Comparative corporate governance

Ilir Haxhi

Ruth V. Aguilera

To be published in

Encyclopedia of International Strategic Management. (Eds.) C. Asmussen, N. Hashai, and D. Minbaeva, Edward Elgar Publishing

July 2022 version

Over the last three decades, systemic corporate misconduct, increased shareholder activism, and recurrent global financial crises have stirred an extensive academic, business, and societal debate over corporate governance (CG) and the way public corporations are directed and controlled (Haxhi, 2010). CG studies ‘‘the power and influence over decision making within the corporation’’ (Aguilera & Jackson, 2010), focusing notably on how to monitor managers, protect minority shareholders, enhance reporting and disclosure, and improve employee and other stakeholder participation in firms’ strategic decisions (Aguilera, Marano & Haxhi, 2019). This brief overview seeks to grasp the state-of-the-art of comparative CG by focusing on its definition, regulation and practices, alternative models, and its internal and external characteristics, and current debates and future trends.

While the literature has focused on the cross-national diversity in CG, less consensus exists on a unifying CG classification as each definition emphasizes different dimensions and their respective goals. For example, while social scientists and economists depict CG as ‘‘the institutions that influence how business corporations allocate resources and returns’’ (O’Sullivan, 2000), legal and finance scholars narrow it down to the ways in which corporate financial suppliers ensure their return on capital or investment (Shleifer & Vishny, 1997). Investors, managers and policy makers understand CG as an ecosystem of tools that shape the control and direction of corporation and that structure the power relations among its stakeholders (Aguilera & Jackson, 2003). These definitions encompass both formal and informal institutions of CG, but also capture the internal arrangements within each corporation as well as the national business context in which these corporations are embedded such as the labor market, capital market, and legal system (Haxhi, van Ees, & Sorge, 2013).

CG practices are regulated through the hard- and soft-law approaches. The former, a one-size-fits-all form of statutory norms entails following legal rules at the risk of penalty; the latter comprises standards of best practices, e.g., CG codes, leaving firms to decide on voluntary compliance levels (Haxhi & Aguilera, 2014). As self-regulation instruments of best practices with respect to boards, management, supervision, disclosure and auditing (Aguilera & Cuervo-Cazurra, 2004), codes are formally nonbinding, issued by expert committees, flexible in their application, built on the market mechanism for evaluation of deviations, and evolutionary in nature (Haxhi & van Ees, 2010). The voluntary self-regulatory nature of codes is exemplified in the widely used comply-or-explain principle, which entails that while compliance with code provisions is voluntary, the disclosure of noncompliance is mandatory (Haxhi & van Manen, 2010). Considered worldwide as the main CG regulatory tool, codes show similarities related to their objectives to improve the CG quality and accountability; however, unlike hard-law, e.g., Sarbanes-Oxley Act (2002), codes may not lead to the optimal CG, but reduce misconduct through self-regulation (Haxhi & Aguilera, 2012).

The comparative CG literature distinguishes between two stylized dichotomous models of CG: the *shareholder-oriented* or Anglo-American model (strong shareholder rights, single powerful CEO, strong market for corporate control, flexible labor market, and disperse ownership), which prevails in Australia, North America and the UK, and the *stakeholder-oriented* or the Continental European model (a broader power distribution among stakeholders, weaker shareholders' rights, and a typical concentrated ownership), which prevails in most of the European continent (Aguilera & Jackson, 2010). The main difference between these two models of CG consists in the primer ownership purpose;

while Anglo-American owners prioritize short-term shareholder value maximization, the longer time horizon for Continental European firms allows to fulfill additional stakeholder demands as both law and policy recognize to varying degrees the fundamental objective of advancing the interests of other stakeholders (employees, suppliers, creditors, customers, and community) that are expected to play a strong monitoring and disciplining role with regard to management (Haxhi, 2022).

However, this schematic depiction of CG provides a relatively loose representation of both dichotomous models, which vary across nations, and acknowledges many particularities and hybrid forms within and across the models. For instance, Japanese CG case, which does not fit into the two stylized models, is characterized by business networks, enterprise unionism, meritocratic seniority system and little transparency despite its strong capital market. Furthermore, within the *stakeholder-oriented* model, Haxhi and Aguilera (2017) identify three distinct CG models. The *State capitalist hybrid* model, which is present in Belgium and France and has a relatively strong capital, confrontational management-labor relations and an interventionist civil-law State. The *stakeholder-oriented consensus* model, which prevails in Germanic and Scandinavian countries and is characterized by consensual and cooperative management-labor relations; however, unlike in Germany, it actually has a more permissive and less interventionist State. Finally, the *mixed market economies* model that is present in Eastern and Southern Europe and has less stringent legal standards and enforcement, where the complementarities between the limited capitalization and the civil-law tradition show the path-dependent and context-specific nature of this model.

Beyond advanced economies, Aguilera, Judge and Terjesen (2018) classify two CG

models: the *State-owned* model prevailing in Russia and China, and the *family-owned* model, present in India and most of South East Asia. Similarly, Aguilera and Haxhi (2019) research CG in emerging markets and uncover the weak institutional enforcement as the common denominator of CG in BRIC countries, characterized by poor creditors' rights, strong owners, lack of transparency, and low investment in human capital.

