voting on pay as a monitoring mechanism available to shareholders, as part of a principal-agent relationship. However, in taking this perspective, the researcher implicitly assumes homogeneity across shareholders, in terms of their interests, their expectations from the firm, and their characteristics. Mangen and Magnan (2012) make an initial attempt to highlight the underlying heterogeneity issue; for various reasons large shareholders have a different relationship with the firm and their voting behavior can be driven by dissimilar determinants compared with smaller owners. Krause et al.'s (2014) study is a first and promising attempt to use a different theoretical framework (i.e, prospect theory) in this context; diverse shareholder characteristics (loss aversion in this case) can explain their, puzzling in many instances, voting behavior when it comes to executive pay. Further research building on these studies seems well warranted.

Following the shareholder activism literature, the application of stakeholder theory to Say-on-Pay could also be a fruitful avenue for future research. Stakeholder theory highlights the importance of the interrelationships between the firm and a number of parties such as its employees, creditors, customers, and shareholders (Donaldson & Preston, 1995; Freeman, 1984). Importantly for our context, company actions that benefit shareholders but harm stakeholders in the short run might also prove to be harmful to shareholders in the long run (Donaldson & Preston, 1995; Freeman, Wicks, & Parmar, 2004). Therefore, the use of stakeholder theory in explaining Say-on-Pay voting patterns could help researchers to further delineate shareholder decisions. In effect, the anticipated divergent impacts of a specific voting proposal on different groups of stakeholders could affect shareholder voting behavior. It is thus plausible that some shareholders do not appreciate (or are not interested in) the impact of their short-termism on the long-term value of the firm. This can create frictions between stakeholders and can impact on the way that other shareholders cast their vote. Any empirical findings confirming the above predictions could have wider implications for corporate governance and the executive pay-setting process.

Intended Consequences

At an empirical level, our previous discussion highlights a number of issues associated with Say-on-Pay that remain unanswered and could be further explored. First, it is fairly evident that the extant literature is primarily oriented towards the Anglo-Saxon setting. We believe that this is mainly due to the fact that the UK in particular provides an ideal setting for archival research on Say-on-Pay as investors in the UK have been required by law to submit non-binding votes on executive pay since 2002. Therefore, there is no selection bias in the voting decision, which until recently was a major problem in other settings. However, given the institutional changes discussed earlier, there is now great scope for expanding the Say-on-Pay analysis to the international domain.

Correa and Lel (2014) is, to our knowledge, one of the first papers to attempt this and it shows significant changes in executive pay practices for countries that have introduced Say-on-Pay provisions compared to countries without such provisions in place; however, the data used are limited in terms of details on voting decisions. Additional cross-country studies would greatly enhance both our understanding of corporate governance mechanisms and the role of regulation in enhancing their effectiveness. Such studies could focus, for example, on cross-country differences in Say-on-Pay's efficiency in promoting corporate transparency. This could provide an important contribution to the literature as our previous analysis demonstrates that the existing UK and US evidence is inconclusive as to the effectiveness of Say-on-Pay for improving transparency in the executive pay-setting process. It would also be interesting to examine whether differences in effectiveness can be associated with dissimilarities in terms of the mandatory or advisory nature of the vote. The adoption process of Say-on-Pay across different countries also offers opportunities for research on the institutional mechanisms leading to the decision to introduce, or not introduce, such legislation.

Second, specific empirical findings from prior studies also open channels for further research on the topic. A common element across all studies focusing on Say-on-Pay voting patterns in the UK is the reported relatively low degree of shareholder dissent. For example, Carter and Zamora (2008) find that negative votes comprise much less than 10 percent of the total votes cast; in 2005, the share was only 3.4 percent. It is still unclear whether the observed low levels of voting dissent are due to efficient monitoring, entrenchment issues, or other firm-related determinants. We believe there is room for further research incorporating additional firm, country, and shareholder characteristics to inform this debate. For example, cultural attributes could be a plausible explanation for this type of voting pattern. It would also be interesting to examine systematic differences in the voting decision by taking into account shareholder heterogeneity.

Stathopoulos and Voulgaris (2015) make a first such attempt by exploring the impact of shareholder characteristics on voting behavior associated with Say-on-Pay and find evidence that the shareholder investment horizon is an important determinant of voting patterns. Short-term investors, who are expected to try to avoid incurring any monitoring costs linked with Say-on-Pay, are more likely to cast an abstaining vote and will only express dissent in the case of excessive (and hence easily identifiable) CEO pay. On the other hand, long-term investors predominantly cast a favorable vote, a behavior that appears to be associated with prior engagement, as opposed to collusion, with the management of the firm. Future studies could explore this issue further to better explain the dynamics of the Say-on-Pay voting process. For instance, it is plausible to expect different voting determinants and patterns for pension funds compared to hedge funds. The role of retail investors in the voting process could be another interesting line of research.

Additional analysis on the role of potential forces of resistance against the introduction of Say-on-Pay could provide us with further insights on the adoption process and its

© 2015 John Wiley & Sons Ltd

impact on firm value and corporate governance arrangements. Resistance of managers or other firm stakeholders, such as investors or debt holders, to corporate governance reforms are well documented in the corporate governance literature (Denis & McConnell, 2003). Therefore, it is highly likely that such institutional impediments are also relevant to Say-on-Pay adoption and effectiveness. We thus encourage further research on the underlying causes of such resistance and its consequences for Say-on-Pay voting outcomes and firm values.

The role of intermediaries, such as proxy advisors, on the Say-on-Pay process also bears further analysis, to help explain some of the conflicting findings of prior studies. In particular, it would be interesting to investigate whether proxy advisors have a mind of their own or simply act as information processors/intermediaries for their end users, that is, firm shareholders and investors at large. Ertimur, Ferri, and Oesch (2013) make a first attempt, but we believe that selection bias issues related to the voluntary adoption of Say-on-Pay in the US prior to the Dodd-Frank Act could have an impact on the interpretation of the findings of this study.

Our review further highlights that there is scope for more research focusing on market reactions and on changes in the portfolio positions of existing shareholders after specific voting outcomes. As discussed earlier, studies have so far focused mainly on market reactions to announcements of the introduction of Say-on-Pay initiatives. Hence, it would be interesting to examine changes in firm value after specific voting outcomes, for example an extremely high level of dissent or even the unanimous acceptance of a proposal. It would also be interesting to study any systematic differences in changes of portfolio positions across different types of existing shareholders after such voting results. The position of Say-on-Pay voting within the overall corporate governance framework of the firm, and its interaction with other governance mechanisms (e.g., managerial ownership, board independence), could be another fruitful avenue of research. Also, specific CEO characteristics associated with the CEO's "power" (or entrenchment) within the firm which could drive shareholder voting behavior remain largely unexplored.

Finally, the fact that Say-on-Pay voting has now been adopted by a large number of countries also offers potentially interesting settings for comparative studies adopting both a quantitative/archival and qualitative/critical approach. In particular, our analysis points out the interdisciplinary nature of the existing research relating to the Say-on-Pay initiative. However, we believe that a multidisciplinary approach to the topic is currently lacking. Including surveys or interviews with key players in the pay-setting process could open up different possibilities to the researcher and give conclusive answers to questions that archival research alone has so far failed to provide. This could also be combined with our previous suggestions on incorporating the impacts of shareholder heterogeneity, management team characteristics, and cultural attributes on the voting process.

Unintended Consequences

An important finding of our review is the lack of studies focusing on the unintended consequences of Say-on-Pay. Given the potential impact of shareholder voting dissent on managerial human capital, we encourage new studies on the impact of the introduction of Say-on-Pay on the managerial labor market. Firms with a history of shareholder revolts over executive pay issues might have problems attracting managerial talent. At the same time, managers and other board members whose proposals have repeatedly received negative votes could find it difficult to secure lucrative employment contracts in other companies. What is more, Say-on-Pay adoption can seriously affect CEO risk taking, with wider implications for the structure of executive pay contracts and for firm decision making in general. For instance, it is reasonable to expect that a number of firms could consider transferring their headquarters to countries that have not introduced mandatory Say-on-Pay voting as a protective measure against potential shareholder revolts.

Future research could also analyze the interaction of Say-on-Pay with debt holder monitoring activities and its impact on agency costs of debt. Although Say-on-Pay and shareholder activism could reduce agency costs of equity, there are no studies so far examining Say-on-Pay's impact on the agency costs of debt. It is reasonable to expect that any changes in executive pay structure to induce CEO risk taking due to Say-on-Pay adoption could lead to an increase in agency costs of debt. Finally, it still remains unclear whether external corporate governance mechanisms, such as bank monitoring, act as a substitute to Say-on-Pay and thus moderate shareholder voting dissent.

POLICY IMPLICATIONS AND CONCLUSION

Our review is informative for regulators regarding the current status of academic research on the effectiveness of Say-on-Pay in improving shareholder engagement and promoting corporate governance transparency. This is of particular importance across EU countries, including the UK, due to the recent proposals for new Say-on-Pay-related legislation (European Commission, 2012, 2014). Our study highlights that, despite the indications that Say-on-Pay has a moderating impact on cases of suboptimal executive pay arrangements, evidence on its effectiveness remains unclear. Therefore, the proposed further advancement of its role in the pay-setting process should not be considered as a panacea for all corporate problems associated with excessive pay. More thought is needed regarding the dynamics of shareholder incentives in relation to Say-on-Pay and the wisdom of changing the nature of the vote from advisory to mandatory. Moreover, we believe that, along with Say-on-Pay, there is scope for additional means of promoting shareholder engagement that will help to further enhance corporate transparency. Our study could also be useful for the media and the general public as it summarizes-current knowledge on this "sensitive" issue and in effect tries to engage the public with relatively less-known aspects of this interesting topic.

To conclude, increasing shareholder empowerment and the associated upsurge in the number of public shareholder activism events have, on many occasions, become a force for institutional change within firms. This study focuses on an important channel for the expression of shareholder voice, a corporate governance mechanism known as Say-on-Pay. Our review and analysis of the relevant literature indicates that Say-on-Pay has been the focus of attention for researchers

© 2015 John Wiley & Sons Ltd

from a number of social science disciplines but that discrepancies, gaps, and inconsistencies across the relevant literature remain. We show that there is scope for extensive further research on Say-on-Pay and identify a number of unanswered questions and potentially fruitful avenues for future studies to explore.

ACKNOWLEDGEMENT

The authors would like to thank the Associate Editor (Chris Florackis) and two reviewers for valuable comments and suggestions.

NOTES

1. Apart from the right to vote on executive pay-related proposals, shareholders in some countries are also required to express their opinion on a number of company-related issues through a voting process. Yermack (2010) provides a detailed review of shareholder voting and its impact on corporate governance arrangements within the firm. Prior studies have focused on the election (or re-election) of the board of directors (Fischer, Gramlich, Miller, & White, 2009; Shivdasani & Yermack, 1999), the approval of new mergers & acquisitions (Kalay, Karakas, & Pant, 2014) and the mechanics behind the voting process (Kahan & Rock, 2008). As mentioned earlier, a number of shareholder activism events are associated with voting (Del Guercio et al., 2008; Greenwood & Schor, 2009; Klein & Zur, 2011). Overall, research in this area indicates the increasing importance both shareholders and firms place on voting. This can be linked to a shift toward democratization within the firm and also to some sharing of responsibility between the shareholders and management for firm decision making. It may also explain the increased interest in Say-on-Pay voting and its gradual introduction in a number of countries, as we analyze in detail in our review.
2. Strictly speaking, this type of voting is not a Say-on-Pay case as presented in the previous sections, as it does not refer to mandatory voting. However, we believe it shares many common characteristics with Say-on-Pay and hence its impact on firm outcomes is worth investigating.

REFERENCES

Admati, A. R. & Pfleiderer, P. 2009. The “Wall Street Walk” and shareholder activism: Exit as a form of voice, ***Review of Financial Studies***, 22: 2645–2685.

Agrawal, A. K. 2012. Corporate governance objectives of labor union shareholders: Evidence from proxy voting, ***Review of Financial Studies***, 25: 187–226.

Alchian, A. A. & Demsetz, H. 1972. Production, information costs, and economic organization, ***The American Economic Review***, 62: 777–795.

Alissa, W. 2015. Boards’ response to shareholders’ dissatisfaction: The case of shareholders’ say on pay in the UK, ***European Accounting Review***, 24: 727–752.

