Ownership as a Form of Corporate Governance

Brian L. Connelly, Robert E. Hoskisson, Laszlo Tihanyi* and S. Trevis Certo

Auburn University; Rice University; Texas A&M University; Arizona State University

ABSTRACT Firm ownership is an increasingly influential form of corporate governance. Although firms might be owned by different types of owners, most studies examine owner influence on a particular firm outcome in isolation. This study synthesizes research from multiple disciplines on different types of owners and offers a unifying framework of governance through ownership. Using this framework, we describe the motivations of various types of owners, the tactics owners use to affect firms in which they are invested, and the dominant firm outcomes these owners seek to influence. We note how heightened managerial awareness of heterogeneous owner interests increases owner influence on firm-level outcomes. We also provide a roadmap for future study and offer research questions about where scholars might turn their attention to better understand the role of owners in directing firm actions. Our study draws attention to emerging forms of ownership, such as hedge funds and sovereign wealth funds, and highlights the changing (and often competing) interests of shareholders and how this impacts theories of governance.

INTRODUCTION

The popular press often associates corporate governance with the board of directors. However, there are a wide range of mechanisms in place that govern, or control, the actions of managers. Some of these mechanisms are internal to the firm, such as the board of directors and executive compensation structures. Others are external, such as the market for corporate control, the competitive environment, local laws, and both formal and informal institutions (Walsh and Seward, 1990). This study reviews the influence of the firm’s owners as an increasingly important, and influential, group that governs the actions of managers and constitutes both an internal and external control mechanism. We focus on general governance problems involving firm owners using the examples of mainly US and UK firms, while a companion study in this issue by Johnson et al. (2010) addresses variation in ownership influences in different institutional contexts.

Address for reprints: Brian L. Connelly, Auburn University, 415 W Magnolia Ave, Auburn, AL 36849, USA (bconnelly@auburn.edu).

*Note that this paper was under review before Laszlo’s appointment as Associate Editor at JMS.
Recent years have seen sweeping changes to ownership structures and their influence on firm actions. Institutional investors have become some of the most active owners in corporate history, often confronting managers and directors and even seeking to change the make-up of boards and top management teams (Dai, 2007). For example, D.E. Shaw Investments played an important role in the 2008 ousting of the CEO of Take-Two, maker of the popular Grand Theft Auto video game. Such drastic actions are often precipitated by activist investors, who now hold the majority of US and UK public equity (Almazan et al., 2005). The reach of these activist investors has extended such that they are often able to pressure management to undertake specific competitive actions (Connelly et al., in press). One example is Relational Investors, a mutual fund headed by Ralph Whitworth, which assumed a large share of Home Depot and quickly forced management to divest its contractor services business (Liang, 2007). Executives today are in regular contact with their most influential shareholders, take actions in response to shareholder desires, and are cognizant that job security lies in the hands of their investors.

Despite broad and rapid changes regarding who owns firms and how they go about imposing pressure on boards and managers to act in specific ways, our academic understanding of these phenomena is advancing more slowly. Research exploring the governance function of firm owners is still dominated by agency theory (Dalton et al., 2007), which may provide an over-simplified view of the nature of relationships between a wide range of shareholders and managers. Furthermore, our understanding of the evolving structures of firm ownership is dispersed throughout an assortment of literatures, including finance (Demsetz and Villalonga, 2001), accounting (Bushee, 2001), economics (Gompers and Metrick, 2001), law (Bainbridge, 2003), and management (Hoskisson et al., 2002). Given the diverse approaches taken by various disciplines, the time is right to take stock of what we know about the behaviour of different owners and how they govern firm actions. In this review, we summarize theory that explains the governance role of owners, gather information that various disciplines have learned regarding the nature and structure of firm ownership, and explore what scholars are discovering about the tactics they use to influence managerial activities.

THEORETICAL FRAMEWORK

The seminal work of Berle and Means (1932) provides the foundation for research examining corporate ownership structures. The central premise of their work was the recognition of problems associated with the separation of ownership and management. Jensen and Meckling (1976) expanded these ideas significantly through the introduction of agency theory. According to agency theory, a firm represents a nexus of contracts between principals (owners) and agents (managers). Jensen and Meckling proposed that owners and managers have contradictory risk preferences which may lead to managerial decisions that depart from shareholder preferences. While some scholars have questioned the extent to which manager and shareholder preferences diverge (Ghoshal, 2005), the vast amount of research relying on agency theory demonstrates that this assumption resonates with scholars (Dalton et al., 2007). Therefore, to ensure the interests of managers and shareholders are aligned, research suggests the appropriateness of
several internal monitoring mechanisms, such as boards of directors and executive compensation contracts (Dalton et al., 1998).

Ownership structures play a central role in determining the extent to which the interests of owners and managers are aligned (Dalton et al., 2003). In an effort to integrate the vast literature on ownership as a form of corporate governance, we have linked ownership structure, the actions owners take, and firm attributes in a descriptive model, shown in Figure 1. Path A illustrates the relationship between a firm’s ownership mix and the various alternatives open to owners in terms of influence. Path B illustrates how shareholder influence may impact important firm attributes such as performance and strategy. Path C highlights the notion that different investors take ownership stakes in companies owing to the presence of certain firm attributes such as performance or strategy. This final path illustrates the influence of endogeneity, which represents an important factor in understanding firm ownership. More specifically, ownership is not exogenous but instead closely tied to the decisions managers make regarding competitive tactics and strategies (Bushee, 2004; Demsetz and Villalonga, 2001). In the following sections, we discuss the three main components of our model and the complex relationships that underlie each path.

**OWNERSHIP STRUCTURE**

Firms may be owned by a diverse mix of different types of investors. With few exceptions, these investors become owners in firms to accomplish financial objectives. However, they...
may differ with respect to their trading styles, clientele, legal and regulatory environments, and their ability to gather and process information. In this section, we review the dominant forms of ownership that researchers have examined in the governance literature and discuss factors that motivate them to own some, or most, of the firm. Table I summarizes some of the key studies that examine the governance role of these different forms of ownership.

**Inside Ownership**

Equity owned by insiders helps align the interests of managers and shareholders, which Dalton et al. (2003) call the ‘alignment’ approach. These insiders tend to be motivated to make decisions that are consistent with interests of the broader constituency of shareholders.

*Executives.* Scholars in finance (Agrawal and Knoeber, 1996), law (Perry and Zenner, 2000), economics (Himmelberg et al., 1999), and strategy (Dalton et al., 2003) have examined when and how insider equity supports alignment between the interests of owners and managers. The appeal of this perspective lies in its simplicity: as executives gain greater ownership stakes, they are more likely to employ firm resources towards long-term profitability and less likely to shirk from executing their fiscal and strategic responsibilities (Jensen and Meckling, 1976). At the same time, however, other scholars note the potential pernicious effects of managerial ownership. High levels of ownership, for example, may provide executives with increased power, which can cause them to become entrenched within the firm (Morck et al., 1988). Once entrenched, managers may consume more perquisites and/or reduce the firm’s risk profile to protect their own interests.

Consistent with these contrasting perspectives, empirical support for the effects of managerial ownership has been mixed (Dalton et al., 2003; Himmelberg et al., 1999; McGuire and Matta, 2003). For example, the results of some studies show that executive ownership leads to greater risk taking (Rajgopal and Shevlin, 2002) whereas others report the opposite effects (Desai and Dharmapala, 2006). Similarly, some studies have sought to establish a link between managerial ownership and goal alignment, but other research has found that managerial ownership may as often lead to goal misalignment with respect to such issues as backdating of stock options, earnings manipulation, and dividend policies (Bhattacharya, 1981; Devers et al., 2007).