While the CG systems describe above have been traditionally conceptualized at the country-level, comparative CG has also distinguished between internal and external CG practices at firm-level (Aguilera, Desender, Bednar & Lee, 2015). The internal encompass mostly the type of owner (e.g., institutional investor, family), the structure of the board, the managerial authority and the employee voice; while, the external CG practices refer to those pressures exerted by actors outside the firm such as rating agencies, auditors, the legal system, media, and social movements. Research has shown that corporations within the different national governance systems have often ample discretion to for instance have a board with majority independent directors in a majority owned firm in the Continental model and have a firm without variable contingent pay in the shareholder-oriented model. What it is clear is that there are certain global CG standards such as those identified by the OECD rules but that firms tend to adopt those CG practices that best fit their strategy.

Several CG debates have emerged in response to greater societal demands for transparency and accountability in part supported by social media and overall digitalization. First, the worldwide Covid health crises has brought closer owners, boards and managers as they had to quickly react to working remotely and shortages of global value chain, challenges that require flexibility as well as agility in quickly adjusting to the new normal. Second, the increased shareholder activism, partly explained by additional

tools for shareholders to express their voice and influence boards and managers, is illustrated by a boom in shareholder proposals dealing with compensation, diversity, sustainability and board renewal. Third, partly motivated by societal pressures on the role of corporations in addressing climate change and social inequalities challenges, and investors' pressure on shareholder-oriented firms to spread the wealth, particularly universal owners such as the BlackRock's CEO and 181 CEOs of Business RoundTable have asked their investee firms to pay attention to *corporate purpose*. It is yet to be seen whether this social movement started by Unilver's CEO and followed by Danone's CEO (subsequently fired) will change how firms relate to its stakeholders. Fourth, although often treated independently in the recent ESG movement the Governance (G) is clearly the pillar that sustains what happens with the environment (E) and the social (S), as more boards spending strategic time to discuss how to incorporate ESG practices into their overall strategy. Finally, as the economy is moving from digital and virtual to big data and artificial intelligence, boards and companies are looking for experts and using these new technologies to be more informed and efficient in their decisions. A big challenge for companies is to assess the risk of cyber security bridges for their companies.

To close, comparative CG examines the risk that corporations are willing to take in monitoring and advising their different stakeholders. Risk is mitigated or exacerbated by adopting a myriad of CG practices that are neither costly nor isolated from the broader eco-system. The advantage of comparative CG is that it allows to assess how to compare and apply these practices across firms, industries, countries or regions. Our last takeaway is that CG is not converging towards a single particular model but it continues to evolve to adjust to societal needs.

Bibliography

Aguilera, V.R. and Cuervo-Cazurra, A. 2004. Codes of good governance worldwide: what is the trigger? *Organization Studies*, **25** (3), 415–443.
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(1): 483-573.
Aguilera, R. and Jackson, G. 2003. The cross-national diversity of corporate governance: dimensions and determinants. *Academy of Management Review*, **28** (3), 447–465.
Aguilera, R.V. and Jackson, G. 2010. Comparative and international corporate governance. *Annals of the Academy of Management*, **4**, 485–556.
Aguilera, R. V., Judge, W. Q., & Terjesen, S. A. 2018. Corporate governance deviance. *Academy of Management Review*, 43(1): 87-109.
Aguilera, R. V. & Haxhi, I. 2019. Comparative Corporate Governance in Emerging Markets, In *The Oxford Handbook of Management in Emerging Markets* (Eds.) R. Grosse & K. Meyer. Oxford University Press: Oxford, UK: 185-218.
Aguilera, R.V., Marano, V., & Haxhi, I. 2019. International Corporate Governance: A Review and Opportunities for Future Research. *Journal of International Business Studies*, 50(4): 457–498.
Haxhi, I. 2010. Institutional contextuality of business best practices: the persistent cross-national diversity in the creation of corporate governance codes. PhD dissertation. University of Groningen Press, Groningen, the Netherlands.
Haxhi, I. (forthcoming). Comparative Corporate Governance, In *Comparative International Management* (3d Eds.) A. Sorge, and N. Noorderhaven. London: Routledge.
Haxhi, I. and Aguilera, R.V. 2012. Are codes fostering convergence in corporate governance? An institutional perspective, in *Convergence of Corporate Governance: Promise and Prospects* (eds A. Rasheed and T. Yoshikawa), Palgrave Macmillan, Basingstoke.
Haxhi I., & Aguilera, R. V. 2014. Corporate Governance Through Codes, In C. Cooper (Ed.) *Wiley Encyclopedia of Management 3rd Edition*, *International Management*, Wiley-Blackwell, 6: 1-3.
Haxhi I., & Aguilera, R. V. 2017. An Institutional Configurational Approach to Cross-National Diversity in Corporate Governance. *Journal of Management Studies.* 54(3): 261–303.
Haxhi, I. and van Ees, H. 2010. Explaining diversity in the worldwide diffusion of codes of good governance. *Journal of International Business Studies*, **41** (4), 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(6): 535-546.
Haxhi, I. and van Manen, J. 2010. Nationale cultuur en de wereldwijde verspreiding van corporate governancecodes. *Goed Bestuur*, **3**, 2010.
O'Sullivan, M. (2000) Corporate governance and globalisation, 570 ANNALS. *AAPSS*, **153**, 154.
Shleifer, A. and Vishny, R.W. 1997. A survey of corporate governance. *Journal of Finance*, **52** (2), 737–783.