Armstrong, C. S., Gow, I. D., & Larcker, D. F. 2013. The efficacy of shareholder voting: Evidence from equity compensation plans, ***Journal of Accounting Research***, 51: 909–950.

Ashraf, R., Jayaraman, N., & Ryan, H. E. J. 2012. Do pension-related business ties influence mutual fund proxy voting? Evidence from shareholder proposals on executive compensation, ***Journal of Financial and Quantitative Analysis***, 47: 567–588.

Bainbridge, S. M. 2009. Is “say on pay” justified?, ***Regulation***, 32: 42–47.

Berle, A. & Means, G. 1932. ***The modern corporation and private property***. New York: Transaction Publishers.

Bhide, A. 1993. The hidden costs of stock market liquidity, ***Journal of Financial Economics***, 34: 31–51.

Bradley, M., Brav, A., Goldstein, I., & Jiang, W. 2010. Activist arbitrage: A study of open-ending attempts of closed-end funds, ***Journal of Financial Economics***, 95: 1–19.

Buchanan, B. G., Netter, J. M., Poulsen, A. B., & Yang, T. 2012. Shareholder proposal rules and practice: Evidence from a comparison of the United States and United Kingdom, ***American Business Law Journal***, 49: 739–803.

Burgess, K. & McCrum, D. 2012. Boards wake up to a shareholder spring. FT Group. Available at http://www.ft.com/cms/s/0/a284e414-95ee-11e1-a163-00144feab49a.html#axzz3prb3oOvV (accessed October 28, 2015).

Burns, N. & Minnick, K. 2013. Does say-on-pay matter? Evidence from say-on-pay proposals in the United States, ***Financial Review***, 48: 233–258.

Cai, J. & Walkling, R. A. 2011. Shareholders’ say on pay: Does it create value?, ***Journal of Financial and Quantitative Analysis***, 46: 299–339.

Carter, M. E. & Zamora, V. 2008. Shareholder remuneration votes and CEO compensation design. AAA 2008 MAS Meeting Paper.

Chowdhury, S. D. & Wang, E. Z. 2009. Institutional activism types and CEO compensation: A time-series analysis of large Canadian corporations, ***Journal of Management***, 35: 5–36.

Clark, C. E. & Crawford, E. P. 2012. Influencing climate change policy: The effect of shareholder pressure and firm environmental performance, ***Business & Society***, 51: 148–175.

Coffee, J. C., Jr.. 1991. Liquidity versus control: The institutional investor as corporate monitor, ***Columbia Law Review***, 91: 1277–1368.

Conyon, M. J. & Murphy, K. J. 2000. The Prince and the Pauper? CEO pay in the United States and United Kingdom, ***The Economic Journal***, 110: 640–671.

Conyon, M. J. & Sadler, G. 2010. Shareholder voting and directors’ remuneration report legislation: Say on pay in the UK, ***Corporate Governance: An International Review***, 18: 296–312.

Correa, R. & Lel, U. 2014. Say on pay laws, executive compensation, CEO pay slice, and firm value around the world. Working Paper.

Cotter, J. F., Palmiter, A. R., & Thomas, R. S. 2013. The first year of say-on-pay under Dodd-Frank: An empirical analysis and look forward, ***George Washington Law Review***, 81: 967–1011.

Cuñat, V., Gine, M., & Guadalupe, M. 2012. The vote is cast: The effect of corporate governance on shareholder value, ***The Journal of Finance***, 67: 1943–1977.

Cziraki, P., Renneboog, L., & Szilagyi, P. G. 2010. Shareholder activism through proxy proposals: The European perspective, ***European Financial Management***, 16: 738–777.

David, P., Bloom, M., & Hillman, A. J. 2007. Investor activism, managerial responsiveness, and corporate social performance, ***Strategic Management Journal***, 28: 91–100.

David, P., Hitt, M. A., & Gimeno, J. 2001. The influence of activism by institutional investors on R&D, ***Academy of Management Journal***, 44: 144–157.

Davis, G. F. & Kim, E. H. 2007. Business ties and proxy voting by mutual funds, ***Journal of Financial Economics***, 85: 552–570.

Davis, G. F. & Thompson, T. A. 1994. A social movement perspective on corporate control, ***Administrative Science Quarterly***, 39: 141–173.

Del Guercio, D. & Hawkins, J. 1999. The motivation and impact of pension fund activism, ***Journal of Financial Economics***, 52: 293–340.

Del Guercio, D., Seery, L., & Woidtke, T. 2008. Do boards pay attention when institutional investor activists “just vote no”?, ***Journal of Financial Economics***, 90: 84–103.

© 2015 John Wiley & Sons Ltd

Denis, D. K. & McConnell, J. J. 2003. International corporate governance, ***Journal of Financial and Quantitative Analysis***, 38: 1–36.
Department for Business Innovation & Skills. 2013. ***Enterprise and Regulatory Reform Act 2013***. London: HM Government.
Donaldson, T. & Preston, L. E. 1995. The stakeholder theory of the corporation: Concepts, evidence, and implications, ***The Academy of Management Review***, 20: 65–91.
DRR. 2002. The Directors' Remuneration Report Regulations 2002. ***Statutory Instruments 1986***. Available at http://www.legislation.gov.uk/uksi/2002/1986/pdfs/uksi_20021986_en.pdf (accessed October 28, 2015).
Edmans, A. 2009. Blockholder trading, market efficiency, and managerial myopia, ***The Journal of Finance***, 64: 2481–2513.
Edmans, A.. 2014. Blockholders and corporate governance. NBER Working Paper No. 19573.
Edmans, A., Fang, V. W., & Zur, E. 2013. The effect of liquidity on governance, ***Review of Financial Studies***, 26: 1443–1482.
Ertimur, Y., Ferri, F., & Muslu, V. 2011. Shareholder activism and CEO pay, ***Review of Financial Studies***, 24: 535–592.
Ertimur, Y., Ferri, F., & Oesch, D. 2013. Shareholder votes and proxy advisors: Evidence from say on pay, ***Journal of Accounting Research***, 51: 951–996.
European Commission. 2012. Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions of 12 December 2012, "Action Plan: European Company Law and Corporate Governance: A Modern Legal Framework for More Engaged Shareholders and Sustainable Companies". COM(2012): 740 (final).
European Commission. 2014. Commission Recommendation on the quality of corporate governance reporting ("comply or explain"), ***Official Journal of the European Union***, L109: 43–47.
Ferreira, M. A. & Matos, P. 2008. The colors of investors' money: The role of institutional investors around the world, ***Journal of Financial Economics***, 88: 499–533.
Ferri, F. & Maber, D. A. 2013. Say on pay votes and CEO compensation: Evidence from the UK, ***Review of Finance***, 17: 527–563.
Ferri, F. & Sandino, T. 2009. The impact of shareholder activism on financial reporting and compensation: The case of employee stock options expensing, ***The Accounting Review***, 84: 433–466.
Fischer, P. E., Gramlich, J. D., Miller, B. P. & White, H. D. 2009. Investor perceptions of board performance: Evidence from uncontested director elections., ***Journal of Accounting and Economics***, 48: 172–189.
Freeman, R. E. 1984. ***Strategic management: A stakeholder approach***. Boston, MA: Cambridge University Press.
Freeman, R. E., Wicks, A. C., & Parmar, B. 2004. Stakeholder theory and "the corporate objective revisited", ***Organization Science***, 15: 364–369.
Gillan, S. L. & Starks, L. T. 2000. Corporate governance proposals and shareholder activism: The role of institutional investors, ***Journal of Financial Economics***, 57: 275–305.
Goranova, M. & Ryan, L. V. 2014. Shareholder activism: A multidisciplinary review, ***Journal of Management***, 40: 1230–1268.
Greenwood, R. & Schor, M. 2009. Investor activism and takeovers, ***Journal of Financial Economics***, 92: 362–375.
Gregory-Smith, I., Thompson, S., & Wright, P. W. 2014. CEO pay and voting dissent before and after the crisis, ***The Economic Journal***, 124: F22–F39.
Guay, T., Doh, J., & Sinclair, G. 2004. Non-governmental organizations, shareholder activism, and socially responsible investments: Ethical, strategic, and governance implications, ***Journal of Business Ethics***, 52: 125–139.
Hausmann, Y. & Bechtold-Orth, E. 2013. Corporate governance: Is Switzerland outpacing Europe? A comparative legal analysis of current developments, ***European Business Organization Law Review***, 14: 535–562.
Hemphill, T. A. & Lillevik, W. 2009. US "say-on-pay" legislation, ***International Journal of Law and Management***, 51: 105–122.
Hillman, A. J., Shropshire, C., Certo, S. T., Dalton, D. R., & Dalton, C. M. 2011. What I like about you: A multilevel study of shareholder discontent with director monitoring, ***Organization Science***, 22: 675–687.
Iliev, P. & Vitanova, S. 2013. The effect of the say-on-pay vote in the US. Working Paper, Pennsylvania State University.
Jensen, M. C. & Meckling, W. H. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure, ***Journal of Financial Economics***, 3: 305–360.
John, K. & Klein, A. 1995. Shareholder proposals and corporate governance. New York University Working Paper No. FIN-98-046.
Kahan, M. & Rock, E. B. 2008. The hanging chads of corporate voting, ***Georgetown Law Journal***, 96: 1227.
Kahneman, D. & Tversky, A. 1979. Prospect theory: An analysis of decision under risk, ***Econometrica***, 47: 263–291.
Kalay, A., Karakas, O. & Pant, S. 2014. The Market Value of Corporate Votes: Theory and Evidence from Option Prices, ***The Journal of Finance***, 69: 1235–1271.
Karpoff, J. M., Malatesta, P. H., & Walkling, R. A. 1996. Corporate governance and shareholder initiatives: Empirical evidence, ***Journal of Financial Economics***, 42: 365–395.
Klein, A. & Zur, E. 2011. The impact of hedge fund activism on the target firm's existing bondholders, ***Review of Financial Studies***, 24: 1735–1771.
Krause, R., Whitler, K., & Semadeni, M. 2014. Power to the principals! An experimental look at shareholder say-on-pay voting, ***Academy of Management Journal***, 57: 94–115.
La Porta, R., Lopez-de-Silanes, F., Shleifer, A., & Vishny, R. 2000. Investor protection and corporate governance, ***Journal of Financial Economics***, 58: 3–27.
Mangen, C. & Magnan, M. 2012. "Say on pay": A wolf in sheep's clothing?, ***The Academy of Management Perspectives***, 26: 86–104.
Maug, E. 1998. Large shareholders as monitors: Is there a trade-off between liquidity and control?, ***The Journal of Finance***, 53: 65–98.
Norli, Ø., Ostergaard, C., & Schindele, I. 2015. Liquidity and shareholder activism, ***Review of Financial Studies***, 28: 486–520.
Nyukorong, R.. 2013. The Swiss binding say-on-pay: The pros and cons. Unpublished manuscript, SMC University, Zurich-Kloten, Switzerland.
Parrino, R., Sias, R. W., & Starks, L. T. 2003. Voting with their feet: Institutional ownership changes around forced CEO turnover, ***Journal of Financial Economics***, 68: 3–46.
Prevost, A. & Rao, R. 2000. Of what value are shareholder proposals sponsored by public pension funds?, ***The Journal of Business***, 73: 177–204.
Rehbein, K., Waddock, S., & Graves, S. B. 2004. Understanding shareholder activism: Which corporations are targeted?, ***Business & Society***, 43: 239–267.
Roe, M. J. 1990. Political and legal restraints on ownership and control of public companies, ***Journal of Financial Economics***, 27: 7–41.
Rowley, T. J. & Moldoveanu, M. 2003. When will stakeholder groups act? An interest- and identity-based model of stakeholder group mobilization, ***The Academy of Management Review***, 28: 204–219.
Shivdasani, A. & Yermack, D. 1999. CEO Involvement in the Selection of New Board Members: An Empirical Analysis, ***The Journal of Finance***, 54: 1829–1853.
Shleifer, A. & Vishny, R. W. 1986. Large shareholders and corporate control, ***Journal of Political Economy***, 94: 461–488.
Smith, M. P. 1996. Shareholder activism by institutional investors: Evidence from CalPERS, ***The Journal of Finance***, 51: 227–252.
Stathopoulos, K. & Voulgaris, G. 2015. The impact of investor horizon on say-on-pay voting. Paper presented at CAAA 2015 Annual Conference, May 28–31, 2015, Toronto, Canada.