*Board members.* Others have applied the alignment principle to board members (Hermlin and Weisbach, 2003). The equity holdings of independent directors have not captured the same research attention as that of inside directors and other executives because, from an agency theory perspective, independent directors should already represent the interests of shareholders. At the same time, independent directors have both access to firm-specific information that may not be available to other investors and some element of control over firm actions (Kosnik, 1990). There is, in fact, some evidence that change in the equity holdings of board members can signal the long-term earnings potential of the firm to other owners (Certo et al., 2001). Although independent directors vary
Table I. Summary of key research on ownership structure as a form of governance

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<thead>
<tr>
<th>Owner type</th>
<th>Key issues</th>
<th>Studies addressing the issue</th>
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<tbody>
<tr>
<td>Executive ownership</td>
<td>Empirical support for the agency theory benefits of executive ownership has been mixed.</td>
<td>Dalton et al., 2003</td>
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<td></td>
<td>Studies show conflicting evidence about how executive ownership influences risk-taking and goal</td>
<td>McGuire and Matta, 2003</td>
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<td>alignment.</td>
<td>Rajgopal and Shevlin, 2002</td>
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<td>Desai and Dharmapala, 2006</td>
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<td>Devers et al., 2007</td>
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<tr>
<td>Board ownership</td>
<td>Board ownership signals long-term earnings potential.</td>
<td>Certo et al., 2001</td>
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<td></td>
<td>Outside directors vary considerably in their ownership, but less empirical research focuses on this group.</td>
<td>Hermelin and Weisbach, 2003</td>
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<td>Kosnik, 1990</td>
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<td>Employee ownership</td>
<td>Creates a social-psychological bond that is linked with effectiveness, satisfaction, and performance.</td>
<td>Blasi et al., 2003</td>
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<td>(non-executive)</td>
<td>Scholars explain these relationships with an extrinsic or instrumental satisfaction model.</td>
<td>Jones and Kato, 1995</td>
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<td>Welbourne and Gomez-Mejia, 1995</td>
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<td></td>
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<td>Buchko, 1993</td>
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<td>Blockholders</td>
<td>Empirical research on individual ownership is focused on insiders, usually ignoring individual outsiders or lumping them together with institutional investors.</td>
<td>Holderness, 2003</td>
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<td></td>
<td>Family ownership rarely creates value as these owners seek to protect their socio-emotional endowment.</td>
<td>Shleifer and Vishny, 1997</td>
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<td></td>
<td>Corporate ownership can have negative implications for the target firm.</td>
<td>Mehran, 1995</td>
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<td></td>
<td>Empirical research highlights the problems associated with state ownership, such as soft budgets, decreased innovation, corruption, and limited competition.</td>
<td>Anderson and Reeb, 2003</td>
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<td></td>
<td>Multiple blockholders create power-dependencies.</td>
<td>Gomez-Mejia et al., 2003</td>
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<tr>
<td>Agent owners</td>
<td>Overcome obstacles to governance encountered by other shareholders, but also create a dual agency relationship.</td>
<td>Arthurs et al., 2008</td>
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<td>Pressure-sensitive institutional investors are poor governors of firm activity.</td>
<td>Grinstein and Michaely, 2005</td>
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<td>Pressure-indeterminate institutional investors do not have a systematic governance role.</td>
<td>Edwards and Hubbard, 2000</td>
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<td></td>
<td>Pressure-resistant institutional investors have a strong influence on a wide range of firm outcomes.</td>
<td>Brickley et al., 1988</td>
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<td></td>
<td>Short-term and long-term institutional investors have different, and sometimes competing, interests.</td>
<td>Tihanyi et al., 2003</td>
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<td>David et al., 2001</td>
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<td>Connelly et al., in press</td>
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<td></td>
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<td>David et al., in press</td>
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<tr>
<td>Private equity</td>
<td>Venture capitalists may be inactive, active-advice-giving, or hands-on; they may work together in syndicates.</td>
<td>Elango et al., 1995</td>
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<td>The influence of business angels and venture capitalists varies with their institutional environment.</td>
<td>Lockett and Wright, 2001</td>
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<td>Bruton et al., 2009</td>
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considerably with respect to their equity positions, the influence of these variations on firm actions and the holdings of other owners remains unclear.

Non-executive employees. Thousands of firms are structured in such a way that most employees own at least some stock; many more utilize programmes where employees as a whole acquire appreciable shares of the firm (Blasi et al., 2003). Although interest alignment and gain sharing (Welbourne and Gomez-Mejia, 1995) are at the heart of this form of ownership, the emphasis is more on creating a social-psychological bond that affects job attitudes (Pierce et al., 1991). Employee ownership can reduce turnover, absenteeism, and grievances while increasing effectiveness, satisfaction, and overall firm performance (Jones and Kato, 1995). Scholars explain these positive results in at least two ways: extrinsically and intrinsically (Buchko, 1993). An extrinsic satisfaction model sees the appreciation of share price as the primary driver behind gains in employee effectiveness and commitment. An instrumental satisfaction model suggests these gains emerge more as a result of added control and influence. Either way, the goal of this ownership structure is to establish a link between an outcome of importance to employees and firm performance. Not all empirical research, however, has supported this link; a meta-analysis by Kruse and Blasi (1995) found no overall conclusion about whether firms with these plans had better performance than firms without them.

Outside Ownership

Complementing the alignment approach, equity held by outsiders may help to motivate these shareholders to monitor more carefully the actions of managers; Dalton et al. (2003) refer to this as the ‘control’ approach.

Blockholders. The Securities and Exchange Commission (SEC) has defined blockholders as any investor with more than a 5% equity stake in the firm. Two main factors motivate large block ownership by outsiders: concentrated control and private benefits. Concentrated control arises from the superior monitoring that blockholders can perform via concentrated decision rights. On the other hand, blockholders also have incentive to use their power over management to enjoy benefits not shared with minority shareholders. Barclay and Holderness (1989), for example, found evidence of the private benefits of blockholders in trades that were, on average, priced at a premium over subsequent trades of other shareholders. Firms may also repurchase stock above market price via private transactions with a dissident blockholder. Firms typically engage in such greenmail transactions to avoid a takeover threat or proxy fight initiated by the blockholder (Kosnik, 1990). Individual blockholders are distinct from institutional investors because they are not beholden to any particular clientele. We also draw a distinction between external blockholders and those inside the firm (i.e. executives and directors) because their objectivity makes them better able to monitor firm actions. However, some have noted that individual large-block shareholders typically serve as directors or officers of the firm (Holderness, 2003). As a result, empirical research usually either ignores
individual outside blockholders or lumps them together with institutional investors, despite potential differences (Mehran, 1995; Shleifer and Vishny, 1997).

Family members, however, are one category of individual blockholder that has been the subject of considerable academic attention (Anderson and Reeb, 2003; Burkart et al., 2003; Schulze et al., 2003). The body of empirical research on family firms shows that family ownership rarely creates value for the firm or its minority shareholders (e.g. Anderson and Reeb, 2003), except in cases where the founder serves as CEO (Villalonga and Amit, 2006). The companion review in this issue discusses the influence of family firms, especially in the broader international context, in greater detail (Johnson et al., 2010).

