# History and development of ownership research

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## Abstract

This article reviews extant research literature relevant to the research topic of ownership research. First, the practical and theoretical aspects of corporate governance are reviewed on a general level, and then the theoretical ownership research frameworks in a historical view.

The importance of ownership research is evident in the fact that corporate governance and the ownership structure of companies is currently characterised by change processes as the economies of the world become more and more globally integrated. Ownership structures are also of major importance in corporate governance because they affect the incentives of managers, and thereby the efficiency of firms.

The basic information search strategy was to search in all relevant information resources by relevant key words. It seems that all research on corporate governance is actually related to ownership research. The topic is interdisciplinary; there found a wide selection of literature in Economics-, Sociologic - and Biologics etc.

The potential problems associated with the separation of ownership and control, have intrigued researchers for well over 70 years. During this time, organizational observers have witnessed an evolution from concentrated ownership to increasingly diffuse ownership, a change that has resulted in the potential for managerial self-interest to dominate shareholders' interests.

The history of economic thought, serves information, from the ancient times until the modern day. Early work in this area was largely descriptive (e.g., Berle et al. 1932). As research became systematic in approach, researchers relied primarily on agency theory to guide their studies. CEO compensation research illustrates the issues attendant on contemporary research in ownership studies more generally. Another important focus of ownership studies are institutional investors and large block holders. One of the more promising areas of investigation with regard to institutional investors is examination of the differing incentives across institutional investor categories (Daily et al. 2003). These important distinctions among ownership categories also suggest that any one theoretical perspective is insufficient for capturing the complexity of the differing interests of ownership types. The trend is toward multi-theoretic ownership structure research.

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## 1. INTRODUCTION

This article reviews extant research literature relevant to the research topic of ownership research. First, the practical and theoretical aspects of corporate governance are reviewed on a general level, and then the theoretical ownership research frameworks in a historical view.
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## 2. MATERIAL AND METHODS

The importance of ownership research is evident in the fact that corporate governance and the ownership structure of companies is currently characterised by change processes as the economies of the world become more and more globally integrated. Ownership structures are also of major importance in corporate governance because they affect the incentives of managers, and thereby the efficiency of firms. The ownership structure is defined by the distribution of equity with regard to votes and capital, but also by the identity of the equity owners.

The term "corporate governance" has come to mean many things. It may describe the processes by which companies are directed and controlled. It can also refer to: the encouragement of companies' compliance with codes (as in corporate governance guidelines); investment techniques which are based on active ownership (as in corporate governance funds); and a field of economics, which studies the many issues arising from the separation of ownership and control. However, the concept of corporate governance is poorly defined because it potentially covers a large number of distinct economic phenomena. Corporate governance is the set of processes, customs, policies, laws and institutions affecting the way a corporation is directed, administered or controlled. Corporate governance also includes the relationships among the many players involved and the goals for which the corporation is governed. The principal players are the owners and management. Other stakeholders include employees, suppliers, customers, banks and other lenders, regulators, the environment and the community at large. (Wahl, 2006)

If we speak about corporate governance we mean usually governance of companies whose securities are listed on the stock exchange. We could easily find Shareholders Lists of those companies (count only 15), but the stock exchange in Estonia is weak and majority of Estonian companies aren't listed so we don't know a lot of them owners. The current research includes all owners of Estonian capital companies (total count 73 867); it wouldn't be easy but possible to find material about all of them.

Since regaining independence in 1991 Estonia has transformed itself to a highly motivated and dynamic center of commerce. The Baltic Sea region is the fastest growing business region in Europe. Estonia's economic success has been built on stable currency, liberal foreign trade regime, liberalization of prices, and abolition of state subsidies, fast privatization and effective bankruptcy legislation. As a result, Estonia has advanced fast in terms of stabilizing and restructuring the economy and has been rewarded with high levels of foreign direct investment.

Estonian legal system is based on the continental European model. The new Commercial Code has been effective since 1. September 1995. The law expresses the basic principles of Estonian entrepreneurship according to the best European traditions and standards and outlines the role of the Commercial Register.

According to the Commercial Code there are five forms of business entities (Companies), which are created by entry into the Commercial Register, also it is shown the amount of them :

- General Partnership (täisühing or TÜ), 376;
- Limited Partnership (usaldusühing or UÜ), 715;
- Commercial Association (tulundusühistu), 687;
- Private Limited Company (osaühing or OÜ), 68963;
- Public Limited Company (aktsiaselts or AS), 5906.

The Council Regulation on the Statute for a European Company of the European Union contains rules for a European Public Company, called a Societas Europaea (SE), there is also a statute allowing a European Cooperative Society (SCE). The 25 different member states of the European Union have widely different company laws. This means that companies have to comply with many different regulatory systems, and merger of companies from different states is often complex and difficult.