© 2015 John Wiley & Sons Ltd

Thomas, R. S. & Martin, K. J. 1999. The effect of shareholder proposals on executive compensation, ***University of Cincinnati Law Review***, 67: 1021–1081.

Thomas, R. S. & Van der Elst, C. 2013. The international scope of say on pay. ECGI – Law Working Paper No. #227.

Wagner, A. F. & Wenk, C. 2015. Agency versus hold-up: On the impact of binding say-on-pay on shareholder value. Swiss Finance Institute Research Paper No. 11-12.

Yermack, D. 2010. Shareholder Voting and Corporate Governance, ***Annual Review of Financial Economics***, 2: 103–125.

Konstantinos Stathopoulos is Associate Professor at Manchester Business School, The University of Manchester, UK. He is an expert in corporate governance. His main research interests seek an understanding of how suboptimal governance practices destroy shareholder wealth and lead to crises in the markets. Some of his latest work investigates the impact of compensation on managerial risk taking, the role of compensation consultants on executive pay, and the effect of accounting standards on optimal contracting. He has published widely and his work has been presented in more than 40 international conferences in the US, Europe, and Asia.

Georgios Voulgaris is Assistant Professor at Warwick Business School, The University of Warwick, UK. His research interests are mainly focused on corporate governance and executive pay issues. His latest work examines the role of compensation consultants on executive pay and the impact of IFRS on corporate contracting. He has presented his work in a number of international academic conferences and has published in internationally excellent academic journals.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 371–385

Searching for Women on Boards: An Analysis from the Supply and Demand Perspective

Patricia Gabaldon*, Celia de Anca, Ruth Mateos de Cabo and Ricardo Gimeno

ABSTRACT

Manuscript Type: Review
Research Question/Issue: This paper seeks to provide a systematic review of the multidisciplinary theoretical approaches to women on boards in order to understand the factors that hinder and facilitate the access of women to boards, to show the instruments that can be used to promote women to senior corporate positions, and to outline a research agenda suggesting gaps that still need to be filled.
Research Finding/Results: Women's access to boards appears to be fragmented in research silos from a variety of areas, lacking a comprehensive view that provides instruments to overcome the barriers hindering the access of women to corporate boards. More in particular, this paper has found very little scientific analysis to understand what instruments can be the most efficient in eliminating barriers for women to reach boardrooms given different cultural environments.
Theoretical Implications: This paper aims to create a comprehensive framework for understanding the presence of women on boards and for indicating existing gaps to be filled by new research in the future. This framework will help future researchers in analyzing specific instruments and to measure their efficiency in eliminating gender imbalance. Depending on the approach taken for research, the theoretical backgrounds used vary. While on the supply side the predominant theories are gender role theory, gender self-schema, and work–family conflict, the demand side is based on gender discrimination, human and social capital theory, resource dependence theory, and institutional environment theory.
Practical Implications: This research provides suggestions to typify causes and provide nuanced policy tools to promote women into leadership positions. Future lines of research are proposed to fill the gaps in understanding female representation in top management positions.

Keywords: Corporate Governance, Demand Side, Literature Review, Supply Side, Women on Boards

INTRODUCTION

In recent decades, research on women on boards (WoB) has emerged and has resulted in a prolific amount of literature. Researchers have analyzed this issue from different angles, especially through the business case for diversity (Bilimoria, 2000; Dezsö & Ross, 2012; Terjesen, Sealy, & Singh, 2009).

Beyond the business case, contingency theorists advocate moral arguments over research results to promote and improve gender diversity (Gregory-Smith, Main, & O'Reilly, 2014; Simpson Carter & D'Souza, 2010). Although previous research has helped to place the issue of WoB on the agenda for both practitioners and policy makers, knowledge is still fragmented without exploring endogenous causes. Understanding all the benefits of a diverse board is essential in creating the most efficient tools to achieve equality. Therefore, our research goal is to shed light on the reasons why barriers preventing gender equality at the board level exist and to understand how to tackle such barriers and gauge their level of success.

We approach this question through a systematic review of the multidisciplinary approaches of women on boards that involves taking major reviews of literature prior to 2009 (Machold, Huse, Hansen, & Brogi, 2013; Terjesen et al., 2009) and updating them with more recent academic findings. In order to frame our analysis for the barriers confronting women in reaching board level, we have considered board directors as a labor market that could be analyzed from the perspective of supply and demand (Withers, Hillman, & Cannella, 2012). We focus on this perspective to shed light on the causes of inequality for WoB and to help analyze the efficacy of instruments that can be used to overcome the identified issues.

In the realm of WoB, the supply and demand perspective has been mentioned in the literature to explain some empirical outcomes, such as the gender gap in pay (Pucheta-Martínez & Bel-Oms, 2015) or differences in firm performance (Martín-Ugedo & Mínguez-Vera, 2014). Nevertheless, studies that have used some strategy to try to isolate demand and supply

*Address for correspondence: IE Business School, María de Molina, 11, 28006 Madrid, Spain. Tel: 915689772; Fax: 915689772; E-mail: patricia.gabaldon@ie.edu

© 2015 John Wiley & Sons Ltd
doi:10.1111/corg.12141

factors for the underrepresentation of female directors are more scarce (e.g., Farrell & Hersch, 2005; Gupta & Raman, 2014; Mateos de Cabo, Gimeno, & Escot, 2011).

Supply and demand-side distinctions are essential in diagnosing the causes for the underrepresentation of WoB. On the demand side, companies' decisions, potential for discrimination, and glass ceilings (Powell & Butterfield, 1997) imply that obstacles for WoB are most formidable at the top of the corporate hierarchy. In contrast, a supply-side analysis holds that gender imbalance is ultimately due to female considerations and constraints, such as different values, personal considerations about the family, and career decisions.

In general, there is a lack of research that links the efficiency of a solution instrument to the deconstruction of identified barriers. Supply and demand-side structures support the existing literature by building a holistic framework to understand the gaps. This framework provides researchers with a more comprehensive structure that can identify barriers preventing women from reaching the board as well as potential solution instruments and their relative efficacy. It also informs policymakers in creating appropriate public policy instruments to tackle gender equality in leadership positions. For instance, if a mandatory quota is above the supply of female directors, the outcome will be worse than voluntary quotas (Labelle, Francoeur, & Lakhal, 2015).

The use of the supply and demand-side perspectives also has important prescriptive implications. Understanding why companies increase the number of WoB is critical to solving this problem; the mechanisms used to promote female representation in the pool of board-member candidates are not necessarily the same as those aimed at eliminating or reducing potential bias in the nomination process.

The paper is organized as follows. We first explain the methodology used to select articles and previous literature reviews. In the next two sections, we analyze literature that explores existing barriers for women from both the supply and demand perspectives. The fourth section links previously identified barriers with recent research that identifies instruments to increase the number of WoB from both the supply and demand sides and their efficacy in achieving parity on boards. Finally, we analyze the identified content and methodological gaps in the existing literature and suggest future areas of research.

METHODOLOGY: SYSTEMATIC LITERATURE REVIEW

In order to understand the latest evolution of the analysis around women on boards in academic literature, a systematic literature review has been adopted (Campopiano, unpublished; Newbert, 2007). The process has employed the selection of articles from recent academic journals, specifically published in English peer academic journals since 2009, when the latest comprehensive review on the field by Terjesen et al. (2009) was published.

The selection criterion included peer-reviewed journal articles from January 1965 to May 2015. The first round of article selection was done on Business Source Complete, EconLit, and Behavioral Sciences Collection databases (EBSCO) using the keywords "female directors," "women on boards," and "women directors" in the title or the abstract. This initial search generated 187 articles. We then looked specifically for the main journals treating the topic of women on boards from the perspective of barriers and instruments to solve them. The journals meeting the criteria were *Academy of Management Journal*, *Corporate Governance: An International Review*, *Harvard Business Review*, *Journal of Business Ethics*, *Journal of Management*, *Journal of Management Studies*, *Scandinavian Journal of Management* and *Strategic Management Journal*. This second phase brought in 12 more articles relevant to the field. In order to ensure the relevance of the articles, all articles were read completely, checking for substantive relevance by identifying the discussion related to women on boards. Additionally, we included eight articles from sociology and psychology that had been cited in the sampled articles and were relevant to the research objectives.

The increasing participation in this discussion is spearheaded by the journals that have targeted this topic since 2009. These outlets are mainly the *Journal of Business Ethics* (13 articles), *Corporate Governance: An International Review* (7) and *Strategic Management Journal* (7) followed by *British Journal of Management* (2) and *Journal of Management and Governance* (3).

BARRIERS TO GENDER EQUALITY ON BOARDS

The underrepresentation of WoB may have supply and demand explanations. On the one hand, supply-side effects such as women's values and attitudes, expected gender roles, or family conflicts, can all result in a relatively limited pool of qualified female candidates for board positions (Bygren & Gähler, 2012; Gregory-Smith et al., 2014). On the other hand, demand-side effects on the side of corporations, such as discrimination, can hinder the progression of women up the corporate ladder.

Supply-Side Barriers

Following Pande and Ford (2011) and Terjesen et al. (2009), we divide supply-side barriers into three different groups: gender differences in values and attitudes, identification with gender role expectations, and work family conflict.

Gender Differences in Values and Attitudes. Potential differences between the genders in terms of values and attitudes can result in motivational differences between men and women to reach top leadership positions (Eagly, 2005). Women have been proven to be generally less hard achievers, less power-oriented (Adams & Funk, 2012) and less power-hungry than men (Schuh, Hernandez-Bark, Van Quaquebeke, Hossiep, Frieg, & Van Dick, 2014). Women sometimes even demonstrate more conservative behavior in boards and managerial decision making (Baixauli-Soler, Belda-Ruiz, & Sanchez-Marin, 2015).

Research that identifies basic differences among gender values and attitudes is mainly grounded in social constructionist theories and individuals' socialization (Weyer, 2007). This can even go further in social constructs, considering that gender differences cannot be assessed by the analysis of the current women managers, as feminine stereotypes might have already been denied. Somehow, these women select a

© 2015 John Wiley & Sons Ltd

management carrier and show features in terms of needs, values, and leadership roles, analogous to those of men who chase managerial careers (Powell, 1990).

Identification with Gender Role Expectations. Women might self-identify with expected cultural gender roles, creating potentially new, internal barriers to leadership positions. In this process, some females would not attempt to go for top management positions as they conflict with their personal self-image (Eddleston, Veiga, & Powell, 2006; Korman, 1970). It may be that individuals who perceive themselves as more masculine are more likely to aspire to senior management positions than those who identify less with masculinity (Powell & Butterfield, 2013). The theoretical basis for this stream of research is often related to gender self-schemas that are internalized during childhood through gender socialization processes (Greenwald, 1980).

A particular form of identification for women leaders is the stereotype threat, the fear that one's behavior may conform to an existing stereotype and thus may negatively impact performance (Steele & Aronson, 1995). This threat leads, paradoxically, to the confirmation of the stereotype by diminishing performance and lessening motivation to succeed, generating vulnerability and anxiety in female leaders (Hoyt, Johnson, Murphy, & Skinnell, 2010).

Work–family Conflict. Women's commitment to family responsibilities, often labeled as work–family conflict, is probably the most commonly identified barrier preventing women from reaching leadership positions (Greenhaus & Beutell, 1985; Newell, 1993; Wirth, 1998). Women tend to devote more hours than men to family activities yet the same number of hours to work (Eby, Casper, Lockwood, Bordeaux, & Brinley, 2005) and this leads to unequal career opportunities (Straub, 2007). Nevertheless, the WoB literature is inconclusive in confirming that family life is a career barrier for women. Contrary to what is typically expected, some women have been found to not experience work–family conflict, but rather a higher positive spillover than men (Powell & Greenhaus, 2010). On the other hand, fathers have found greater chances of promotion, whereas women's opportunities remain unaffected by motherhood (Bygren & Gähler, 2012).