Corporations also may become blockholders by acquiring a minority share of another firm. Motivation for this type of blockholding varies, but more often than not it precedes either a takeover or complete sale of the stock within a short period of time. Corporate blockholding is a mixed blessing for the target firm. The arrival of a corporate blockholder provides fresh capital that the firm may use to facilitate growth. However, this capital comes at a price because the target firm transfers some level of control to the corporate blockholder, who itself is likely to have an interest in how the target firm’s resources are allocated. Rosenstein and Rush (1990) find that wealth transfer of goods and services at prices favourable to the blockholder have negative implications for the target. This explains in part why empirical research has shown a negative association between corporate blockholders and target firm performance (Bogert, 1996; Mikkelson and Ruback, 1985).

A form of outside blockholding that has garnered popular attention in recent years is state ownership. Although state ownership tends to be higher in emerging economies and those with poorer protection of property rights (La Porta et al., 2002), it is also of interest in developed countries, including the USA and UK, where it has come about as a result of market failures. Such a response may occur in industries characterized by natural monopolies and in markets of public goods or among firms that are deemed too big to fail. The question of which firms and industries should have state ownership and which should compete in open markets occupies a vast literature of its own (Anderson et al., 1999). Although there remains some theoretical debate on the issue, most empirical studies highlight the problems of state ownership (D’Souza and Megginson, 1999; Shleifer, 1998). These problems include ‘soft’ budget constraints, lack of innovation, poor financial performance, and increased corruption (Megginson and Netter, 2001; Tihanyi and Hegarty, 2007). Recognition of the benefits of private ownership has spawned research about how best to privatize state owned firms (Shirley and Walsh, 2001), with the preponderance of research being focused on transition economies (Djankov and Murrell, 2002).

A more subtle form of state ownership revolves around investors that are broadly categorized as sovereign wealth funds (SWFs); these are investment vehicles owned and managed by a national government. In the last few years, SWFs have invested large sums of capital in US, UK, and other developed economy firms, which has drawn the attention, and sometimes ire, of policymakers. Critics raise two main concerns: the lack of transparency of these owners and their potential for preferring political interests over economic and strategic gains (Jen, 2007). Others point out that SWFs are typically...
dedicated, patient investors that look beyond quarterly results and can be a stabilizing force in turbulent markets (Gilson and Milhaupt, 2008). Most of the evidence to date, however, is anecdotal; academics have yet to fully address the issues surrounding the largely political debate about how SWFs may potentially influence the firms in which they invest (Fotak et al., 2009).

Researchers examining blockholder ownership mainly consider the influence of a primary outside blockholder with a very large stake (e.g. the state or a corporate ‘raider’). However, in most firms the presence of several smaller blockholders is more common than a single majority blockholder (Maury and Pajuste, 2005). To the extent their interests are aligned, blockholders may work together to enhance their concentrated control. However, the SEC imposes limits on the collective action of shareholders in an effort to maintain stock market liquidity and avoid collusion among blockholders. Furthermore, blockholders may be in competition with each other to gain private benefits. The interests and influence of blockholders do not exist in isolation. There is therefore a good deal we do not yet understand about how blockholders interact with one another to influence a firm’s actions.

Agent owners. Another set of outside owners is those that invest in the firm as representatives of an underlying fractionated ownership. This creates a dual agency relationship (Arthurs et al., 2008) wherein shareholders serve as principals, discharging duties with regard to managerial agents, and also as agents who are themselves charged with the duty of investing towards particular objectives of ultimate shareholders in a particular fund.

There are several reasons to suggest that agent owners are able to overcome obstacles to firm governance encountered by other shareholders. Agent owners represent fractionated clients who sign over their voting rights, centralizing bargaining power in a single entity and avoiding campaign costs. Owing to a changing regulatory environment in their favour, agent owners can sometimes combine their bargaining strength. With their large holdings, these owners have the incentive and resources to monitor firm actions (Pound, 1988). They benefit from membership in dedicated coordinating bodies, which gives them access to research and inside information not available to other investors (Grinstein and Michaely, 2005). These organizations combine with agent owners’ own professional staff to increase monitoring effectiveness (Ke and Petroni, 2004).

Researchers have categorized various forms of agent owners differently in the finance (Brickley et al., 1988), management (Tihanyi et al., 2003), and accounting (Bushee, 1998) literatures. These include categories such as pressure-sensitive/pressure-indeterminate/pressure-resistant, dedicated/transient/quasi-indexer, and transactional/relational. A common theme among these disparate classifications is that agent owners have different investment preferences and abilities to govern firm actions (Hoskisson et al., 2002). Agent owners have received considerable research attention, as discussed by Johnson et al. (2010) in their review.

Private equity. In the landscape of firm ownership there are also a great many organizations that compete in the marketplace but are not publicly traded. From the early stages of a firm’s life, their ownership is often composed of some combination of founding
investors and close associates, or ‘business angels’. Business angels are early stage investors that arrive at a time when the venture is too small and risky for more formal private equity funds (Prowse, 1998). An often-studied form of private equity is venture capital, which is long-term, unquoted, risk equity from professional investors whose primary reward is capital gain (Wright and Robbie, 1998). Venture capitalists govern firms by controlling the flow of cash disbursements and providing oversight of managerial activity (Gompers, 1995). Because young firms rely heavily on the cash provided by venture capitalists, these owners have particularly strong bargaining power over managers (Zacharakis and Shepherd, 2001). In a manner similar to the categorization of institutional investors, the literature distinguishes between ‘inactive’, ‘active advice giving’, and ‘hands-on’ venture capitalists (Elango et al., 1995), with the latter exercising the most extensive governance. Many venture capitalists are also agent owners that represent the interests of a group of principals who seek to ensure that gains are distributed equitably and that the venture capitalists fulfil their monitoring role. However, recent research suggests that venture capital interests, as well as those of business angels, can vary given the institutional setting of the country in which they are based (Bruton et al., 2009).

As firms grow, other private equity may come to the fore, often in the form of leveraged buyouts (Jensen, 1989). In contrast to the limited involvement of venture capital firms in early stage investments, private equity firms in leveraged buyouts tend to obtain majority control in mature firms (Kaplan and Strömberg, 2009). The involvement of private equity firms in the management of corporations may bring important changes to firm governance, including the development of corporate codes, reduction of agency problems, and improved monitoring of management (Cumming et al., 2007). Private equity firms may also develop highly leveraged capital structures and performance-based managerial compensation (Kaplan and Strömberg, 2009). The involvement of private equity firms has been found to result in reduced innovation but higher return to shareholders (Cumming et al., 2007).

A MODEL OF OWNERSHIP, INFLUENCE, AND FIRM OUTCOMES

Having summarized the dominant forms of ownership in the USA and UK, we turn our attention to firm-level outcomes that have occupied the attention of owners and how they influence those outcomes. The model in Figure 1 incorporates three paths across the three primary components, including a feedback loop. The following sections outline extant research examining each of these paths.