In Estonia the management of a public limited company operates through general meetings of shareholders, the Management Board and the Supervisory Board. A private limited company operates through the Management Board. The general meeting of the shareholders has the highest authority in the corporation and is to be convened at least once a year. It approves the annual report, distributes profits, elects the Supervisory Board and the auditors of the corporation, amends the Article of Association, increases and decreases the share capital, decides on dissolution the public limited company according to law. Resolutions are usually passed by a simple majority vote. However, for a change in the Articles of Association or termination of its operations and for a resolution to decrease or increase share capital, a majority of 2/3 is required. The Management Board is the executive body of the corporation, which represents and manages the corporation. The Management Board must report the corporation's activities and economic situation to the Supervisory Board at least once every four months. The Supervisory Board plans the strategic activities of the corporation, arranges its management, and controls the Management Board. A member of the Management Board cannot be a member of the Supervisory Board.

The basic information search strategy is to search in all relevant information resources by key words: corporate governance, ownership research, ownership structure, ownership, ownership typology, ownership theory, governance and ownership, owner type, owner identity, ownership configuration etc. Found relevant books and journals are critically evaluated information sources. It seems that all research on corporate governance is actually research on ownership. Ownership is the exclusive possession or control of some thing, which may be an object or some kind of property. Some consider the term to be closely associated with the idea of private or public wealth. It is also claimed by some that the exclusivity of ownership underlies much social injustice, and facilitates tyranny and oppression on an individual and societal scale. Ownership research needs delicate and sensitive information. Publications by type speak about the quality of the selected publications. Articles and dissertations include fresh and very high quality peer reviewed information. Journals by topic gave a clear picture of the interdisciplinary of the topic; there is a wide selection of Journals in Economics-, Sociologic- and Biologics. Interdisciplinary is the act of drawing from two or more academic disciplines and integrating their insights to work together in pursuit of a common goal (Brunnengräber et al., 2004). Interdisciplinary Studies use interdisciplinary to develop a greater understanding of a problem that is too complex or wide-ranging to be dealt with using the knowledge and methodology of just one discipline (e.g. ownership research).

## 3. HISTORY OF OWNERSHIP RESEARCH

The potential problems associated with the separation of ownership and control in the corporate form of organization have intrigued researchers for well over 70 years.

During this time, organizational observers have witnessed an evolution from concentrated ownership to increasingly diffuse ownership, a change that has resulted in the potential for managerial self-interest to dominate shareholders' interests. Whereas organizations at the beginning of the 20th century were largely dominated by owner-managers, contemporary organizations are characterized by professional managers with modest, if any, ownership stakes in the firms they manage.(Daily et al., 2003)

The corporation as an entity predates early research on ownership and control by several hundred years. The corporate form of organization has been traced to the reign of Queen Elizabeth I. It wasn't until the 1800s, however, that public corporations structured as we know them today began emerging. The corporate form of organization proved popular, as a function of the protection that limited liability provided investors. (Daily et al., 2003)

The history of economic thought, serves information, from the ancient times until the modern day. One of the earliest treatments of ownership and control issues is the seminal work of Berle and Means (1932), “The Modern Corporation and Private Property”. Means captured the general premise behind this series of work when he observed: "Ownership of wealth without appreciable control, and control of wealth without appreciable ownership, appear to be the logical outcome of present corporate development" (Berle et al., 1932).

Early work in this area was largely descriptive (e.g., Berle et al., 1932). As research became systematic in approach, researchers relied primarily on agency theory to guide their studies.

The central premise of this theory is that managers, as agents of shareholders (principals), can engage in decision making and behaviours that may be inconsistent with maximizing shareholder wealth (Fama, 1980; Jensen et al., 1976). As evidence of its applicability to ownership studies, agency theory has been characterized as "a theory of the ownership (or capital) structure of the firm" (Jensen et al., 1976). More recent research has also noted the dominance of agency theory as the guiding framework for corporate governance studies generally and ownership structure studies more specifically (Daily et al., 2003).

CEO compensation research illustrates the issues attendant on contemporary research in ownership studies more generally. Much of this research incorporates examination of equity-based elements of CEO compensation, with the vast majority of these studies being grounded in agency theory. Demsetz and Lehn captured in their examination of the antecedents and outcomes of ownership structure: "If diffuseness in control allows managers to serve their needs rather than tend to the profits of owners, then more concentrated ownership by establishing a stronger link between managerial behaviour and owner interests, ought to yield higher profit rates". (Daily et al., 2003)

Beyond the dominance of agency theory as the guiding framework for this body of research, compensation studies serve as an excellent exemplar of ownership research due to the variety in their reported findings. There is little apparent consistency in relationships between ownership and firm processes or outcomes. (Daily et al., 2003).