Demand-Side Barriers

Gender Discrimination. Gender discrimination can be defined as a prejudice or bias based on gender (Becker, 1957). We can identify different types of potential discrimination affecting women in top positions. First, gender can be used to proxy unmeasured specific and differential group characteristics. This might lead to judgments based on average group characteristics rather than individuals, resulting in *statistical discrimination* (Phelps, 1972). This concept is closely related to *mistake-based discrimination*, the systematic underestimation of women's skills (Wolfers, 2006). Along the same lines, *taste-based discrimination* or a preference for male leaders is often ingrained in cultural and social conventions that associate corporate leadership with masculinity (Heilman, 2001; Pande & Ford, 2011). Such cultural norms ascribe socialized characteristics to men and women, shaping expectations on what constitutes appropriate behavior (Eagly, 1987) and can result in a biased promotional system (Hoobler, Wayne, & Lemmon, 2009). Finally, *implicit discrimination* (Bertrand, Chugh, & Mullainathan, 2005) refers to biases that people may never consciously acknowledge.

In the WoB literature, there is support for gender bias in the appointment of female directors. This has been proven recently through the case study of UK listed companies (Gregory-Smith et al., 2014) and Spanish corporations (Mateos de Cabo et al., 2011).

One particular type of discrimination that explains the low numbers of WoB is *tokenism* (Kanter, 1977). *Tokenism* posits that when the presence of different types of persons within a given work group are reduced, those minority members became symbols or "tokens," and they are viewed as representatives of their social category rather than as individuals. Therefore, boards where female representation is zero or low are more likely to appoint a female director (Gregory-Smith et al., 2014). However, WoB do not always comply with the pressures of conformity, and in these cases, tokenism's visibility mechanism does not affect them. Female ratios are positively related with WoB's perceptions to information sharing, social interaction, and influence, giving credence to some kind of isolation and role entrapment mechanism (Elstad & Ladegard, 2012).

Social identity theory (Tajfel, 1972) attempts to explain why some agents, men in this case, tend to be appointed to senior corporate positions. The similarity and identification among members of groups create a division between in- and out-group members. This implies that in-group members would receive better evaluations, creating a barrier for the out-group individuals to join these networks (Terjesen et al., 2009). Furthermore, group dynamics may hinder the influence of WoB as they may be considered different from the rest of the members, i.e. as out-group members (Carter, D'Souza, Simkins, & Simpson, 2010; Westphal & Milton, 2000; Zhu, Shen, & Hillman, 2014). Additionally, social identity theory addresses the way identity influences interactions among individuals from different groups. In this realm, Chen, Crossland, and Huang (2014) argue that higher levels of WoB influence intra-board social psychological processes increasing decision-making comprehensiveness, which in turn results in more exhaustive evaluations of major strategic proposals. Indeed, within the context of mergers and acquisitions of S&P 1,500 firms, greater female board representation was negatively associated with both overall firm acquisitiveness and target acquisition size.

Finally, the *glass cliff* (Ryan & Haslam, 2007) is described as the tendency to prefer women for senior positions for organizations in crisis (Haslam, Ryan, Kulich, Trojanowski, & Atkins, 2010). Cook and Glass (2014b) found that women are more likely than men to become the promoted CEO of weakly performing firms and that when firm performance declines during the tenure of women CEOs, they are likely to be replaced by white men. Even in extreme scenarios, when a woman manager asserts directive authority, these implicit biases can make others struggle with it, through hostility and resistance (Eagly & Karau, 2002). In order to escape this criticism, female leaders need to be perceived as effective, but also show strength and sensitivity, while only strength is needed for male leaders (Johnson, Murphy, Zewdie, & Reichard, 2008).

© 2015 John Wiley & Sons Ltd

Biased Perceptions of What Women May Bring to the Board. Thorough research finds generalized biased perceptions toward female directors' capabilities, expertise, resources, and networking capacity. These biases manifest into additional barriers for women in leadership. Board selectors usually assume that women lack the adequate expertise or knowledge, i.e., human capital (Becker, 1964; Ragins, Townsend, & Mattis, 1998). Hence, WoB face the stereotype of being underprepared and less effective than their male counterparts (Mensi-Klarbach, 2014; Nielsen & Huse, 2010). Nevertheless, certain literature has a different view, suggesting that rather than less human capital, women have unconventional backgrounds and, therefore, merely have different types of human capital (Hillman, Cannella, & Harris, 2002; Ruigrok, Peck, & Tacheva, 2007). In terms of experience, lack of or reduced board experience is often seen as the main barrier for women (Groysberg & Bell, 2013) when looking for independent directorships. However, it appears that women are more likely to have alternative experiences as directors, for instance, on the boards of NGOs or small firms, but less in top managerial positions. These women tend to compensate their reduced board experience with formal education, leading to higher numbers of women with MBA degrees and international experience (Singh, Terjesen, & Vinnicombe, 2008). In Canada, for instance, women appointed to all-male Canadian boards have a specialized skill, either by being insiders or being specialists (Dunn, 2012).

Another common assumption, based on social capital theory (Coleman, 1988; Loury, 1977) resides on the connections that candidates bring to boards, from inside and outside the firm (Kim & Cannella, 2008). Women's traditional reduced access to networks has been identified as one important problem in accessing leadership positions (Ibarra, 1992; Kanter, 1977; McGuire, 2002; Ragins et al., 1998). One solution is the creation of women's professional networks, but such communities yield fewer leadership opportunities, provide less visibility, and generate less recognition and endorsement (Ely, Ibarra, & Kolb, 2011).

The capacity of influence has also been widely analyzed in the WoB literature. Ingratiation, the interpersonal influence behavior that enhances one's interpersonal attractiveness to become more likeable to specific others (Kumar & Beyerlein, 1991) can be a key element for the potential demand of WoB. The deferential and submissive quality of ingratiation can be of especial importance in environments where personal trust has been and still is essential, as in top management teams (Kanter, 1977). Directors' ingratiatory behaviors toward colleagues could yield board appointments at other firms. This behavior implies relatively refined forms of adulation and conformity. In some cases, women could benefit from more sophisticated tactics that are difficult to be interpreted as manipulative when indulging in ingratiatory behavior (Stern & Westphal, 2010).

Resource dependency theory (Pfeffer & Salancik, 1978) is also often mentioned as a theoretical framework to explore general perceptions about the resources women can bring to a directorship. This theory relies on the idea that female resources could provide critical benefits to the firm that may provide them with greater opportunity to attain top positions. Hill, Upadhyay, and Beekun (2015) found that female CEOs receive higher compensation and are less likely to exit the position than white males. Nevertheless, these perceptions also serve as barriers to women's aspirations, linking the resource dependence role of directors with committees' assignments and gender. Therefore, women are more prone to be appointed to public affairs committees and less to executive committees (Peterson & Philpot, 2007). Having women in charge of audit committee chairs reduces audit fees for corporations, as women seem to improve the effectiveness of internal control activities (Ittonen, Miettinen, & Vähämaa, 2010).

Institutional Environment. Some institutions and their potential rigidities in the external environmental may produce structural barriers for women on corporate boards (Cook & Glass, 2014a; North, 1990). Countries with higher numbers of WoB also show more women in senior management positions, smaller gender pay gaps, and shorter periods of women's political representation (Terjesen & Singh, 2008). Additionally, institutional elements, such as female presence in the labor market, welfare state attitude toward gender, and the presence of left parties in government, influence gender equality policies (Terjesen, Aguilera, & Lorenz, 2015). Accordingly, cultural and legal institutional systems seem to have a highly significant effect on board diversity (Grosvold & Brammer, 2011) as well as the main actors in charge of the national public policies for WoB (Seierstad, Warner-Søderholm, Torchia, & Huse, 2015).

INSTRUMENTS THAT INCREASE THE NUMBER OF WOMEN ON BOARDS

Supply Side

The reduced numbers of female candidates in the pipeline to boards is one of the most highly cited reasons for the implementation of public policies promoting WoB. Although the literature does not normally link barriers with solution instruments, research that analyzes instruments for female leadership in business often assumes particular barriers that women face. Gender differences in values and attitudes might make women less visible than men for leadership promotions. To tackle this problem, research on the topic has already offered instruments to help increase women's visibility and other talent pools (Mateos de Cabo et al., 2011). Among these tools are the presence of role models and mentoring or training programs available to women with professional aspirations. The final set of instruments focuses on policies to reduce work–family conflicts. Policies to achieve a more equal distribution of domestic responsibilities between men and women (e.g., equal and non-transferable paternity leave), have been by far the most widely analyzed solutions in the literature.

Aspirations and **V**isibility. Visibility encourages and motivates women to attain leadership positions (Pande & Ford, 2011). These initiatives include candidate databases, such as Europe's Global Board Ready Women. The utility and efficacy of such databases were discovered more than a decade ago (Zelechowski & Bilimoria, 2004) but have not been the focus of academic research. Another way to increase the public profile of female candidates is through visibility in the media,

© 2015 John Wiley & Sons Ltd

although women still seem to be underrepresented across this medium (De Anca & Gabaldon, 2014a; Mateos de Cabo, Gimeno, Martínez, & López, 2014).

Role Models and Mentorship. Role models can strongly influence career development (Gibson, 2003, 2004). Individuals identify themselves with role models by looking for similarities among a large pool of numerous positive examples (Gibson, 2004; Vinnicombe & Singh, 2002) with whom they may interact in different moments in time. Motivation to attain positions of power can be enhanced by female role models (Waldman, Galvin, & Walumbwa, 2013) in top positions; they particularly motivate women and help guide their individual development (Gibson, 2003, 2004) in many cases through admiration and idealization (Kelan & Mah, 2014). Professional identification is key for women in business as it helps them to discover role models they could emulate (Sealy & Singh, 2010).

The lack of female role models is often cited as a reason for the low numbers of women in managerial positions (Sealy & Singh, 2010). People usually look for role models similar in gender or race (Eriksson-Zetterquist, 2008; Kelan & Mah, 2014; Sealy & Singh, 2010). Women frequently find themselves having to look externally because of the dearth of role models in their close professional settings (Singh et al., 2006).

Mentors could also be considered eventual role models, but relationships in this case are more rooted in both parties' interactions, usually more limited and longer term (Durbin & Tomlinson, 2014). However, role modeling can be formalized through mentorship or even sponsorship, offering women extra guidance in their professional track.

When men mentor women, it is believed they offer less psychosocial support. When women mentor other women, facilitating integration into the firm's culture might become more difficult, as these women might be less well integrated themselves (Groysberg, 2008) and, in some cases, even considered for fewer positions and receive less mentoring (McDonald & Westphal, 2013). Female mentors usually provide more personal and emotional support, career development guidance, and role modeling identification than men (Fowler & O'Gorman, 2005), and thus more psychosocial help than male mentors (Okurame, 2007). Although senior women are more likely than other women to have mentors, they are still less likely when compared to their male colleagues (Groysberg, 2008). However, any extra help provided by sponsorship to female candidates has been considered as the best way to break the glass ceiling (Hewlett, Peraino, Sherbin, & Sumberg, 2010).

Work–Family Policies. Conciliation seems to be an issue for all working women, but it has a tangible effect on the number of candidates for WoB. Work–family policies are structured as organizational policies and practices to help employees in controlling their work hours and workload (Kossek, Baltes, & Matthews, 2011). Some of the most relevant work–family arrangements by employers are leave to take care of dependants (Den Dulk, Groeneveld, Ollier-Malaterre, & Valcour, 2013) and flexible working hours (Allen, Johnson, Kiburz, & Shockley, 2013). There is general agreement that providing flexible work measures benefits women's work–life structures (O'Neil, Hopkins, & Bilimoria, 2008). Women with university degrees and postgraduate qualifications also must contend with work–family conflicts, sometimes choosing to opt out of the workforce (Leslie & Manchester, 2011), reducing of the number of candidates for WoB.

However, taking advantage of these policies is frequently incompatible with climbing up to management positions (Drew & Murtagh, 2005). Career consequences of an employee's decision to use family-friendly policies can be negative (Manchester, Leslie, & Kramer, 2010). In this sense, everyone who uses parental leave policies would be perceived as uncommitted and, therefore, unlikely to be considered for promotions (Leslie & Manchester, 2011). The main issue here is that work–family practices are framed as women's issues, perpetuating the assumption of work–family conflict as an obstacle faced only by women (Leslie & Manchester, 2011). In fact, work–family conflict is cited more frequently for women than for men as the reason behind career withdrawal (Moe & Shandy, 2010).

Given that gender equality programs are intended to encourage and support women in their careers, women are more likely to support these programs while men might perceive them as a threat to their careers (Van den Brink & Stobbe, 2014). The idea that work–family policies are targeted only at women is why these initiatives are looked down upon (Kossek et al., 2011); consequently, men using work–family arrangements might be seen as violating traditional gender-based roles (Leslie & Manchester, 2011).