Ownership Structure and Owner Influence

Path A in Figure 1 illustrates the relationship between ownership structure and owner influence. The ‘Wall Street walk’ suggests that owners can sell their shares if they do not agree with executive decision making. However, in recent years shareholders of US and UK firms increasingly use tactics that are more sophisticated than the threat of exit. For example, owners may (a) seek to restructure the firm’s business activities or ownership, (b) work within the existing ownership structure but seek to influence managerial behaviour
through various forms of activism, or (c) adopt a non-activist, buy-and-hold strategy. Providing a realistic picture of the effectiveness of these owner tactics is complicated by a number of factors. For example, different owners may use different tactics based on their interest, organizational characteristics, and power (Ryan and Schneider, 2002). Firms are normally owned by multiple owners that interpret business conditions differently and apply different tactics with a mixed overall effect on firm behaviour (Connelly et al., in press). Also, recent research has shown that managers use forms of ingratiation and persuasion to limit powerful investors from using their coercive power to force changes that could benefit shareholders at the expense of top management (Westphal and Bednar, 2008). Nevertheless, the potential influence of firm owners on corporate governance and strategies remains.

Restructuring. Restructuring tactics by firm owners are illustrated by such examples as Kraft Foods, EchoStar Holding, and Time Warner Cable. Employing corporate restructuring tactics successfully requires power, supporting institutions, and collective action (Davis and Thompson, 1994; Pfeffer and Salancik, 1978). Blockholders may exercise their power through restructuring when their tactic is consistent among a group of blockholders. However, if their action is inconsistent with others, exit of a single blockholder may transfer power to the remaining blockholders (Admati and Pfleiderer, 2007). There is therefore a need for greater understanding of the actions of multiple owners and the ways various forms of owners interact with each other.

Two common approaches to restructuring are spin-offs and sell-offs. Spin-offs create an additional publicly traded security for a new firm separate from the parent, while sell-offs are assets sold to another parent. The spin-off of Philip Morris International (PMI), producer of Marlboro and other leading tobacco brands, for instance, was motivated by increasing regulatory constraints faced by parent company Altria. The spin-off allowed shareholders to benefit from growth in emerging markets while reducing the risk of litigation in Altria’s domestic market. Spin-offs are often used as restructuring tactics when firm performance is high or when it is difficult to find a buyer because of a close relationship with the parent firm (Bergh et al., 2008; Johnson, 1996). Sell-offs, on the other hand, are normally used to improve sagging firm performance. Sell-offs might also be used to generate state revenue (in privatization programmes), save employment, and improve production quality or service (Meggison and Netter, 2001; Tihanyi and Hegarty, 2007).

Another common restructuring tactic is a leveraged buy-out (LBO), which is a private purchase of public equity, and its counterpart management buy-out (MBO), which is a private purchase by individuals inside the firm. In recent years, there has been considerable increase in MBOs and LBOs, resulting in vast private equity markets and renewed scholarly and policy attention (Cumming et al., 2007). CEOs and managers are interested in participating in LBOs for a variety of reasons. First, executives are likely to benefit personally from the deals, given their influence in establishing the ‘fair price’. They also may envision an LBO offering as an opportunity to run the company more efficiently and entrepreneurially (Wright et al., 2000). LBOs may improve corporate governance by reducing agency costs and increasing firm value through improved operating efficiency (Renneboog et al., 2007). These benefits are achieved primarily by
the actions managers take subsequent to an LBO, which include divesting poorly performing units, paring the workforce, and reducing managerial perquisites. Nikoskelainen and Wright (2007) show that this type of activity is most beneficial when LBOs are dominated by outsiders rather than managers. In either case, however, there appear to be advantages to a firm’s governance structure (Wright et al., 2000).

Private equity firms using LBOs may restructure their firms by financial, governance, and operational engineering (Jensen, 1989). Financial engineering occurs when private equity firms not only require management to obtain substantial investment in the firm, but also make their investments illiquid until sale or valuation of the private firm (Kaplan and Strömberg, 2009). Leverage used to obtain control by private equity firms might also motivate managers to more carefully allocate capital resources. Governance engineering refers to direct involvement in boards by private investors. Operational engineering describes value creation by private equity firms owing to their industry and operating knowledge (Kaplan and Strömberg, 2009). By specializing in familiar industry settings, private equity firms are able to develop LBO expertise in repositioning, productivity improvements, and restructuring tactics that may be more effective under specific environmental conditions.

Restructuring often results in improved firm performance. Thompson and Wright (1995) suggest three interrelated areas that tend to change as a result of restructuring tactics. First, managers may increase their efforts in cutting costs; MBOs and LBOs, in particular, provide additional incentives for managers’ cost minimization efforts (Green, 1992). Second, restructuring allows firms to divest unprofitable businesses (Johnson, 1996). Third, restructuring facilitates firms’ adaptation to changing market conditions (Wiersema and Bowen, 2008). Because restructuring tactics are not implemented in isolation, there may be groups of owners and other stakeholders who do not realize gains in the short term or suffer in the long term. These stakeholders may include owners with a long-term equity stake in the firm, employees, or tax authorities (Fox and Marcus, 1992; Thompson and Wright, 1995).

Activism. Owners in recent years have relied on diverse means to influence firms and their managers. The rise in owner activism may be an outcome of increasing ownership concentration, the upsurge of business information from multiple sources, and growing expertise in investment firms and financial institutions. Davis and Thompson (1994) compare this process to social movements, in which owners define their common interest, develop social ties, and mobilize to jointly influence firm behaviour. Owners that engage in activism tend to be large and pressure-resistant, have long time horizons, and own a considerable percentage of the firm (Ryan and Schneider, 2002). Such activism takes a variety of forms, ranging from private meetings with management to hostile media campaigns. Meetings and behind-the-scenes bargaining with management are non-aggressive ways to intervene in the firm’s daily operations. Shareholders can also put forward proposals under SEC Rule 14A-8, which is a relatively inexpensive tactic for owners because they can address issues without the costs associated with lobbying individual managers or shareholders (Sundaramurthy and Lyon, 1998). O’Rourke (2003), for example, identified 287 shareholder proposals aimed at improving corporate social performance (CSP), 98 of which were withdrawn because of compromise or
resolution. This suggests that shareholder proposals may be an effective means of accomplishing desired ends, even if the proposal does not ultimately come to a vote.

Del Guercio et al. (2008) suggest that, despite their low cost, shareholder proposals have not been very effective in changing firm behaviour and performance. These authors consider the effectiveness of ‘just vote no’ campaigns, which activist investors use to persuade other shareholders to withhold their vote on board members. These campaigns often take place in the printed media or on the internet. In a separate analysis, Del Guercio et al. (2003) argue that the effectiveness of these campaigns may lie in the reputation of directors, who are likely concerned about a vote of no confidence being reported in media outlets. These authors find evidence for the effectiveness of ‘just vote no’ campaigns in the forms of disciplinary CEO turnover and performance improvements. There remains therefore some degree of uncertainty about the extent to which the ultimate fate of board members resides in the hands of shareholders and how shareholder power to remove directors could affect decisions on the board.

Some owners increase their direct influence on firms by acquiring seats on the board of directors. Ralph Whitworth’s Relational Investors, the activist mutual fund noted earlier, often attempts to take two board positions through its significant ownership. By doing so, Relational Investors is able to second its motions and the board must then record its vote on critical issues (Liang, 2007). Another means of activism, proxy contests, can be employed to unseat boards of directors whose decisions do not adequately represent the goals of activist owners. Proxy contests are often associated with failed takeover attempts or managers who refuse a takeover offer that otherwise is attractive to groups of influential owners.