Another important focus of ownership studies are institutional investors and large blockholders. Institutional investors and large blockholders control an increasing amount of corporate equity. (Daily et al., 2003)

One of the more promising areas of investigation with regard to institutional investors is examination of the differing incentives across institutional investor categories (Daily et al., 2003). There are only a handful of studies that actually focus on developing a classification system for ownership. Many authors and institutions have come up with different classification features that basically reflect their special interest in the field. Jensen et al. (1976) differentiated between owners with inside equity, outside equity, and debt. Charkham (1995) classified owners as foreign, miscellaneous, privately held corporations, legal persons in public law, private persons, insurance companies, banks, pension funds, and mutual funds. Gerndof (1998) observed many of the same classifications, but also differentiated between majority owners, minority owners, long term owners, 'wildcat' investors, foreign investors, domestic investors, risk spreaders, actives owners, passive owners, known owners, absent owners, and strategic owners. Djakov (1999) also differentiated ownership between management, employees, the state, and local outsiders. La Porta et al. (1999) further categorized owners between that which is widely held, family owned, state owned, and that which is controlled by corporations. These and other similar classifications have also been adopted by authors such as Thomsen et al (2000), Mathiesen (2002), Kalmi (2003), Vitols (2003), Heubischl (2006). Ownership categories can also be seen through a national perspective, such as Estonian insiders and Estonian outsiders (Generalistide intervjuude kokkuvõte, 2004), or Estonian corporate, foreign corporate, Estonian individual and foreign individual (Estonian CSD, 2006). Each author's ownership classification system is a theoretical framework, and the first step to develop an ownership typology that could be used in various ownership studies. The issues underlying ownership structure studies are complex. The differing objective functions attendant on various owner categories must be accounted for in any examination of the nature of the relationship between ownership structure and firm processes and outcomes (Daily et al., 2003).

These important distinctions among ownership categories also suggest that any one theoretical perspective is insufficient for capturing the complexity of the differing interests of ownership types. Although agency theory is applicable where effective alignment of interests and control of managers dominate, alternative theoretical perspectives provide necessary alternative lenses through which to view ownership structure. Resource dependence theory and stewardship theory, for example, have gained currency as researchers have sought more comprehensive explanations for corporate governance relationships in general. (Daily et al., 2003)

Research on the bases of power within organizations began as early as Weber (1922) and included much of the early work conducted by social exchange theorists and political scientists. Resource dependence theory focuses on the process through which organizations reduce their environmental dependencies using various strategies, which enhance their power within the inter-organizational system (Parvinen, 2003).

Agency theory suggests that the interests of opportunistic, self-interested agents conflict with those of principals. Stewardship theory suggests instead that executives' interests are aligned with company interests and that executives are thus more intrinsically motivated than agency theory implies. The biggest difference between stewardship theory and agency theory lies in their divergent views of executive identification and motivation. Research results suggest significant differences between founder-stewards and no founder agents that diminish with company growth, and significant effects of equity ownership and outside rounds of financing (Wasserman, 2006).

Stakeholder theory begins with the assumption that values are necessarily and explicitly a part of doing business. It asks managers to articulate the shared sense of the value they create, and what brings its core stakeholders together. It also pushes managers to be clear about how they want to do business, specifically what kinds of relationships they want and need to create with their stakeholders to deliver on their purpose. Truth and freedom are best served by seeing business and ethics as connected. (Freeman et al., 2004)

One contribution of evolutionary approaches to governance and management of companies is that evolution is not a static process and that company development is path dependent, i.e. history matters. A review of the literature shows that evolutionary approaches are not explicitly used as a theoretical framework in corporate governance, although the evolutionary perspective is consistent with it (Mustakallio, 2002).

For example the overall research question of the dissertation Mustakallio (2002) is: What are the impacts of the governance mechanisms on the performance of family firms? The study specifically focuses on relationships between family firm governance and strategic decision-making quality, defined in terms of decision quality and decision commitment. This study develops and tests two models of family firm governance, one focusing on contractual, and the other on relational, governance. Mirroring the prescriptions of agency theory, contractual governance addresses aspects of the formal control exercised by the boards of directors. Drawing on social capital theory, the relational governance model addresses different forms of social capital embedded in social relationships. Decision quality and decision commitment are used as dependent variables in the models. Constructs related to both contractual and relational governance are employed as independent and mediating variables. Links between decision-making quality and overall firm performance are tested in a third model. The hypotheses are tested using mail survey data from 192 family firms in Finland. The study uses confirmatory factor analysis to validate the constructs and multiple regression analysis to test the hypothesized relationships. The validity and reliability of the constructs are further checked using secondary proxies obtained through telephone interviews. The hypotheses on governance mechanisms, as well as those on the influence of these on decision-making quality, are mostly supported in the empirical analyses. Also, the results suggest that contractual and relational governance mechanisms are complementary rather than mutually exclusive. Hypotheses on the relationship between the decision-making quality variables and the overall family firm performance received partial support. This dissertation contributes to the understanding of how family firms are governed and of the impacts of various governance mechanisms on family firm performance. The results of the dissertation support the claim in the extant literature that family firms need to address the governance of the family in addition to the governance of the business. The dissertation proposes relevant practical implications for family firm owners and executives, and suggests directions for future research. (Mustakallio, 2002)

Articles included in the report incorporate multiple theoretical foci and extend across multiple contexts. The trend toward multi-theoretic ownership structure research (Daily et al., 2003). Among the theoretical frameworks represented are agency theory, stewardship theory, and behavioural decision theory.

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