However, resistance toward equality initiatives is not limited to men; some women perceive little necessity for such changes, especially if beneficiaries of equality programs are confronted with unwarranted doubts about their qualifications (Van den Brink & Stobbe, 2014). The main problem with these benefits is that they must be supported by workplace culture. Can these policies be used without backlash? Users of such programs must also find ways to avoid cultural stigmatization and being seen by one's employer as less committed or performing less effectively (Kossek et al., 2011).

Demand Side

Demand side policies are designed to raise the number of WoB by affecting the behavior of company-hiring directors. The most commonly used tools to fight any kind of discrimination, conscious or unconscious, are affirmative action policies, promoting the presence of the most unrepresented gender, women in the majority of cases. Affirmative action can be differentiated into "equality of outcomes" and "equality of opportunity" (Seierstad & Opsahl, 2011). Equality of outcome refers to hard measures against gender inequality to increase the number of WoB (quotas, targets, or earmarking). Equality of opportunities looks instead to stimulate demand rather than forcing it: soft law initiatives, corporate governance codes, and the "comply or explain" principle (Nielsen & Tvarnø, 2012), or even voluntary quotas or raising awareness (Pande & Ford, 2011).

Legislative gender quotas have been applied to different arenas in the political, social, and economic domains of life (Meier, 2014). The fact is that all over the world, barriers for women remain, and only countries with mandatory quotas have been able to get close to gender equality in the boardroom. Moreover, quotas can provide a way for women to sidestep discrimination (Pande & Ford, 2011).

© 2015 John Wiley & Sons Ltd

Quotas are meant to disrupt structural barriers and create endogenous instruments to sustain female recruitment and presence beyond specific numbers. Critical mass theory (Kanter, 1977) shows that when a certain level is reached, the subgroup's degree of influence grows. Some studies have tested this critical mass theory, exploring women's contributions to corporate boards of directors. Achieving this critical mass might affect innovation (Torchia, Calabro, & Huse, 2011), quality of corporate social responsibility (CSR) reporting (Fernandez-Feijoo, Romero, & Ruiz, 2012), or CSR perceptions (Post, Rahman, & Rubow, 2011). Furthermore, women's perceived influence increases when they are more highly represented on the board (Elstad & Ladegard, 2012).

As not all countries have implemented gender quotas for corporate boards, simulations have been run to test their potential effects. Kogut, Colomer, and Belinky (2014) used a simulation to understand what kind and what level of mandatory quotas would be needed in the United States to significantly increase gender equality on boards. Their results suggest that quotas improve women's clustering and connectivity, thus benefitting women's positions. However, without this improvement, women's positions worsen. In general terms, gender quotas force firms to find, "identify, develop, promote, and retain suitable female talent" for their boards (Terjesen et al., 2015: 235). France has also approved a gender quota recently, as the presence of women was much lower than men, but there were similar candidates in terms of education and expertise (Dang, Bender, & Scotto, 2014). Mateos de Cabo et al. (2011) found that the presence of women on Spanish boards also made the appointment of additional women more likely.

However, gender quotas can come with drawbacks, especially if they are analyzed beyond the business case (Seierstad, 2015). They might create more gender diverse boards, but shareholders might suffer if previous male directors are replaced by less competent women just because of the gender quota requirement and other corporate legislation (Ahern & Dittmar, 2012). Due to the reduced number of women in the pipeline, the appointment of less experienced directors may result in poorer performance; women may invest less in their careers given their relatively easier career path, and eventually lead owners and shareholders to reject policies imposed on their boards based just on gender (Pande & Ford, 2011). Some of the effects, initially unexpected, are the creation of a group of women holding multiple seats on boards – "the golden skirts" (Seierstad & Opsahl, 2011).

Gender quotas could also affect companies in unexpected ways. In Norway, one of the negative effects of gender quotas was that some firms ended up with the right organizational form but the wrong board, as women on average were younger and had less board experience (Bøhren & Staubo, 2013). Going even further, some firms exposed to the gender balance law in Norway chose to exit into an organizational form not regulated under the gender quota, citing mandatory regulation on gender balance in the boardroom as lowering the firm's value (Bøhren & Staubo, 2013). Additionally, some chairmen were less satisfied with female board members not contributing positively to perceptions of the board's decisions (Brunzell & Liljeblom, 2014).

Alternatives or complements to mandatory quotas are soft quotas or voluntary efforts to meet quotas, which serve as other examples of instruments for equality of opportunity. In a recent initiative, Australia introduced a soft regulatory approach through recommendations regarding gender diversity policies, creating strong external pressures to conform. This voluntary period approach has been successful in creating more gender diverse boards in Australia (Chapple & Humphrey, 2014), even creating high expectations for the country's future economic development (Galbreath, 2011). In Spain (Lucas-Pérez, Mínguez-Vera, Baixauli-Soler, Martín-Ugedo, & Sánchez-Marín, 2015) and the Netherlands (Lückerath-Rovers, 2013), business cases linking effectiveness of boards to gender diversity have also proven to be effective. Extreme examples have been seen in transitional economies, usually with underdeveloped corporate governance systems and no regulations on gender diversity (Nguyen, Locke, & Reddy, 2014); nevertheless, some positive effects from the business-based argument have been felt (Abdullah, Ismail, & Nachum, 2015), bringing talent into candidate pipelines (Tatli, Vassilopoulou, & Özbilgin, 2012). Meanwhile, in New Zealand, the number of WoB has remained stagnant and may require mandated quotas in order to move forward (McGregor, 2014).

However, in most countries, voluntary approaches to gender equality on boards go hand in hand with corporate governance codes (Seierstad & Opsahl, 2011). Usually, private companies respond to the warning of potential legislated gender quotas by including references to the need for diversity on their boards in their corporate governance reports. The effect of these codes relies on peer pressure among corporations and pressure from stakeholders and media, as corporate governance codes usually do not imply penalties for non-compliance.

High levels of transparency create higher pressure on companies to comply, and ultimately to cope with any kind of biases in selection or treatment. For instance, nomination committees influence gender diversity in boards (Kaczmarek, Kimino, & Pye, 2012). The presence of women can have direct effects on corporate reputation (Bernardi, Bosco, & Columb, 2009; De Anca & Gabaldon, 2014b) as well as CSR actions (Bear, Rahman, & Post, 2010; Boulouta, 2013), and corporate sustainability (Galbreath, 2011). Furthermore, media can have a great impact in breaking stereotypes and influencing decisions. In this regard, journalistic concerns, for example, can lead to less social discrimination in top positions (Park & Westphal, 2013).

Finally, national context idiosyncrasies can play a very important role in establishing roots for the equal presence of women in top managerial positions. In this sense, understanding different national realities from the structural-institutional side (Terjesen et al., 2015) and the different actors involved in launching different national public policies (Seierstad, 2015) can determine the outcome in terms of female presence. Socio-cultural contexts, such as gender parity (Post & Byron, 2015) or Hofstede's cultural dimensions (Carrasco, Francoeur, Labelle, Laffarga, & Ruiz-Barbadillo, 2015) illustrate tolerance for inequality and can be critical for the demands of WoB.

FUTURE DEVELOPMENTS

This research attempts to understand the factors that hinder or facilitate women's access to boards and, for that purpose, we have conducted a literature review on issues and constructs

© 2015 John Wiley & Sons Ltd

that explain the reasons behind this inequality at board level, using a theoretical framework of supply and demand. Results indicate that, while barriers have been the object of academic research, instruments' efficiency is gauged through case study analyses, making it difficult to draw general conclusions. Results also illustrate that there is more scientific research on the demand side than on the supply side with the exception of the focus on work–family issues.

The paper proposes a more holistic approach using the theoretical framework of supply and demand. Linking supply and demand is complex from an empirical point of view, due to the great difficulty involved in both matching processes (Withers et al., 2012). However, the structure helps to identify existing gaps and thus is vital for building a more comprehensive framework for future research.

Therefore our recommendation is to conduct scientific research that can combine supply and demand in the different areas identified. In order to do this, the research should be conducted: (a) differentiating supply and demand to determine in which cases the reasons behind inequality on boards are due to supply or demand factors; and (b) linking barriers with instruments to analyze the effectiveness of those instruments on the identified barriers.

An interdisciplinary approach, based on the supply and demand-side framework can help to move the existing literature forward by identifying the most appropriate methodology for measuring and selecting the appropriate linkages among problems and policies, bringing together different methods, to help policymakers in the design of policies to achieve gender parity on boards.

In addition to the general recommendation, and in more specific terms through the review, it has identified that certain concrete areas are still not sufficiently covered by research and they would benefit from further research. The following sections state those in more detail.

Supply Side

The review has found abundant literature demonstrating concrete gender differences in values and attitudes, identification with gender role expectations and work–family conflicts (see Table 1 for more detail). The review, however, has also found some important gaps. First, no conclusive evidence exists regarding specific attitudes and behaviors of female directors, such as risk aversion; given that this preconception is one of the main obstacles preventing women from reaching leadership positions, it is crucial that it should be properly understood and thoroughly researched. Controlled experiments across two distinct societies, such as the one by Gneezy, Leonard, and List (2009), could play a pivotal role when it comes to testing gender differences in values and attitudes.

Previous studies on potential biases in the selection process of directors only observe the characteristics of successfully appointed candidates (Farrell & Hersch, 2005; Gregory-Smith et al., 2014). Therefore, there is need of an empirical set-up where director candidates as well as the recruiters and final decision makers, could be observed to identify whether the low percentage of female directors is actually rooted in the searching and hiring processes. Future research should look for new methodologies, such as simulations, laboratory experiments, and event studies to help uncover knowledge that may be difficult to obtain through traditional secondary data (Finkelstein, Hambrick, & Cannella, 2009; Joshi, Liao, & Roh, 2011).

Supply-Side Instruments

In the case of supply policies, we see a general scarcity of research linking these solution initiatives with actual improvement in the presence of WoB. Promising future research, as indicated by Withers et al. (2012), could be the integration of economic and social approaches.

The small numbers of women in top positions, as well as the time lag needed for the effectiveness of policy initiatives, has made it difficult to analyze the role of career instruments such as mentoring or sponsorship, as well as the family–work implications for these women. For instance, we need to know whether the inclusion in databases of female candidates increases the likelihood of these candidates to be nominated to a board, or whether mentoring or sponsorship create a real difference in women's career climbs to the top.

We also encourage future research to investigate the impact of different organizational career structures. Organizations that accept and support women will clearly have a competitive edge in keeping their most talented employees (O'Neil et al., 2008).

Demand Side

There is solid literature that identifies the barriers on the demand side in different areas including: gender discrimination, biased perceptions of women's attitudes due to lack of human capital, lack of social capital, and ingratiation (see Table 2 for more detail).

There are several types of discrimination in labor markets; indeed, the characteristics of these different types of discrimination are usually mixed. To prescribe the right instruments to increase WoB, we must first identify the type of gender discrimination that occurs. Other forms of gender discrimination can be based on sociological theories such as status construction theory (Berger, Ridgeway, & Zelditch, 2002) or social dominance theory (Sidanius & Pratto, 2004). Researching the effects of these forms of discrimination on WoB would lead to greater insight into developing effective instruments to increase WoB.

If bias exists at the board level, it would be very useful to propose a model to try to understand the internal psychological/organizational mechanism through which these processes take place. In this sense, structural equation modeling can be very useful to measure and relate constructs and variables than could be part of the game.