Buy-and-hold. Many owners hesitate to intervene when they see performance problems in a firm, preferring instead to display loyalty to management. For example, the indexing approach used by many mutual and pension funds disregards individual firm behaviour, concentrating on portfolios of firms across different industries. When an index investor adopts a buy-and-hold investment strategy, it does not necessarily abdicate its governance role because the owner may have an important long-term influence on a firm’s ability to compete. For instance, Hoskisson et al. (2002) found that these owners can foster greater innovation, a finding confirmed in the accounting literature by Bushee (1998, 2001).

One way these owners affect firm strategies is via the patient capital they provide. When firms are burdened with transient ownership, they are required to focus more on consistent, positive quarterly earnings. This limits the range of options available to them when they consider possible R&D investments or strategic competitive actions that may entail short-term earnings shortfalls with long-term potential benefits. For example, General Mills acquired the worldwide Pillsbury business in October 2001. As a result, earnings fell 48 per cent in the third quarter of that year. Although painful in the short term, General Mills was in a better position to compete with Kellogg’s in the ensuing years. Owners using a buy-and-hold strategy appear to have a greater tolerance for, and understanding of, this kind of strategic competitive activity, and in fact may even be able to provide some of the resources necessary to implement such actions.
Executives recognize that those employing a buy-and-hold strategy are particularly beneficial for the long-term health of a firm. These managers sometimes even take action to woo such investors. Examples of firms trying to accomplish this include Coca-Cola, PepsiCo, and AT&T, all of whom stopped issuing quarterly earnings reports because they were drawing attention away from long-term strategy (Bushee, 2004). Managers also attempt to attract buy-and-hold investors via the content of their public disclosures. To do so, they focus disclosure activity on information that helps investors monitor long-term prospects rather than earnings forecasts that may invite speculative trading.

Not all owners are equal in their ability to know about firms in their investment portfolio. Some invest in a small number of firms and may be better able to understand the business activity in which those firms operate; others are more broadly invested and cannot maintain such in-depth knowledge because of the bounded rationality of investment managers. As large, powerful investors adopt a buy-and-hold strategy with a firm, smaller investors may mimic their investment strategy as a means of sharing some of the value provided by the large staff and voting power of the larger owner. The academic literature has not fully addressed how mimetic isomorphism (Meyer and Rowan, 1977) among owners might affect firm outcomes, although examples in the popular press indicate this may be an important phenomenon.

**Owner Influence and Firm Outcomes/Attributes**

In this section, we review the relationship between the influence mechanisms owners employ and subsequent firm outcomes and attributes such as performance, strategy, and governance processes. It is important to note that not all owner activism is immediately apparent. A phone call from an owner to an executive suggesting a new strategy, for example, is not likely to be visible to outsiders. As a result, a great deal of research examines relationships between owners and firm outcomes in broad forms, without necessarily delineating a specific means of influence. The following discussion summarizes this research, as indicated by Path B in Figure 1.

**Performance.** There is some evidence that internal ownership, the presence of outside blockholders, and dedicated (i.e. long-term) agent owners all lead to better firm performance. The rationale for each of these relationships is different. Insider equity induces managers to focus on performance (Jensen and Meckling, 1976). While blockholders gain larger stakes in the firm, they become increasingly interested in the effectiveness of wealth-creating activities (Mikkelson and Ruback, 1985). Agent owners have greater leverage in pressuring firms to focus on performance-enhancing activities because concentrated holdings provide them with additional voting shares and greater bargaining power with managers (Pound, 1988).

However, empirical evidence for owner influence on firm performance is mixed (Bainbridge, 2003; Dalton et al., 2003). This may be due in part to the preponderance of empirical studies that amalgamate diverse forms of owners despite important differences in their investment horizons and ability to affect firm actions. Some scholars have uncovered significant relationships by grouping together owners that represent particular types of clients (e.g. Hoskisson et al., 2002; Ramaswamy et al., 2002). In this
sense, the influence of agent owners on firm performance appears to exist in the presence of moderator variables (Grinstein and Michaely, 2005; Ramaswamy, 2001; Villalonga and Amit, 2006). The same is likely to be true for other forms of ownership, which explains why meta-analyses often point to the presence of moderators (Dalton et al., 2003).

Besides maintaining positive earnings, firms also have a responsibility to their communities, employees, customers, and other stakeholders (Graves and Waddock, 1994). Recent research on the influence of owners on corporate social performance (CSP) shows that mutual funds are negatively associated with CSP whereas pension funds are positively associated (Johnson and Greening, 1999). Neubaum and Zahra (2006) confirmed these results, finding that long-term and short-term agent owners maintain differing views about CSP. These studies show initial promise that owners have an important bearing on CSP, but scholars have yet to develop a comprehensive body of empirical research examining other forms of ownership or specific aspects of CSP, such as employee wages or the natural environment (Yoshikawa et al., 2005).

**Strategy.** Perhaps the most highly investigated link between owners and decisions within the firm involves the examination of owner influence on innovation. Baysinger et al. (1991) initially found a positive relationship between ownership concentration and corporate R&D spending. Later research found that professional investment funds prefer external innovation whereas pension funds prefer internal innovation (Hoskisson et al., 2002). David et al. (2001) added the notion that owners affect R&D through the medium of activism. One important distinction that this line of research has discovered is that pressure-resistant institutions are positively associated with innovation, but pressure-sensitive institutions are negatively associated with innovation (Kochchar and David, 1996). Bushee (1998) captured this difference more explicitly, finding that transient owners are more likely to pressure firms to cut R&D spending to meet short-term earnings goals.

Research on the relationship between a firm’s ownership structure and corporate diversification has also received considerable attention. Financial economists often cite a study by Amihud and Lev (1981) to show that the absence of large and powerful shareholders results in greater unrelated product diversification. Strategic management researchers, however, questioned these findings (Boyd et al., 2005), Lane et al. (1998), for example, found that ownership concentration was not related to product diversification. Ramaswamy et al. (2002) found that pressure-sensitive owners are associated with unrelated product diversification whereas the association is negative for pressure-resistant owners. Firm owners also appear to influence international diversification (Tihanyi and Ellstrand, 1998). In contrast to product diversification, all types of institutional owners generally support international diversification (George et al., 2005), but for different reasons (Tihanyi et al., 2003).

Strategic management scholars also have examined owner influence on a number of other firm-level outcomes. For example, early research showed that institutional owners foster restructuring activity in order to create more efficient organizations (Bethel and Liebeskind, 1993). Ownership structure also influences a firm’s acquisition strategies, with higher internal equity fostering less risky acquisitions but blockholders and certain
institutional owners pressing for higher risk acquisitions (Wright et al., 1996, 2002). Because research has demonstrated that owners shape the incentives of managers who make competitive decisions, scholars are also beginning to consider the influence of ownership forms on competitive activity between firms. Initial findings suggest that owners may affect both vertical relationships (i.e. upstream suppliers and downstream buyers) and horizontal relationships (i.e. competitive behaviour between firms) (Vroom and Gimeno, 2007).

**Governance processes.** A large body of research considers the effects of specific forms of ownership on other governance structures. For example, research and anecdotal evidence suggests that ownership structure influences board independence as well as the implementation of a variety of governance policies related to issues such as classified boards, greenmail, directors’ duties, and golden parachutes (Bushee et al., 2004). Large, activist shareholders are often successful in their efforts to induce governance changes, but there is little evidence for the systematic effectiveness of those changes in adding value to firms. Others have found more complex relationships between owners and boards wherein they interact in their influence on firm strategies. For example, Tihanyi et al. (2003) found that international diversification was favoured by professional investment funds with outside board members and by pension funds with inside board members. This indicates that particular types of board members may represent the interests of some shareholders better than others.

Executive compensation is also a function of ownership structure (Hartzell and Starks, 2003). In firms with some family ownership, Gomez-Mejia et al. (2003) found that CEO family ties have a negative impact on their pay. However, CEO pay and job status is also more secure because the emotional, familial ties of family owners makes them poor monitors of executive actions. These authors also found that the presence of institutional investors compensates for poor monitoring because institutional investors take an active policing role. Others have provided a more fine-grained understanding of the role of ownership structure on compensation, finding that pressure-resistant owners and outside blockholders negatively influence CEO pay (Almazan et al., 2005; David et al., 1998). The motivation and ability of investors to monitor executive compensation may be compromised depending on what other firms simultaneously reside in their portfolio of holdings (Dharwadkar et al., 2008). Research on ownership structure and executive compensation overlaps in the literature on equity-based incentives (Core et al., 2003). Firms use ownership as a means of compensation with a view towards linking changes in executive wealth directly to changes in stock price.

Ownership structure also affects the market for corporate control. Ownership and the market for corporate control are highly interrelated, because the market will not correct for poor management until stock price declines. For the market for corporate control to work effectively, managerial teams must essentially compete to control specific corporate assets, but the ownership structure of firms that are supposed to serve as the disciplinarian in the market for corporate control also comes into play. For example, Wright et al.’s (1996) finding that managers with more equity in their own firm pursue less risky acquisition strategies suggests that such managerial teams will be hindered in their ability to compete in the market for corporate control. Similarly, there is some evidence that
family-owned firms are insulated from the market for corporate control (Villalonga and Amit, 2006). Public firms also attempt to insulate themselves from the market for corporate control by implementing takeover defences, but many owners recognize these tactics and pressure firms in which they invest not to adopt such defences (Kabir et al., 1997). For this reason, effectiveness of the market for corporate control is often criticized by policymakers and academics (Hitt et al., 1996). In fact, there is even recent evidence that anti-takeover provisions may protect managers from short-term thinking and thus potentially improve shareholder wealth (Turk et al., 2007).

**Firm Outcomes/Attributes and Ownership Structure**

The third and final aspect of our model suggests that potential owners make investment decisions based on information about the firm’s outcomes and attributes. This research is represented by Path C in Figure 1. Research based on signalling theory (Spence, 1973) underscores the influence of these attributes on ownership decisions. Potential owners face a great deal of information asymmetry regarding the future prospects of firms in which they might invest. According to the signalling perspective, firms signal potential owners to indicate firm quality, legitimacy, top management team quality, or strategic direction. Signalling theory proposes that these signals are particularly effective when they are costly and difficult to imitate (Certo, 2003).

Scholars in economics and finance have used signalling theory to better understand how firm attributes may influence investor decision making. Ross (1977), for example, examined debt as a signal of firm quality. Presumably, investors perceive that firms with higher debt levels demonstrate firm quality by inferring that such firms will earn enough income over time to repay their debt. Similarly, Bhattacharya (1979) proposed that firm dividends, which are difficult to reduce or eliminate, serve as signals of firm quality. Dividends serve as a costly signal because only high quality firms will earn enough money in the future to issue large dividends. Other research indicates that a variety of firm characteristics may influence ownership decisions. For example, the equity held by top executives serves as one signal of firm quality, as executives will buy stock when they forecast high levels of future performance and sell stock when the firm’s prospects are not as high (Busenitz et al., 2005; Filatotchev and Bishop, 2002). Other signals that firms may use to communicate desirable characteristics to potential shareholders include incentive-based executive compensation structures (Core et al., 1999), inter-organizational ties (Gulati and Higgins, 2003), top management team and board prestige (Lester et al., 2006), and internal equity holdings (Goranova et al., 2007).

Much of the research examining the effects of firm attributes on ownership decisions occurs in the context of studying firms undertaking initial public offerings (IPOs). As the IPO process transitions privately-held firms to public equity markets, the context provides a natural setting in which to examine investor decision making. Research indicates, for example, that the firm’s human capital may serve as a signal of firm quality. Certo (2003) suggests that investors may use information about boards of directors to make investment decisions. As prestigious outsiders join an IPO firm’s board, investors may deduce that the firm is legitimate enough to attract outsiders who are concerned with protecting their reputations. Additional research using similar logic indicates that aspects
of the firm’s top management team also influence investor decision making (Cohen and Dean, 2005; Higgins and Gulati, 2003; Jain and Tabak, 2008).

Other research in the IPO context examines the extent to which relationships with third parties influence investor decision making. According to this point of view, relationships with prestigious third parties may help to ‘certify’ firm quality. Research indicates, for example, that relationships with prestigious venture capitalists or investment bankers may influence investor decision making (Elitzur and Gavious, 2003; Megginson and Weiss, 1991). Complementing these studies, other research suggests that relationships with prestigious strategic alliance partners influence investor perceptions of firm quality (Chang, 2004; Park and Mezias, 2005). Compared to paths A and B, the research examining path C is less developed. Nonetheless, firms actively use different firm outcomes and attributes, such as debt levels, dividend issues, human capital, and social relationships, to engage future owners and influence investor decision making.

**EMERGING ISSUES**

The landscape of firm ownership has seen dramatic change in recent decades. In the USA and UK, concentrated ownership has shifted from blockholders to more fractionated agent owners, new forms of owners such as hedge funds have dominated the headlines, state and foreign ownership of domestic enterprises have become increasingly common, and managers are more acutely aware of, and beholden to, their ownership structures. We discuss a number of such emerging issues against the backdrop of our basic model and describe avenues for research that the scholarly community might consider to address these issues. While the concepts we cover in this section are at the core of general governance research, the developing nature of owner behaviour and governance systems vary substantially around the world, which Johnson et al. (2010) discuss in their article.

**Emerging Issues in Ownership Structure and Owner Influence**

Ownership of US and UK firms is becoming increasingly concentrated in the hands of agent-owners, which in some ways contradicts what we know about agency theory, which is based on ownership diffusion. Via activism, agent-owners are taking back powers that seemingly were delegated strictly to managers in traditional agency theory. Furthermore, scholars are beginning to recognize the importance of differing interests among these owners. A growing body of literature on ownership heterogeneity reveals that some agent-owners are short-term oriented because their annual portfolio turnovers range as high as 60–80 per cent (Bushee, 1998). Hedge fund owners even take positions expecting the stock price to go down, thus adopting a contrary view of ownership; in so doing, they seek to gain wealth through ‘shorting’ firms by betting that firms will actually reduce the wealth of other shareholders (Kahan and Rock, 2009). Owner heterogeneity is also changing as foreign institutional investors and state owned funds increasingly invest in a wide range of developed economy firms (Aggarwal et al., 2005). For instance, recent increases in state ownership attempting to rescue firms, and even industries, have raised questions about the nature and extent of their involvement in the strategic
decisions of those firms. Similarly, Chinese and Middle East sovereign wealth funds are investing in the USA and other developed economies through acquisition and minority positions (Kaplan and Teslik, 2007). More research is needed to examine what firm strategies this increasing variety of agent-owners will support. Table II presents a range of research questions that scholars might consider with respect to the changing nature of ownership structures and how this new breed of owners might affect the firms in which they invest.