Demand-Side Instruments

When it comes to demand instruments, research is still expanding, looking more comprehensively at its applications to the real world. The implementation of quotas or pseudo-quotas at national level can force companies to comply but not necessarily believe. For this reason, analysis of voluntary positive gender policies versus mandatory approaches is needed to understand their potential effects and counter-effects in increasing gender equality (Hillman,

© 2015 John Wiley & Sons Ltd

TABLE 1
Summary of References on the Supply Side: Barriers and Instruments

Supply				**Main literature gaps**
General references	– Pande and Ford (2011) – Terjesen et al. (2009) – Bygren and Gähler (2012) – Gregory-Smith et al. (2014)		Content: – Lack of linkage between barriers and instruments in the supply side – Find appropriate measures to analyze the effectiveness of instruments to eliminate identified barriers Methodology: – Difficulty in traditional secondary data, need new methodologies, simulations, laboratory experiments, collaborative methodologies – Interdisciplinary – Cross-cultural – Qualitative methodologies to give voice to women's itineraries	
Problem/barrier	**Key references + recent updates**	**Instrument**	**Key references + recent updates**	**Main literature gaps**
Gender differences in values and attitudes	Powell (1990) Eagly (2005) Weyer (2007) Adams and Funk (2012) Schuh et al. (2014) Baixauli-Soler et al. (2015)	Aspirations and visibility	Mateos de Cabo et al. (2011) Pande and Ford (2011) Zelechowski and Bilimoria (2004) De Anca and Gabaldon (2014a) Mateos de Cabo et al. (2014)	Content: Deep analysis on attitudes such as risk aversion Methodologies: Selection process analysis
Identification with gender role expectations	Korman (1970) Greenwald (1980) Steele and Aronson (1995) Eddleston, Veiga, & Powell (2006) Hoyt et al. (2010) Powell and Butterfield (2013)	Role models and mentors	Singh, Kumra, and Vinnicombe (2002) Vinnicombe and Singh (2002) Gibson (2003, 2004) Fowler and O'Gorman (2005) Okurame (2007) Eriksson-Zetterquist (2008) Groysberg (2008) Sealy and Singh (2010) Hewlett et al. (2010) Sealy and Singh (2010) Waldman et al. (2013) McDonald and Westphal (2013) Kelan and Mah (2014) Cook and Glass (2014a, 2014b) Durbin and Tomlinson (2014)	Content: Women identification to role expectations Nature or nurture?
Work–family conflict	Greenhaus and Beutell (1985) Newell (1993) Wirth (1998)	Work and family policies	Drew and Murtagh (2005)	Content

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 1 (Continued)

Supply				**Main literature gaps**
	Straub (2007) Powell and Greenhaus (2010) Bygren and Gähler (2012)		O'Neil et al. (2008) Kossek et al. (2011) Leslie and Manchester (2011) Manchester et al. (2010) Moe and Shandy (2010) Den Dulk et al. (2013) Allen et al. (2013) Durbin and Tomlinson (2014) Van den Brink and Stobbe (2014)	Link problems and instruments combining social and economic approaches

TABLE 2
Summary of References on the Demand Side: Barriers and Instruments

Demand				**Main literature gaps**
Problem/barrier	**Key references + recent updates**	**Instrument**	**Key references + recent updates**	**Lack of linkage between barriers and instruments in the demand side**
Gender discrimination	Becker (1957) Phelps (1972) Eagly (1987) Heilman (2001) Bertrand et al. (2005) Wolfers (2006) Hoobler et al. (2009) Mateos de Cabo et al. (2011) Pande and Ford (2011) Gregory-Smith et al. (2014) Tokenism Kanter (1977) Elstad and Ladegard (2012) Tajfel (1972) Westphal and Milton (2000) Terjesen et al. (2009) Carter et al. (2010) Gregory-Smith et al. (2014) Zhu et al. (2014) Eagly and Karau (2002) Ryan and Haslam (2007)	Quotas and other legislative approaches Company self-regulatory policies Corporate governance codes Company policies and training in awareness Critical Mass numbers	Quotas, Legislation & Corporate Governance Pande and Ford (2011) Seierstad and Opsahl (2011) Post et al. (2011) Torchia et al. (2011) Elstad and Ladegard (2012) Fernandez-Feijoo et al. (2012) Nielsen and Tvarnø (2012) Meier (2014) Mateos de Cabo et al. (2011) Ahern and Dittmar (2012) Dang et al. (2014) Kogut et al. (2014) Terjesen et al. (2015)	Content barriers: Other forms of discrimination based on sociological theory or sociological theory and how this can be applied to WoB literature Specific type of discrimination that is applied in order to apply the specific targeted instrument Barriers Methodology Structural equation modeling methodology to try to understand the internal psychological/organizational mechanisms Content Instruments: Analysis of the outcomes quotas as well as voluntary policies Analysis of the potential counter effects of quotas and voluntary approaches. Methodology instruments:

(Continues)

© 2015 John Wiley & Sons Ltd

TABLE 2 (Continued)

Demand				Main literature gaps
Problem/barrier	Key references + recent updates	Instrument	Key references + recent updates	Lack of linkage between barriers and instruments in the demand side
			Seierstad (2015)	
	Johnson et al. (2008)			
	Haslam et al. (2010)		Bernardi et al. (2009)	Cross-company analysis of how different companies apply the different instruments
			Bear et al. (2010)	
Biased perception of women's attitudes	Lack of human capital perception		Galbreath (2011)	
	Becker (1964)		Bøhren and Staubo (2013)	
	Ragins et al. (1998)			
	Hillman et al. (2002)		Boulouta (2013)	
	Ruigrok et al. (2007)		Kaczmarek et al. (2012)	
	Singh et al. (2008)			
	Nielsen and Huse (2010)		Brunzell and Liljeblom (2014)	
	Dunn (2012)		Tatli et al. (2012)	
	Groysberg and Bell (2013)		Lückerath-Rovers (2013)	
	Mensi-Klarbach (2014)		Park and Westphal (2013)	
	Social Capital theory			
	Loury (1977)		Chapple and Humphrey (2014)	
	Kanter (1977)			
	Coleman (1988)			
	Ibarra (1992)		De Anca and Gabaldon (2014b)	
	Ragins et al. (1998)			
	McGuire (2002)			
	Kim and Cannella (2008)		Lucas-Pérez et al. (2015)	
	Ely et al. (2011)		McGregor (2014)	
	Ingratiation		Nguyen et al. (2014)	
	Kanter (1977)			
	Kumar and Beyerlein (1991)		Abdullah et al. (2015)	
	Stern and Westphal (2010)			
	Resource dependency theory			
	Pfeffer and Salancik (1978)			
	Peterson and Philpot (2007)			
	Ittonen et al. (2010)			
Institutional and cultural barriers	North (1990)		Post and Byron (2015)	Cross-cultural research on the different barriers as well as the different drives to introduce the quotas and other instruments
	Terjesen and Singh (2008)		Carrasco et al. (2015)	
	Grosvold and Brammer (2011)		Terjesen et al. (2015)	
	Cook and Glass (2014a, 2014b)		Seierstad et al. (2015)	In-depth analysis of the different agents involved and their reasons for involvement
	Terjesen et al. (2015)			
	Seierstad et al. (2015)			

© 2015 John Wiley & Sons Ltd

2015). Furthermore, we need to understand how companies interpret and apply these regulations on a day-to-day basis. Comparisons between countries implementing the same gender quotas will allow researchers to understand where barriers to gender equality originate and to tackle them more efficiently (Hillman, 2015).

Finally, the golden skirt phenomenon has been used to criticize the implementation of quota policies. Contrary to what has been found in Norway (Seierstad & Opsahl, 2011), in Italy quotas are not associated with more female members on multiple boards (Profeta, Aliberti, Casarico, S'Amico, & Puccio, 2014). This discrepancy shows us that we must look for methodologies to help us test this assertion. If it is true, then we should ask which part of the phenomenon is due to demand-side (glass ceiling) and what part is due to supply-side factors such as a reduced pool of eligible women.

Cross-Cultural Research

The WoB literature would benefit from a more cross-cultural perspective, analyzing whether the gender gap on boards is due to supply or demand factors and how this varies across cultures. In analyzing the cultural context, it is important to acknowledge that the same instruments may have varying levels of success in different cultural contexts. For instance, Farrell and Hersch (2005) found that the presence of WoB was an obstacle for the appointment of new female directors in the US, but Mateos de Cabo et al. (2011) found the opposite effect in Spain.

Starting from a general approximation, several papers have looked at WoB in different national and cultural environments (Ahern & Dittmar, 2012; Bianco, Ciavarella, & Signoretti, 2015; Mateos de Cabo et al., 2011). However, results do not always point in the same direction. Therefore, more research is needed in cross- or multi-cultural samples, following Terjesen et al. (2015); Seierstad and Opsahl (2011), or Mateos de Cabo, Gimeno, and Nieto (2012), or in other new national contexts such as emerging markets (Abdullah et al., 2015).

Contribution to the Literature

By framing the issue around supply and demand-side factors throughout a systematic review of recent research, we have garnered new insights, loops and gaps in the actual research, with a comprehensive holistic framework centered on the issue of WoB. This research framework can be used in future research and can fill in existing gaps in the literature, collectively enabling policymakers to correctly diagnose the issue of inequality and provide efficient instruments to correct existing disparities.

ACKNOWLEDGEMENTS

We thank the anonymous referees and the Associate Editor, Prof. Ruth Aguilera, for their many helpful comments and suggestions. Prof. Ruth Mateos de Cabo also thanks the Spanish Ministry of Economy and Competitiveness (grant ECO2012-32554) for financial support. The usual disclaimer applies.

REFERENCES

Abdullah, S. N., Ismail, K. N. I., & Nachum, L. 2015. Does having women on boards create value? The impact of societal perceptions and corporate governance in emerging markets, ***Strategic Management Journal***, forthcoming. DOI:10.1002/smj.2352.

Adams, R. B. & Funk, P. 2012. Beyond the glass ceiling: Does gender matter?, ***Management Science***, 58: 219–235.

Ahern, K. R. & Dittmar, A. K. 2012. The changing of the boards: The impact of firm valuation on mandated female board representation, ***The Quarterly Journal of Economics***, 127: 137–197.

Allen, T. D., Johnson, R. C., Kiburz, K. M., & Shockley, K. M. 2013. Work–family conflict and flexible work arrangements: Deconstructing flexibility, ***Personnel Psychology***, 66: 345–376.

Baixauli-Soler, J. S., Belda-Ruiz, M., & Sanchez-Marin, G. 2015. Executive stock-options, gender diversity in the top management team, and firm risk taking, ***Journal of Business Research***, 68: 451–463.

Bear, S., Rahman, N., & Post, C. 2010. The impact of board diversity and gender composition on corporate social responsibility and firm reputation, ***Journal of Business Ethics***, 97: 207–221.

Becker, G. 1957. ***The economics of discrimination***, 2nd edn. Chicago, IL: University of Chicago Press.

Becker, G. 1964. ***Human capital***. Chicago, IL: University of Chicago Press.

Berger, J., Ridgeway, C. L., & Zelditch, M. 2002. Construction of status and referential structures, ***Sociological Theory***, 20: 157–179.

Bernardi, R., Bosco, S., & Columb, V. L. 2009. Does female representation on boards of directors associate with the "Most Ethical Companies' list?", ***Corporate Reputation Review***, 123: 270–280.

Bertrand, M., Chugh, D., & Mullainathan, S. 2005. Implicit discrimination, ***American Economic Review***, 95: 94–98.

Bianco, M., Ciavarella, A., & Signoretti, R. 2015. Women on corporate boards in Italy: The role of family connections, ***Corporate Governance: An International Review***, 23: 129–144.

Bilimoria, D. 2000. Building the business case for women corporate directors. In R. Burke & M. Mattis (Eds.), ***Women on corporate boards of directors: International challenges and opportunities***: 25–40. Dordrecht: Kluwer.

Bøhren, Ø. & Staubo, S. 2013. Does mandatory gender balance work? Changing organizational form to avoid board upheaval, ***Journal of Corporate Finance***, 28: 152–168.

Boulouta, I. 2013. Hidden connections: The link between board gender diversity and corporate social performance, ***Journal of Business Ethics***, 113: 185–197.

Brunzell, T. & Liljeblom, E. 2014. Chairmen's perceptions of female board representation: A study on Nordic listed companies, ***Equality, Diversity and Inclusion: An International Journal***, 33: 523–534.

Bygren, M. & Gähler, M. 2012. Family formation and men's and women's attainment of workplace authority, ***Social Forces***, 90: 795–816.

Carrasco, A., Francoeur, C., Labelle, R., Laffarga, J., & Ruiz-Barbadillo, E. 2015. Appointing women to boards: Is there a cultural bias?, ***Journal of Business Ethics***, 129: 429–444.

Carter, D. A., D'Souza, F., Simkins, B. J., & Simpson, W. G. 2010. The gender and ethnic diversity of US boards and board committees and firm financial performance, ***Corporate Governance: An International Review***, 18: 396–414.

Chapple, L. & Humphrey, J. E. 2014. Does board gender diversity have a financial impact? Evidence using stock portfolio performance, ***Journal of Business Ethics***, 122: 709–723.

Chen, G., Crossland, C., & Huang, S. 2014. Female board representation and corporate acquisition intensity, ***Strategic Management Journal***, forthcoming. DOI:10.1002/smj.2323.

Coleman, J. S. 1988. Social capital in the creation of human capital, ***American Journal of Sociology***, 94: 95–120.

© 2015 John Wiley & Sons Ltd

Cook, A. & Glass, C. 2014a. Women and top leadership positions: Towards an institutional analysis, ***Gender, Work & Organization***, 21: 91–103.

Cook, A. & Glass, C. 2014b. Above the glass ceiling: When are women and racial/ethnic minorities promoted to CEO?, ***Strategic Management Journal***, 35: 1080–1089.

Dang, R., Bender, A. F., & Scotto, M. J. 2014. Women on French corporate board of directors: How do they differ from their male counterparts?, ***Journal of Applied Business Research***, 30: 489–508.

De Anca, C. & Gabaldon, P. 2014a. Female directors and the media: Stereotypes of board members, ***Gender in Management: An International Journal***, 29: 334–351.

De Anca, C. & Gabaldon, P. 2014b. The media impact of board member appointments in Spanish-listed companies: A gender perspective, ***Journal of Business Ethics***, 122: 425–438.

Den Dulk, L., Groeneveld, S., Ollier-Malaterre, A., & Valcour, M. 2013. National context in work-life research: A multi-level cross-national analysis of the adoption of workplace work-life arrangements in Europe, ***European Management Journal***, 31: 478–494.

Dezsö, C. & Ross, D. G. 2012. Does female representation in top management improve firm performance? A panel data investigation, ***Strategic Management Journal***, 33: 1072–1089.

Drew, E. & Murtagh, E. M. 2005. Work/life balance: Senior management champions or laggards?, ***Women in Management Review***, 20: 262–278.

Dunn, P. 2012. Breaking the boardroom gender barrier: The human capital of female corporate directors, ***Journal of Management & Governance***, 16: 557–570.

Durbin, S. & Tomlinson, J. 2014. Female part-time managers: Careers, mentors and role models, ***Gender, Work & Organization***, 21: 308–320.

Eagly, A. H. 1987. ***Sex differences in social behavior: A social role interpretation***. Hillsdale, NJ: Erlbaum.

Eagly, A. H. 2005. Achieving relational authenticity in leadership: Does gender matter?, ***Leadership Quarterly***, 16: 459–474.

Eagly, A. H. & Karau, S. J. 2002. Role congruity theory of prejudice toward female leaders, ***Psychological Review***, 109: 573–598.

Eby, L. T., Casper, W. J., Lockwood, A., Bordeaux, C., & Brinley, A. 2005. Work and family research in IO/OB: Content analysis and review of the literature (1980–2002), ***Journal of Vocational Behavior***, 66: 124–197.

Eddleston, K. A., Veiga, J. F., & Powell, G. N. 2006. Explaining sex differences in managerial career satisfier preferences: The role of gender self-schema, ***Journal of Applied Psychology***, 91: 437–445.

Elstad, B. & Ladegard, G. 2012. Women on corporate boards: Key influencers or tokens?, ***Journal of Management & Governance***, 16: 595–615.

Ely, R. J., Ibarra, H., & Kolb, D. M. 2011. Taking gender into account: Theory and design for women's leadership development programs, ***Academy of Management Learning & Education***, 10: 474–493.

Eriksson-Zetterquist, U. 2008. Gendered role modelling – a paradoxical construction process, ***Scandinavian Journal of Management***, 24: 259–270.

Farrell, K. A. & Hersch, P. L. 2005. Additions to corporate boards: The effect of gender, ***Journal of Corporate Finance***, 11: 85–106.

Fernandez-Feijoo, B., Romero, S., & Ruiz, S. 2012. Does board gender composition affect corporate social responsibility reporting?, ***International Journal of Business and Social Science***, 3: 31–38.

Finkelstein, S., Hambrick, D. C., & Cannella, A. A. 2009. ***Strategic leadership: Theory and research on executives, top management teams, and boards***. New York: Oxford University Press.

Fowler, J. L. & O'Gorman, J. G. 2005. Mentoring functions: A contemporary view of the perceptions of mentees and mentors, ***British Journal of Management***, 16: 51–57.

Galbreath, J. 2011. Are there gender-related influences on corporate sustainability? A study of women on boards of directors, ***Journal of Management and Organization***, 17: 17–38.

Gibson, D. E. 2003. Developing the professional self-concept: Role model construals in early, middle, and late career stages, ***Organization Science***, 14: 591–610.

Gibson, D. E. 2004. Role models in career development: New directions for theory and research, ***Journal of Vocational Behavior***, 65: 134–156.

Gneezy, U., Leonard, K. L., & List, J. A. 2009. Gender differences in competition: Evidence from a matrilineal and a patriarchal society, ***Econometrica***, 77: 1637–1664.

Greenhaus, J. H. & Beutell, N. J. 1985. Sources of conflict between work and family roles, ***Academy of Management Review***, 10: 76–88.

Greenwald, A. G. 1980. The totalitarian ego: Fabrication and revision of personal history, ***American Psychologist***, 35: 603–618.

Gregory-Smith, I., Main, B. G., & O'Reilly, C. A., III. 2014. Appointments, pay and performance in UK boardrooms by gender, ***The Economic Journal***, 124: 109–128.

Grosvold, J. & Brammer, S. 2011. National institutional systems as antecedents of female board representation: An empirical study, ***Corporate Governance: An International Review***, 19: 116–135.

Groysberg, B. 2008. How star women build portable skills, ***Harvard Business Review***, 86: 74–81.

Groysberg, B. & Bell, D. 2013. Dysfunction in the boardroom, ***Harvard Business Review***, 91: 88–97.

Gupta, A. & Raman, K. 2014. Board diversity and CEO selection, ***Journal of Financial Research***, 37: 495–517.

Haslam, S. A., Ryan, M. K., Kulich, C., Trojanowski, G., & Atkins, C. 2010. Investing with prejudice: The relationship between women's presence on company boards and objective and subjective measures of company performance, ***British Journal of Management***, 21: 484–497.

Heilman, M. E. 2001. Description and prescription: How gender stereotypes prevent women's ascent up the organizational ladder, ***Journal of Social Issues***, 57: 657–674.

Hewlett, S. A., Peraino, K., Sherbin, L., & Sumberg, K. 2010. The sponsor effect: Breaking through the last glass ceiling. Harvard Business Review Research Report.

Hill, A., Upadhyay, A., & Beekun, R. 2015. Do female and ethnically diverse executives endure inequity in the CEO position or do they benefit from their minority status? An empirical examination, ***Strategic Management Journal***, 36: 1115–1134.

Hillman, A. J. 2015. Board diversity: Beginning to unpeel the onion, ***Corporate Governance: An International Review***, 23: 104–107.

Hillman, A. J., Cannella, A. A., Jr., & Harris, I. C. 2002. Women and racial minorities in the boardroom: How do directors differ?, ***Journal of Management***, 28: 747–763.

Hoobler, J. M., Wayne, S. J., & Lemmon, G. 2009. Bosses' perceptions of family-work conflict and women's promotability: Glass ceiling effects, ***Academy of Management Journal***, 52: 939–957.

Hoyt, C. L., Johnson, S. K., Murphy, S. E., & Skinnell, K. H. 2010. The impact of blatant stereotype activation and group sex-composition on female leaders, ***The Leadership Quarterly***, 21: 716–732.

Ibarra, H. 1992. Homophily and differential returns: Sex differences in network structure and access in an advertising firm, ***Administrative Science Quarterly***, 37: 422–447.

Ittonen, K., Miettinen, J., & Vähämaa, S. 2010. Does female representation on audit committees affect audit fees?, ***Quarterly Journal of Finance and Accounting***, 49: 113–139.

Johnson, S. K., Murphy, S. E., Zewdie, S., & Reichard, R. J. 2008. The strong, sensitive type: Effects of gender stereotypes and leadership prototypes on the evaluation of male and female leaders, ***Organizational Behavior and Human Decision Processes***, 106: 39–60.

© 2015 John Wiley & Sons Ltd

Joshi, A., Liao, H., & Roh, H. 2011. Bridging domains in workplace demography research: A review and reconceptualization, ***Journal of Management***, 37: 521–552.

Kaczmarek, S., Kimino, S., & Pye, A. 2012. Antecedents of board composition: The role of nomination committees, ***Corporate Governance: An International Review***, 20: 474–489.

Kanter, R. M. 1977. ***Men and women of the corporation***. New York: Basic Books.

Kelan, E. K. & Mah, A. 2014. Gendered identification: Between idealization and admiration, ***British Journal of Management***, 25: 91–101.

Kim, Y. & Cannella, A. A. 2008. Toward a social capital theory of director selection, ***Corporate Governance: An International Review***, 16: 282–293.

Kogut, B., Colomer, J., & Belinky, M. 2014. Structural equality at the top of the corporation: Mandated quotas for women directors, ***Strategic Management Journal***, 35: 891–902.

Korman, A. K. 1970. Toward a hypothesis of work behavior, ***Journal of Applied Psychology***, 54: 31–41.

Kossek, E. E., Baltes, B. B., & Matthews, R. A. 2011. How work-family research can finally have an impact in organizations, ***Industrial and Organizational Psychology***, 4: 352–369.

Kumar, K. & Beyerlein, M. 1991. Construction and validation of an instrument for measuring ingratiatory behaviors in organizational settings, ***Journal of Applied Psychology***, 76: 619–627.

Labelle, R., Francoeur, C., & Lakhal, F. 2015. To regulate or not to regulate? Early evidence on the means used around the world to promote gender diversity in the boardroom, ***Gender, Work & Organization***, 22: 339–363.

Leslie, L. M. & Manchester, C. F. 2011. Work-family conflict is a social issue not a women's issue, ***Industrial and Organizational Psychology***, 4: 414–417.

Loury, G. 1977. A dynamic theory of racial income differences, ***Women, Minorities, and Employment Discrimination***, 153: 86–153.

Lucas-Pérez, M. E., Mínguez-Vera, A., Baixauli-Soler, J. S., Martín-Ugedo, J. F., & Sánchez-Marín, G. 2015. Women on the board and managers' pay: Evidence from Spain, ***Journal of Business Ethics***, 129: 265–280.

Lückerath-Rovers, M. 2013. Women on boards and firm performance, ***Journal of Management & Governance***, 17: 491–509.

Machold, S., Huse, M., Hansen, K., & Brogi, M. 2013. ***Getting women on corporate boards: A snowball starting in Norway***. Cheltenham: Edward Elgar.

Manchester, C. F., Leslie, L. M., & Kramer, A. 2010. Stop the clock policies and career success in academia, ***American Economic Review***, 100: 219–223.

Martín-Ugedo, J. F. & Mínguez-Vera, A. 2014. Firm performance and women on the board: Evidence from Spanish small and medium-sized enterprises, ***Feminist Economics***, 20: 136–162.

Mateos de Cabo, R., Gimeno, R., & Escot, L. 2011. Disentangling discrimination on Spanish boards of directors, ***Corporate Governance: An International Review***, 19: 77–95.

Mateos de Cabo, R., Gimeno, R., & Nieto, M. 2012. Gender diversity on European banks' boards of directors, ***Journal of Business Ethics***, 109: 145–162.

Mateos de Cabo, R., Gimeno, R., Martínez, M., & López, L. 2014. Perpetuating gender inequality via the internet? An analysis of women's presence in Spanish online newspapers, ***Sex Roles***, 70: 57–71.

McDonald, M. L. & Westphal, J. D. 2013. Access denied: Low mentoring of women and minority first-time directors and its negative effects on appointments to additional boards, ***Academy of Management Journal***, 56: 1169–1198.

McGregor, J. 2014. New Zealand's boardroom blues: Time for quotas, ***Women's Studies Journal***, 28: 4–23.

McGuire, G. M. 2002. Gender, race, and the shadow structure: A study of informal networks and inequality in a work organization, ***Gender & Society***, 16: 303–322.

Meier, P. 2014. Quotas for advisory committees, business and politics: Just more of the same?, ***International Political Science Review***, 35: 106–118.

Mensi-Klarbach, H. 2014. Gender in top management research: Towards a comprehensive research framework, ***Management Research Review***, 37: 538–552.