Heterogeneity in ownership types suggests that we need new theoretical development to guide the relationship between increasingly diverse and dynamic ownership structures and the strategic behaviours they encourage. An emerging theory in this area is multiple agency theory, where agent-owners are examined in relation to the particular interests of their ultimate shareholders and how they compare, contrast, and conflict with other agent-owners (Arthurs et al., 2008). Recent work by Connelly et al. (in press) reveals that owners with differing interests not only affect firm strategies differently but also interact with each other in the way they influence firms to engage, or not engage, in competitive activity. These authors also capture the changing nature of owner interests over time, suggesting that owner interests and owner influence are not static propositions. Bruton et al. (2009) add to these ideas, finding that not only are the varied interests of agent-owners and private equity investors (e.g. business angels and venture capitalists) signifi-

### Table II. Emerging issues in ownership structure and owner influence

<table>
<thead>
<tr>
<th>Area of study</th>
<th>Key research questions for future study</th>
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<tbody>
<tr>
<td>Inside ownership and restructuring</td>
<td>How does disparity of ownership among members of the top management team affect organizational structure and change? How is firm expansion influenced by board members that own large shares of the firm and are also on the boards of potential competitors and/or acquisition targets?</td>
</tr>
<tr>
<td>Inside ownership and activism</td>
<td>Does increased inside ownership change executive responsiveness to the pressures of activist investors? How do ownership differences between the board and the top management team affect the ability of the board to represent other shareholders?</td>
</tr>
<tr>
<td>Inside ownership and buy-and-hold</td>
<td>How does inside ownership influence the extent to which executives disclose information to their investment base? How do owners interpret multiple, potentially conflicting, signals from inside owners?</td>
</tr>
<tr>
<td>Outside ownership and restructuring</td>
<td>How does State ownership affect the way firms organize themselves for the competitive marketplace? How do the interests of private equity investors (e.g. business angels and venture capitalists) clash with those of public investors after an IPO?</td>
</tr>
<tr>
<td>Outside ownership and activism</td>
<td>Do agent owners effectively represent the interests of their clients? To what extent to owners work together, or in competition with each other, to influence firms in their portfolio?</td>
</tr>
<tr>
<td>Outside ownership and buy-and-hold</td>
<td>How do long term investors help firms manage their resource dependencies? What are the long-term implications of foreign ownership and sovereign wealth funds?</td>
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</table>
significantly different, but interests also vary across institutional settings. Johnson et al. (2010) in this issue provide a more detailed account of these institutional differences; their international analysis supports our conclusion that more studies are needed to examine varied owner interests and to provide more complex and dynamic theoretical frames that account for the changing nature of ownership structures. Furthermore, future research might examine differences in context between more developed economies such as the USA and UK. For example, historical research in the UK focuses on ‘gentlemanly capitalism’, which helped to manage and spread the power of the British empire (Webster, 2006). Remnants of this approach remain today and have led to firm governance policies which are more informal for firms headquartered in the UK as compared to US firms, especially under the Sarbanes–Oxley regime in the USA (see the Combined Code of Corporate Governance, 2003).

Multiple agency theory also applies to the case of venture capital syndicates (Lockett and Wright, 2001). Recent work on venture capitalists highlights heterogeneity in venture capitalist specialization. De Clercq and Dimov (2008), for instance, suggest that some venture capitalists specialize in internal knowledge (e.g. industry), whereas others specialize in external knowledge through inter-firm relationships. Importantly, this research indicates that venture capitalist specializations have alternative influences on portfolio firm performance. In fact, multiple venture capitalists may even work together, sharing information, capital contributions, and monitoring efforts, to improve firm performance (De Clercq et al., 2008). Despite this sharing, Lockett and Wright (2001) highlight potential agency costs that can arise from the presence of multiple investors in these types of syndicates.

Emerging Issues in Owner Influence and Firm Outcomes/Attributes

The governance efforts of owners are often jointly present and interact with the effects of other forms of governance. However, we know very little about what happens to governance after restructuring efforts. Hoskisson and Turk (1990) discuss this issue, but there remains a dearth of empirical research exploring these relationships or examining the extent to which forms of governance are reformed after ownership changes hands. For example, Haynes et al. (2007) begin to address this subject by examining the impact of refocusing on executive compensation practices. An opportunity exists therefore to expand our understanding of the interaction of governance structures by exploring the consequences of major ownership change. Given increasing managerial attention to ownership structures, resource-dependence theory (RDT) may provide an appropriate theoretical lens through which to better understand principal–agent relationships (Pfeffer and Salancik, 1978). RDT provides a useful perspective for understanding how managers might supervise an increased dependence on agent-owner capital providers. RDT generally incorporates a wide array of constituencies (e.g. suppliers, customers, government entities, and special interest groups) as compared to agency theory’s focus on shareholders. Nonetheless, as sources of capital, owners represent a significant group of resource providers and could potentially serve as an important source of uncertainty (or uncertainty-reducing information) and interference (or strategic assistance).
This is especially true because agent-owners have different interests, which can result in competing demands on managers (Bushee, 2001; Hoskisson et al., 2002). While agency theory is based on issues of efficiency, RDT assumes that issues of power take precedence in establishing governance arrangements. Accordingly, managers of firms that are experiencing conflicting pressures might undertake to influence owners in a way that will be supportive of the firm’s strategic position, independent of efficiency considerations. This would lead to research focused on how managers influence owners, especially agent owners, in a range of activities, including: less aggressive cooperative strategies such as ingratiating, moderate strategies such as monitoring through an investor relations department, and more aggressive influence strategies such as appeasement of particular blockholders (Marcus, 2005; Westphal and Bednar, 2008). For example, top executives may employ strategies to ‘recruit’ certain types of owners that will allow for modification or mollification of the firm’s owners in order to lobby them in a way that would lessen dependence (Bushee, 2004).

Agency theory contains an explicit assumption of potential managerial opportunism. However, an important topic in the future will likely be owner opportunism. As owners become more proactive, they may undertake actions that benefit themselves at the expense of managers and the long-term health of the firm. For example, some shareholders may be so concerned with short-term, quarterly results that they intentionally vote against and discourage long-term projects that may be necessary for the firm to gain strategic competitive advantage (Connelly et al. in press). White and Hoskisson (2009) suggest that one of the difficulties in fashioning effective models of agency relationships may be that researchers have not fully considered the possibility that principals may act opportunistically towards agents. We further suggest that many observed corporate governance outcomes may, at least partially, have their roots in protecting agents against unwarranted principal opportunism, such as short selling. We review these and other future research questions pertaining to owner influence on firm outcomes/attributes in Table III.