Moe, K. S. & Shandy, D. J. 2010. ***Glass ceilings and 100-hour couples: What the opt-out phenomenon can teach us about work and family***. Athens, GA: Georgia University Press.

Newbert, S. L. 2007. Empirical research on the resource-based view of the firm: An assessment and suggestions for future research, ***Strategic Management Journal***, 28: 121–146.

Newell, S. 1993. The superwomen syndrome: Gender differences in attitudes towards equal opportunities at work and towards domestic responsibilities at home, ***Work, Employment and Society***, 7: 275–289.

Nguyen, T., Locke, S., & Reddy, K. 2014. Does boardroom gender diversity matter? Evidence from a transitional economy, ***International Review of Economics & Finance***, 37: 184–202.

Nielsen, R. & Tvarnø, C. D. 2012. ***Scandinavian women's law in the 21st century***. Copenhagen: Djøf Publishing.

Nielsen, S. & Huse, M. 2010. The contribution of women on boards of directors: Going beyond the surface, ***Corporate Governance: An International Review***, 18: 136–148.

North, D. C. 1990. ***Institutions, institutional change, and economic performance***. New York: Cambridge University Press.

Okurame, D. E. 2007. Perceived mentoring functions: Does mentor's gender matter?, ***Women in Management Review***, 22: 418–427.

O'Neil, D. A., Hopkins, M. M., & Bilimoria, D. 2008. Women's careers at the start of the 21st century: Patterns and paradoxes, ***Journal of Business Ethics***, 80: 727–743.

Pande, R. & Ford, D. 2011. ***Gender quotas and female leadership: A review***. Washington, DC: World Bank.

Park, S. H. & Westphal, J. D. 2013. Social discrimination in the corporate elite: How status affects the propensity for minority CEOs to receive blame for low firm performance, ***Administrative Science Quarterly***, 58: 542–586.

Peterson, C. A. & Philpot, J. 2007. Women's roles on US Fortune 500 boards: Director expertise and committee memberships, ***Journal of Business Ethics***, 72: 177–196.

Pfeffer, J. & Salancik, G. 1978. ***The external control of organizations: A resource-dependence perspective***. New York: Harper and Row.

Phelps, E. S. 1972. The statistical theory of racism and sexism, ***American Economic Review***, 62: 659–661.

Post, C. & Byron, K. 2015. Women on boards and firm financial performance: A meta-analysis, ***Academy of Management Journal***, forthcoming. DOI:10.5465/amj.2013.0319.

Post, C., Rahman, N., & Rubow, E. 2011. Green governance: Boards of directors' composition and environmental corporate social responsibility, ***Business & Society***, 50: 189–223.

Powell, G. N. 1990. One more time: Do female and male managers differ?, ***Academy of Management Perspectives***, 4: 68–75.

Powell, G. N. & Butterfield, D. A. 1997. Effect of race on promotions to top management in a federal department. ***Academy of Management Journal***, 40(1): 112–128.

Powell, G. N. & Butterfield, D. A. 2013. Sex, gender, and aspirations to top management: Who's opting out? Who's opting in?, ***Journal of Vocational Behavior***, 82: 30–36.

Powell, G. N. & Greenhaus, J. H. 2010. Sex, gender, and the work-to-family interface: Exploring negative and positive interdependencies, ***Academy of Management Journal***, 53: 513–534.

Profeta, P., Aliberti, L. A., Casarico, A., S'Amico, M., & Puccio, A. 2014. ***Women directors: The Italian way and beyond***. Basingstoke: Palgrave Macmillan.

Pucheta-Martínez, M. C. & Bel-Oms, I. 2015. The gender gap in pay in company boards, ***Industrial and Corporate Change***, 24: 467–510.

© 2015 John Wiley & Sons Ltd

Ragins, B. R., Townsend, B., & Mattis, M. 1998. Gender gap in the executive suite: CEOs and female executives report on breaking the glass ceiling, ***The Academy of Management Executive***, 12: 28–42.

Ruigrok, W., Peck, S., & Tacheva, S. 2007. Nationality and gender diversity on Swiss corporate boards, ***Corporate Governance: An International Review***, 15: 546–557.

Ryan, M. K. & Haslam, S. A. 2007. The glass cliff: Exploring the dynamics surrounding the appointment of women to precarious leadership positions, ***Academy of Management Review***, 32: 549–572.

Schuh, S. C., Hernandez-Bark, A. S., Van Quaquebeke, N., Hossiep, R., Frieg, P., & Van Dick, R. 2014. Gender differences in leadership role occupancy: The mediating role of power motivation, ***Journal of Business Ethics***, 120: 363–379.

Sealy, R. H. V. & Singh, V. 2010. The importance of role models and demographic context for senior women's work identity development, ***International Journal of Management Reviews***, 12: 284–300.

Seierstad, C. 2015. Beyond the business case: The need for both utility and justice rationales for increasing the share of women on boards, ***Corporate Governance: An International Review***, forthcoming. DOI:10.1111/corg.12117.

Seierstad, C. & Opsahl, T. 2011. For the few not the many? The effects of affirmative action on presence, prominence, and social capital of women directors in Norway, ***Scandinavian Journal of Management***, 27: 44–54.

Seierstad, C., Warner-Søderholm, G., Torchia, M., & Huse, M. 2015. Increasing the number of women on boards: The role of actors and processes, ***Journal of Business Ethics***, forthcoming. DOI:10.1007/s10551-015-2715-0.

Sidanius, J. & Pratto, F. 2004. Social dominance theory: A new synthesis. In J. T. Jost & J. Sidanius (Eds.), ***Political psychology: Key readings***: 315–332. New York: Psychology Press.

Simpson, W. G., Carter, D. A., & D'Souza, F. 2010. What Do We Know About Women on Boards? ***Journal of Applied Finance***, 20(2): 27–39.

Singh, V., Kumra, S., & Vinnicombe, S. 2002. Gender and impression management: Playing the promotion game, ***Journal of Business Ethics***, 37: 77–89.

Singh, V., Terjesen, S., & Vinnicombe, S. 2008. Newly appointed directors in the boardroom: How do women and men differ?, ***European Management Journal***, 26: 48–58.

Singh, V., Vinnicombe, S., & James, K. 2006. Constructing a professional identity: how young female managers use role models, ***Women in Management Review***, 21: 67–81.

Steele, C. M. & Aronson, J. 1995. Stereotype threat and the intellectual test performance of African Americans, ***Journal of Personality and Social Psychology***, 69: 797–811.

Stern, I. & Westphal, J. D. 2010. Stealthy footsteps to the boardroom: Executives' backgrounds, sophisticated interpersonal influence behavior, and board appointments, ***Administrative Science Quarterly***, 55: 278–319.

Straub, C. 2007. A comparative analysis of the use of work–life balance practices in Europe: Do practices enhance females' career advancement?, ***Women in Management Review***, 22: 289–304.

Tajfel, H. 1972. La catégorisation sociale. In S. Moscovici (Ed.), ***Introduction à la Psychologie Sociale, Vol. 1***: 272–302. Paris: Larousse.

Tatli, A., Vassilopoulou, J., & Özbilgin, M. 2012. An unrequited affinity between talent shortages and untapped female potential: The relevance of gender quotas for talent management in high growth potential economies of the Asia Pacific region, ***International Business Review***, 22: 539–553.

Terjesen, S., Aguilera, R., & Lorenz, R. 2015. Legislating a woman's seat on the board: Institutional factors driving gender quotas for boards of directors, ***Journal of Business Ethics***, 128: 233–251.

Terjesen, S., Sealy, R., & Singh, V. 2009. Women directors on corporate boards: A review and research agenda, ***Corporate Governance: An International Review***, 17: 320–337.

Terjesen, S. & Singh, V. 2008. Female presence on corporate boards: A multi-country study of environmental context, ***Journal of Business Ethics***, 83: 55–63.

Torchia, M., Calabro, A., & Huse, M. 2011. Women directors on corporate boards: From tokenism to critical mass, ***Journal of Business Ethics***, 102: 299–317.

Van den Brink, M. & Stobbe, L. 2014. The support paradox: Overcoming dilemmas in gender equality programs, ***Scandinavian Journal of Management***, 30: 163–174.

Vinnicombe, S. & Singh, V. 2002. Sex role stereotyping and requisites of successful top managers, ***Women in Management Review***, 17: 120–130.

Waldman, D. A., Galvin, B. M., & Walumbwa, F. O. 2013. The development of motivation to lead and leader role identity, ***Journal of Leadership & Organizational Studies***, 20: 156–168.

Westphal, J. D. & Milton, L. P. 2000. How experience and network ties affect the influence of demographic minorities on corporate boards, ***Administrative Science Quarterly***, 45: 366–398.

Weyer, B. 2007. Twenty years later: Explaining the persistence of the glass ceiling for women leaders, ***Women in Management Review***, 22: 482–496.

Wirth, L. 1998. Women in management: Closer to breaking the glass ceiling?, ***International Labour Review***, 137: 239–249.

Withers, M. C., Hillman, A. J., & Cannella, A. A. 2012. A multidisciplinary review of the director selection literature, ***Journal of Management***, 38: 243–277.

Wolfers, J. 2006. Diagnosing discrimination: Stock returns and CEO gender, ***Journal of the European Economic Association***, 4: 531–541.

Zelechowski, D. D. & Bilimoria, D. 2004. Characteristics of women and men corporate inside directors in the US, ***Corporate Governance: An International Review***, 12: 337–342.

Zhu, D. H., Shen, W., & Hillman, A. J. 2014. Recategorization into the in-group. The appointment of demographically different new directors and their subsequent positions on corporate boards, ***Administrative Science Quarterly***, 59: 240–270.

Patricia Gabaldon is Assistant Professor of Economic Environment at IE Business School in Madrid (Spain). Patricia Gabaldon received her PhD in Economics from the University of Alcala, Spain. Her research interests focus on the role of women in the economy, corporate governance, and policies regarding women on boards.

Celia de Anca is currently the Director of the Center for Diversity in Global Management, and professor of Diversity at IE Business School, Madrid (Spain). She is the author of *Beyond Tribalism* (Macmillan, 2012) and co-author of *Managing Diversity in the Global Organization* (Macmillan, 2007). She is a member of Ethics Committee of InverCaixa's Ethics Fund. She has received the woman executive of the year award 2008 by ASEME and was listed among the top50 global management thinkers in 2013. Celia is fluent in Spanish, English, French, and Arabic.

Ruth Mateos de Cabo is an Associate Professor in Marketing Research at the University CEU San Pablo in Madrid (Spain). She earned her PhD in Business Administration at the University CEU San Pablo. She has worked for CUNEF (Universidad Complutense) and Universidad Europea. Her research areas include gender economics, corporate governance with a focus on board of directors, gender diversity, and discrimination in the labor market.

© 2015 John Wiley & Sons Ltd

Ricardo Gimeno is Senior Economist in the Research Department of Banco de España. He earned his PhD in finance at Universidad Pontificia Comillas, ICADE Business School, Madrid (Spain). He is also visiting professor of finance at New York University. Previously, he has worked for the European Central Bank, CUNEF (Universidad Complutense) and ICADE Business School. His research interests include corporate governance, gender discrimination, household finance, and financial markets.

© 2015 John Wiley & Sons Ltd

Corporate Governance: An International Review, 2016, 24(3): 386

Erratum

Ruth V. Aguilera, Till Talaulicar, Chi-Nien Chung, Gonzalo Jimenez and Sanjay Goel (2015). Cross-National Perspectives on Ownership and Governance in Family Firms. Corporate Governance: An International Review, 23(3): 161–166, DOI: 10.1111/corg.12112

In the published Editorial "Cross-National Perspective on Ownership and Governance in Family Firms", which appeared as the first article of the special issue on Corporate Governance: An International Review, the affiliations of the guest editors were inadvertently omitted.

The missing details of their affiliations are shown below and have also been added in the online version.

- Ruth V. Aguilera, University of Illinois Urbana-Champaign
- Chi-Nien Chung, National University of Singapore
- Sanjay Goel, University of Minnesota Duluth
- Gonzalo Jimenez, Universidad Adolfo Ibañez
- Till Talaulicar, University of Erfurt, Germany

We apologize for any inconvenience caused.

© 2016 John Wiley & Sons Ltd
doi:10.1111/corg.12162