Emerging Issues in Firm Outcomes/Attributes and Ownership Structure

Although researchers have established a clear pattern of shareholders influencing a range of firm outcomes and attributes, they have devoted less attention to the possibility of reverse causality (Chenchuramaiah et al., 2005; Demsetz and Villalonga, 2001). There is some possibility that owners are not necessarily bringing about change in firms that they own, but rather investors tend to invest in certain types of firms. For example, research shows a positive relationship between institutional investor ownership and the presence/absence of certain governance policies, such as classified boards and poison pill adoption (Gillan and Starks, 2007). Can we necessarily conclude that these investors actively brought about change in those firms to establish classified boards or not adopt a poison pill? Perhaps not, given that the same association would hold true if shareholders were simply more likely to invest in firms that have classified boards and no poison pills (Bushee et al., 2004). This highlights the need for governance researchers to further address the extent to which endogeneity complicates the relationships under investigation.
A related concern pertains to how returns of the firm are distributed and appropriated by various owners. Agency theory, as the dominant perspective in this area, assumes a nexus of contracts (Jensen and Meckling, 1976), with only one contractual representative, the owners, with an incomplete contract and a claim on residuals of the firm’s wealth creation process. All other parties in the firm, according to agency theory, possess a formal contract, so their costs are expensed by the firm. This has led to the notion of shareholder supremacy, which has become a mantra in schools of business. However, when owners are not unified in their interests, different types of owners may claim different types of residuals, based on their assumed property rights.

Table III. Emerging issues in owner influence and firm outcomes/attributes

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<tr>
<th>Area of study</th>
<th>Key research questions for future study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Activism and firm performance</td>
<td>How do hedge funds change the way firms assess their performance? What influence does ‘shorting’ have on firm performance?</td>
</tr>
<tr>
<td>Activism and firm strategies</td>
<td>How do activist investors with differing preferences affect firm competitive strategies? How is managerial attention allocated when they are presented with competing activist demands?</td>
</tr>
<tr>
<td>Activism and governance processes</td>
<td>How do third-party advisors (e.g. Glass Lewis, Institutional Shareholder Services) influence the effectiveness of activist investors? Who monitors the monitors?</td>
</tr>
<tr>
<td>Buy-and-hold and firm performance</td>
<td>Are long-term investors more concerned about the triple bottom line than other types of owners? To what extent do more powerful and influential investors appropriate rents due to other investors or other stakeholders?</td>
</tr>
<tr>
<td>Buy-and-hold and firm strategies</td>
<td>To what extent do firms learn from the experience of their long-term owners, as those owners are also invested in other firms? Are the strategic recommendations coming from long-term investors wise?</td>
</tr>
<tr>
<td>Buy-and-hold and governance processes</td>
<td>How does an institutional investor’s portfolio of firms influence the effectiveness of the market for corporate control? How do institutional differences among foreign owners affect executive compensation?</td>
</tr>
<tr>
<td>Restructuring and firm performance</td>
<td>What happens to the entrepreneurial orientation of executives following a managerial buy-out? How do corporate spin-offs diffuse through a cluster of firms with activity in similar markets?</td>
</tr>
<tr>
<td>Restructuring and firm strategies</td>
<td>How does the entry, or exit, of a single powerful blockholder influence a firm’s tactical and strategic competitive activity? How is a firm’s involvement in corporate entrepreneurship affected by a leveraged buy-out?</td>
</tr>
<tr>
<td>Restructuring and governance processes</td>
<td>How do owner-initiated restructuring activities influence other stakeholders with long-term stakes? How can governments efficiently privatize firms while still holding executives accountable to their new ownership structure?</td>
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Some may desire dividends, others stock buy backs or stock value appreciation, and still others may seek to change the way residual claims are allocated by changing the firm’s basic strategy.

Going further, if one changes the assumption to incomplete contracting (Aghion and Bolton, 1992) rather than formal contracting for all stakeholders (e.g. suppliers, buyers, employees, government entities), then appropriation of the firm’s wealth becomes a more salient issue (Foss and Foss, 2005). One of the central bodies involved in the appropriation process would be the board of directors, because owners lobby to become board members based on their ownership positions (Liang, 2007). As well, in the USA some parties (e.g. commercial banks) are prevented from ownership through legal institutions. Therefore, understanding the criticality of the board in managing the competing demands of multiple stakeholders, including capital stakeholders, is a key issue for future research. Team production theory (Blair and Stout, 1999) may be useful in this regard insofar as it explains how a hierarchical body, such as the board of directors, can help to manage the appropriation process for various stakeholders, including a range of diverse capital holders. Understanding the appropriation process is critical for any property rights system because without trust in the appropriation process, not only do markets break down but managers and employees are unwilling to make firm specific investments that are the basis for value creation (Wang and Barney, 2006).

Issues of endogeneity and rent appropriation may be particularly sensitive to the sources of data researchers use to understand the phenomena. Governance research has often relied on archival sources of ownership information, making use of corporate proxy statements and surrogate databases such as Value Line, Compac Disclosure, Corporate Text, and Spectrum, among others (e.g. Bushee, 2001; Dalton et al., 2003; David et al., 2001). There is considerable discrepancy between these sources, suggesting that not all data sources will yield similar results in empirical governance research (Anderson and Lee, 1997). Further, governance researchers often consider various forms of owners, but devote little academic attention to understanding owners from a behavioural standpoint. Future research could begin to explore the actions of owners more qualitatively and via surveys so that we might gain a more nuanced understanding of how owners affect firms and their managers. This and the other issues described in this sub-section raise a number of pertinent research questions, which we present in Table IV.

Conclusion

In summary, we have reviewed research and theory on firm ownership using examples of US and UK firms and studies to foster a better understanding of the relationships between a firm’s ownership structure, the interests and influences of owners, and how they affect firm-level outcomes. Evidenced by their presence in the headlines of the Wall Street Journal, a diverse and rapidly changing range of firm owners has become increasingly involved in corporate activity. As scholars and custodians of the theories describing corporate governance, it behoves us to understand the changes taking place and to consider how they modify, or even transform, what we know about owners as a form of corporate governance.
Table IV. Emerging issues in firm outcomes/attributes and ownership structure

<table>
<thead>
<tr>
<th>Area of study</th>
<th>Key research questions for future study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Performance and inside ownership</td>
<td>How do crisis situations influence insider ownership decisions (i.e. buy/sell)? Do industry characteristics (i.e. munificence, dynamism, complexity) moderate the relationship between past performance and inside ownership?</td>
</tr>
<tr>
<td>Performance and outside ownership</td>
<td>How do firms use the information provided in earnings reports to attract particular types of investors? How do investors react to firms that are early adopters, majority adopters, and laggard adopters of corporate social performance initiatives?</td>
</tr>
<tr>
<td>Firm strategies and inside ownership</td>
<td>How do risky firm strategies (e.g. R&amp;D expenditures, M&amp;As) influence subsequent insider ownership decisions? How does international diversification change the role of inside ownership as a means of alleviating agency concerns?</td>
</tr>
<tr>
<td>Firm strategies and outside ownership</td>
<td>To what extent do internationalization strategies help firms attract foreign investors? How does a firm’s balance of tactical and strategic competitive actions influence its mix of transient and dedicated institutional investors?</td>
</tr>
<tr>
<td>Governance processes and inside ownership</td>
<td>What are the ownership implications of pay disparity between the CEO and other members of the top management team? How do an insider’s social relationships, such as board interlocks, influence insider ownership?</td>
</tr>
<tr>
<td>Governance processes and outside ownership</td>
<td>How can firms establish legitimacy with investors following a governance failure? What governance practices can a firm implement to avoid being targeted by Institutional Shareholder Services and other activist coordinating bodies?</td>
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<td>Ownership as a Form of Corporate Governance 1583 © 2010 The Authors Journal of Management Studies © 2010 Blackwell Publishing Ltd and Society for the Advancement of Management Studies</td>
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